

Liberalization of the Mozambican Cashew Industry
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Introduction

The cashew industry has a long history in Mozambique and was once the mainstay of this African country's economy. The industry, which was born in the early 20th century, was cultivated during the period of Portuguese colonization. During this time, Mozambique produced half of the world's raw (unprocessed) cashew nuts and export earnings from processed cashews exceeded \$30 million per year. However, the industry suffered a precipitous decline after its zenith in the 1960s and early 1970s.

Following independence in 1975 and a civil war from 1976-1992, the Mozambican economy and cashew industry laid in ruins. President Joaquim Chissano relied on the World Bank and International Monetary Fund for financial support in rebuilding Mozambique, which was one of the poorest, most indebted countries in the world. In 1995, the World Bank required the Mozambican government to liberalize its raw cashew nut export market in order to qualify for additional loan assistance.

The liberalization policy involved privatizing cashew processing factories and subsequently gradually eliminating the export tax on raw cashew nuts. Based on economic theory, the World Bank expected that eliminating the export tax would increase the price the farmers received for their raw cashews and alleviate poverty. However, the industrialists who had purchased the processing factories under a regime of protection, were unable to afford raw cashew nuts at the higher prices that prevailed following the tax reduction. When World Bank president James Wolfensohn visited Mozambique in 1997, he was faced with fierce opposition from the Mozambican processing industry. He was forced to determine whether the World Bank should enforce the agreement that additional loan assistance was dependent on Mozambique fully liberalizing its cashew market or whether it should change course and allow the government full responsibility in determining its own cashew policy.

Background

Colonial Roots of Cashew Industry: 1930-1975

Cashew production has been extremely important to Mozambique throughout much of the 20th century. While the cashew tree, imported by the Portuguese, is not indigenous to Mozambique, it has proved to be well-suited to the Mozambican climate. The tree crop was particularly well-suited to Nampula province in the northern region of the country, as illustrated in Exhibit 1¹. Beginning in the 1930s, cashew cultivation in Mozambique expanded dramatically, primarily on small and medium scale African farms in rural areas of the country.

¹ Nampula generates 70% of marketed cashew output, compared to Gaza and Inhambane provinces in the south which each produce 12% and 10%, respectively, of overall marketed output.

As the cashew industry developed, it had, and continued to have throughout the 20th century, three primary sub-sectors: the rural farmers (known as “producers”), traders, and processors, as illustrated in Exhibit 3. After harvesting the cashew nuts, called “raw” or unprocessed nuts, the farmers sold them to local traders. Local traders then sold the raw cashew nuts to larger-scale traders who transported them to exporters or to domestic processing factories.

The Portuguese supported the growth of the cashew industry at each level. They actively promoted cashew cultivation during the colonial period and by the 1960s Mozambique had established itself as the world leader in cashew production. During the 1960s, Mozambique produced half the world’s cashew nuts. In 1968, there were 45 million cashew trees in Mozambique and the country produced 185,000 tons of raw (unprocessed) cashew nuts².

Mozambique became the first African country to process cashews on an industrial scale³. Beginning in 1950, small, manual processing systems were replaced by large, mechanized factories that extracted the edible kernel from the raw cashew nut (Deloitte and Touche, 1997). Under the Portuguese, Mozambique’s cashew processing industry grew dramatically in the 1960s and early 1970s as raw nut production increased. By 1973, there were 12 processing factories with a total processing capacity of 150,000 tons of raw nuts. These factories employed highly capital-intensive technology that enabled them to automatically process large quantities of raw nuts.

The Portuguese took an active role in promoting and regulating the industry during the colonial period. Throughout the 1950s and 1960s, the Portuguese government engaged in large-scale planting efforts in order to dramatically increase the cashew crop. The colonial government established producer prices. The multi-tiered marketing system, comprised of primarily Portuguese and Asian traders, was also regulated by the colonial government that established specified marketing margins to be paid at each level. Such producer and marketer prices depressed the domestic price of raw cashews, effectively subsidizing the domestic processors who relied on an affordable supply of raw cashew nuts.

Early Period of Independence and Civil War: 1975-1982

Mozambique gained its independence in 1975, an event which had an enormous impact both on the overall economy and the cashew industry. The Portuguese had excluded most Mozambicans from skilled jobs and positions of authority within the colonial government. When approximately 90% of the Portuguese in Mozambique emigrated within two years of independence, the country was left without the leaders of the cashew industry. Upon independence, government-led planting campaigns ceased. The rural trading network collapsed as most of the Portuguese traders left the country and the Asian traders migrated to urban areas and gave up trading activities. Many Portuguese processing factory owners fled the country, literally abandoning their businesses.

