



Challenges and Opportunities for Growth in the Sunflower Oilseed Sector in Tanzania

- Options for Fiscal and non-fiscal Reforms

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Summary

Context of the Study

- Tanzania's annual demand for edible oils is estimated at almost 600,000 tonnes. Domestic production covers about a third of the demand and the deficit is covered by imports.
- Prices of edible oils in Tanzania have increased dramatically following the COVID-19 pandemic and the effects of the Russia-Ukraine conflict.
- The government is keen to increase domestic production of edible oils, with an initial focus on sunflower which is suited to Tanzania's climate and can support economic growth through increased farm incomes, employment creation, and a reduced import bill.
- This brief discusses various options for fiscal incentives and their effects on government revenue, employment, and prices. Non-fiscal reforms are also proposed to complement the fiscal incentives.

Key findings

- The partial reduction of import duty on imported palm and sunflower oils from 25% for crude oil and 35% for refined oil to 10% and 25% respectively, will result in a welfare improvement for consumers that outweighs the associated losses in government revenue.
- However, the reduction of import duty alone without corresponding non-fiscal support to local producers will negatively affect the competitiveness of the local sunflower seed and oil sector.
- For a productive sunflower seed and oil sector, a partial reduction of import duty must be accompanied by the removal of VAT on locally produced sunflower seed oil and support to farmers in the form of inputs (seeds and fertilizers), extension services, and market linkages.

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Introduction

The Global Outlook

Sunflower is the most produced oilseed in the world, the fourth most consumed vegetable oil, and the third oilseed used as protein feed (Pilorgé, 2020). According to data obtained from FAOSTAT, the Russian Federation was the leading producer of sunflower seeds in 2020, followed by Ukraine, Argentina, and China. Tanzania was the 13th leading producer in the World and the leading producer in Africa, ahead of South Africa and Uganda (Figure 1).

The Tanzania context

The average annual demand for edible oils in Tanzania is almost 600,000 tonnes. Approximately 60 percent of the 600,000 tonnes is palm oil, of which over 90 percent (of the palm oil) is imported. The

remaining 40 percent is mainly sunflower oil, which is processed from locally produced sunflower seeds. However, local production of sunflower seed oil has remained low due to the unavailability of sufficient raw materials in the country. Local sunflower seed production is less than industrial demand – by over 1.3 million tonnes - leading to idle capacity in processing industries². The quantity of locally produced sunflower seed has dropped from a peak of 2.9 million tonnes in 2015 to a low of 352,000 tonnes in 2017, before rebounding slightly to 561,000 tonnes in 2019. The drop is consistent with a drop in the area under production from 1.8 million hectares in 2015 to 557,000 hectares in 2019 (Figure 2). According to unofficial statistics from FAOSTAT, production has rebound to over 1 million tonnes by 2020 (figure 1).

² <https://www.theeastafrican.co.ke/tea/business/tanzania-eyes-edible-oils-market-3649132#:~:text=The%20major%20crops%20for%20edible,for%20edible%20oil%20in%20Tanzania>

