



Evolution of China's Fertilizer Distribution System

SINOFERT
November, 2011




0



Overview


- China's fertilizer distribution system has developed for about 60 years
- As an important agricultural material for national economy and the people's livelihood, fertilizer is managed by the government all the time, with the purpose of safeguarding the agricultural production and ensuring the farmers' income
- Moving from the fully planned management phase to the market allocation phase, China's fertilizer distribution system is in the process of developing and perfecting gradually
- In the foreseeable future, government policy will still play an important role in the evolution of China's fertilizer distribution system, and the market competition will continuously be strengthened



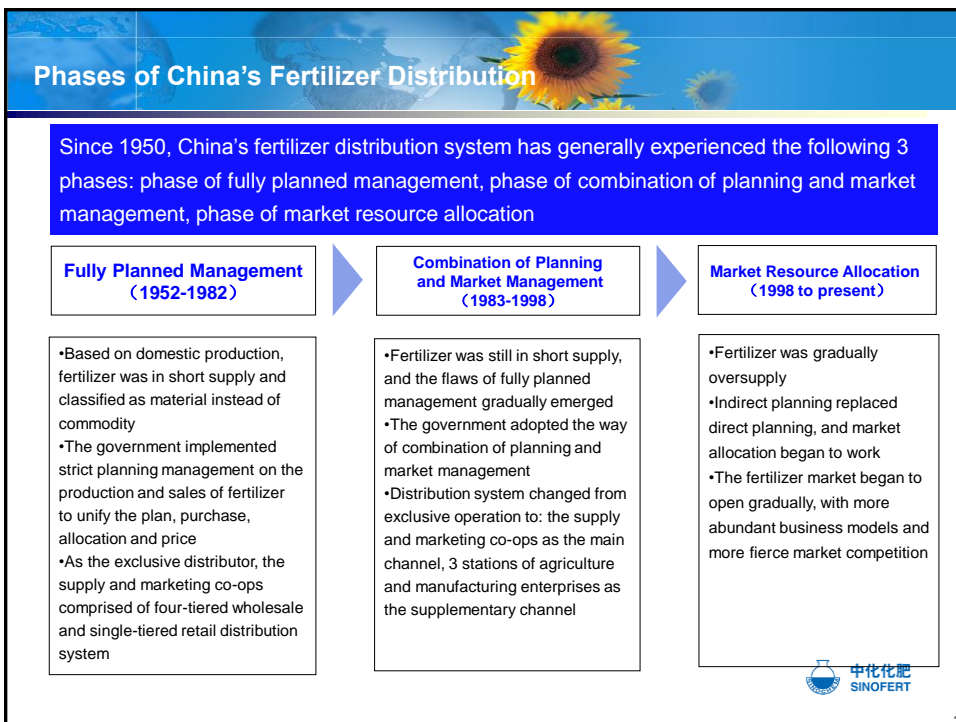
1

Table of contents

- 1. Introduction on the development of China's fertilizer distribution**
- 2. Trend on the development of China's fertilizer distribution**
- 3. Introduction on Sinofert's fertilizer distribution system**



2



Phase One: Fully Planned Management (1952-1982)

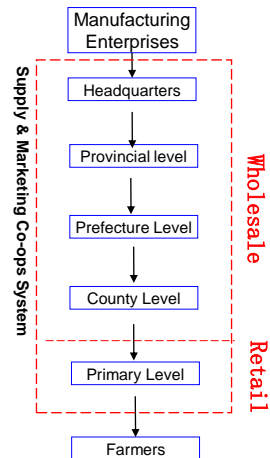
Main Features

- In the period of planned economy, fertilizer was in short supply and classified as farming material
- The country implemented strict planning and management on production and sales of agricultural production material to unify the plan, purchase, allocation and price.
- Fertilizer was operated exclusively by agricultural companies at all levels of the supply and marketing co-ops, with state monopoly for purchase and marketing, and few imports
- Built distribution system with four-tiered wholesale and single-tiered retail network

Problems

- Fertilizer was considered as farming material instead of commodity, and "low price and small profit margin" policies were executed in terms of fertilizer price, thus leading to long-term losses for manufacturing enterprises and great burdens for state finance

Fertilizer Circulation Links



4

Phase Two: Combination of Planning and Market (1983-1998)

As the flaws of fully planned management getting serious constantly, the government began to adopt the management with combination of planning and market. During the transition process from 1983 to 1998, the conflicts between planned management and market allocation unavoidably emerged. There were 3 main periods in the transition process:

Period 1: Dual-track Management(1983-1988)

Period 2: Exclusive-operation Management(1988-1992)

Period 3: Deregulation of Operation(1992-1998)



5

Phase Two: Combination of Planning and Market (1983-1998)

Period 1: Dual-track Management(1983-1988)

- From 1983 to 1984, the government raised the ex-factory and sales price of major types of domestic and imported fertilizer for 3 times in order to reduce losses
- At the beginning of 1985, with implementation of "dual-track system" for prices of energy and raw materials, the state also began to execute "dual-track system" for fertilizer price. That is to say, price within the plan would be uniformly determined by the country; while that beyond the plan should conform to market adjustment
- Due to the rise of raw material price and short-supply of fertilizer, the market price beyond the plan increased rather fast while the price within the plan stayed stagnant, leading to constantly increasing of the price gap
- Fertilizer was faced with continuous short supply and various price forms coexisted, so fraudulent buying and selling phenomena in fertilizer field was serious, and fertilizer circulation was in chaos, which promoted the rising of actual sales price.



