Africa: Opportunities and Challenges

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BACKGROUND

Poverty. Drought. Backwardness. Despotic. Civil wars. Those are some of the words that are associated with the African continent. Most of the heavily indebted poor countries (HIPC) are located in Africa. The Gross National Income (GNI) of many of the African countries is among the lowest in the world. The per capita GNI of Burundi for example was USD 400 in 2010 (World Bank). For many of the African countries, things are changing for the better in the last few years. China's need for raw materials, natural resources and energy has brought in billions of dollars of investments in Africa, which the continent badly needs to improve infrastructure, provide jobs and stimulate economic development. By 2015, China's investments in Africa will reach USD 50 billion and the bilateral trade between China and Africa will reach USD 300 billion, double the figure for 2010 (The Asset Magazine, 2011). There are many criticisms over China's dealings in Africa but the fact remains that China has brought prosperity and developments into many African countries. Discoveries of oil and gas in the continent have also contributed to the robust economic growths in recent years. World Bank predicted that the GDP growths for Sub-Saharan Africa in 2011 and 2012 will be 5.3% and 5.8% respectively (The Economist, 2011).

With a population of over one billion and positive economic prospects, Africa has become a large consumer market for almost everything including food products. The robust economic growth over the past decades has increased the number of middle class population in Africa. The middle class group is now estimated at 313 million, double the number from 151 million in 1990 (Reuters, 2011). By any standard, this is a big increase in the middle class population which can increase the purchasing power of the African countries. The need for resources by the world's major economies will ensure that Africa will continue to receive investments in agriculture and mining sectors. The alleged 'land grabbing' issue reported in the media is the result of the race among the investors to capture the best deals. Not all the investments are successful. But the successful ones are likely to provide Africa with prosperity.

Palm oil is one of the commodities imported and consumed in large quantities in Africa. According to *Oil World Annual* (2011), Africa consumes about 10.7 million tonnes of oils and fats annually of which more than 60% are palm oil. Africa should no longer be viewed as high risk for trade but rather as a potential market for trade and investments. Should the economic problems worsen in Eurozone and USA, Africa should be able to mitigate the effects of lower demand from those economic powers.

FACTORS AFFECTING PALM OIL IMPORT

Africa is a very diverse continent in terms of culture, climate, language, *etc*. Thus, each region or country has its own issues pertaining to oils and fats. A few countries may share common issues on oils

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reported that Sime Darby is going to invest in a refinery in France for its palm oil production in Liberia. Countries in North Africa, Egypt and East Africa will continue importing from Southeast Asia depending on the costs of freight.

Government Policies and Duty Structure

Government policies will determine the categories of palm oil to be imported into Africa. East African countries namely Kenya, Tanzania and Uganda used to import refined, bleached and deodorised (RBD) palm oil but then shifted to crude palm oil when a new duty structure favours the import of crude palm oil. For example, the East African Community has set the customs tariff at 0% for crude, 10% for intermediate and 25% for refined/finished product. The edible oils companies have set up refining and fractionation facilities to respond to this change.

Although the three East Africa countries share common customs tariff, the palm fractions imported differ to suit local requirements. Kenya is a solid fats market and more RBD palm oil is imported compared to Tanzania, a liquid fats market, which needs to import more palm olein.

The duty structure does not only change the components of import but also changes the oils and fats industry in the country. For example, there used to be about 18 soap producers in Tanzania but with the new duty structure, stand-alone soap producers are no longer competitive and today only two stand-alone soap producers remain.

Uganda is a predominantly liquid oil market dominated by palm olein. Local edible oil production is small of mainly sunflower oil. Uganda has an oil palm plantation by Bidco on Bungala Island in Lake Victoria, a private sector investment with the support of IFAD and government of Uganda. The production from this plantation will partly replace the imported oils.

In Ethiopia, the government introduced a price cap for a number of food products in January 2011 following the double effects of 17% currency devaluation in December 2010 and high world prices of commodities. According to the new commodities price, the government urged traders to minimise the prices of some commodities, which are essential to the majority of the people, especially for the poor.

The price reduction affects food items such as edible oil, bread, pasta and macaroni, meat, sugar, tea leaf, bananas, oranges, soft drinks, wheat flour, soap, construction steel, steel sheets, paintings, clothes, textiles, shoes, bottled water and beer. Some of the commodities had their prices reduced by 50% and above, especially edible oil and sugar.

