

# Pricing Farmers out of Cotton:

## The costs of World Bank reforms in Mali

With global trade talks stalled at the World Trade Organisation (WTO), rich-country cotton subsidies remain unabated, hurting poor cotton farmers. World Bank led reforms to privatise the Malian cotton sector, including the adoption of a new price-setting mechanism, are further exacerbating the dire conditions in cotton-producing communities. A minimum level of price stability is vital for income security in the cotton sector and to prevent further slides into poverty. The wider donor community should provide adequate funds to finance a cotton-sector support fund, as well as invest in rural extension services and sustain capacity building of farmers to enable them to maximise their returns from new market opportunities.



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## Summary

Mali is one of the world's poorest countries, with over two-thirds of the population – mostly in rural areas – living on less than a dollar a day. Mali is also the second largest cotton producer in sub-Saharan Africa after Burkina Faso.

Cotton production is generally heralded as a success story in much of West and Central Africa, providing a critical development strategy for poor African countries such as Mali and enabling both governments and farm households to access income. The World Bank, International Monetary Fund (IMF), and the wider donor community have also recognised the importance of cotton in reducing poverty and supporting the country's economy. However, in recent years, much of this success has been undermined by depressed and volatile cotton prices, partly as the result of unchecked US subsidies, and the downward trend of commodity prices.

Since 2003, the government of Mali, along with the governments of Benin, Burkina Faso, and Chad (called the C4), has been battling at the World Trade Organisation (WTO) to end trade-distorting cotton subsidies in industrialised countries that suppress world prices. This effort has renewed debate around the role of cotton in economic development and poverty reduction in West Africa and the need for support to the sector to achieve these ends.

Against the background of stalled global trade talks, and persistent use of trade-distorting cotton subsidies, the World Bank and the IMF continue pressuring Mali to implement policies started in the late 1990s of promoting cotton-sector reform through privatisation. This paper examines in detail one element of this reform: the new price-setting mechanism agreed in January 2005. Instead of improving the livelihoods of cotton farmers, this particular measure is destabilising cotton as a source of revenue for millions of farmers.

The new price-setting mechanism essentially transmits the downward trend in world cotton prices direct to the cotton farmer, with a strong likelihood of increasing poverty in rural Mali by up to five per cent. With cotton producer prices now 20 per cent lower than in previous years, cotton-growing areas of Mali are increasingly facing rising indebtedness and food insecurity. This undermines not only their productive capacity but also their capacity to provide basic education and health care. As cotton-dependent communities face these challenges, there are also wider implications for the overall agricultural economy and growth, since the knock-on effects of the fall in cotton prices could slow GDP growth by as much as five per cent in coming years. Cotton-sector reform strategies should be reviewed in the light of the importance of cotton to overall growth and poverty reduction in Mali.

While reform may create economic opportunities for cotton producers, such as the chance to negotiate a higher share of the world price and participate in the management of the sector, producers cannot manage the risks associated with depressed, volatile, and generally declining prices. Transferring the risks of a highly volatile world market down to the bottom of

the chain may benefit the ginning companies and exporters, but only at the expense of poor farmers. It also begs the question of why those least capable of managing these risks are increasingly expected to pick up the responsibility. At the very least, price risk should be shared between the farmers, the ginning companies, and the traders. Government and donor communities should intervene in cases of extreme or sustained risk, in line with public-policy goals.

Maintaining minimum price guarantees for cotton farmers is critical if the trend of increasing rural poverty in Mali is to be slowed or halted, especially as farmers face greater uncertainty from sectoral reforms. National level support or insurance funds which underpin minimum prices are essential for preventing increased poverty. Constituting or replenishing these funds will require significant contributions from governments and donor agencies to complement those contributions made by farmers. The current price-setting mechanism should also be reviewed to ensure that it is effective and coherent, with a properly functioning support fund.

More broadly, as privatisation proceeds in the Malian cotton sector, enhanced technical assistance and capacity building for farmer organisations is critical to ensuring their effective participation in the management of the sector in advance of privatisation. In particular, sustained support is required to ensure that producers develop their capacities to manage co-operative enterprises, diversify their activities and negotiate with finance institutions and suppliers at local level. Otherwise, the fragile, newly formed local co-operatives risk being undermined by indebtedness, falling literacy rates, and associated social tensions.

Further, a renewed commitment and strategy for reviving rural development and extension services previously undertaken by the Compagnie Malienne du Développement des Textiles (CMDT) is desperately needed from both government and donor agencies.

# 1 Introduction

Mali is one of the world's poorest countries, with well over two-thirds of the population – mostly in rural areas – living on less than a dollar a day. Annual per capita income was \$242 in 2005 and the country ranked 172 out of 175 on the Human Development Index (HDI) in 2003.<sup>1</sup> Mali is also one of the largest cotton producers in sub-Saharan Africa, averaging around 550,000 tonnes over the last five years.<sup>2</sup>

Cotton production provided a critical development strategy for Mali and other poor countries in West and Central Africa, enabling both governments and populations to access much-needed development resources.<sup>3</sup> The importance of cotton in Mali in recent decades – in terms of food security, livelihoods, and the fight against rural poverty – cannot be overstated. Cotton has become acknowledged by the World Bank and other donors as a strategic commodity in poverty eradication as its inclusion in Poverty Reduction Strategies and heavily indebted poor countries (HIPC) programmes of debt reduction indicates.<sup>4</sup>

However, in recent years, much of this success has been undermined by depressed and volatile cotton prices, partly as the result of uncurbed US subsidies, and the ongoing downward trend of commodity prices. To address these problems, Mali along with the other members of the C-4 (Benin, Burkina Faso, and Chad), has been battling at the World Trade Organisation (WTO) since 2003 to end trade-distorting cotton subsidies paid by industrialised countries to their farmers, which suppress world prices.<sup>5</sup> These policies caused losses of \$400m to these West African economies in the period 2001–2003 alone.<sup>6</sup> In the context of these negotiations, Africa's cotton-exporting countries, led by the C4, have also sought compensation, or at least financial support, to offset the impact of world price declines on their economies. This has led to a renewed debate around the role of African cotton sectors in economic development and poverty reduction in these countries, and the need for donor support to achieve these ends.

Against this background of stalled world trade talks and unabated trade-distorting cotton subsidies, the World Bank and the IMF as well as other donors are continuing a policy started in the late 1990s of promoting cotton-sector reform through privatisation. World Bank and IMF budget support and HIPC debt reduction have been closely tied to conditionalities for cotton-sector reform.<sup>7</sup> Central to these

policies is the introduction of private actors in the management of the sector and the alignment of farmer purchase prices with world prices.

Although few doubt the need for reform in the sector, the timing and scope of reforms – and the necessary institutional framework for their success – have been causes of concern for both government and farmers. Moreover, some aspects of World Bank proposed reforms seem to fly in the face of stated poverty-reduction goals. While reform has the potential to create market opportunities for cotton producers, transferring the risks of a highly volatile world market down to the bottom of the chain may benefit the ginning companies and traders, but only at the expense of poor farmers. It also begs the question of why those least capable of managing these risks are increasingly expected to assume the responsibility.

At the very least, price risk should be shared between the farmers, the ginning companies, and the traders. The government and the donor community should intervene in cases of extreme or sustained risk, in line with public-policy goals.

The experience of Burkina Faso, which went through privatisation in the late 1990s provides some lessons which can be drawn on for Mali. There are many similarities in the ways in which the two countries' cotton sectors are managed. The example of Burkina Faso demonstrates that a well-designed and producer-managed support fund can in fact stabilise cotton incomes. Proposals emerging for a support fund in Mali are similar in structure to the new price-setting mechanism and smoothing fund created for Burkina Faso, which is designed to sustain producer livelihoods while also adjusting to the downward trend in prices.

This paper argues that recent changes to the cotton price-setting mechanism in Mali promoted by the World Bank have wider repercussions for the Malian economy and are likely to jeopardise the existing poverty-reduction strategy. Falling prices are increasing poverty in cotton-growing areas and worsening food insecurity and indebtedness. In light of these rising pressures on cotton farmers, and the uncertainties of privatisation, support funds can play a critical role in ensuring a minimum price, so that Malian cotton farmers may sustain their main income-earning activity and avoid sliding further into poverty.

## 2 Cotton and poverty reduction in Mali

Cotton production contributes directly to the incomes and livelihoods of up to three million people in Mali, over a quarter of the total population. Cotton is also the main agricultural export in Mali accounting for over half of agricultural export revenues, at least 20 per cent of total export revenues and seven per cent of GDP. Thus growth in the cotton sector has a major impact on overall economic performance.