6

Phase Two: Combination of Planning and Market (1983-1998)

Period 2: Exclusive-operation Management(1988-1992)

- Under the situation of fertilizer short supply in 1988 and 1989, the government, in order to deal with the chaos of the market and price, decided to implement exclusive-operation management on fertilizer and other agricultural production material by China Agricultural Production Material Company and the Supply & Marketing Co-ops at all levels
- With regard to the sales price, the pricing department of provincial government set the comprehensive average sales price which was the weighted average of ex-factory prices within and without the plan, plus the commercial circulation fees
- Exclusive-operation management and comprehensive sales price curbed, to some extent, the phenomenon of mixed fertilizer market, circulation disorder, and soaring prices



7

Phase Two: Combination of Planning and Market (1983-1998)

Period 3: Deregulation of Operation(1992-1998)

- In 1992, the government, in order to further improve the management of fertilizer circulation, issued a series of initiatives on price management, business entities, and fertilizer circulation links
- Price management: The right of price management was transferred to lower levels or adjusted by the market; the price was set according to different raw material used; price management shifted from pricing to price limiting, allowing the price to float in a certain range
- Business entities: China Agricultural Production Material Company and the Supply & Marketing Co-ops at all levels were the main distribution channel, while 3 stations of agriculture and manufacturing enterprises were the supplementary channel
- In order to solve the problems in fertilizer circulation links, the government decided to shorten fertilizer circulation links and reform the circulation system: it was changed from four-tiered wholesale & single-tiered retail to two-tiered wholesale & single-tiered retail when fertilizer was distributed at the state level; while from three-tiered wholesale & single-tiered retail to single-tiered wholesale & single-tiered retail at the provincial level

Notes: As the primary agricultural service sector set by the government, 3 stations of agriculture represents Agricultural Plant Protection Station, Soil Testing Station, and Agricultural Technology Station.



8

Phase Three: Market Allocation (1998 to present)

Although the government constantly adjusted the management mechanism of fertilizer circulation, the contradiction between fertilizer production and circulation links intensified day by day, and further reform on circulation system was unavoidable. Under such circumstance, the government issued *Notice on Deepening Reform of Fertilizer Circulation System* (called Document No. 39 for short), which opened a new chapter for fertilizer circulation

Description of Problems on Circulation Links

- Existing management system couldn't adapt to the changes of market supply and demand; manufacturing and operation enterprises suffered from serious losses
- Operation links were too many while cost too high
- The price formation mechanism was not flexible and couldn't play the market regulation role easily
- The import agency mechanism was not complete,
- Market order lacked of standardization

It was necessary to further deepen the reform of fertilizer circulation system, and set up the fertilizer circulation system which adapted the requirements of socialist market economy and stuck to the principle of market resource allocation under national macro-control, in order to promote the healthy development of fertilizer production and circulation



9

Phase Three: Market Allocation (1998 to present)

Major Reform Measures in Document No. 39

- 1. Self-purchase and self-sale.** Cancel the mandatory production and unified distribution. Manufacturing and operational enterprises are free to purchase and sell fertilizer
- 2. Broaden the channel of fertilizer circulation.** Fertilizer manufacturing enterprises, agricultural material companies at all levels, and 3 stations of agriculture are clients with each other. China National Chemicals Import and Export Corporation (predecessor of Sinochem) is entitled to domestic trade operation right of fertilizer
- 3. Improve the price management of fertilizer.** Set up market price formation mechanism under the guidance of the government: ex-factory price of fertilizer is the guidance price of the government; limitations are removed on the retail price of fertilizer; and Price Department Sector of provincial level could set a price ceiling on some types of products when necessary
- 4. Improve fertilizer import agency system.** Imported fertilizer of all types by trades and channels are subject to import quota administration; appropriately increase import agency channel of fertilizer by giving China Agricultural Production Material Group, in addition to Sinochem, the operation right of fertilizer import agency
- 5. Establish reserve system of disaster relief fertilizer .** (Has set up off-season commercial reserve system of fertilizer since 2004)



10

Phase Three: Market Allocation (1998 to present)

The implement of Document No. 39 had great significance in the building of China's fertilizer market-oriented circulation system. With the change of supply and demand situation and the development of market economy, the government issued *Decision on Further Deepening Reform of Fertilizer Circulation System by the State Council* (called Document No. 31 for short), which further strengthened the market-oriented circulation system of fertilizer