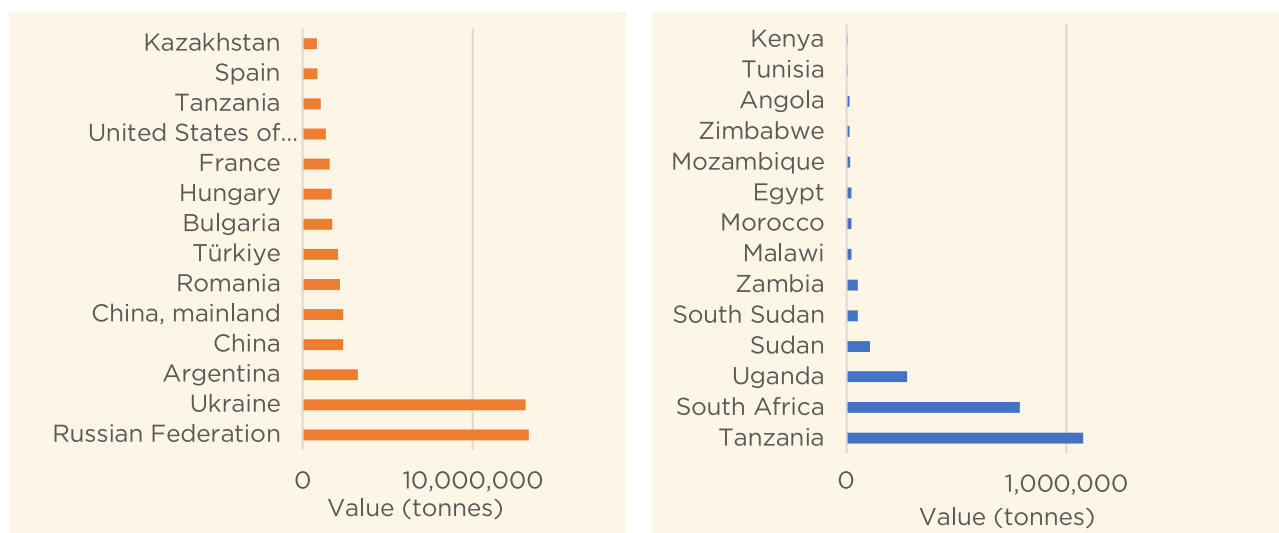


Figure 1: Leading Producers of Sunflower seeds in the World and Africa in 2020

(Source: Authors compilation from Tanzania Revenue Authority data)

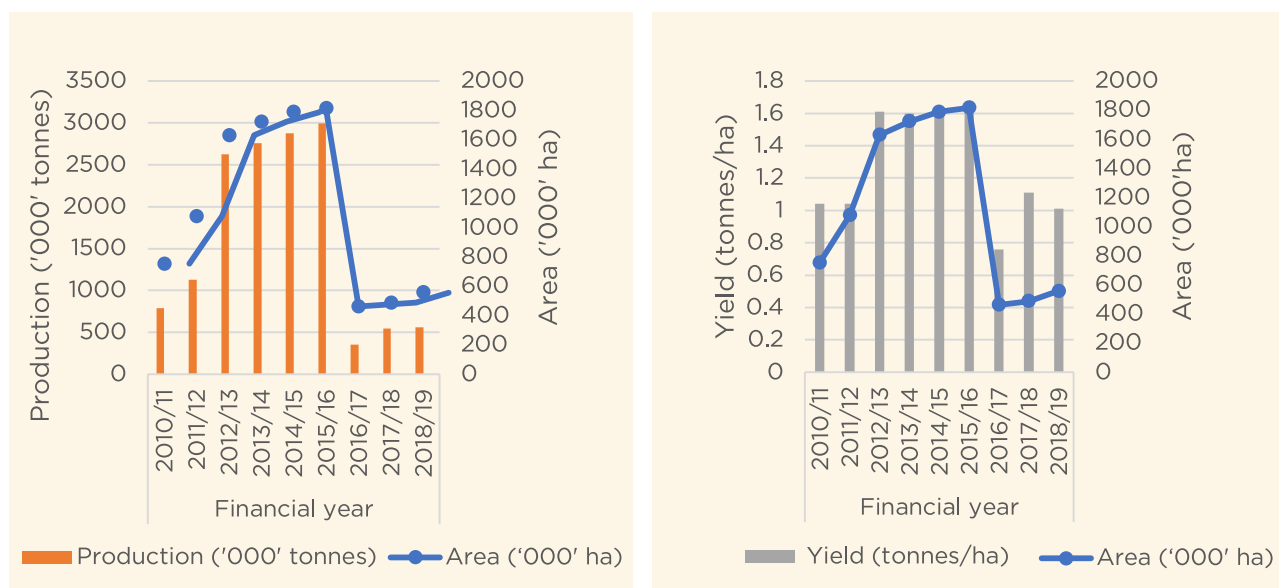


Figure 2: Production, yield, and area under sunflower seed production in Tanzania

(Source: Authors compilation from Tanzania Revenue Authority data).