² See Exhibits 4 and 5.

³ Raw cashews must be processed in order to extract the edible kernel from the shell.

The Front for Liberation of Mozambique, or Frelimo, that had led the campaign to gain independence, emerged as the dominant political party. Its socialist ideology was reflected in the centralized control it maintained over the cashew industry. Following independence, the cashew trade was brought under the control of Enacomo, a state trading company. Like its colonial predecessor, the Mozambican government continued to set producer prices, known as minimum or “reference” prices, as well as trading margins. Such prices were based on the world kernel price and the domestic industry’s processing costs rather than the raw cashew world market price in order to ensure that the processing factories could remain competitive in the processed cashew market. The government imposed a ban on exporting raw nuts in 1978 and in 1979 established Caju de Moçambique, a state holding company, which operated the majority of Mozambican processing factories after the original owners had abandoned their businesses.

After gaining independence, Mozambique entered a protracted civil war that devastated the country until 1992. An estimated 1 million Mozambicans perished during the civil war, 1.7 million took refuge in neighboring states, and several million more were internally displaced.

Mozambique’s cashew production was severely impacted by the civil conflict. Production levels that had peaked in 1972/73⁴ during the colonial era, had already begun a long period of decline beginning with the 1973/74 season. The national cashew orchard suffered during the prolonged civil war. Existing cashew trees were abandoned and increasingly plagued by pests and disease. Furthermore, new trees were not being planted. The marketing system, which linked rural producers with urban processing factories or coastal exporters (before the export ban), operated in the rural areas that were plagued by violence. As a result, marketing activity was severely limited.

The processing sector was also severely impacted during the civil war years when Caju de Moçambique was confronted with serious problems in operating the processing plants. It was forced to shut down the factory at Majacaze in both 1982 and 1984 due to a lack of raw material. During the period, state managers did not make the necessary investments and the factories and machinery deteriorated. According to Ewen Cobban, an investment officer at the IFC, the Mocita factory was forced to close because the government had failed to maintain the plant and make the necessary investments.

Mozambique Turns to the West: 1982-1995

The economic problems confronting the cashew industry were only a part of the overall political and economic crisis in Mozambique. The civil war, along with a severe drought and famine in 1983 that contributed to an estimated 100,000 deaths, forced the Frelimo government to deviate from its socialist ideology and realign itself with the West in an

⁴ Cashew is a perennial tree crop that is harvested between October and early February in the northern part of the country and from late January to early May in the southern part of the country (Abt Associates, 1999). Cashew production is generally reported on this seasonal year rather than a calendar year basis. For example, cashew harvested between October 2000 and May 2001 is reported as the 2000/01 seasonal year.

effort to obtain financial assistance. While this realignment did not lead to an end in the civil war, which did not end until 1992, it marked a fundamental shift toward capitalist, free-market principles and the beginning of a relationship with the World Bank.

Mozambique became a member of the Bretton Woods Institutions in 1984. The 1987-1990 Economic Rehabilitation Program, the country's first stabilization and structural adjustment program, was agreed between the government and the World Bank in 1987. This ERP was aimed at decreasing overall administrative controls in order to restore market incentives to promote production and trade (Tarp, 1990). While it was not specifically focused on the cashew industry, it impacted the cashew sector along with other sectors of the economy and marked the beginning of the liberalization process (Pomerantz, 2001b). Among other things, this program called for a substantial increase in the government-established cashew producer price and the establishment of the minimum producer price system that was implemented in the early 1990s.

The early to mid-1990s were a period of restructuring for the processing industry, as Mozambique emerged from civil war and the Bretton Woods institutions advised a strategy of privatization. Privatization of Caju de Mozambique, the holding company of the state-owned processing factories, began in 1991 when a privatization unit (UTRE) was created within the Ministry of Finance (World Bank, 1995). By the end of 1995, all of the formerly state-owned factories had been privatized (Hilmarsson, 1995)⁵.