Boosted by devaluation in 1994 that improved export prices and by favourable rainfall, Mali's cotton sector grew on average by more than ten per cent annually in 1994–1999, with production more than doubling from 250,000 to over 500,000 tonnes.<sup>8</sup> Production of food crops – particularly rice and maize – as well as livestock production also grew significantly during this period.<sup>9</sup>

**Table 1: Cotton in the Malian economy**

Agriculture % of GDP*	Cotton % of GDP*	Mali cotton exports % of West African cotton exports**	Cotton share of agriculture exports**	Cotton share of total exports**
45%	7%	20%	62.1%	25%

Sources: \*Wodon *et al.* 2006. \*\*Average for 1998–2002, OECD 2005, citing World Bank Development Indicators 2004 and FAOSTAT.

Cotton is grown on 200,000 relatively small family farms on plots averaging between two and three hectares in the regions of Sikasso, Koulikoro, Segou, and Kayes. In these regions, cotton is the cornerstone of a diversified agricultural system that also includes cereals (maize, sorghum, and millet); other food crops such as cowpeas, legumes, yams, and groundnuts; fruits (mangos, bananas); and livestock (cattle and donkey for manure and draft power).<sup>10</sup> Maize and other cereals provide staple food but household incomes are mainly drawn from cotton production. In southern Mali, for instance, all but the poorest rural households rely on cotton for most of their income (45–57 per cent) with the rest made up of food production, livestock rearing (for better-off households), and non-farming activities.<sup>11</sup>

### Cotton, cereals, and food security

There is a strong relationship between growth in cotton production and growth in cereals production. In southern regions of Mali where

most of the cotton is produced, maize production has expanded rapidly alongside cotton production. Cereal production has also continued to rise even though cotton production levels have stagnated in recent years. The availability of inputs via the cotton-production system has been vital to this trend, as have higher levels of access to technology and innovation in cotton-growing areas.<sup>12</sup>

## Cotton and rural development

In general, cotton production has stabilised incomes in rural areas, enabled access to credit and inputs as well as other services, and contributed to poverty reduction.<sup>13</sup> Payments for cotton, if made in a timely fashion, mean that farmers are not obligated to sell their cereals at low prices to access cash to cover household needs. And the multiplier effects of cotton income in the wider rural economy cannot be underestimated, especially in terms of demand for consumer goods and services, particularly transportation.

The cotton system in Mali has enabled the development of infrastructure and rural services via state involvement as well as communities' use of cotton incomes to fund local services. Data from the late 1980s show that Mali's cotton-producing regions had a higher density of schools, drinking-water points, and health services than non-cotton-growing areas.<sup>14</sup> Village associations have also invested in wells, schools, medical facilities and other community facilities with revenues from cotton.

Created in 1974 by the *Compagnie Française du Développement des Fibres Textiles* (CFDT) and the Malian government to enable greater national participation in the sector, the CMDT (*Compagnie Malienne du Développement des Fibres Textiles*) provided all the inputs required to cotton farmers, via financing guaranteed through exclusive marketing rights on all the cotton produced. The company gradually became the main service provider to cotton-producing regions. As well as ginning and marketing, the CMDT's services included transport, agricultural extension, rural literacy, and organisation and training of producers. Support also involved road maintenance, support for marketing cereals, promotion of livestock production, and income-generating activities for women, as well as facilitating access to credit for these activities.<sup>15</sup>

Similarly, in Burkina Faso, Mali's neighbour, cotton production increased in 2005–6 to a record 713,000 tonnes of seed cotton<sup>16</sup>. In the period 1998–2003, cotton production also contributed to growth and to poverty reduction, with poverty levels falling from 62 to 47 per cent overall and in rural areas from 69 to 53 per cent.<sup>17,18</sup> Cotton producers are considered better off and more capable of emerging

from poverty than other farmers.<sup>19</sup> In fact, between 1994 and 1998, the incidence in poverty among cash-crop farmers declined from 50 per cent to 42 per cent, compared to a two per cent increase among food producers.<sup>20</sup>

Additionally in Burkina Faso, between 1997–8 and 2002–3, cotton farmers invested up to half of the 6.7 billion FCFA (Franc Communauté Financière Africaine) funds received as a cotton price supplement into community resources such as schools and hospitals, with visible results.<sup>21</sup> Literacy and school attendance rates in cotton-producing regions are higher than the national average at 34 per cent and 56 per cent respectively, compared with 21.8 per cent and 44.1 per cent.<sup>22</sup>

## Poverty on the horizon

Promoting cotton production is not in itself a panacea for poverty reduction. In some parts of the old cotton basin in Mali, with rising population pressure, soil fertility is in decline and little quality land is available, affecting yields and prompting migration to more productive areas.<sup>23</sup> Wealthier families have benefited more from market opportunities, accumulating cattle and equipment and contributing to rising inequality. Nor do increasing household incomes from cotton always translate into improved nutrition, health, or education indicators.<sup>24</sup>

The privatisation underway in Mali has stripped away the broader rural development functions of the CMDT while other institutions which supply such services remain underdeveloped and lacking in financial support. Also, as cotton prices have fallen, locally generated resources to invest in social and physical infrastructure are dwindling.

Given these trends, current policies of privatisation and liberalisation in the cotton sector are likely to exacerbate rural poverty and further increase inequality as they expose poor producers to increasing levels of risk associated with price declines. In the absence of reliable systems of credit and inputs accessible to small farmers outside of the cotton system, or of reliable and remunerative market opportunities for other crops, it is difficult for poorer farmers to diversify out of cotton or into non-farm activities.<sup>25</sup> Consequently, they may stay in cotton farming even though incomes are in decline, and be forced to sell their remaining assets or eventually be pushed out by indebtedness.

### 3 The World Bank and cotton sector reform in Mali

Through their lending operations and associated conditionalities, the World Bank and IMF have played a central role in determining policy in Mali's cotton sector. Other actors, in particular the French government and the French controlled company DAGRIS which remains a shareholder in many of the regions' cotton companies, including the CMDT, have also been very influential. During the 1990s, the World Bank and IMF promoted the virtues of a privatised sector and liberalised marketing system, in contrast to the prevailing model of vertically integrated production with monospony purchasing power by the cotton company, which also supplies all inputs, favoured by the French.<sup>26</sup>

The influence of the World Bank and IMF in Mali intensified from 1998 when world price declines precipitated a financial crisis in the cotton sector and the launch of the first reform programme.<sup>27</sup> In the 2000–2001 growing season, an unprecedented producers' strike erupted in response to a huge fall in prices paid to farmers for the previous season's crop.<sup>28</sup> The strike halved the volume of cotton production, prompting an overall review of the cotton sector in early 2001. The resolutions adopted paved the way for the approval of new privatisation policy, drafted in consultation with the World Bank and subsequently approved by the National Assembly. The newly established Malian Mission for Cotton Sector Restructuring (MRSC) was charged with overseeing the implementation process.

Submitting a proposal for cotton-sector reform was required in order to receive the Structural Adjustment Credit (SAC) III, a loan totalling \$70m, finally approved in December 2001. The reform strategy targeted the breaking up of the public monopoly held by the CMDT in addition to public-expenditure management, reinforcing the 1999 IMF Poverty Reduction and Growth Facility. Privatisation of the CMDT was scheduled for 2006.<sup>29</sup>

The current structural adjustment credit IV (SAC IV), equally targeted towards cotton-sector reform, was adopted only after much disagreement between the World Bank and the government of Mali. The World Bank considered the producer price agreed for 2004–5 fiscally unsustainable in relation to world prices, initially demanding that this be reduced, which the government refused. This disagreement led to the suspension of the SAC IV negotiations and World Bank financing, pending the fulfilment of certain conditions.<sup>30</sup> The Bank's conditions included: a revision of the price-fixing

mechanism so that seed-cotton prices in the future would better reflect world market prices; a clear signal from the government of Mali demonstrating its seriousness to privatise the cotton sector; and a commitment to a new timetable.<sup>31</sup> The new timetable delayed privatisation until 2008.

## The rationale for privatising cotton

Aiming to improve the competitiveness of the sector, reforms centred on withdrawing the state from productive activities in order to prevent ‘rent seeking’ and financial mismanagement such as that uncovered following a 1998 audit of the CMDT. The underlying assumption is that competition and more liberal economic conditions will squeeze out mismanagement and inefficiency, providing higher prices for cotton farmers and better, cheaper farm inputs, technical support, and cotton-marketing services.

### **Box 1: Key elements of World Bank cotton sector reform policy**

1. A new price-setting mechanism, taking into account world prices
2. Downsizing of the CMDT and divesting ‘non-core’ functions such as transport and input supply
3. Outsourcing extension services to private operators
4. Liberalisation of the sector by entry of private operators in ginning and privatising the CMDT
5. Liberalising marketing of seed cotton and other by-products (e.g. oil seed and cotton meal)
6. Establishing an inter-professional body including farmers, ginners, and other stakeholders

Since the severe world price declines in the late 1990s which continued in 2001–2 and 2004–5, the Malian cotton sector has been kept afloat through public financing. The international financial institutions (IFIs) argue that this must stop in order to reduce public-sector deficits, and thus require that prices paid by cotton companies to farmers are closely aligned with world prices. They also argue that these funds would be more effectively spent on other poverty-reducing activities.