The sunflower value chain is capable of significantly contributing to the economic development of Tanzania by increasing the income of smallholder farmers, creating employment opportunities for the youth, and reducing the edible oil import bill. Tanzania possesses a huge potential to close the demand gap from local production due to the diverse agroecological zones suitable for the production of sunflower oilseed and the availability of expansive arable land. Currently, the country has the largest area under sunflower production in Africa but with less yield. In 2020/2021, Tanzania had a yield of around 1 tonne/ha, while the world average was 2 tonnes/ha (Aspires & Dalberg, 2018; BFAP, 2018). Studies have identified stiff competition from cheap imported crude and refined palm oil, unavailability and high prices of improved seeds, poor agronomic practices, limited financial support, and land competition with maize, as the main factors causing the poor performance of the sector (Aspires & Dalberg, 2018; BFAP, 2018).

This brief focuses on the fiscal incentives and non-fiscal reforms to fast-track the transformation of the sunflower oilseed industry. Various options for fiscal incentives are analysed and their effects on government revenue, employment, and prices are estimated. Non-fiscal reforms are also proposed to complement the fiscal incentives.

The Case for Fiscal reforms

In the fiscal year, 2018/19 the Government of Tanzania increased the import duty on crude and refined edible oils from 10 to 25% and from 25 to 35%, respectively. It was anticipated that these reforms would make imported oils relatively costly and hence discourage imports, thus stimulating increased domestic production and growth of the edible oils industry, predominantly the sunflower oil.

Consistent with expectations, there was a slight (17%) decline in imported edible oils between 2018 and 2019 (Figure 3). This decline has been maintained since, with a marginal growth rate but at low absolute values.

Further, while an increase in the import duty lowered the average imported quantity of crude palm oil by 98%, it resulted in an increase in the importation of refined palm oil by 459% within the same period (table 1). Similarly, while the imported crude sunflower oil declined by 93%, that of refined sunflower increased by 347%. Therefore, the tax reform resulted in within-product substitution accompanied by the switch from importing crude oil to refined oil.

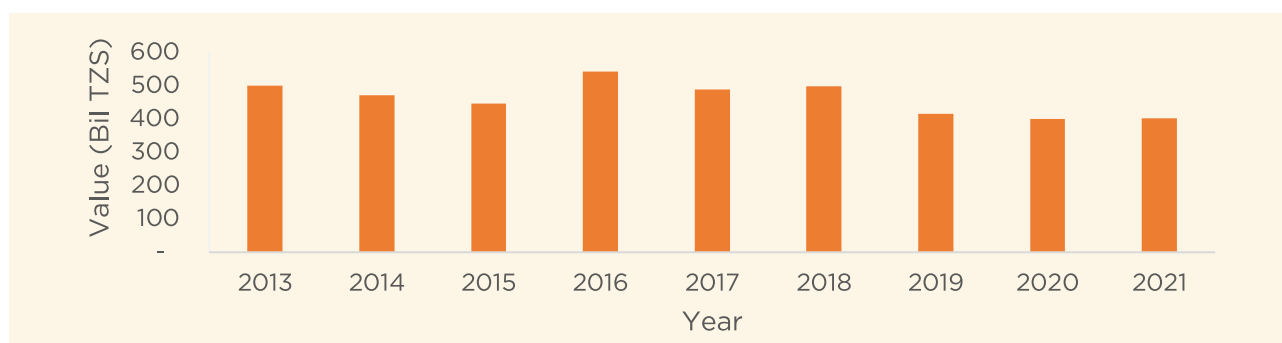


Figure 3: Total imported quantity (in '000' tonnes) of all edible oils in Tanzania
(Source: Authors compilation from Tanzania Revenue Authority data)

Table 1. Total imported edible oils before & after-tax reforms, oil status (crude vs refined oils)
(Source: Authors compilation from Tanzania Revenue Authority data).