The price ceiling has affected not only those who are in the retail business but also those who have already ordered items from outside the country. The effect of the unreasonable price control is equally devastating to the palm olein exporters. Buyers have simply stopped importing bottled cooking oil to avoid further losses. There was a sharp drop in palm olein import into Ethiopia after the enforcement of the ceiling price.

The government decided to form a company to import the goods and sell them at the capped prices. The Merchandise Wholesale and Trade Enterprise was allowed credit by the Commercial Bank of Ethiopia to import 12 500 t of palm oil. The government had purchased all palm oil imports ordered by Ethiopian traders and supplied them to the market at subsidised rate. The government has also invited a few companies to participate in a long-term supply of cooking oil to Ethiopia.

In April 2009, Cameroon imposed a high import duty on cooking oil to USD 3 per litre. With this import duty, there was a sudden stop to the import of cooking oil in consumer packs. Before the introduction of the new import duty on cooking oil, imported palm olein in consumer packs was cheaper than the locally produced palm oil despite paying about 55% import tax. The local industry has reacted by urging the government to increase the import duty on palm oil arguing that it would boost local production of palm oil. Those with refining capacity have benefited because they are allowed to import crude palm oil for further processing, and many have increased their capacity. Soap factories are also allowed to import crude palm oil and palm stearin for soap production at the normal rate of import duty. Other palm oil products are not affected by the new import duty.

For a long time, Nigeria has banned import of edible oils and fats. Although the ban has managed to increase the local prices of crude palm oil, it took a very long time before investors were

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convinced to venture into oil palm plantations. Production has not improved much while the demands kept on increasing. Traders took the opportunity to bring cooking oils from Benin and other neighbouring countries through border trade.

In December 2008, the ban on crude palm oil import was lifted. An import duty of 35% is imposed on crude palm oil but if the oil is imported from Economic Community of West African States (ECOWAS) countries, the duty does not apply. Fats and fat products for the usage of food industries as well as soap producers are also allowed to be imported with duties ranging from 5% to 20%. For example, the import duty on tallow is 5% and that of soap noodles is 20%.

With the ban of edible oil import, a number of refineries have been built but most of them faced a scarcity of crude palm oil. As the ban on crude palm oil is lifted, the refineries receive a new lifeline. A few refineries started to import crude palm oil, resulting in a surge of export to Nigeria in 2011.

The food industries particularly biscuits and frying establishments and restaurants are the major users of palm oil and products. Biscuits manufacturers are allowed to import shortening as a raw material and most soap manufacturers use soap noodles as raw materials although tallow can be imported at only 5% import duty. However, only a few soap companies continue to use tallow. Restaurants mainly use refined edible oils which are mainly imported through the borders. Big frying establishments such as instant noodle producers, obtain their frying oil from local refineries while some would import crude palm oil for contract refining.

The subsidy scheme has a big impact on the consumption pattern of oils and fats in Egypt. In the 1980s and 1990s, Egypt used to be solid fat dominated market. The trend shifted slowly to liquid oil because of the subsidised cooking oil which is a blend of sunflower and soyabean oils. The scheme has also encouraged the installation of crushing plants in Egypt for soyabean.

Despite the subsidy scheme favouring liquid oils, imports of palm oil have grown to reach almost one million tonnes in 2010. Palm oil is mainly used by industrial consumers, and while the closure of factories during the peak of the political unrest had slightly reduced volume of consumption, the demand for palm oil continues to remain strong.

Imports of vegetable oils and fats into Egypt are duty free in any form, *i.e.* bulk or packed but other taxes are higher on packed products. The favourable duty structure has made Egypt an emerging centre for re-export of palm oil. Egypt exports oils and fats to Sudan, Libya, Algeria, Yemen and other neighbouring countries. This trend is still maintained amid disruptions in the political situation. The oils and fats industry in Egypt has the scale to be competitive in the regional market. Its food industry is the biggest in the Arab countries helped by exports of manufactured food products.

The recent political disturbances have prompted the Egyptian government to increase the supply of cooking oil under the subsidy scheme to contain inflation and to avoid further chaos. The volume of subsidised cooking oil which was only about 250 000 t per year is expected to reach more than 900 000 t by end of 2011.

