

## Fostering FDI in the Agriculture Sector

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### I. INTRODUCTION

Irrespective of the level of sophistication and technological advancement achieved by mankind, agriculture remains the backbone of human existence and survival. Despite the benefits arising from technological progress, the corresponding higher yields and more resistant crop varieties, the basic need and fundamental problem still facing the world is food security.

With approximately 65 percent of Pakistan's population living in rural areas, and agriculture contributing approximately 20 percent to its GDP, it is clear that at the core of any sustainable development and poverty reduction strategy is the development of agriculture.<sup>1</sup> Gallup (1997) shows that an additional one percent increase in per capita agricultural output would result a 1.6 percent increase in the incomes of the poorest 20 percent of the population. These findings are further supported by Thirtle, *et al.* (2001), who on the basis of cross-country analysis, found that a 1 percent increase in agriculture yields would reduce the number of people living on less than \$1 a day by 0.83 percent. In addition, the growth linkages/multiplier effects between agriculture and the rest of the economy are relatively strong with every \$1 of additional farm income creating a further \$0.8 non-farm income in Asia [Bell, *et al.* (1982); Hazell and Ramaswamy (1991)]. The multipliers are even stronger in the case of Africa where it ranges from \$0.96 in Niger to \$1.68 in Burkina Faso [Delgado, *et al.* (1998)].

The importance attributed to the agriculture sector was given further impetus in 2008, when food prices surged, and limited food supplies threatened food security in several countries, and triggered civil unrest in several others. This resulted in many countries (notably the GCC), exploring alternatives for investing in the agriculture sector. In the case of the GCC, investing in agriculture is a shift from previous self-sufficiency schemes, and is being undertaken to firstly ensure food security, and secondly to maintain price stability and reduce exposure to market volatilities in their home countries. This presents a unique opportunity for countries such as Pakistan which have under-utilised agriculture land to benefit from the potential FDI in agriculture.

However, despite significant interest in FDI in the agriculture, and the desire to promote FDI in the sector, progress with investment remains minimal, and the constraints

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*Author's Note:* This paper is a distillation of the findings of the IDB occasional paper on "Fostering Intra-OIC FDI in the Agriculture Sector" prepared by the author.

<sup>1</sup>IDB (2008a).

to the FDI continue to pose a serious challenge for countries wishing to attract FDI in the agriculture sector. It is submitted that without appropriate investment in creating an enabling environment in Pakistan that is at least as good (if not better) than those available in elsewhere in the world, investment flows will remain unsatisfactory.

## **II. SCOPE AND OBJECTIVES**

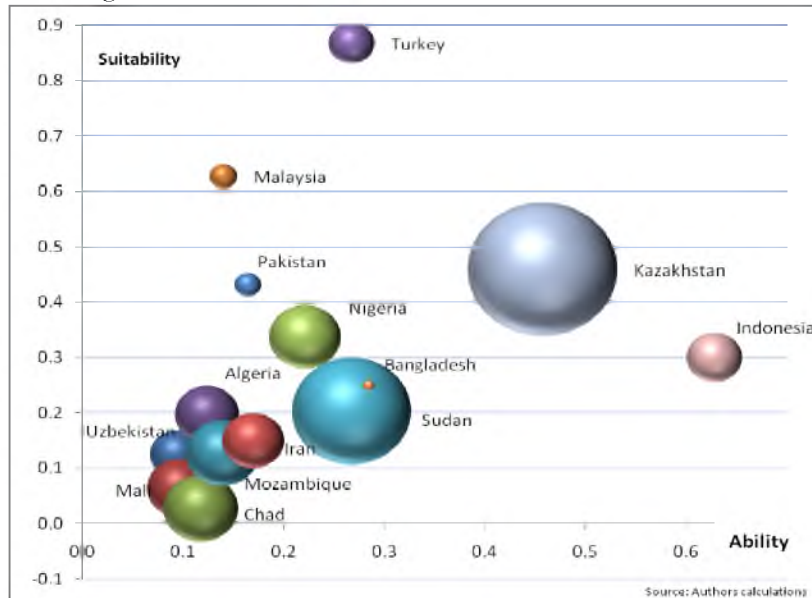
This paper seeks to: (i) highlight the agriculture potential in Pakistan; (ii) review the experiences of potential investors in the agriculture sector; and (iii) identify potential roles for countries seeking FDI and their development partners including the IDB in fostering FDI in the agriculture sector.