| Item | Period | Import duty Rate (%) | Average import quantity (MT) | Growth rate (%) |
|------------------------------|-----------------|----------------------|------------------------------|-----------------|
| Crude palm oil | 2012/13-2015/16 | 0 | 196,700,000 | |
| | 2018/19-2020/21 | 25 | 3,620,000 | -98 |
| Refined palm Oil | 2012/13-2015/16 | 25 | 9,220,000 | |
| | 2016/17-2017/18 | 25 | 39,700,000 | |
| | 2018/19-2020/21 | 35 | 221,800,000 | 459 |
| Crude sunflower oil | 2012/13-2017/18 | 10 | 4,313,000 | |
| | 2018/19-2020/21 | 25 | 311,000 | -93 |
| Refined sunflower oil | 2012/13-2017/18 | 25 | 2,564,000 | |
| | 2018/19-2020/21 | 35 | 11,451,000 | 347 |

The reforms did not contribute to a significant increase in domestic production of edible oils nor any significant drop in the volume of imported oils in Tanzania. The consequence of the reforms was an increased final price of the edible oils in the country, the burden that largely falls to the final consumers, the majority of whom are poor. Following the COVID-19 pandemic and the invasion of Ukraine by Russia CIF prices of edible oils (and many other products) have soared, increasing the burden on poor consumers.

This Policy Brief discusses alternative fiscal and non-fiscal options to enhance the affordability of imported edible oils while increasing sunflower seed and oil production in Tanzania for domestic and international markets. The fiscal options analysed are a reduction of import duties on edible oils back to their original values, that is, 10% for crude and 25% for refined, while also removing Value-Added Tax (VAT) on domestically produced edible oils including sunflower.

Fiscal reform options and their effects

The three fiscal reform options were assessed using the cost-benefit analysis framework to determine their net impact on various facets of the Tanzanian economy. The findings are presented below.

Option 1: Partial reduction of import duty on the imported edible oils

This option considers reversing import duty to the pre-2017 rate of 10% for crude oil and 25% for refined oil. Reduction of the import duty rate to 10% for crude

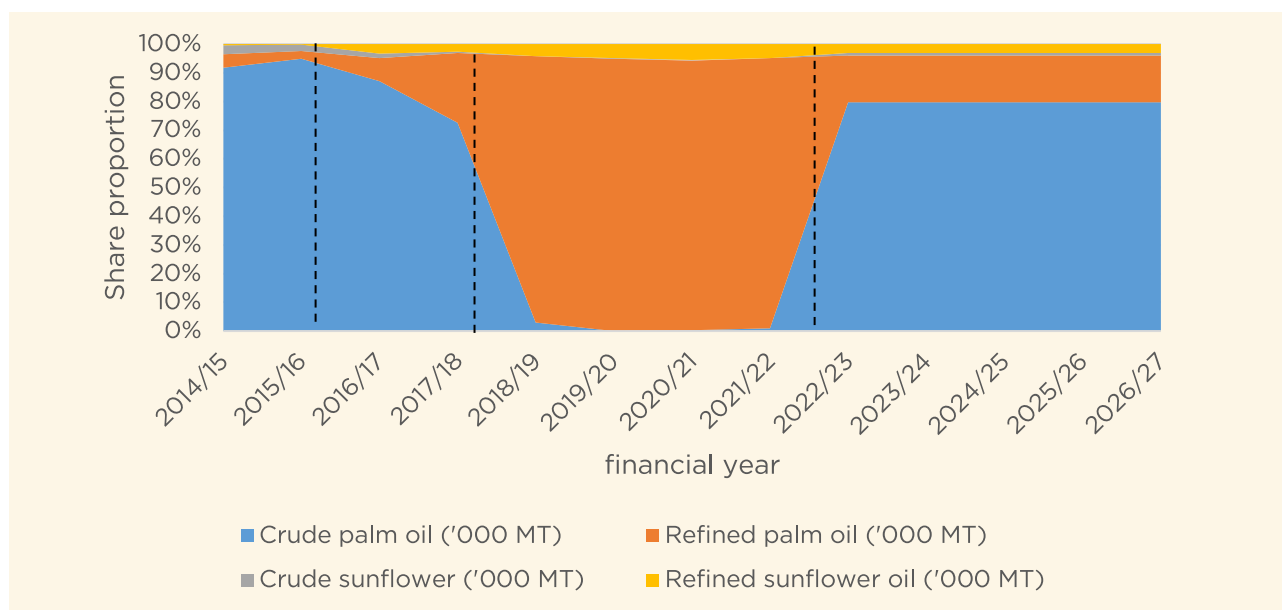
oil and 25% for refined oil will result in increased importation of crude oil relative to refined, resulting in a loss of government revenue collection from the potential import duty and VAT because of the importation of more crude oil, which is lower in value relative to refined oil and has a lower import duty rate (Figure 4). Although it will reduce the domestic price of edible oil in Tanzania and create more jobs in refining, this action on its own will lower the price of imported edible oil relative to domestically produced edible oil, thus negatively affecting the competitiveness of locally produced edible oil.