Controls on raw cashew exports were gradually reduced during the early 1990s. In 1991/92, the export ban on raw cashew nuts was lifted and limited quantities of raw nuts could be exported. However, a 60% tax on the difference of the FOB and factory gate prices and a quantitative restriction of 10,000 tons were imposed (Desai, 2001). In 1992/93, the tax (on the difference between the FOB and factory gate prices) was lowered to 30%, but the quantitative restriction was maintained at 10,000 tons. In 1993/94, the export tax was maintained, but the quantitative restriction was loosened. While the initial export quota remained fixed at 10,000 tons, additional quantities were auctioned off in 5,000-ton lots to registered exporters. The quantitative restriction on raw nut exports was completely eliminated in 1994/95 and the government introduced a graduated export tax that was equivalent to a 32% tax on the FOB value (Desai, 2001a).⁶

Producer prices were significantly increased in 1987/88 from 10 mt/kg to 105 mt/kg⁷. At this time, the government also announced that a minimum producer price would replace the fixed producer price as the liberalization program progressed. Over the period 1988/89 through 1994/95, the actual producer price gradually increased from 165 mt/kg to 2,000 mt/kg, 500 mt/kg more than the government-recommended producer price⁸.

⁵ Refer to Exhibits 6 and 7 for further information regarding the processing factories and their privatization.

⁶ This consisted of a 25% tax on unit values up to \$600 per ton, and a 70% tax on the difference between the actual FOB value and \$600 per ton.

⁷ The local currency unit in Mozambique is the metical (mt). During the 1990s, the average official exchange rate was 9,640 mt/\$; the average parallel market exchange rate was 10,123 mt/\$.

⁸ See Exhibit 8

Enacomo, the state trading agency, was privatized during the late 1980s and further market liberalization occurred during the early 1990s. Through this market liberalization, additional marketing channels opened and new players entered the multi-tiered trading system that was comprised of four primary levels: local traders, retail traders, larger wholesale traders, and exporters^{9 10}. Most notably, informal traders entered the market at both the local and retail levels. However, according to Raimundo Matule, the amount of competition remained limited due to capital constraints, the cost of transportation, and generally loyal relationships among traders at different levels of the supply chain.

World Bank Advises Further Liberalization: 1995 - 2001

Policy Formation

In the 1995 Country Assistance Strategy (CAS) Report, the World Bank required Mozambique to further liberalize cashew marketing and exporting in order to satisfy the “base case” conditions and qualify for approximately \$400 million of loan assistance (World Bank, 1995a).¹¹ The policy was part of the World Bank’s broader effort to promote Mozambique’s transition from a socialist to a free-market economy.

Two individuals who were directly involved in advising the Mozambican government to further liberalize its cashew industry were Phyllis Pomerantz and Jehan Arulpragasam. Phyllis Pomerantz had become the Country Manager for a group of African countries including Mozambique in July 1994 and then became the Country Director of Mozambique when this position was created in July, 1996. Jehan Arulpragasam was the World Bank Country Economist for Mozambique during this period¹².

According to both Phyllis Pomerantz and Jehan Arulpragasam, the World Bank’s decision to advise Mozambique to further liberalize its cashew industry was based on a 1995 report by Hilmar Hilmarsson, a World Bank consultant¹³. This report concluded that the export tax was a means of artificially subsidizing inefficient processing factories at the expense of the rural, peasant raw cashew nut producers. In other words, the report concluded that eliminating the export tax would increase the domestic price to the higher world market price. This would, theoretically, increase the price paid to the producers, but also increase the price the processors had to pay for raw nuts.

⁹ Producers sell raw cashew nuts to local traders, traditionally at local collection posts. These local traders then sell the raw cashew nuts to retail traders who then transport and sell them to wholesale traders who are located in larger towns or along key trading routes. Finally, the wholesalers sell the raw nuts to either exporters in Maputo or Nacala (when raw cashew exports are not banned) or domestic processing factories.

¹⁰ See Exhibit 3 for further information regarding the structure of the marketing system

¹¹ The World Bank’s proposed lending program for FY96-00 included low and base scenarios. Liberalizing the cashew industry was a condition for the latter, in which it would receive a loan package of \$665 million. Under the former, the loan package would be reduced to \$240 million. The \$400 million figure is the approximate difference between the two scenarios that was a function of the cashew liberalization.

¹² Both the Country Director and the Country Economist positions are based in the World Bank’s Washington, D.C. headquarters.

¹³ This report was also included as a chapter in the 1995 World Bank Report, “Mozambique: Impediments to Industrial Sector Recovery” which is the source cited in this case.