Key Points of Document No. 31


- **Eliminate the restrictions on the ownership of fertilizer operational enterprises.** Qualified market entities are allowed to enter into the fertilizer circulation system to participate in the operation and compete fairly, such as enterprises of all kinds of ownership, farmer specialized cooperatives and individual industrial and commercial households
- **Encourage chain and intensive operation.** The country encourages large fertilizer manufacturing and circulation enterprises as well as social capital with some power and scale to integrate the resource, and develop chain and intensive operation through merge and acquisition

So far, China's fertilizer circulation system has stepped into the new phase with various entities and models, market pricing and autonomous operation. And the major problem we are faced with at present is how to build a high-efficient, low-cost, and well-developing circulation system



11

Table of contents	
1. Introduction on the development of China's fertilizer distribution	
2. Trend on the development of China's fertilizer distribution	
3. Introduction on Sinofert's fertilizer distribution system	

 中化化肥
SINOFERT

12

Trend of China's Fertilizer Distribution Development	
Macro-environment and the Status Quo	
<ul style="list-style-type: none"> ➢ Supply and demand. Fertilizer oversupply will last for a certain period of time. In the 12th five year plan, the government is to make more efforts to optimize the fertilizer structure and upgrade the industry, and encourage the development of new fertilizer and soil testing and formulated fertilization ➢ Agricultural development. The government encourages the agriculture to develop on the basis of industrialization, large-scale, technology and mechanization ➢ Trend of industry. The government encourages large enterprises to develop on the basis of intensive management and large scale in circulation links ➢ Client demand. Circulation of land use right and large scale planting promote the emerging of new clients and demand ➢ Business entities. It has been the major form that manufacturing enterprises extend business to circulation links and circulation enterprises accelerate the pace to acquire upstream resource; unconventional entities fasten the step into the fertilizer circulation system 	

 中化化肥
SINOFERT

13

Full Market Economy Period (Since 2009)

Trend on the Development of China's Fertilizer Distribution

- **Macro-policies.** Under the overall regulation, the government will further play the regulatory role of the market, and promote the reintegration of resource allocation in fertilizer circulation based on market mechanism, in order to accomplish the adjustment and upgrade of industrial structure
- **Business Entities.** Under the mechanism of market, the nature of business entities will be more abundant; further accelerate the integration of primary business entities on the premise of healthy development of the industry
- **Operation Model.** Considering the changes of the agricultural production and client demand, the conventional operation model of product sale will be transformed into comprehensive marketing model of "product plus service". Apart from the products, the enterprises will attach more importance to the accomplishment of diversified values such as brand, and service

Fertilizer is an important commodity related to national stability. Although the government promotes the perfection of circulation system through market mechanism, policy will still be the important factor of circulation system



14

Table of contents

1. Introduction on the development of China's fertilizer distribution

2. Trend on the development of China's fertilizer distribution

3. Introduction on SinoFert's fertilizer distribution system



15

Introduction on Sinofert's Fertilizer Distribution System

Established in 1993, Sinofert is responsible for fertilizer business of Sinochem Group. From fertilizer import agency to setting up the largest fertilizer distribution network, Sinofert has participated in the process of evolution of China's fertilizer distribution system all the time. The distribution system of Sinofert could be mainly divided into two phases:

Phase One: 1993-1998

- On 5th April 1993, Sinochem Group set up Sinochem International Fertilizer Trading Corporation (predecessor of Sinofert), which was engaged in exclusive agency business of fertilizer import in China while couldn't involve in domestic fertilizer distribution
- In 1998, the State Council issued Document No. 39, which added the number of fertilizer import agency entities while helped Sinofert acquire the right of domestic trade operation



16

Introduction on Sinofert's Fertilizer Distribution System

Phase Two: 1998 to present

- The first port office was established in 1999
- The first branch office was set up in 2000. From then on, Sinofert started the massive construction of domestic distribution network
- By the end of 2010, Sinofert has set up 17 provincial branch offices and 2100 distribution centers, covering more than 90% of arable land in China and forming a 3-tiered distribution system of "province-city-county"
- In 2010, the sales volume of fertilizer for Sinofert was 15 million tons, with more than 40,000 distribution clients among which 75% were primary retail stores



17

Introduction on Sinofert's Fertilizer Distribution System

Trend on the Development of Sinofert's Distribution System

Combined with internal and external environment, the objective of Sinofert's distribution system is to focus on end customers, and become the leading enterprise in the agricultural material circulation field of China through building the channel with profession, technology, facility, and end-customers

- **Profession:** Professional personnel, service, products, and operational system
- **Technology:** Based on connotative technology, create value for the long-term development of agriculture and farmers, and acquire the position in the industrial chain
- **Facility:** Logistics facility, service facility, office facility, R&D facility, information facility
- **End-customers:** Apart from enhancing the conventional market, constantly penetrate into end customers in order to seek a steady, sustainable market position and earnings