Option 2: Removal of VAT on locally refined sunflower oil

Zero-rating VAT on crude and refined sunflower oil from domestically produced sunflower oil seeds will lower the price of sunflower oil. According to BFAP (2018), locally produced sunflower oil is competitive relative to imported sunflower oil at a VAT reduction of equal to or more than 12%. The resulting import substitution will cause an annual growth of approximately 26% in the production of both crude and refined sunflower. The lost government revenue (import duty and corporate tax from importers) will be replaced by corporate tax, PAYE, cess, and skills development levy from increased sunflower oil production by industries. Additional benefits of VAT removal include employment creation in all levels of the sunflower value chain - farm production, transportation, processing, distribution, and marketing.

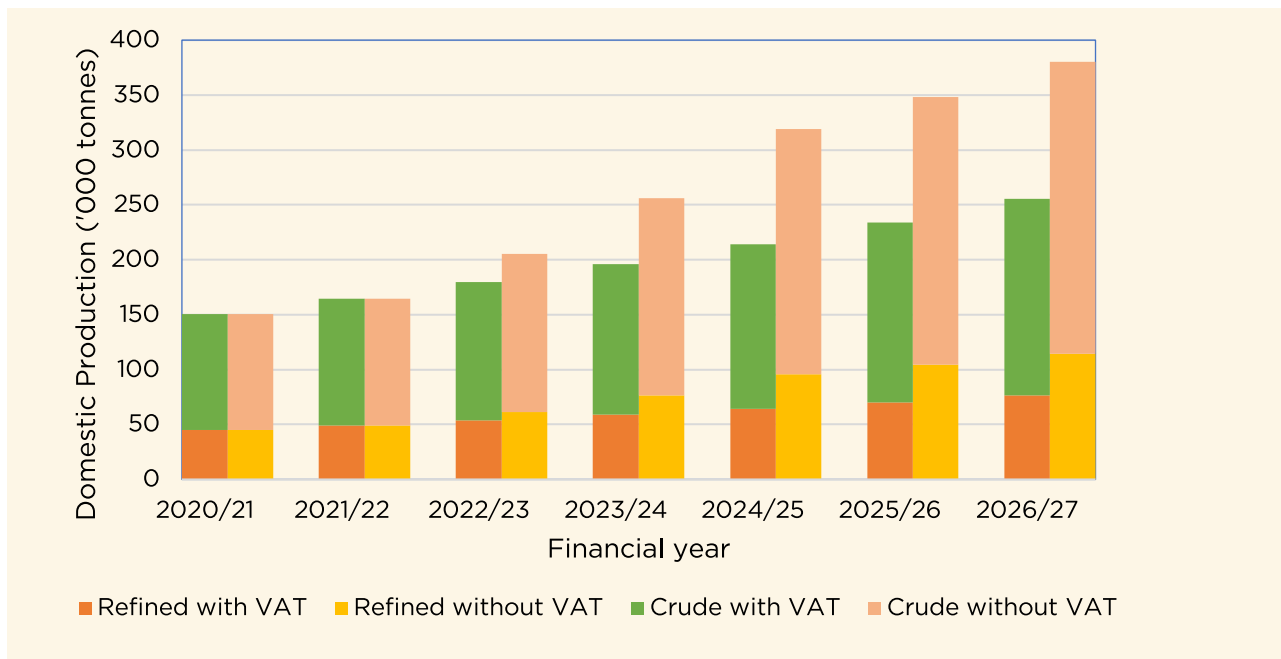
Figure 4: Projections of shares of crude and refined palm and sunflower oils imported after import duty changes rate to 10% for crude oil and 25% for refined oil