In line with World Bank conditionalities, the government of Mali’s cotton-sector development policy calls for the progressive withdrawal of government from cotton marketing and associated activities and a greater role for the private sector, producer organisations, and local government.

The government’s strategy highlights three objectives: 1) reducing and consolidating the CMDT’s public missions in rural development

and extension service provision as well as in input supplies and transport; 2) increasing producer participation in the sector as shareholders in the new privatised companies, and producer management of input supplies; and 3) opening oilseed production, cotton ginning, and marketing sectors to private operators.

### **Delays in implementation**

A number of factors including government and farmer concerns about the impact of privatisation have led to delays in implementation. These concerns reflect the mixed experiences of other countries in the region.<sup>32</sup> In the case of Benin, which liberalised its sector relatively early and extensively, farmers have faced – among other challenges – serious problems of non-payment by private operators and lack of a clear price-setting mechanism.<sup>33</sup> Moreover, the sector as a whole experienced a financial crisis leading to a significant decline in production. By contrast, Burkina Faso adopted a gradualist approach widely viewed as more positive and successful. In this case, the farmers gained a central role as 30 per cent shareholders in SOFITEX (the state cotton-marketing company) that remained a mixed ownership monopsony until 2004, when two new companies entered the sector.

Nevertheless, some aspects of the reforms have moved ahead. Since 2003, the CMDT has significantly downsized its staff and functions, and privatised HUICOMA, the oilseed processing and manufacturing company. The break-up of the CMDT into four zones has been agreed and is now planned for 2007, preceding complete privatisation in 2008.<sup>34</sup>

All actors including farmers envisage a much greater role for producer organisations in the management of the sector, in particular as shareholders in the privatised companies. However, there are concerns that the Malian producer organisations are not sufficiently well-structured, organised, or prepared to adequately fulfil all the roles expected of them. In fact, farmers' need for more time to prepare for privatisation was a key reason the Malian President delayed privatisation to 2008.

### **Privatisation and producer organisations**

Prior to the privatisation process, at local level most farmers were organised in village associations through which inputs and credit were distributed and the first stage marketing of the cotton carried out. However, these associations did not have a legally recognised status enabling them to engage in economic activities. Moreover,

many had accumulated severe problems of indebtedness between members as well as with finance institutions.

A new law introduced in 2001 (Law 076 N°01 of 18 July) created the framework for the establishment of cotton-farmer co-operatives with a legally recognised status and liability as enterprises to enable them to play an increased role in sector management. The law also provides for the federation of these co-operatives at higher levels, up to the national level, allowing for the possibility of their becoming shareholders in the cotton companies.

Throughout 2004–2005, support through the French government-funded Programme d'Amélioration des Systèmes d'Exploitations en Zones Cotonnières (PASE) facilitated the creation of the local co-operatives and their unions, and some training in financial management for co-operative leaders. Since 2004, nearly 7,000 local-level cotton-farmer co-operatives have been established across most of the country, and in most of the cotton regions, unions have also been established at the communal level.<sup>35</sup> Higher-level unions (sector, region) are on track to be formed culminating in a national union later in 2007, which will represent farmers in an inter-professional body.

National and regional cotton farmer leaders under the umbrella of the Groupement des Syndicats des Cotonniers et Vivriers du Mali (GSCVM – a trade union coalition) have also received training and support from the PASE to undertake strategic reflection on the future of the sector and for their new role managing the purchase and distribution of inputs for cereals, formerly a function of the CMDT.

## The new cotton price-fixing mechanism

One of the most significant – and contentious – aspects of the reform undertaken so far is the adoption, in January 2005, of the new price-fixing mechanism for seed cotton.

From 1989–2000, the cotton sector was governed by a series of 'Contract Plans' between the government, the CMDT, and the farmers. As part of these agreements, a floor price for cotton was fixed in advance of the growing season, based on the cotton company's and farmer's production costs. Thirty-five per cent of the net benefits to the sector were allocated to farmers via an end-of-season price supplement or 'ristourne'.<sup>36</sup> A stabilisation fund was intended to maintain the floor price and smooth fluctuations between seasons. However, the stabilisation fund previously in operation in Mali ceased to function by 1999 due to mismanagement and exhaustion on the part of the CMDT.<sup>37</sup>

From 2002–2004, following the crises experienced in the sector, a new price mechanism was introduced to align the seed-cotton price more closely with world prices.<sup>38</sup> This system established a minimum guaranteed price for the three-year period. An initial price was negotiated at the start of each campaign and a definitive price negotiated the following May or June at the end of the campaign, on the basis of which a ‘price complement’ was attributed to producers if a profit was made. In the event of a profitable campaign, 49 per cent of the sector’s profits went to producers, nine per cent to a support fund used to maintain the minimum price, and the remainder was kept by CMDT<sup>39</sup>. The price itself was based on a formula, accounting for costs of production and regional and world prices. However, it was difficult to obtain a consensus on costs of production borne by producers (notably, the value of family labour, hired labour wage rates, and depreciation of capital). Producers were also understandably suspicious of the cost structures presented by the CMDT.

In April 2004 the CMDT, in negotiation with farmer unions, agreed upon a price of 210 FCFA/kg for seed-cotton purchases. At the time, the International Cotton Advisory Committee (ICAC) made promising forecasts estimating that world prices would reach 64 cents per pound, following a favourable season in 2003–4 and a relatively favourable US dollar to euro exchange rate. Unfortunately, in the second half of 2004, both cotton prices and exchange rates moved against Mali, leading to a collapse of cotton prices. ICAC, like the Malian cotton company, failed to predict these trends.<sup>40</sup>

The World Bank argued that the producer price of 210 FCFA was too high, and politically motivated. The World Bank’s concerns were essentially fixed on budget reduction, given the large deficit faced by the CMDT. Additionally, the World Bank was convinced that using government resources to shore up deficits in the cotton sector was diverting funds from spending on other areas of poverty reduction such as health and education.<sup>41</sup>

Initially, the World Bank asked the Malian government to reduce the current year price. This was later rescinded but the World Bank did insist on the immediate implementation of a new price-setting mechanism, as well as the presentation of a credible proposal for financing the CMDT deficit in 2005.

During the latter half of 2004, intense negotiations took place between the Malian government and the World Bank, on a proposed new price-setting mechanism.<sup>42</sup> As part of these discussions, the price range for seed-cotton payments to farmers was between 160 and 175 FCFA/kg. The new price-fixing mechanism was adopted by the

government, the cotton company, and cotton trade unions after considerable pressure from the World Bank on 13 January 2005.<sup>43,44</sup>

**Box 2: The problems with Mali's price-setting mechanism for seed cotton**

The new mechanism agreed in 2005 for a three-year period is calculated based on an initial price and a final campaign price.<sup>45</sup> However, it differs from the previous system in the following ways:

- There is no longer any direct relation to farmer production costs. The Cotlook index A (West Africa) – a reference for world price trends – is the key variable determining the producer price.
- In Article 3, the band for the base price was at 160-175 FCFA/ kg for the three-year period, a considerable drop from previous years.
- Article 4 establishes a 60:40 per cent split of profits from the sector between producers and the CMDT. However, in reality the formula adopted in Article 5 splits the benefits according to the proportion of the (world) price, rather than the proportion of revenues.
- Articles 6 and 7 discuss setting up a support fund (*fonds de soutien*) to maintain prices when market conditions are unfavourable. However, in the principles set out in Article 2, the price-setting mechanism must enter into force, whether or not the support fund is resourced.
- Article 8 of the mechanism allows – in cases of 'force majeure' – for a downward revision of prices up to August of the growing season, undermining the security of the minimum price guarantee.

Sources: *République du Mali 2005a; République du Mali 2005c; Nubukpo and Keita 2005; Wodon et al. 2006.*

However, the World Bank gave little attention to the wider economic and social impacts of the new policy. No prior impact studies were conducted by the World Bank, while an earlier government study had predicted serious economic losses and reduced production if the price of seed cotton fell to 160 FCFA.<sup>46</sup> Given the scale of the potential effects which producer price of cotton has on growth and government revenue, this is a serious oversight. Equally, the lack of poverty analysis on a policy directly affecting the incomes of one-third of the population is very worrying in light of the importance given to cotton in the national poverty-reduction strategy in Mali.

Farmers' organisations and other commentators expressed a great deal of concern about Article 8 of the mechanism, which permits a fall in the seed-cotton price over the course of the growing season.<sup>47</sup> This development means that farmers could decide to borrow and invest based on a cotton price agreed in April, but end up heavily indebted if prices fell subsequent to harvesting in August. Although this theoretically should only occur in case of a *force majeure*, given the lack of clarity on the criteria for such an event, the volatility in world

markets and the non-existence to date of a support fund to maintain minimum prices, this provision certainly increases the risk and uncertainty for farmers in cotton production.