Based on the Hilmarsson report, Phyllis Pomerantz and Jehan Arulpragasam assumed that liberalization would increase the producer share of the FOB price to 50%-70% and as a result, increase production and income for the 1 million households that cultivated cashews and the overall export value of cashews, as illustrated in Exhibit 9. Thus, decreasing the export tax was consistent with the goal of poverty alleviation, which was rapidly becoming one of the World Bank's priorities after James Wolfensohn became president in 1995. According to John Zutt, Operations Officer in the Mozambique Country Director's office, the World Bank's aim in liberalizing the cashew industry was to "increase the poverty reducing potential of the cashew industry in Mozambique...and this was one of the few pro-poor things the World Bank could implement at the time" (Zutt, 2001). Pomerantz also noted that removing the export tax was "an easy thing to do to alleviate poverty" for the over 1 million peasant cashew producers.

The Hilmarsson report also concluded that the Mozambican processing industry, as structured in 1994, was unviable. It found that the Mozambican processing industry had a "fundamental structural competitive disadvantage because of the technologies employed" (World Bank, 1995b), particularly when compared with the relatively manual, labor-intensive Indian processing industry. At the time, there were four types of processing systems that were in operation in Mozambique. The first type was the hand processing system that was low-cost and labor intensive. The second method was the impact decortication system. While this system operated efficiently with smaller quantities of raw nuts, they had to be of a consistent size in order to minimize kernel breakage. The third system was the semi-mechanical system, which could efficiently process smaller quantities of nuts regardless of nut size. Finally, the automated cutter, known as the Oltremare system, was a fully automated system. It was well-suited for processing large, high quality cashews. However, its high capital cost necessitated large volumes of raw nuts in order to operate efficiently¹⁴.

In 1993, 97% of Mozambique's installed processing capacity was either impact or Oltremare technology. According to the report, these highly mechanized processing techniques yielded a relatively low proportion of whole kernels¹⁵. Because of the technical limitations of the Mozambican processing system and the substantial price differences between whole kernels and broken kernels (reaching as high as 50% per unit), the value added by the Mozambican processing industry was marginal or negative in the early 1990s, according to the World Bank (1995b), as illustrated in exhibit 10.3¹⁶.

Based on this comparison with other countries and the type of technology the Mozambican processing industry employed, the Hilmarsson report recommended restructuring the processing industry in addition to liberalizing raw cashew exports by

¹⁴ See Exhibit 2 for further information on each type of processing system.

¹⁵ See Exhibit 10 for a comparison of whole kernel yield in Mozambique and other processing countries and Exhibit 2 for a more detailed description of the various processing systems.

¹⁶ Note, however, in Exhibit 10.3 that the finding that the value added by the Mozambican processing industry has been marginal or negative has a small margin of error. The finding is highly dependent on the prices of raw and processed cashews and the kernel yield per ton of raw nuts that are assumed. As illustrated in Exhibit 10.4, which is based on Deloitte and Touche (1997), the value added by the Mozambican industry was positive between 1994/95 and 1996/97.

replacing the highly mechanized processing system with manual or semi-mechanical technology¹⁷. Although the 1995 Country Assistant Strategy (CAS) Report did not directly advise the government to restructure the processing industry, Phyllis Pomerantz assumed that the liberalization process would increase the overall industry's competitiveness. She said that the World Bank "wanted and expected the inefficient processing factories to close (after the export tax was removed), but assumed that the viable, competitive factories would be able to survive."

Political Economy and Conditionality

The World Bank's policy was met with intense opposition from leaders of the processing industry who had withstood the war years in Mozambique and felt entitled to continued protection. According to Phyllis Pomerantz, "the World Bank was working with a new government team. (President) Chissano had recently appointed a group of technicians as his cabinet who did not fully understand or expect the degree of domestic opposition to liberalizing the cashew industry or did not understand the World Bank." However, the Mozambican government recognized the political power of the urban factory owners and workers compared with the relatively limited political influence of the producers who, despite numbering over one million households, were relatively disorganized and dispersed throughout the rural areas of the country.

Despite the domestic opposition, the government was dependent on continued support from the Bretton Woods institutions. Mozambique was one of the poorest countries in the world in the mid-1990s and international aid accounted for 60% of its GDP. Therefore, the government of Mozambique recognized that it needed to "stay on track with the World Bank," according to Jehan Arulpragasam. In addition, Mozambique was in the process of applying for debt relief under the HIPC initiative¹⁸. According to Mozambican President Joaquim Chissano, Mozambique "had to liberalize the export of raw cashews in order to obtain other benefits from the Bretton Woods institutions." Specifically, he asserts that Mozambique complied with the World Bank's liberalization policy in order to qualify for HIPC debt relief (AIM, June 25, 2001).