(Source: Authors compilation from Tanzania Revenue Authority data)³



³ Dotted lines indicate years when the different fiscal changes were instituted

Figure 5: Domestic production of crude and refined oils under the current scenario and with zero-rated VAT
(Source: Authors compilation from Tanzania Revenue Authority data)



Option 3: Reduction of import duty on edible oil and removal of VAT on locally refined sunflower oil

The combined action of reducing the import duty (to 10% for crude edible oil and 25% for refined edible oil) and removing VAT on locally produced sunflower will lower the prices of edible oil while increasing the domestic production of sunflower seed and oil. The resulting consumer surplus will outweigh the government losses in the first year of the intervention (TZS 175.5 billion) if the pass-through rate is at least 72%,

and if 10% of crude sunflower oil (12,600 tonnes) and 50% of refined sunflower oil (27,000 tonnes) is traded under the VAT system. If VAT is zero-rated and the pass-through rate is 72%, then the price will be reduced by 13%, leading to a consumer surplus of about TZS 31.7 billion. What this implies is that if suppliers of edible oil were to lower the domestic prices by at least 72% of import duty and VAT reduction, the consumer surplus will outweigh the government revenue collection loss and the net welfare will be positive.

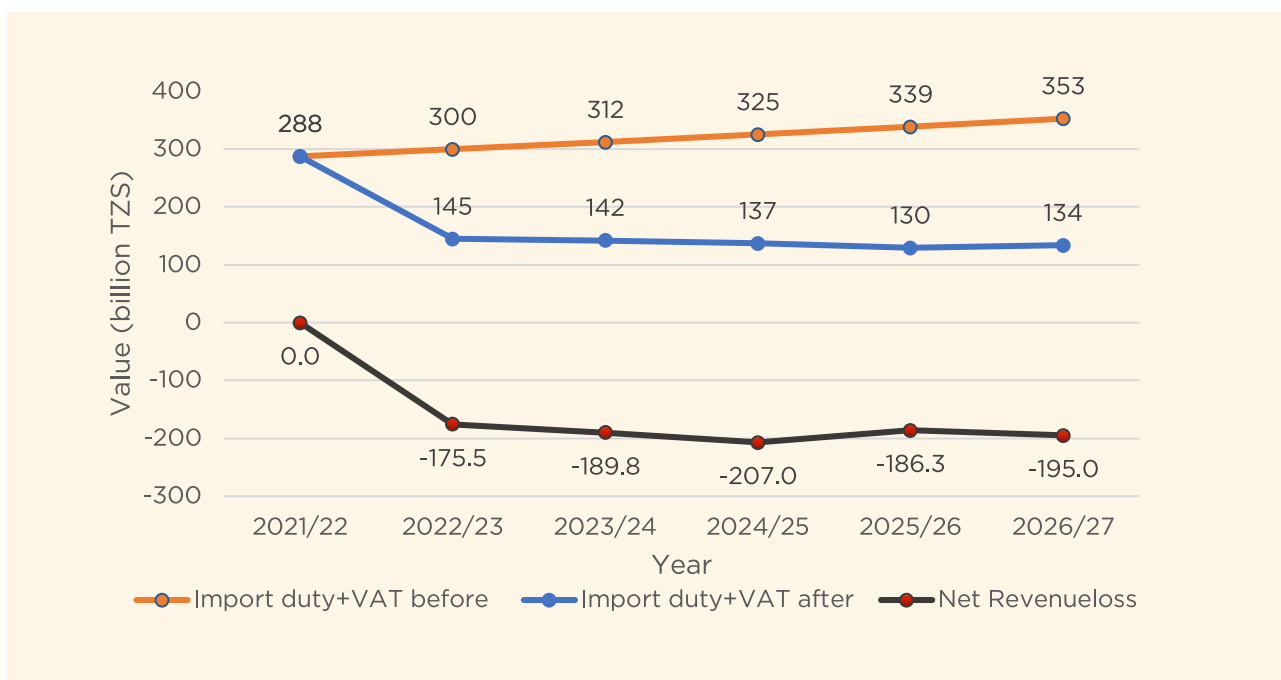


Figure 6: Revenue effect after removal of VAT and partial reduction of import duty
(Source: Authors compilation from Tanzania Revenue Authority data)