As a result, Mali's cotton farmers, the government, and other stakeholders are eager to see a support fund set up. Without a support fund it is unclear how the base price will be maintained if – as has been the case for most of the past five years – the world price continues on a downward trend. Given the crisis facing the sector and the income drop already accepted by farmers, the constitution of a support fund requires substantial external resources to complement the limited contributions which producers could make.

## 4 Costly reforms for cotton farmers

*'Before, at harvest time, a part of the income was given to the women. But this year, that was not the case. On the contrary, the livestock we have accumulated over many years had to be sold to enable us to cover our food costs, in particular the purchase of cereals. As a result, we have almost nothing left in terms of savings to protect us from the difficult times to come...'*

*Villager in Wacoro, August 2006.*

Reforms in the Malian cotton sector intend to improve overall efficiency and competitiveness while reducing government expenditures. While it is too early to know whether in fact the sector will become more competitive as a result of these reforms, reforms are already proving to be very costly for cotton farmers.

Preliminary evidence suggests that the implementation of the new price-setting mechanism has further lowered growers' returns from cotton, exacerbating poverty, food insecurity, indebtedness, and the viability of the fragile newly formed co-operatives. The impacts are exacerbating the effects of the withdrawal of rural development services under privatisation. Unless measures are taken to stabilise the situation and secure farmer incomes, the sustainability of the cotton sector and thus the reform process itself may be in jeopardy.

### The new price-setting mechanism: impacts on farmers

In spite of volatile world markets, given the importance of cotton to the overall Malian economy and excepting the year preceding the strike in 2000-1, the price paid to farmers for seed cotton has been relatively stable (see Table 2).

With the application of this new mechanism, prices for seed cotton were set at 160 FCFA/kg in April 2005 for the 2005-6 growing season, 24 per cent lower than the previous year's price and 15 per cent lower than the previous three years' average price when accounting for the end-of-season price supplements. When the eight FCFA supplement paid at the end of the growing season is included, the drop is 20 per cent compared to the previous year.

Furthermore, this trend is confirmed for 2006-7, with the initial price set at 165 FCFA. It is clear that the impact of falling world prices is now to a much greater extent being passed directly on to the producers.

**Table 2: Producer prices for seed cotton in Mali, 1997-2006**

Year	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Base price <sup>48</sup> FCFA/kg	170	145	150	160	180	180	200	210	160	165
Price supplement	0	50	0	10	20	0	0	0	08	-
Total	170	195	150	170	200	180	200	210	168	-

Source: République du Mali 2005.

Lower cotton prices directly reduce farmer incomes and, given the strong linkages between cotton and other sectors, also have wider impacts on the overall economy. Separate studies by Oxfam and the World Bank suggest that price change will increase poverty and food insecurity levels among Mali's cotton farmers in particular, and its rural population in general, and is likely to reduce economic growth.<sup>49</sup>

## Effects of price changes on farmers' livelihoods

A comprehensive assessment of the impact of price changes on the livelihoods of farmers requires data over a period of time, which are not yet available. However, some observations can be made on immediate effects of the price drop and likely responses of farmers based on recent field studies.

### Falling returns to cotton farming

Table 3 presents information on farmer production costs, yields, and net revenues based on 2004–5 data. Average costs of production across all types of farmers were estimated at 166 FCFA/kg. At 2004–5 prices, farmers were on average making a net profit of around 40,000 FCFA on their cotton (or approximately \$80).

**Table 3: Costs and benefits of cotton production for Malian farmers in FCFA per hectare (ha), 2004-5**

<b>Variable</b>	<b>Average value</b>
Average area planted to cotton (hectares)	2.45
Production costs	
Depreciation <sup>(1)</sup> (FCFA/ha)	19482
Hired labour costs (FCFA/ ha)	4313
Family labour costs (FCFA/ha)	70313
Total (FCFA/ha)	83008
Yield of cotton seed per hectare (kg)	929.21
Yield of cotton fibre per hectare (kg)	390.27
Cost of production per kilo of seed cotton <sup>(3)</sup> FCFA/kg	165.88
Total costs (FCFA/ha)	178831
Income per hectare (FCFA) (at 210 FCFA/kg)	195135
Net revenue per hectare (FCFA)	16304

(1) Annuity/ hectare calculated on the basis of a linear depreciation of production material and equipment calculated on a per hectare basis.

(2) Cost with family labour. Without family labour the cost is 85.45 FCFA/kg.

Source : Nubukpo and Keita 2005

The initial price of 160 FCFA/kg fixed for the 2005-6 campaign falls below the average costs of production, such that at this price, on average, farmers are producing at a loss. Even with the small upwards adjustment of the final price to 168 FCFA, this implies on average only a tiny margin of 2-3 FCFA kilo. Moreover, rising input costs and falling yields are increasingly weakening the profitability of cotton production.

According to World Bank data, even these reduced national price levels may exaggerate the net prices paid to farmers, once cotton inputs and loan repayments are taken into account, which can be as low as 100 FCFA/kg. This means that many households are producing at a significant loss. The poorest households tend to be those for whom cotton is least profitable - implying that the most impoverished households will be hurt the most.

### **Growing food insecurity, indebtedness, and poverty**

Recent reports from farmers in central and western Mali confirm that falling cotton prices are making poverty and food insecurity worse. Interviews with farmers in the Kita and Fana areas of Mali, revealed that declining household incomes resulting from the falling cotton price means that farmers often have insufficient income to feed their families. In some households, families cope by skipping meals. Households are also struggling to meet other basic needs, such as costs of health and education.

This collapse in household purchasing power is fuelling another phenomenon – seasonal or permanent migration of household members searching for supplementary sources of income. Most of these migrants are young men who would normally work in cotton or other agricultural production. Among households interviewed in the Kita area, 86 per cent had seen at least one member migrate since the drop in the set cotton price; 60 per cent witnessed the same occurrence in the Fana district of the region of Koulikoro.<sup>50</sup>

Levels of indebtedness are on the rise, rendering the newly established farmer co-operatives fragile. In the village of N'Garadougou in the district of Dioïla, farmers were quite successful in repaying their loans until the 2005–6 season, when the price of cotton fell sharply. Villagers claim that only four out of ten can repay their credit now, compared to nine out of ten before. As farmers increase their debt, they become less likely to qualify for future loans.

Some farmers are forced to sell assets such as livestock or farming equipment, reducing their productive capacity for the next farming season. According to Sidi Togola from N'Garadougou in the Dioïla district, he will be unable to use any of the ten cattle that he financed through loans for the 2005–6 campaign, as all of them had to be sold to repay his debts. Box 3 describes similar trends in another village in the same district.

**Box 3: From celebration to crisis: cotton in the village of Kola**

In 1997, the village of Kola in the district of Dioïla (population of 1540) hosted the 'Cotton Carnival' to celebrate the record levels of national cotton production at more than 400,000 tonnes, double that from a decade earlier. The CMDT with its monopoly on cotton purchases had also made significant profits as a result of the positive effects of devaluation. The income from cotton enabled the whole community to benefit from the construction of facilities such as a literacy centre, a village savings bank, a weighing machine, and a health centre.

Now the situation has reversed, especially in the past two years. According to Niansoon Traore, secretary of the same co-operative *'We can hardly cover the costs of our inputs. My co-operative is not in debt but its purchasing power is considerably weakened. Due to the group solidarity system, certain members are covering the losses of others. In the longer term this risks undermining our co-operative'*.

Women in the village are not spared these hardships. According to Niama Fomba and Many Mariko, *'When our husbands' incomes increase, the whole household benefits. Previously our husbands used to ask us to help with the cotton harvest. And they gave us funds during the dry season to enable us to cover household expenses. Today we are forced to sell our goats to repay the credit on inputs for the cotton and in order to feed ourselves. Our economic development projects – a mill and a bore-well for kitchen gardening – have been put on hold'*.

Source: summarised extract from Traore 2006.

Falling income also has immediate and dire consequences for the newly formed cotton co-operatives and their ability to provide services at the village level. Local co-operatives are losing income because members are having difficulties making contributions and because their receipts from first-level cotton marketing are falling. Additionally, some members are unable to repay their credit, leaving the co-operative to foot the bill. At village levels, farmers have had difficulty in paying taxes. One disastrous outcome has been the lack of funds to pay schoolteachers formerly funded from cotton incomes.

A major risk of the current privatisation process is that there will be a further decline in social investment at local level, widening the poverty gap and increasing inequality.