Accepting the need to comply with the World Bank's policy, the government and industry leaders disagreed with the World Bank regarding the extent and time-frame for the liberalization. The Bank favored immediate and complete elimination of the tax, while the government and processing industry favored a partial and gradual reduction in the tax. According to Phyllis Pomerantz, when the government proposed a 10-year time-horizon for eliminating the tax, she advised that the tax should be eliminated in a shorter period of time and the 5-year time-horizon was agreed by the World Bank and government¹⁹.

¹⁷ The Hilmarsson report also noted that infant-industry protection in the form of a *low, temporary* tax on raw cashew exports may have been beneficial in order to allow the processing factories to adopt new technology.

¹⁸ The Highly Indebted Poor Country (HIPC) Initiative was a joint World Bank/IMF program that was aimed at reducing the external debt of the world's poorest, most heavily indebted countries. It was initiated in 1996.

¹⁹ See Exhibit 11 for a schedule of the proposed and actual decrease in the export tax.

Opposition

As initially agreed by the Mozambican government and the World Bank, the export tax was reduced from 20% to 14% between the 1995/96 and 1996/97 seasons. The producer price increased 14%, from 3,500 mt/kg to 4,000 mt/kg between 1995/96 and 1996/97 and it became increasingly difficult for the factories to obtain raw cashews and nearly impossible to make larger-scale capital improvements. Opposition to the liberalization, among both individuals involved in the processing industry as well as others who more generally opposed the Frelimo government and World Bank, was quite intense.

The processing industry condemned the World Bank for requiring the government to reduce and eventually eliminate the export tax and criticized the government for agreeing to the policy. The factory owners who purchased the processing factories from the government in 1995 asserted that they required a period of protection in order to rehabilitate the factories following the civil war and the period of government operation in which the equipment had deteriorated. According to Joseph Hanlon (2000), a journalist and leading opponent of the liberalization policy, “there was an informal agreement with the owners of the newly privatized companies that they would be given a period of protection while they rehabilitated and modernized the factories.” In the extreme case of one factory, Angocaju, the government actually had entered into a contract guaranteeing the supply of raw nuts to the factories, and only nuts surplus to the factories’ requirements would be exported. Other factories at least assumed that given the long history of protection that dates back to the colonial era, it would continue, despite warnings to the contrary.

The factory owners further asserted that they could not afford sufficient quantities of raw cashews at higher prices without an export ban or prohibitively high export tax and therefore could not obtain enough raw material to operate. Derek Higgs, managing director of the Mocita processing factory, claimed that the inadequate supply of raw nuts was a key problem of the policy (Whewell, 2001). Boaventura Mondlane, the general secretary of the cashew processing industry workers’ union, said that the World Bank policy “effectively stimulated the export of raw nuts to India, starving the local processing industry of its raw material” (Panafrikan News Agency, 1999).

Factory owners also argued that protection was warranted given Indian labor standards and trade policies and that the processing industry could not compete with Indian cashew processors without trade protection. They claimed that raw cashews contain a corrosive and toxic liquid called cashew nut shell liquid (CNSL) that can be harmful to workers’ hands. They asserted that the manual processing methods employed in India subjected workers to such health risks while the highly-mechanized impact and Oltremare processing systems employed in Mozambique prevented workers from coming in direct

contact with CNSL²⁰. Furthermore, they argued that, “Indian subsidies to its industry ‘tilt the playing field’ and made competition unfair.” (Hanlon, 2000)

World Bank President Wolfensohn Visits Mozambique

In response to domestic and international criticism, World Bank president Wolfensohn visited Mozambique in February 1997. He was confronted by intense opposition from the processing industry and forced to determine whether the World Bank should change its course in Mozambique. He considered his options. He could require Mozambique to implement the agreed cashew market liberalization policies in order to obtain additional assistance. Alternatively, he could remove the conditionality and allow the Mozambican government to determine its own cashew market policies. He tried to project the outcome of both scenarios and considered the potential impacts each would have on the production, marketing, and processing sectors of the industry. He realized the magnitude of this decision and that it would have significant implications, not only for the cashew industry in Mozambique, but also for how the World Bank would work with other governments in promoting sustainable development in the future.

²⁰ However, according to Dr. Raimundo Matule, the Deputy Director of the Mozambican Ministry of Agriculture’s cashew agency, INCAJU, workers’ safety is not compromised by the use of semi-mechanical technology because coconut oil is used to fully protect workers’ hands from the harmful effects of CNSL.