Discussions

The reduction in VAT to boost local production is only feasible if primary producers respond to the incentive. Current production constraints make it unlikely for producers to respond immediately. Farmers fail to respond to fiscal incentives to increase production due to low prices and a small profit margin compared to other players due to their price-taking position in the value chain, among other reasons. Currently, farmers sell sunflower oil seeds between TZS 700-1,300 per kilogram, earning a paltry profit margin of TZS 48,000 per tonne of sunflower seed produced. A large proportion of farmers sell at the lowest price point during harvest season due to the immediate need for cash and the lack of a warehousing system. With a yield of about one tonne per hectare, farmers, therefore, earn TZS 48,300 per hectare of sunflower. This largely discourages farmers from expanding production or investing in improving productivity. But it also implies that yield increases are fundamental in unlocking per hectare gross margin increases for farmers.

Recommendations

Regarding fiscal reform findings, we conclude that the fiscal interventions should be implemented in a phased approach, starting with the reduction of import duty which has a potential direct effect on consumer welfare followed by zero-rating VAT after mitigating production constraints. Non-fiscal measures introduced along with the fiscal incentives will unlock the production potential of farmers and increase the supply of raw materials to industries.

To unlock production constraints, the following non-fiscal Reforms are proposed to complement the fiscal reforms:

- a) **Enhance adoption of modern agronomic practices through:**
 - i. Strengthening extension services to train farmers.
 - ii. Promoting irrigation.

- iii. Support the seed sector to increase access to high-yielding and high oil content seeds.

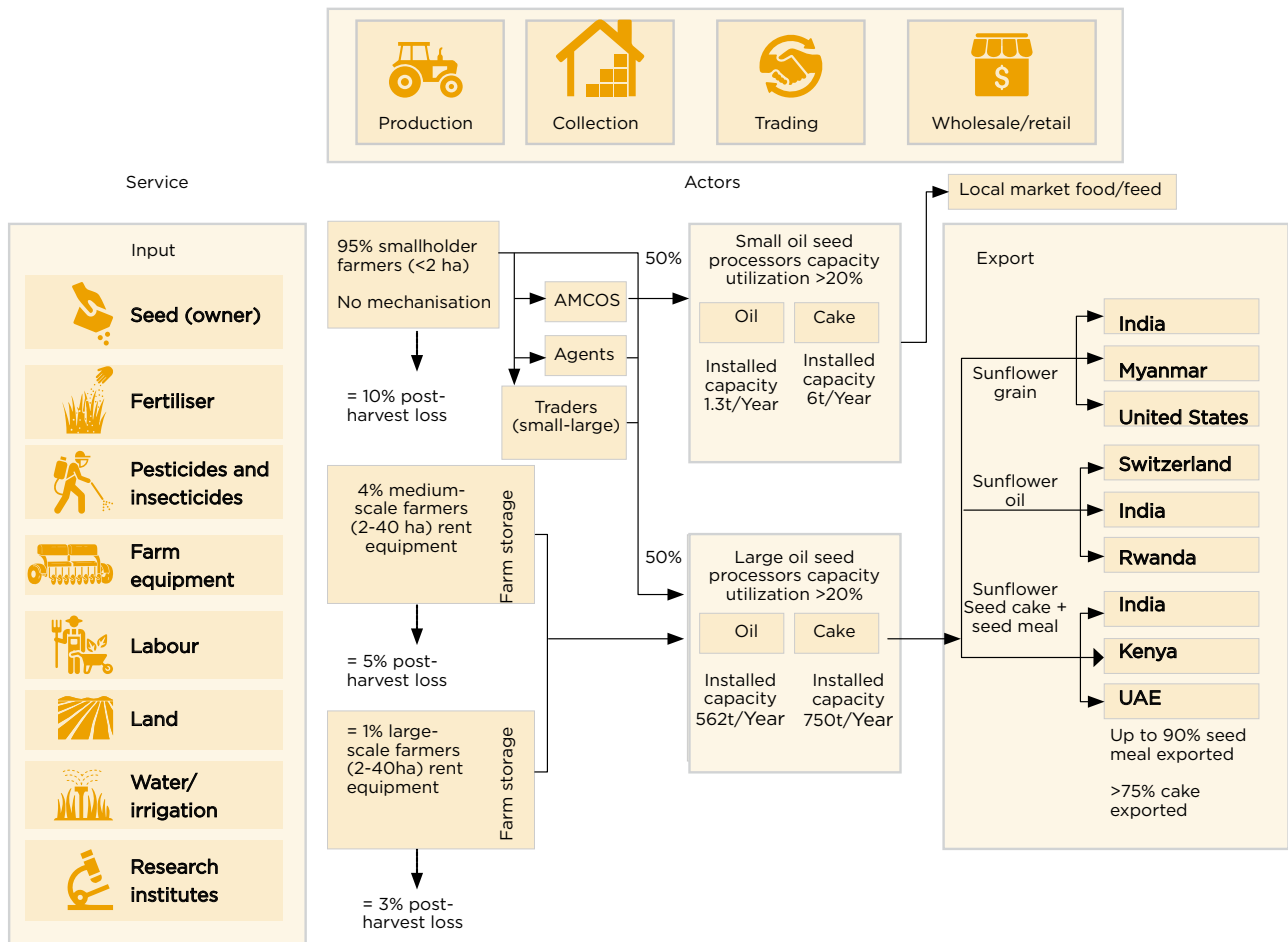
- iv. Integrating sunflower farms with beekeeping which facilitates pollination and increases yield.