Since cotton is such an important crop throughout Mali, these local experiences suggest that lower cotton prices will exacerbate poverty at the national level. While no data exist to measure this impact at a national level, recent World Bank studies have projected that falls in cotton prices of between 20 and 40 per cent could lead to increases in overall rural poverty of 3.4–4.6 per cent, and even higher increases among cotton-farming households.<sup>51</sup> Moreover, these studies may even underestimate the effects as they do not take into account the indirect effects of declining household income on consumption.<sup>52</sup>

## **Longer-term impacts**

A government study carried out in 2003 predicted that a reduction of the seed-cotton price to 160 FCFA would lead to a reduction in the areas planted between ten and 25 per cent. This effect has not been registered for the year 2005–6 when the area planted to cotton has, overall, remained similar to that of 2004–5. But in the medium term, the effect of falling cotton prices may indeed reduce the area planted to cotton and thus overall production volumes. While some may choose to diversify into other crops, others will undoubtedly leave the sector involuntarily when they become too indebted to continue production, have no remaining assets to sell, and cannot borrow any further.

Field interviews in central and western Mali revealed that locally the incidence of farmers reducing the area planted to cotton in order to increase the planted cereal area is already occurring.<sup>53</sup> If this proceeds on a large scale, cereal output will increase, causing a decline in cereal prices paid to farmers for sale of their surplus. In the absence of market regulation, switching out of cotton into cereals is therefore unlikely to be a viable alternative on a large scale and underscores that a guaranteed minimum price for cotton is critical to securing farmers' livelihoods and food security.<sup>54</sup>

However, diversification is certainly possible for some better-off households, particularly in the higher rainfall areas of southern Mali, which are also near urban markets.<sup>55</sup> Around Kita in the region of Kayes, some farmers are abandoning cotton altogether to produce food crops and alternative crops such as groundnuts or rice. A recent initiative to promote 'fair trade' cotton in the region also has a growing number of adherents.<sup>56</sup> In the Sikasso region, also, many farmers are adopting fair trade and organic cotton production as a more secure alternative<sup>57</sup>.

But there still remain relatively few viable alternatives for the majority of farmers in Mali's cotton growing regions. To date, cotton growing remains the only reliable source of finance and markets. Diversification on a larger scale would require much wider access to finance and other rural services than is currently available.

## **Economy-wide impacts**

Between 1995 and 2000, cotton accounted for 7–8 per cent of Mali's GDP. The cotton sector has significant backward linkages to inputs and forward linkages to industrial processing, so changes in the cotton sector will have multiplier effects throughout the economy. A study commissioned by Oxfam to estimate these multiplier effects

suggests, for instance, that reducing the price to 160 FCFA/kg without changes to output could reduce GDP by nearly two per cent.

In a worst case scenario, a combined drop in price to 160 FCFA and a 25 per cent fall in cotton production could potentially lower GDP by nearly four per cent and export revenues by up to 53bn FCFA (more than \$100m). Meanwhile, the deficit of the cotton sector for 2004–5 was estimated at 65bn FCFA.<sup>58,59</sup>

These results are corroborated by a 2006 World Bank study which estimates that a 20 per cent cut in producer prices could reduce GDP by up to 9.5 per cent, incomes of agricultural households by up to 20 per cent and increase overall poverty levels by as much as 4.6 per cent.<sup>60,61</sup>

Meanwhile, in the context of the poverty-reduction strategy paper (PRSP), the growth target set for the agricultural sector in Mali is 6.7 per cent annually from 2002–6, already an ambitious target, according to some commentators.<sup>62</sup> Such severe downward pressure on these growth rates from cotton-price change is thus likely to compromise the existing poverty-reduction strategy.

### **Farmers' responses**

Despite falling prices and increasing poverty, many farmers express their intention to continue producing cotton, since up to now cotton provides them with the following benefits:<sup>63</sup>

- A minimum guaranteed price and a guaranteed market with a known buyer which provides a predictable income (the CMDT pays 80 per cent of the crop value soon after collection);
- Access to inputs and credit through the cotton-production system;
- A positive impact on yields of rotation crops via the effect of cotton inputs;

Cotton is a relatively stable source of income to complement volatile and uncertain cereal prices. In light of these benefits, and with few if any reliable alternatives, farmers are more likely to reduce cotton-production costs rather than abandon cotton altogether, at least in the short term.

One cost-cutting measure is to substitute purchased inputs (chemical fertilisers and pesticides) with organic fertilisers when possible. Farmers in the villages of Wacoro and N'Garadougou greatly reduced their use of chemical inputs in the 2004–5 and 2005–6

growing seasons. This practice, while environmentally sustainable, can lead to lower yields initially, exacerbating income losses. Equally important to this alternative is the availability of sufficient organic manure to supplement chemical inputs. However, anecdotes suggest that farmers are selling their livestock to avoid indebtedness, which makes a switch to organic inputs an increasingly less viable option for reducing production costs.

Another way of cutting costs has been to reduce use of hired labour, particularly of women who harvest cotton in groups at the end of the season. Instead, farmers have been relying more on male family members or simply not paying the women. These earnings allow women to finance small-scale trading and cover vital daily household expenses. The drying up of these funds is posing a problem in meeting household needs.

Reduced demand for hired labour could translate into greater poverty of agricultural wage workers who tend to be members of poorer households. At the same time, reducing hired labour in key operations such as weeding and harvesting could in turn have a negative impact on yields, increasing the decline in productivity.<sup>64</sup>

The crop year 2005–6 witnessed a drop in average yields, which could be due to many factors – particularly erratic rainfall – but equally could be the result of the price fall and related strategies to reduce production costs via lower input or labour uses.<sup>65</sup>

Selling assets to pay back loans that cannot be reimbursed from cotton income is another strategy employed by farmers. If debts accumulate, this will affect not just individual farmers but also the viability of the newly formed village-level co-operatives. During interviews in June 2006 in the village of Lofigué in Sikasso, for example, co-operative leaders indicated that they were obliged to renegotiate their debt repayments with the National Agricultural Development Bank (Banque Nationale de Développement Agricole – BNDA) in order to have sufficient funds to pay their members for the 2005–6 campaign.<sup>66</sup>

## **Producer organisation restructuring and strengthening**

Political will and donor commitment undoubtedly exist to strengthen the producer organisations to take on new responsibilities in the privatised cotton sector. The rural population appear to have welcomed the introduction of the co-operatives, given the failings of the previous village associations.

But in Mali, the process by which the cotton farmer co-operatives were formed was a 'top-down' one, driven by the timetable of privatisation, rather than a bottom-up process driven by the farmers themselves, as for example in Burkina Faso. As such the newly formed co-operatives are extremely fragile. Many co-operatives exist in name only, but do not function according to the provisions of the co-operative law, due to lack of awareness of its provisions and lack of capacity to implement its requirements.

The level of illiteracy in rural areas of Mali remains high, and is thought to be increasing following the withdrawal of the CMDT from literacy training at least five years ago. This means that the functioning of the co-operatives is tending to rely on a few individuals, with a high risk of concentrating decision making. Technical training programmes which focus only on the leaders may exacerbate this problem.

Moreover, the accumulation of indebtedness and past mismanagement in the village associations has left behind many social tensions, so that village associations have split into several co-operatives, some of which are too small in size to remain viable.

Given these constraints, it is critical that the government and donor community sustain and increase support to the development of the co-operative movement, as well as invest in improving rural literacy. In so doing, it will be important that a more 'bottom-up' approach be adopted, based on concrete needs defined and expressed by the farmers themselves through their organisations.

These issues cannot be resolved by one-time technical training programmes. Sustained support is required to ensure that producer organisations develop capacities to manage enterprises, take and manage risks, and diversify their activities, from the village to the regional and national levels. The government of Mali, donors, and producers must work together to develop a clearly defined strategy for the revival of development and extension services, including literacy provision, to cotton-producing regions. Otherwise, the newly formed local co-operatives risk becoming undermined by indebtedness, falling literacy rates, and associated social tensions.

## 5 The case for support funds

As a result of the C4 cotton initiative at the WTO and the debate around the crisis in the sector, donors have offered some new aid to the cotton sectors in the West and Central Africa region. To date, however, barely any of this aid has been disbursed. Further, there are some areas of common agreement but also considerable divergence of views between donors, governments, and producers on the priorities for its use. One key area of divergence has been around the creation or replenishment of cotton-sector support funds.

The donor community has been slow to respond or resistant to requests from governments and farmers' organisations for contributions to support funds, in spite of specific requests dating back to the EU Africa Cotton Forum in July 2004.<sup>67</sup> In light of the increased vulnerability of cotton farmers in Mali, a minimum price floor backed up by support funds is critical to securing their livelihoods as they face the triple challenge of declining and volatile world prices and privatisation. Moreover, donors should contribute significant resources to kick-starting these funds that – when well-designed and managed – have proven to be relatively successful in sustaining farmer incomes and livelihoods.

### What are support funds?

Support funds provide a minimum guaranteed price to small farmers over time, reducing the impact of price fluctuations in commodity markets on farmers. This system transfers the risk of cotton sales on the world market from the farmer to the cotton company, which is better placed to manage the uncertainty of world markets by using forward sales and other risk-management strategies.