Exhibit 2: Overview of the Mozambican Cashew Processing Industry

Raw cashews must be processed in order to extract the edible kernel from the shell.²¹ Cashew processing consists of two primary steps. The first step is to heat the cashew in order to harden the naturally pliable shell so that it can be broken open through either steaming or roasting. The second step is to break the outer shell and decorticate the kernel. Besides the cost of the raw material, these two steps represent the primary costs of processing and also are the most significant steps in determining overall kernel quality. The final steps in the production process involve peeling an outer layer off of the kernel, sorting the kernels based on size and quality, and packing them.

Open-fire roasting or pan-frying (both referred to as “roasting”) have been the traditional methods used to heat raw nuts in Mozambique (Abt Associates, 1999). The kernel price is a function of both the size and quality of the nut. Whole, white (un-scorched) nuts obtain the highest returns. Therefore, recently, certain factories have employed steaming techniques for heating the raw nuts in order to decrease the amount of raw nuts that are scorched in the roasting process.

There are currently five general cashew processing systems available to extract the kernel from the shell. Four of these processes are in operation (or were until the late 1990s) in Mozambique. First, the hand processing system is the most prevalent form of shelling world-wide (Abt Associates, 1999). In this low-cost, labor-intensive method of shelling, workers simply crack open the heated raw nut with a wooden or metal hammer. According to Deloitte and Touche (1997), “the work is arduous and slow, but skilled hands are able to produce the highest out-turn of all (processing) systems.”

The second method of shelling is impact decortication. This method was mechanized during the 1950s when centrifugal impellers were introduced. This technology uses centrifugal force to hurl roasted nuts against impellers mounted on the inside wall of a metal impact cylinder (Abt Associates, 1999). This was a major system of processing 30 years ago and is still the main system used in Mozambique²² (Deloitte and Touche, 1997). While an advantage of this system is that it can effectively process small nuts in a mechanized manner, the raw nuts must be of a consistent size in order to accurately control the system’s speed and minimize kernel breakage.

The third system is the mechanical hand or semi-mechanical system that involves cutting open the nut. This method, which was developed in India during the 1950s, is currently the most common system in Mozambique. Following either roasting or steaming, shelling is done using a mechanical device which is fed by hand to cut individual nuts. A foot pedal is usually used to clamp the nut, the shell of which is then cut with blades as

²¹ Historically, cashew processing extracted and marketed not only the kernel, but also the cashew nut shell liquid (CNSL), which had industrial uses and was more valuable than the kernel at one time. However, synthetic substitutes have been developed for CNSL and it is not extensively marketed. In certain cases this caustic by-product that is harmful to workers’ skin if not properly protected can be utilized as a heating medium for new raw nuts.