The growth in agriculture is dependent on investments at all levels from investments in agriculture inputs, infrastructure and across the value chain. Due to resource constraints and other development priorities, FDI in the agriculture sector is critical, and an important tool in the fight against poverty. In order to ascertain the investment potential two indices “Ability” and “Suitability” were developed. These are combined to create an overall Agriculture Potential Index. In order to explore what needs to be done to attract FDI in the agriculture sector, the initiatives to invest in the sector by the GCC is examined in detail. This leads to the identification of key challenges and agriculture bottlenecks that could hamper investment in this sector. The potential role of the IDB and other MDBs in helping foster FDI throughout the agriculture value-chain is also presented.

## **III. AGRICULTURE POTENTIAL IN SELECTED COUNTRIES**

Many OIC member countries including Pakistan have large tracts of under-developed arable land, sufficient water resources and high levels of unemployment in rural areas. These countries were identified in order to ascertain their potential for encouraging investment in the agriculture sector. In order to determine the potential to attract investment into the agriculture sector, two indices were computed. The first is based on the agricultural ability of the country (“Ability Index”). The “Ability Index” was computed using three variables, namely, water resource availability, land available for agriculture development and transport infrastructure (amount of paved roads was used as a proxy for transport infrastructure). The second index computed was the “Suitability Index”. This was derived by combining the net FDI inflows to the country (as an indicator of the attractiveness of the country for FDI/investment climate) with the “ease of doing business index” (as an indicator of the overall business environment). Thus, the suitability index may be viewed as a proxy for the overall enabling environment. By combining these two indices, it was possible to determine the overall potential of a country to attract FDI specifically into the agriculture sector. In Figure 1, the horizontal axis shows the resource “ability” of the country with regards to arable land, renewable water resources and availability of infrastructure. The vertical axis portrays the “suitability” of the country as a destination for FDI based on historic FDI flows and the conduciveness of the business and investment climate. The size of the “bubble” depicts the available land size for FDI in the agriculture sector (the larger the size of the bubble, the more land is available for agriculture development).

**Fig. 1. OIC Member Countries with High Potential to Attract FDI in the Agriculture Sector**



It may be noted that the countries are classified based on an overall availability of agriculture land, water resources and infrastructure. This does not in any manner suggest that there are no potentials for agriculture in countries not identified as having high potential. Clearly specific investment opportunities may well exist, and yield potentially high rates of return. Rather, the information presented must be viewed as highlighting countries that could generally be targeted for FDI in the agriculture sector. In terms of the overall agriculture potential index, the countries exhibiting the most potential are Pakistan, Turkey, Indonesia, Kazakhstan, Malaysia and Sudan. From a resource perspective (Ability), Indonesia and Kazakhstan are the countries with the highest ability to attract FDI. Purely in terms of land available for agriculture development, the largest amounts are available in Kazakhstan and Sudan. From an investor perspective, with a focus on specific projects, Turkey emerges as arguably the first choice given its very strong business climate and is reasonable ability for agriculture. In terms of suitable business and investment climate for FDI, the top ranking countries are Turkey and Malaysia. Although Turkey does not have as much un-utilised agriculture land as countries like Iran and Mozambique, due to the very conducive business and investment environment, it features prominently as a potential destination for FDI in the agriculture sector. It may be noted that the above research provides an overall country level perspective, and gives an indication of the potential of countries to attract FDI in the agriculture sector. There is still a need to identify specific projects and investment opportunities. In countries with limited land availability, there may exist excellent agriculture projects that could yield high returns on investments. If the other issues surrounding the investment are easily resolved, then such countries may be among the early recipients of FDI in the agriculture sector. However, from the perspective of broadly targeting specific countries, then the study provides a good indication of which

destinations make the most sense to be considered first. On the basis of the above analysis, it is clear that there exists significant potential for the development of the agriculture sector in several countries including Pakistan.

#### **IV. EXPERIENCES OF FDI IN THE AGRICULTURE SECTOR**

The rising oil prices from 2005 through July 2008, resulted in an increased focus on bio-fuels as an alternative and viable source of energy. This coupled with subsidies on bio-fuels resulted in the diversion of croplands away from production for food towards bio-fuels. The overall impact was a scarcity of key agriculture commodities, and higher food prices. This exposed an important vulnerability and created panic in some countries (specifically the GCC). In response to this phenomenon, there was an increased desire to acquire land and secure food resources by these countries. Many private sector investors and governments hastened to secure agriculture land that exhibited potential in anticipation that this land would be used to secure food supplies for their home countries. The increased activity surrounding FDI in the agriculture sector peaked towards the end of 2008, with new announcements published in the media on virtually a weekly basis from GCC investors stating their intentions to undertake FDI in the agriculture sector. In this context, countries identified as potential recipients of FDI included Pakistan, Sudan, Morocco, Algeria, Egypt, Syria, Kazakhstan, Indonesia, Turkey, Vietnam, Philippines and South Africa. In many instances, Sudan was highlighted as the initial destination of choice, with some announcements stating that investments were already being undertaken in Sudan.