In cases where world prices are unfavourable, the funds are used to offset the gap between the price for seed cotton announced at the beginning of the season and the final price at which the cotton fibre is sold on world markets, minus the various charges and fixed costs which companies bear in transformation, transport, and other essential functions. In periods of favourable world prices, reserves can be accumulated, bonuses distributed to farmers, and support funds replenished.

Unlike commodity subsidies, the price-support system is in principle intended to redistribute revenue from the cotton sector itself between surplus and deficit years to stabilise prices and increase predictability and efficiency in the sector. In practice, public funds may be used to support prices in cases of prolonged crises or cases of extreme

volatility. In order to ensure that the floor price does not become unsustainable against long-term world price declines, it can be adjusted periodically by negotiation among actors.

A number of different studies stress the value that farmers place on the guaranteed price system in the West and Central Africa region, especially given that few other agricultural product markets offer any such certainty<sup>68</sup>. Without such mechanisms to ensure the livelihood security of small farmers, not only does the viability of the cotton-production system in West and Central Africa risk being undermined, but poverty will certainly increase.

## World Bank positions on support funds

The World Bank and IMF in particular have eschewed the idea of price-support funds.<sup>69</sup> This is linked to their market-driven model of sector reform which treats the global price distortions due to industrialised country subsidies to their farmers as a 'given'. While farmers in other countries continue to benefit from subsidies, for the IFIs, prices received by farmers in Mali should be as closely aligned as possible to world prices. Hence the World Bank resists the idea of a minimum guaranteed price and a support fund to uphold this price because they fear it will create unsustainable subsidies and a drain on public funds.

In order to alleviate poverty, the World Bank and IMF argue that government resources should be prioritised for 'pro-poor' spending on health and education, for example. No one is arguing against public spending on health and education services for poor people but in reality the trade-off may not be as simple as some models predict. Research commissioned by the World Bank reveals that the majority (more than 80 per cent) of cotton farmers are poor, and reductions in the cotton price will decrease farmer incomes leading to an increase in poverty, and in all likelihood decreased access to basic services.<sup>70</sup> In addition, targeted welfare schemes are notoriously difficult and costly to administer.

The IFIs have argued that market-based risk-management mechanisms could play the role of cushioning price volatility for small farmers, which is currently played by support funds, but these tools are not widely available or accessible in the cotton sectors of West and Central Africa – and certainly not to farmers.<sup>71</sup>

## Lessons from experience and innovation in support funds

The IFIs' views are also influenced by past experiences of old-style 'stabilisation funds', where there were undoubtedly cases of serious mismanagement by cotton companies to the extent that the funds were no longer available to uphold the price when needed. Indeed, in Mali, farmers have regularly claimed that they are owed as much as 15bn FCFA (\$30m) from these misappropriated funds.

But lessons have been learned from these experiences. Today's stronger farmer organisations have a direct role in the management of the cotton sector and the support funds to ensure that these problems are significantly minimised.<sup>72</sup>

In Burkina Faso, a support fund was created in 1992 that ensured a floor price to producers when actual prices fell below a certain reference price. Producers became active in the management of the fund in 1999. The fund also ensured that cotton companies were reimbursed the difference between the actual sale price and the reference price for the tonnage sold, when actual prices fell below this reference price. Other rules allowed for adjustments in surplus years. The fund was generated by paying in 50 per cent of the surplus of the sector to constitute the fund, and enabled the stabilisation of producer prices in the sector for a period of 12 years to 2003<sup>73</sup>.

This experience – as well as those of other countries such as Cameroon – shows that support funds where well-managed can function without the intervention of external funds over a number of years. But in prolonged periods of crisis in world cotton prices as well as unfavourable exchange rates, such funds will require additional support.

The strengthening of producer organisations was also a critical feature of the relative success of support funds experienced in Burkina Faso. The management of the cotton sector in Burkina Faso improved with limited reforms in the late 1990s. SOFITEX retained its monopoly for the purchase of seed cotton, but producers gained a 30 per cent share in the capital of the company using surplus revenues acquired when prices were favourable. In addition, producers also obtained two seats on the cotton marketing board of SOFITEX,

established in 2000, and charged with reviewing input bids and selecting distributors.

Restructuring was highly successful in Burkina because it was coupled with the emergence of strong producer organisations. These organisations jointly managed the stabilisation funds. By cautiously managing their finances after the revenue surpluses from the 1994 devaluation of the FCFA against the French franc (and now euro), Burkina Faso has successfully supported cotton-producer revenues even in times of drastically low world prices. Due to prudent and sensible management of surpluses from previous years, SOFITEX was able to cover a small part of the deficit accumulated in 2000-2001 and even distribute a 25 FCFA bonus at the end of the year. By contrast, in Mali and Côte d'Ivoire, the producers received higher prices the previous two years but did not receive a bonus in the 2000-2001 crop year.

Learning from these lessons – and adapted to the context of a liberalised sector with three separate cotton companies – a new 'price smoothing' fund has been proposed for Burkina Faso to ensure maximum price stability between years for farmers, considered to have been a factor in the success of the sector in that country.

**Box 4: Burkina Faso's price 'smoothing' fund**

With the entry of two new companies into the cotton sector in Burkina Faso since 2004, the current agreement on price setting has been revised to take account of the new actors and of changing conditions in the sector. In this context, the inter-professional body which brings together the companies and farmers in the sector is discussing the establishment of a 'price smoothing fund' with the following features:

- A set floor price range over a seven year moving average. The forecasted floor price for the following season is based on expected Cotlook A Index prices. The 2006–7 floor price was set at FCFA 165/kg of seed cotton in April 2006.
- Producers are paid the floor price minus the cost of inputs at the time of delivery of the cotton to the ginnery. If the actual price of cotton lint when marketed exceeds the floor price, producers will receive a supplement in May when the profit is made. The profit is calculated on the basis of the average daily value of the Cotlook Index A expressed in FCFA over the previous year, ending in March of the same year. The surplus is then split between the producers, the cotton companies and the fund. The amount of the surplus to be dedicated to the fund is modified according to the size of the surplus and the level of existing funds. The remainder of the surplus is divided 60:40 between the producers and the cotton companies, leaving producers with approximately 60 per cent of the FOB price.
- When there is a deficit, the fund is used to ensure the producer floor price and finance the deficit incurred by the cotton company. In years

when world prices fall less than five per cent of the bottom of the floor price range or rise no more than one per cent of the high end of the range, the fund does nothing.

- In the event that there are successive bad years and the fund falls into arrears, companies will need to extend a loan to the fund which will need to be repaid with interest as soon as the fund is capable. If the loan exceeds the credit limit set by the companies, the floor price range needs to be reduced the following year.

Source: Goreux 2006

## Moving forward

Fortunately, some donors have recognised that support or ‘price smoothing’ funds can be an important element in poverty-reduction strategies in the cotton-dependent countries of West and Central Africa. In Mali, the Malian Mission for Cotton Sector Restructuring (MRSC) has spearheaded government attempts to get a fund off the ground. In July 2006, after a year-long research and consultation process, farmer agreement was reached on basic principles of farmer contribution and management. In spite of the low prices, farmers will contribute 3 FCFA/kg of the surplus from the 2005–6 season to kick-start the fund, and 50 per cent of the surplus in future years.

Following these proposals, some of the EU’s 15m euro support to the cotton sector will be allocated to this fund, but this is unlikely to be sufficient. Similarly, in Burkina Faso, the French government through the Agence Française de Développement has agreed to support the price-smoothing fund but only with committed support from other donors to make the initiative workable in the longer term. This still leaves a considerable gap between the funds available and the funds required for these mechanisms to function effectively. Another possible resource includes Mali’s HIPC funds which could possibly be allocated to this purpose.<sup>74</sup>

Donors should acknowledge farmers’ efforts and allocate more funds to the support fund. In allocating funds to the support fund, a review of the price-setting mechanism should also be undertaken to ensure that it is sustainable as well as consistent with poverty-reduction objectives.<sup>75</sup>

**Box 5: Proposals for a support fund in Mali**

The Malian Mission for Cotton Sector Restructuring (MRSC) has been undertaking a process of analysis and consultation since June 2005 regarding the modalities for setting up a support fund, seen as indispensable to the proper working of the new price mechanism. A feasibility study was commissioned from a cotton-sector expert in June 2005 and the report presented to key stakeholders in May 2006. A copy of the report in Bambara, the national language, was made widely available to farmers' groups in the regions, and consultations were carried out in June and July 2006, leading to a national workshop.

The consultant's report recommends the setting up of a fund to the level of between 12 and 28 billion FCFA. The national federation of cotton-farmer co-operative unions, once constituted, should manage the fund, which would be the property of the farmers. In the meantime, a transitional body should be formed to manage the fund. The support fund itself should be managed as a co-operative enterprise according to the provisions of the 2001 co-operative law.