In Egypt, cocoa butter substitutes (CBS), cocoa butter equivalent (CBE), cocoa butter replacer (CBR) and other specialty fats are all categorised as CBS. The classification is not accurate as some of the products do not fall within the standard specifications of CBS. The products therefore are declared as 'other oils and fats' which attract 10% import duty while CBS is exempted from import duty. In order to take advantage of the current import duty structure, importers restrict themselves to importing those specialty fats which are in compliance with the standard specifications. Otherwise, Egypt could have more options on the specialty fats imported into the country. Egypt is the largest importers of palm kernel oil products in Africa.

In Algeria, the edible oil sector used to be controlled by the public sector. The economic liberalisation in late 1990s opened up opportunities for private sector to get involved in the industry. Since then, a private company, Cevital has been the major oils and fats importer and is the single major palm oil buyer. In 2006, the edible oil industry was totally in the hand of the private sector after ENCG units were sold to a number of private companies. The new companies are keen to develop more palm-based products but logistics issues are the major problems holding back higher consumption of palm oil in Algeria.

The import duty before May 2005 was 5% for bulk refined palm oil/refined olein but after that it was taxed at 30% making it uneconomical for importers and processors to import RBD palm oil/RBD palm olein. Import duty had been at 5% on crude oils, 30% on refined. In September 2006, the duty was reverted to the old duty structure. However, since the importers had started importing crude palm oil, they have continued importing the oil as it is more economical although refined palm oil is again competitive in Algeria. Hydrogenated oils for industrial use are also taxed at 5% making it competitive to import shortening, CBS and other hydrogenated fats. Due to the duty structure, local manufacturers control the cooking oil sector while the solid fats market is dominated by imported products.

In Tunisia, the cooking oil sector is subsidised by the government, with Office National de l' Huile (ONH), the government agency responsible for the purchase and distribution of cooking oil. ONH imported palm olein for the first time in 2004 and since then it has become the largest importer of palm oil. In 2008, the import of cooking oil for the industrial and frying sector was liberalised and not controlled by ONH alone prompting construction of new refineries. Local manufacturers started to supply cooking oil to the industrial sector. Palm olein was set to become the largest oil consumed by the industrial sector, however as a result of the revolution in December 2010, the import of edible oils has dropped sharply. It is expected that the situation will stabilise soon.

Morocco is a sizeable oil/fat market but palm oil has a small share due to the traditional use of soft oils, and secondly, the high import duty of palm oil at 303% had discouraged companies from purchasing palm oil. The tariff was later revised. However, there is an import duty differential of 22.5% between crude (2.5%) and refined oil (25%); hence refined palm oil is out of competition.

A company tried to introduce palm oil in a big way by installing a physical refining capacity and a fractionation plant but the project was a failure owing to logistics problems. Freight was expensive for the company to import small quantities of crude palm oil direct from Southeast Asia. Thus, it is imported from Rotterdam but the price is not competitive once the product is processed into palm olein. The situation might change if Morocco could get supplies of crude palm oil from West Africa. However, production in the region is still not large enough to make an impact on exports.

Senegal is predominantly a liquid oil market, mainly sourced from locally produced groundnut. Soyabean oil imports sometimes reach more than 100 000 t, with SUNEOR (previously known as SONACOS), a government company, as the main edible oil company. It deals with the local oilseeds activities including groundnut purchasing, crushing and refining, and imports soyabean oil for refining and packing as cooking oil.

Import duty is 10% for crude oil and 20% for refined oil. However, other taxes are imposed that the cumulative taxes can vary from around 27% to about 66%. In combination, the duties and taxes have caused refined palm oil products to be generally uncompetitive. From Malaysia, the main palm products are palm olein and palm fatty acid distillate (PFAD).

It was also reported that Senegal has gazetted that only double fractionated palm olein is allowed as cooking oil, making it uncompetitive compared to soyabean oil.

Similarly in the soap sector, import duty regime and other taxes make RBD palm stearin uncompetitive compared to tallow, which has a duty of only 5%. Crude palm oil destined for soap manufacture also carries a similar import duty of 5%. But RBD stearin as refined oil is levied an import duty 20%, which is discouraging soap makers from using it and a few laundry soap producers are using PFAD.

Since 2000, South African import duty structure has remained unchanged. Under the general duty, all oils are imposed 10% import duty. Full industrial rebates of custom duties are given if they are used as raw materials in manufacturing industry such as margarine and shortening, soap and washing preparations, plastics, chemical preparations, sugar confectionery, bread and pastry cakes, tanning and dyeing. However, oils and fats imported for the purposes of refining, hydrogenation or blending and finished products such as cooking oil, margarines and cooking fats are not eligible for the rebate of the paid import duty. Effectively there is zero import duty on palm stearin and 10% import duty on palm olein, whether crude or refined.