Simultaneously, many countries that are well endowed with arable land and sufficient water resources sought to benefit from this revived interest in agriculture and welcomed the additional attention their economies were receiving from foreign investors.

Although one cannot generalise from these limited discussions on the key issues, it is possible to get some indications of the private and public sector perspectives on this important subject. Lessons learnt and best-practices from the case study may also provide an indication to other investors and recipient countries of some of the key issues affecting the investment decision.

#### **V. INVESTOR COUNTRY INITIATIVE: SAUDI ARABIA**

The King Abdullah Initiative for Saudi Investment in Agriculture Abroad (KAI) was announced with the aim of achieving national food security through building integrative partnerships with countries that have high agricultural potential to develop and manage agricultural investments in various strategic crops. The wisdom behind the Initiative is also to move away from providing aid to stimulating growth and employment opportunities in LDCs that are abundant in natural resources (trade not aid). The KAI aims at stimulating and encouraging the Saudi Arabian private sector to invest in agriculture abroad.

##### **The Role of KAI**

The KAI acts as an investment facilitator, and its role in a potential host country begins by undertaking bilateral discussions on behalf of the Kingdom. It will focus on paving the way in making it easy for investors to undertake FDI in third countries. Important elements of their focus and role would include:

- Facilitating the identification of potential investment opportunities;
- Securing land and undertaking negotiations with the host country to ensure appropriate quality and quantity of land is made available to the Saudi investor in a manner which is conducive to long-term development; and
- Undertaking discussions with host countries to ensure that an appropriate incentive basket is made available to Saudi investors. This to a large extent will focus on ensuring that other investors are not receiving preferential treatment as opposed to the Saudi investor.

The focus of the investment facilitated by the King Abdullah Initiative is strategic in nature focusing to a large extent on food security as opposed to purely economic merit. Although economic merit is an important element of the investment decision, the investment destination and investment supported would be of a strategic nature, this would allow the Initiative to assist Saudi investors undertake strategic investment while simultaneously meeting the objectives of facilitating development in these third countries. Thus, focusing on development via trade and investment as opposed to merely aid.

In addition, the investment mindset is based on a “win-win” principle where the interests of the Kingdom as well as the receiving country are protected. In this regard, it is anticipated that the agricultural produce from the investment should be exported to the Kingdom, with reasonable proportion of the produce going to the markets in which they are produced. Although preference is laid on production of strategic crops such as rice, wheat and barley, the investing firms will have the freedom of choosing the type of crops they grow.

The Initiative will only support agriculture investments in countries with abundant agricultural resources that are long-term in nature, based on either land ownership or long-term leases. It is envisaged that the Initiative will sign bilateral agreements between Saudi Arabia and the government of receiving country as a means of paving the road for Saudi investment in the agriculture sector. In addition, the KAI pays attention to the proximity of the country to Saudi Arabia. Among others the KAI has initiated discussions with Senegal, Turkey, Ukraine, Egypt, Sudan, Kazakhstan, Ethiopia, South Africa, and Brazil. The logic behind considering many countries is simply to spread risk and capitalise on the best opportunities.

A key feature of the KAI is that it will only entertain discussion on Saudi investment in agriculture abroad in instances where the host/recipient country is not a net importer. It will also not focus on countries that are not keen on attracting FDI in Agriculture (e.g. India and China). In addition, countries that impose restrictions on the trade of agriculture output will be disregarded.

Although the KAI is intended to be short-term, a longer term mechanism in the form of an agricultural holding company is under establishment. This holding company will be 100 percent government owned (via the Public Investment Fund) and is called Saudi Company for Agricultural Investment and Animal Production. It will be an important source of financing for the investors, and act as a catalyst and facilitator, fostering cooperation at government level in order to ensure that the private sector can undertake the necessary investments. However, its modus operandi, actual focus areas and nature of its assistance are being finalised.

It is anticipated that it will provide soft loans to investors in the agriculture sector along with undertaking equity participation where applicable and subsidising to some

extent the investment. In addition, the holding company may be responsible for off-take agreements to purchase the output of the FDI investment in agriculture.