At the national workshop, farmers declared their support for the principle of setting up a fund to support the seed-cotton price and to its management by the co-operative federation and in the meantime by a transitional group. In order to resource the fund, a contribution will be made from the additional income from the 2005–6 season, with 5 FCFA/kg being reserved as a price complement to farmers. For the two following campaigns, any additional resources allocated to farmers above the base price will be split 50:50 between the support fund and farmers' incomes. Farmers also requested that the government and its partners provide financial support to bring the fund to an adequate level of financing.

Sources: République du Mali 2005b; 2006<sup>76</sup>

## 6 Conclusions and recommendations

The World Bank's privatisation and liberalisation policies set up to reform Mali's cotton sector are transferring all the risk associated with the downward trend in world cotton prices to the cotton farmer, possibly increasing poverty in rural Mali by up to five per cent. Continued downward pressures on cotton-producer incomes will hurt production, food security, the wider agricultural economy, and overall economic growth. These pressures, along with policy 'shocks' will constrain the execution of Mali's comprehensive poverty-reduction strategy.

To avoid further major increases in rural poverty in Mali and the related impacts on the wider economy, farmers should be guaranteed minimum prices, particularly when facing the uncertainties associated with privatisation. Without such guarantees, the costs of world price fluctuations will be passed directly on to the poorest of the poor – agricultural wage workers and unpaid family labourers. These prices should be set to take into account world market trends, but should also ensure that the returns to agricultural workers do not fall below poverty levels.

A national-level support or insurance fund as proposed recently in Mali and as currently being developed in Burkina Faso, can help farmers better absorb the shocks of volatile world markets over time. To kick-start or rehabilitate these funds, significant contributions are also required from governments and donor agencies. Experience from Cameroon and especially Burkina Faso shows that where producers have a strong voice in the management and where rules are simple and transparent, these mechanisms can function effectively in the long term, relying on external support in exceptional circumstances or prolonged crises.

In the longer term, investment is required to enable improvements in yields and ensure competitiveness, as well as the development of alternative crops, to enable some farmers to shift out of cotton.

Oxfam strongly urges that:

- Donors facilitate the establishment of a producer-managed fund to maintain minimum prices through increased contributions;
- A review of the poverty and sustainability impact of the new price-setting mechanism be conducted;

- Article 8 of the current price-setting mechanism be revised so the price floor cannot be lowered within the same growing season;
- Governments and donors ensure any new or future policies are accompanied by poverty-impact analyses and these policies improve the security of farmers' livelihoods and the sustainability of the sector;
- Government and the donor community sustain and increase their support to the development of the co-operative movement, through enhanced technical assistance and capacity-building efforts to ensure effective producer management of the sector, including the capacity to participate in national-level policy-setting and negotiating effectively to receive a more equitable share of world price;
- In supporting producer organisations, government and donors assist in developing a more coordinated and sustained 'bottom-up' approach, based on concrete needs expressed by farmers themselves, so that at local level, producer organisations develop the capacity to fulfil their new obligations and roles, manage enterprises, and diversify their activities;
- Government and producer organisations with donor support work together to develop a clearly defined strategy for the revival of development and extension services to cotton-producing regions, including literacy provision.

## Notes

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<sup>1</sup> Income data from World Development Indicators, HDI ranking from 2005 Human Development Report.

<sup>2</sup> République du Mali (2006a) 'Etude pour l'elaboration du schema operationnel de la privatisation de la CMDT', Rapport Provisoire, Bamako, June, Annex 4.

<sup>3</sup> WCA region produces around one million tonnes of fibre: about four per cent of the total world production of 25 million tonnes. ICAC, Review of the World Situation, Volume 58, No. 2, November – December 2004.

<sup>4</sup> IMF (2003), Mali : Enhanced Initiative for Highly Indebted Poor countries, completion point document, IMF country report 03/61, Washington DC: IMF, March; Republic of Mali (2002) Final PRSP: Poverty reduction strategy paper, document prepared and adopted by the Government of Mali, Bamako, May 29

<sup>5</sup> Estimates of the price suppression effect vary but converge at around 11–12 per cent. A recent World Bank study puts the effect at 12 per cent. K. Andersen and E. Valenzuela (2006) 'WTO's Doha Cotton Initiative: Who Would Gain from Subsidy and Tariff Cuts?', Washington DC: World Bank, February.

<sup>6</sup> Although the Hong Kong talks led to a decision to eliminate cotton-export subsidies, with the WTO negotiations suspended, and US elections approaching in 2008, the prospect of wider subsidy reform is looking increasingly doubtful.

<sup>7</sup> See Oxfam (2006) 'Kicking the Habit: How the World Bank and the IMF are still addicted to attaching economic policy conditions to aid', Oxfam Briefing Paper No. 96, Oxford: Oxfam. This gives full details of the conditionalities attached to World Bank and IMF lending programmes in the cotton sector.

<sup>8</sup> Wodon, Q., Briand, V., Labaste, P., Nouve, K. and Sangho, Yeyande, (2006) 'Cotton and Poverty in Mali', World Bank Working Paper, Draft, Washington DC: World Bank, p 31.

<sup>9</sup> During this period overall growth was 5.5 per cent on average and agricultural growth 4.2 per cent. M. Marouani and M. Raffinot (2005) 'Perspectives on growth and poverty reduction in Mali', Développement, Institutions et Analyses de Long Terme (DIAL) Working Paper, Paris: DIAL, CIRAD, AFD.

<sup>10</sup> IDS 'Sustainability Amidst Diversity, 9', cited in K. Pfeifer (2005) 'No Fluff, Just Cotton: The Strategic Importance of Cotton Production to Development in West Africa', Oxfam America paper presented to ICAC conference, Liverpool, September.

<sup>11</sup> M. Marouani and M. Raffinot (2005), *op.cit.*; Wodon *et al.* (2006), *op.cit.*

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<sup>12</sup> OECD (2005a) 'Economic and Social Importance of Cotton in West Africa, role of cotton in regional development, trade and livelihoods', Sahel and West Africa club secretariat/OECD, November, SAH/D(2005)556.

<sup>13</sup> M. Marouani and M. Raffinot (2005), *op.cit.*

<sup>14</sup> OECD (2005a) *op cit*: 52-3.

<sup>15</sup> OECD (2005a) *op cit*

<sup>16</sup> Personal communication, François Traore, President, UNPCB.

<sup>17</sup> M. Grimm and I. Gunther (2005) 'Growth and poverty in Burkina Faso: A reassessment of the paradox', Développement, Institutions et Analyses de Long Terme (DIAL) Working Paper, Paris: DIAL, CIRAD, AFD.

<sup>18</sup> Poverty among cotton farmers fell even in the immediate aftermath of devaluation. World Bank (2004) 'Cotton cultivation in Burkina Faso: A 30 year success story', A case study from Reducing Poverty and Sustaining Growth – What works, what doesn't and why, Washington DC: World Bank.

<sup>19</sup> OECD (2005a) *op.cit.*, p 38.

<sup>20</sup> World Bank (2004), *op.cit.*, p 12.

<sup>21</sup> *Ibid.*, p. 13.

<sup>22</sup> *Ibid.*

<sup>23</sup> For example, from the Koutiala area of the region of Sikasso, to the Kita area of the region of Kayes, where cotton production is expanding and there is considerable land available. Personal communications: Drissa Traore, Soloba Mady Keita, AOPP Cotton Commission.

<sup>24</sup> HDI rankings for the main cotton-growing region in Mali – Sikasso – were relatively low according to a 1999 survey by the Human Development Report. Michigan State University data also show poor nutrition rates among children in the region. M. Marouani and M. Raffinot (2005), *op. cit.* Note however that these data are not universally supported (see Wodon *et al.* (2006) *op.cit.*).

<sup>25</sup> For example, gains in cereals production in Mali in recent years have been accompanied by a downward trend in prices. M. Marouani and M. Raffinot (2005) *op. cit.*

<sup>26</sup> P. Ton (2002) 'Cotton production and rural livelihoods in West Africa', Dakar: ENDA/ Oxfam.

<sup>27</sup> At this stage following a World Bank commissioned audit, serious mismanagement was uncovered and several leading managers were jailed. This reduced the credibility of previous claims by the French that CMDT was a model company.

<sup>28</sup> In 1999–2000, the price paid to producers was 150 FCFA compared to 195 the previous year (see Table 2).

<sup>29</sup> The Office de la Haute Vallée du Niger (OHVN) region as well as the oilseed processing and marketing company HUICOMA were initially scheduled for privatisation in advance of this date.

<sup>30</sup> OECD (2005b) 'Mali: Africa Economic Outlook', Paris: OECD

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<sup>31</sup> As a result of these Bank concerns around the cotton-sector reform, the approval of SAC IV, originally scheduled for December 2004, thus did not happen until February 2005, delaying budget support to the Mali government for several months.

<sup>32</sup> République du Mali (2005a) 'Chronogramme Revise du processus de reforme du secteur coton', Bamako : Ministere de l'Economie et des Finances.