The consistent oils and fats import policy of South Africa over many years have encouraged investments and mergers, with a big customer base and the potential for exports.

In recent years, South Africa has made it mandatory to keep the level of *trans* fatty acids to below 2%. Edible oil manufacturers have reformulated their products to eliminate hydrogenated fats to conform to the regulation and meet customers' demand. The *trans*-free claim has been used as a strong selling point to the institutional users and household consumers.

Soft oils still dominate the cooking oil of South Africa. Palm oil and products are mainly used in the industrial sector. Soaps are mainly palm-based. The major problem of producing toilet soap in South Africa is the unavailability of soft stearin. Only hard stearin is available but it causes the soap to crack. The solution is by blending hard stearin with palm olein, which is a costly blend for soap. The palm olein-hard stearin blend also finds its usage in margarine. Manufacturers also put alpha olefin or foam booster to the soap to reduce the production cost. The high production cost of soap and demand from border trade could be the reasons for soap noodles to be imported despite 20% import duty.

Regional Economic Grouping

Africa has many regional blocs. Common Market for Eastern and Southern Africa (COMESA), ECOWAS, South African Development Committee (SADC), East African Community (EAC), Economic Community of Central African States (ECCAS), The Intergovernmental Authority on Development (IGAD), Economic and Monetary Community of Central Africa (CEMAC), Southern Africa Customs Union (SACU), *etc*. and perhaps one day it might merge them all into only one regional bloc, the African Union. Since the formation of these regional blocs, customs tariff has been harmonised among most members, and agreements are paving the way for more trade.

The formation of these regional blocs has so far no negative impact on palm oil import. In fact, it helps facilitate movements of goods among member countries as the procedures are simplified. For example, if a country restricts the import of a certain product, the same product might enter the country through the neighbouring member country.

Almost all African countries are importers of palm oil. Thus, the preferential tariff given to member countries does not affect palm oil import as all of them import palm oil. The preferential tariff is beneficial only to the producing countries. In case of palm oil, currently, only Ivory Coast is a net exporter of palm oil and benefits from the preferential tariff. In short, the regional bloc has no effect on the export of palm oil to Africa until the African countries start to export palm oil themselves.

Climate and Culture

Africa is big continent with a population of about one billion people and geographical locations in both hemispheres encompassing diverse climate and culture differences across the continent.

The geographical locations have an influence on the eating habits of the local population. Those residing in the tropical region use mainly crude palm oil which can be produced locally. Oil is imported to meet additional demand. The urban populations are getting used to refined palm olein.

Republic of South Africa and North African countries are still major consumers of soft oils. In these countries, palm oil is used mainly by the industrial sector, *i.e*. the frying establishments, margarine, vegetable ghee and shortening producers. The use of palm oil is limited by the cold weather in winter when palm olein solidifies. In Egypt, the solid fats market is shifting to be more of a soft oil market. The production of vegetable ghee has remained stagnant.

Political Stability

The recent Arab uprising has temporarily disrupted the import of palm oil in Egypt but since then, the import has returned to normalcy. In Libya, the civil war has totally disrupted the import of edible oils. It is expected to return to normalcy as well once the new government is formed and stabilised. The impact in Tunisia is also negative, but import is also expected to recover.

The political instability in many sub-Saharan countries has limited the rate of progress in all sectors including agriculture. Many oil palm plantations have been abandoned and became unproductive to the extent that these countries have to import palm oil to meet demand.

CONCLUSION

Africa should no longer be viewed as high risk for trade but rather a potential market for trade and investments. Upstream activity is one of the most potential investments need to be explored by Malaysian investors.

Oils and fats consumption in Africa is on an upward trend moving with the positive economic growth of most countries while the production has stagnated for many years. Self-sufficiency is still far away and therefore imports will still be needed for many years.

Formation of regional bloc grouping facilitates movements of goods among member countries as the procedures are simplified. It is possible to establish a hub to cater to the need of each region.

Egypt, Kenya, and South Africa are the best places for the establishment of regional hubs due to the size of their oils and fats industry and ability to re-export to other neighbouring countries. Egypt is not imposing any import duty on oils and fats including palm oil while South Africa imposed a general flat rate 10% import duty to all oils and fats products.

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