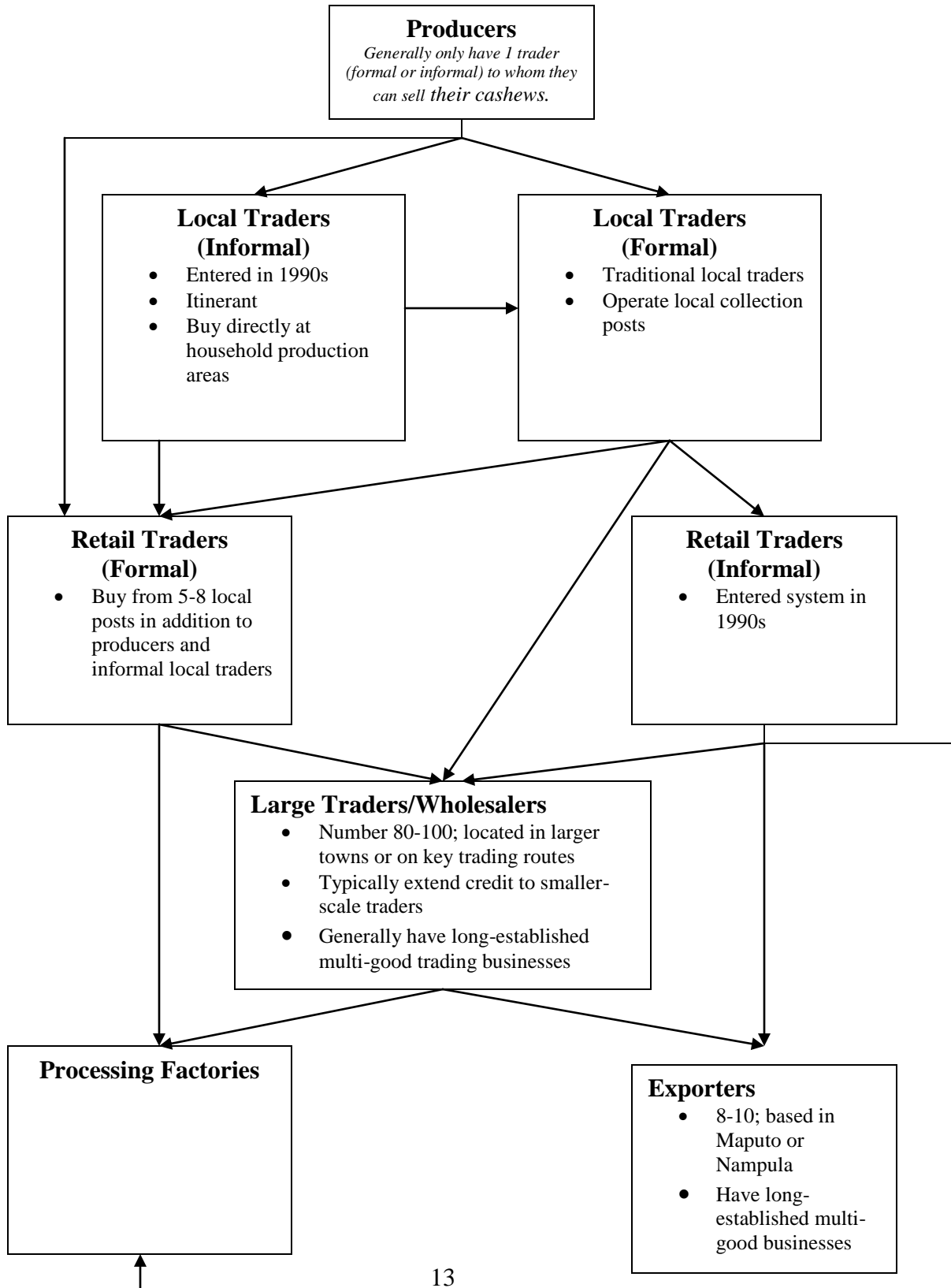
²² While impact technology was the main system used in Mozambique in 1997, this is no longer the case.

the handle is lifted (Deloitte and Touche, 1997). The primary advantages to this system are that it is not imperative that the raw nuts are presorted by size and that it produces a higher out-turn of whole kernels. However, workers' hands may still come in contact with the caustic CNSL.

The final type of shelling employed in Mozambique is the automated cutter that was first designed by Oltremare, an Italian engineering firm. This system, the only fully automated cashew processing system currently available, is essentially an automated version of the mechanical hand or semi-mechanical system described above. This system may involve either hand or automated feed mechanisms. It is well-suited for processing large, high quality cashews. However, its high capital cost necessitates large volumes of raw nut throughput (Deloitte and Touche, 1997).

Exhibit 3 Marketing Structure

Sources: Deloitte and Touche, 1997 and Matule, 2001



Liberalization of the Mozambican Cashew Industry: An Epilogue

During Wolfensohn's visit to Mozambique in 1997, he commissioned a new study (Deloitte and Touche, 1997) and suspended the demand for further cuts in the export tax (Hanlon, 2000). Faced with continued domestic opposition to the reductions in the export tax, Mozambique's parliament later passed a bill in 1999 that increased the tax to between 18% and 22%, the exact amount to be determined each year, depending on market conditions. In both the 1999/00 and 2000/01 seasons, the export tax was 18% (Desai, 2001a). The World Bank, under continuing international criticism, had not challenged the increased export tax as of 2002.

Impact on the Cashew Industry: Producers, Traders, and Processors

Producers and Production Levels

As illustrated in Exhibit E-8, the producer prices increased throughout the 1990s, before falling in 2000/01. When the producer price was fully liberalized and the government ceased establishing a minimum, or reference, producer price in 1998/99, it increased to 5,100 mt/kg and then 7,179 mt/kg in 1999/2000. However, the producer price dropped precipitously to 3,950mt/kg in 2000/01 when the world market price collapsed (INCAJU, 2001) and the real producer price only increased 8% between 1990/91 and 2000/01. Overall, the producers' share of the FOB price increased throughout the 1990s. Following an initial decline between 1991/92 and 1993/94, the share increased until the end of the 1990s. The share at the official market rate was 24% in 1993/94 and increased steadily to 57% in 1999/00. However, the producers' share decreased to 45% in 2000/01.