<sup>33</sup> Goreux, L. and Macrae, J.(2003) "Reforming the Cotton Sector in Sub-Saharan Africa" Africa Region Working Paper Series Number 43, Washington: World Bank, March.

<sup>34</sup> République du Mali (2005a), *op cit*

<sup>35</sup> As at June 2006, 6907 co-operatives had been formed and 286 communal unions. In early 2007, sectoral unions were being put in place.

<sup>36</sup> République du Mali (2005b) 'Etude du Fonds de soutien des prix du CG – Rapport provisoire', Bamako: Mission de Restructuration du Secteur Coton, pp 18–23. The 35 per cent share was increased to 40 per cent at the end of this period (1999–2000).

<sup>37</sup> Farmers' leaders have regularly claimed that they are owed as much as 15bn FCFA (about \$30m) from these misappropriated funds.

<sup>38</sup> Arrêté interministériel n°02-1445/MDRE-MEF-MICT du 05 juillet 2002 déterminant le mécanisme de détermination du prix d'achat du coton graine.

<sup>39</sup> *Ibid.*, pp 16-23

<sup>40</sup> *Ibid.*

<sup>41</sup> Wodon *et al.* (2006), *op.cit.*, p 7.

<sup>42</sup> M. S. Keita and K. N. Nubukpo (2005) 'L'impact du nouveau mechanism de determination du prix de coton grain sur l'economie Malienne', Bamako: CIRAD/ Oxfam. According to the authors, the first detailed proposal for the mechanism was presented in a note dated 11 November 2004 as part of a follow-up mission in the SAC IV negotiations.

<sup>43</sup> République de Mali (2005c) 'Protocole d'Accord Etat – CMDT – Producteurs sur le mechanism determination du prix d'achat du coton graine', Bamako: Mali.

<sup>44</sup> Prior to signing the agreement, farmers' leaders organised a consultation process during which they analysed the mechanism and then toured the country to discuss the implications with their members in the regions. As a result, some modifications were proposed to the agreement on the new mechanism – and farmers requested that the price should be fixed at the upper end of the proposed band, or 175 FCFA. In the event, under heavy political pressure, the agreement on the new mechanism was signed as drafted by the CMDT, cotton union leader, and Minister of Economy and Finance on 13 January 2005.

<sup>45</sup> As pointed out in the study on the feasibility of the support fund, the text talks about the 'final income to producers' which would normally include a measure of volume, whilst the actual formula gives a percentage of a price in

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kg. This has given rise to some confusion of how the results of the campaign and their distribution will be determined. République de Mali (2005b), *op cit.*

<sup>46</sup> DNSI (2003) cited in M. S. Keita and K. N. Nubukpo (2005), *op.cit.*

<sup>47</sup> Unpublished note from producer consultation, Bamako: 5 January 2005.

<sup>48</sup> Seed-cotton payments are made in two parts: the base price, which is paid on delivery of cotton at the end of the growing season and a supplement or 'ristourne' paid in the subsequent year depending on the level of surplus in the sector once all the cotton has been sold.

<sup>49</sup> M. S. Keita and K. N. Nubukpo (2005), *op.cit.* ; A. Traore (2006) 'Effets préliminaires de la baisse du prix du coton sur le revenu et les conditions de vie des exploitations cotonnières au Mali', rapport final pour Oxfam America, December.

<sup>50</sup> A. Traore (2006), *op.cit.*

<sup>51</sup> Wodon *et al.* (2006), *op.cit.*, p 10.

<sup>52</sup> Wodon *et al.* (2006), *op.cit.*, p 10.

<sup>53</sup> A. Traore (2006), *op.cit.*

<sup>54</sup> Marouani, M. and Raffinot, M. 2005 Perspectives on growth and poverty reduction in Mali, Développement, Institutions et Analyses de Long Terme (DIAL) Working Paper, 2004-5, DIAL, CIRAD, AFD, Paris.

<sup>55</sup> M. Dufumier (2005), Etude des systèmes agraires et typologie des systèmes de production agricole dans la région cotonnière du Mali. Rapport de synthèse (document de travail provisoire pour discussion), Bamako: PASE.!

<sup>56</sup> In 2005-6, 4780 farmers in Mali were involved in fair trade cotton production in 72 cooperatives producing 5100 tonnes of seed cotton. The number of farmers and production levels were at similar levels in 2006-7. Personal communication, Soloba Mady Keita.

<sup>57</sup> In 2005-6, 3170 farmers produced approximately 828 tonnes of seed cotton in the three districts of Kolondieba, Bougouni and Yanfolila. Communication of Helvetas and Mobiom to Oxfam consultation meeting, Bamako, 22-23 January 2007.

<sup>58</sup> M. S. Keita and K. N. Nubukpo (2005), *op.cit.* Table 6 p 22.

<sup>59</sup> Wodon *et al.*, *op cit.*

<sup>60</sup> Kofi Nouve, Jean-Pascal Nganou and Quentin Wodon (2006) 'Should Cotton Policies Aim for Higher Producer Prices or Yields? A CGE Analysis for Mali, in Wodon *et al.* (2006), *op cit*

<sup>61</sup> Wodon *et al.* (2006), *op cit.*: 16

<sup>62</sup> World Bank (2004) 'Joint Staff Assessment of the Poverty Reduction Strategy Paper, Annual Progress Report', Africa region, PREM 4, report no. 29061, Washington DC: World Bank, p 11; M. Marouani and M. Raffinot (2005), *op cit.*

<sup>63</sup> M. S. Keita and K. N. Nubukpo (2005), *op.cit.* This assertion is based on focus-group interviews in six villages in the districts of Koutiala. Dans le

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Mpessoba, and Molobala. A. Traore (2006), *op cit*, spoke with farmers and farmer representatives in four villages around Kita and Fana on their intentions.

<sup>64</sup> A. Traore, *op cit*.

<sup>65</sup> DNSI (2003) cited in M. S. Keita and K. N. Nubukpo (2005), *op.cit.*, p16.

<sup>66</sup> Sally Baden, field notes from evaluation mission, June-July 2006.

<sup>67</sup> République du Mali (2004), Le programme de reforme du secteur coton au Mali: Mesures et état d'exécution. Communication de la délégation malienne au Forum Union Européenne Afrique sur le coton, Paris, 5-6 juillet. Cadre Stratégique pour le développement de la filière coton au Burkina Faso, Ouagadougou, 18 juin, 2004. .

<sup>68</sup> Goreux (2003), *op.cit.*; USAID, 2005, Summary and Findings of the West Africa Cotton Assessment, September 25-October 14, 2004, Washington DC: USAID, January; M. S. Keita and K. N. Nubukpo (2005), *op.cit.*, p 16.

<sup>69</sup> See section 5. République du Mali (2005b), p 58; IMF Cotonou meeting declaration, May 2005. <http://www.imf.org/external/np/sec/pr/2005/pr05121.htm>; Personal communications, John McIntyre, World Bank, April 2005; John Baffes, World Bank, September 2005.

<sup>70</sup> Wodon *et al.* (2006), *op.cit.*

<sup>71</sup> Estur, G. Role of price risk management in cotton sectors, presentation to the Annual meeting of the ITF Interlaken, Switzerland, May 19, 2005, ICAC

<sup>72</sup> S. Baden (2005) 'Between a rock and a hard place: The case for support to Africa's cotton sectors,' in E. Hazard (ed.) 'The White paper on cotton', Dakar: ENDA Tiers Monde

<sup>73</sup> 'Fonds de soutien : performances et limites ' Présentation par le Burkina Faso, Séminaire technique sur les outils de gestion, des effets de la volatilité des cours du coton sur les revenus des filières et des producteurs

Dakar 24-25 November 2005. When the fund reached \$8.5bn at the end of the 1996–7 campaign, contributions were relaxed. It was left to farmer discretion to decide whether to pay in from their surplus, which never happened. Subsequently the fund was exhausted when prices fell dramatically below the reference price for two years running and an accumulation of debts to the company had to be paid. As of March 2003, there were no funds left. If the 50 per cent surplus had been paid on an ongoing basis, there would have been \$16bn in the fund. While even this could not have absorbed the entire deficit from the 2004–5 campaign of \$26bn, it certainly would have covered 60 per cent of losses.

<sup>74</sup> République du Mali (2005b), *op cit*.

<sup>75</sup> Aside from these key concerns, there are also technical reasons why the current price mechanism may urgently need revision to ensure that it does not create further instability in the sector. Simulations carried out on the mechanism by a senior expert show that – under reasonable assumptions about price and exchange-rate trends and industry performance – the current mechanism is likely to lead to a structural deficit of the CMDT,

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ironically the opposite of what was intended. République du Mali (2005c), *op cit.*, pp 33–8.

<sup>76</sup> République du Mali (2006b) 'Rapport de Synthèse de l'atelier national sur la mise en place d'un fonds de soutien du prix du coton graine', Primature, Mission de Restructuration de Secteur Coton, July.

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