- b) **Promote contract farming:** despite the obvious advantages of contract farming such as guaranteeing prices to farmers, contract farming in Tanzania faces enormous challenges of enforceability because of default (side-selling) and lower than market prices offered by processors. There is a need to create awareness among farmers on the importance of contract farming while exploring legal mechanisms for enforcing contracts.
- c) **Encourage large-scale commercial farming and reduce bureaucracies that derail access to land:** large-scale farming reduces the cost of production and increases yields because of economies of scale. Although Tanzania possesses huge arable land that is idle, a large proportion of the land is held by communities and regional and local government authorities. These authorities should facilitate access to such land by reforming the current bureaucratic processes. Block farming can also be adopted by engaging the youth in large blocks of land equipped with necessary facilities for irrigation, production, and marketing.

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Mapping of the sunflower value chain



Source: Adapted from Sunflower Sector Development Strategy.

About HAPA

Across African countries today, there is a need for better, more timely use of evidence, and more targeted approaches, to improve the quality of policymaking by governments. The Hub for Agriculture Policy Action (HAPA), is a Unit within AGRA that provides policy advisory services to governments seeking to reform, refine, and/ or develop a more clearly defined policy direction. The approach recognizes the urgent need for timely policy support to the agriculture sector, which plays an important role in ensuring inclusive growth. It also recognizes the demands for political expediency and the need to ensure that a particular policy direction is anchored in evidence.

The purpose of the Hub for Agriculture Policy Action (HAPA) is to support AGRA to catalyze and sustain an inclusive agricultural transformation in Africa to increase incomes and improve food security of millions of Africans. The creation of HAPA was in response to a noticeable gap in the utilization of evidence within the policy-making cycle to drive policy change. Through Consolidation and Translation (C&T) of evidence, HAPA's work entails collating existing evidence, expertise and best practice that are relevant to a government request for policy support and processing these into a set of rationalized and costed policy options. Through HAPA, AGRA aims to increase the use of evidence to inform decisions for policymaking and implementation. HAPA works with local partners such as research actors to collate existing data and evidence, expertise, and best practices that respond to a government request for policy support and package these into a set of actionable policy recommendations.

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