The limited gains in producer prices have not reversed the collapse in marketed cashew production that Mozambique has suffered since independence and the civil war, despite the supply elasticities assumed by the World Bank²³. By 1989/90, Mozambique marketed 22,106 tons of raw cashews (INCAJU, 2001) and its share of world raw cashew nut production had dropped to 5% (Desai, 2001). Throughout the early 1990s, marketed production ranged from 23,935 tons in 1992/93 to 66,510 tons in 1995/96, before decreasing to an average of 51,571 tons between 1996/97 and 2000/01, as illustrated in Exhibit E-5. In addition to the civil war, INCAJU cites insufficient economic incentives, inadequate technical assistance, and significant incidence of epidemics and diseases as the factors that have limited raw cashew production over the last decade. It is unclear whether the revenue from the export tax has been allocated toward increasing production, supporting the processing factories, or uses unrelated to the cashew industry.

²³ See Tables 9 and 12 for further information on the World Bank's assumptions and empirical evidence regarding changes in producer price, area harvested, and quantity of raw cashew nuts marketed.

Processing Industry

The cashew processing industry was transformed between 1995 and 2001²⁴. 12 of 18 factories ceased operations during this period and only six processing factories were operational in 2001 (Abt Associates, 1999, Mole and Weber, 1999, AIM, 2001, INCAJU, 2001b). However, 90% of the sector's 11,000 workers were unemployed (AIM, May 15, 2001).

By 2001, the processing industry was no longer characterized by many large, capital-intensive processing factories. All of the processing factories that were established during the colonial era had closed. Those 12 factories were large-scale operations that had installed capacities averaging 6,570 tons and produced kernels almost exclusively for export to the United States and Western European markets (Abt Associates, 1999, Mole and Weber, 1999, AIM, 2001, INCAJU, 2001b). The majority of such firms employed relatively capital-intensive processing technology known as either impact decortication or Oltremare.

The profiles of the six processing factories that remained in operation were very different from the large-scale processors that had failed during the end of the 1990s. These factories were all new; each had been established since 1995. They were privately owned by individuals and were relatively small operations that had installed capacities ranging from 200 to 3,500 tons. Rather than producing for the traditional international market, these factories succeeded in supplying primarily the domestic and regional markets. They all employed semi-mechanical processing technology, which is more labor and less capital-intensive than the techniques employed by the older, larger processing operations. As a result, they were less dependent on a large, constant supply of raw cashew nuts in order to operate efficiently.

Many owners of the large-scale processing factories cited the export tax reduction as the reason for the industry's failure. As a result of the export tax reduction, raw nut prices had increased to the level where it was no longer profitable to process them (Abt, Associates, 1999). Factory owners, World Bank officials, and other sources, however, also cited additional reasons for the older, larger-scale factories' failures, including poor business decisions, extensive labor costs, and the limited supply and poor quality of raw nuts in Mozambique.

Recent Developments and Longer-Term Impact of the World Bank-Advised Liberalization

Regardless of the precise causes of the industry's decline and partial restructuring, the effects of the World Bank's involvement in determining Mozambique's cashew policy have had a broader impact on both the cashew industry and the Bretton Woods institutions' on-going relationships with Mozambique and other developing countries. According to Jehan Arulpragasam, the World Bank has not been as active in cashew policy in recent years because it is attempting to avoid the issue and control its reputation in the public arena. According to Raimundo Matule, this has cost Mozambique in the

²⁴ See Exhibit E-6

form of needed support for the country's current cashew projects that focus on increasing production.

The World Bank's involvement in the cashew case (and opposition it received) has also affected Mozambican sugar policy. In this case, the government refused to reduce sugar tariffs despite IMF recommendations. However, rather than requiring compliance as the World Bank had in the case of the cashew liberalization, the IMF accepted the government's decision to maintain the sugar tax until 2005. Horst Kohler, Managing Director of the IMF, stated that, "Sugar tariffs may be important...and they mean that poor people pay to protect domestic industry – but sugar tariffs do not have a decisive impact on macroeconomic stability...I would like to see the (International Monetary) Fund and the Fund staff developing options, where governments based on what they feel is right, take a choice" (Fidler, 2000).

However, according to Bruce Bolnik, Harvard advisor to the Mozambican Ministry of Finance, poor sugar consumers have been forced to bear the cost of the World Bank's failure in the cashew industry. The government agreed to guarantee continued protection of the sugar industry, despite the fact that such a high level of protection was not required by the industry. However, the World Bank and IMF accepted the government's decision in order to avoid further reputational damage.

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