## VI. FACTORS DETERMINING THE INVESTMENT DESTINATION

The key issues considered by the KAI to ascertain the suitability of a country as an investment destination include:

- **Security of Tenure/Land Ownership:** A minimum renewable lease period of 25 years is considered suitable, with the ideal situation being land ownership.
- **Availability of Suitable Land, Water, and Infrastructure:** Electricity; transport and logistics are among the key success factors for potential investments.
- **Government and Political Stability:** Is an important consideration by the investor.
- **Existing Relationship with Host Government:** Countries that have mutual relationships may be the first to be targeted for investments. The underlying purpose for the investments are to guarantee food supply from the source country and as such, existing relationships with potential host governments would facilitate access to resources and output even in times of crisis.
- **Appropriate Legal and Regulatory Framework:** It is contended that the legal and regulatory framework of the potential recipient country must be conducive for investors.
- **Friendly Investment Policies:** Consideration is also given to the willingness of government to attract FDI in the agriculture sector and an appropriate policy environment.
- **Proximity to Saudi Arabia:** The distance of the receiving country to the investor country is essential because cost and security issues before the food reaches the destination.

The KAI has recognised that in order to facilitate security of investment, local communities in the host countries should benefit from the investments in the form of having access to some of the output along with employment, technology and knowledge transfer. Although the KAI expressed preference for investments to flow to Muslim world, it is recognised that the investment is undertaken by the private sector who seek to maximise profitability and rate of return on their investments and long-term sustainability of the projects. Thus, the investment will go to the country that offers the best overall “package” for the investor, and the decision will not be made on an emotional basis, but rather based on economic merit.

In addition, the focus will be on large scale commercial farming predominantly on unutilised agricultural land. However, in order for the projects to be viable, appropriate infrastructure must be put in place. Downstream beneficiation would take place either in the recipient country or closer to market depending on economic merit and competitiveness.

### Envisaged Role for Development Partners

The KAI was clear that development partners such as MDBs have an important role to play in facilitating FDI in the agriculture sector. The soon to be established holding company will play a complementary role to that of MDBs who may assist by:

- Adopting a more proactive approach to agriculture through the provision of funding to host/recipient countries for de-bottlenecking infrastructure (e.g. electricity, transport and logistics) that could unlock the agriculture potential in their countries and facilitate the flow of FDI into the agriculture sector in these countries;
- Committing funds for technical assistance grants (TAs) in order to assist in the training of labour in recipient country, to benefit more directly from the investment from the perspective and employability and ability to assimilate new technology. The TAs could also be utilised to set-up appropriate research institutions;
- Engaging their member countries in dialogue on the guiding principles and requirements to attract FDI specifically in the agriculture sector. This could provide additional security to the investment;
- Sharing of risk via equity participation in the actual commercial enterprises, and providing insurance and guarantees. MDBs “putting their money where their mouth is” will not only reduce the commercial risk, but also the political risk given their relationship and leverage with their member countries; and
- Undertaking detailed studies on the agriculture potential of their member countries including their legal and regulatory environments, land ownership regulations, status of infrastructure and willingness to attract FDI into these countries.

## VII. INVESTOR INITIATIVES

### **Abraaj Capital**

Abraaj Capital is a Dubai based private equity investment firm with a focus on the MENA and South Asian (MENASA) regions. The firm is widely recognised as an important player in private equity in the region and has undertaken several key investments across the MENASA region. It has also received several awards including ‘Middle Eastern Private Equity of the Year’ in 2005, 2006 and 2007; the Banker Middle East Award for ‘Best Private Equity Institution’ in 2006 and ‘Best Private Equity House’ at the World Private Equity Awards in 2007.

### **The Role of Abraaj**

Abraaj as a private equity investor follows an investment strategy that is based on the acquisition of controlling or significant interests with board representation in stable, mature, well-managed businesses. It aims to create value through operational and financial improvements and management incentives. In some instances, it focuses on a ‘Buy and Build’ strategy where it will help further develop a company that exhibits growth potential. Its focus is on businesses that maximise shareholder return through strong operational growth and significant capital appreciation.

As a private equity investor, it has clear exit strategies up-front, and embarks on investments with the ultimate aim of profitably exiting from these investments. The ultimate objective of the firm is to attain “value through structured exits to strategic and trade buyers or onto public markets in the region and beyond, within a three to five year investment horizon”. The focus of Abraaj in the agriculture sector is that of a financial

and strategic partner that would be in a position to provide overall strategic and management expertise. However, the nature of the firm is such that it needs to find suitable technical partners with experience in the management of large scale commercial agriculture in order to invest in the sector. Based on its modus operandi, it is not part of its business model to start-up new projects, but rather to buy existing well managed entities, and increase their value by bringing in specific management skills, and increasing productivity and efficiency. This would allow it to increase the value of the business, and yield a healthy profit for its shareholders on exiting the investment.

### **Factors Determining the Investment Destination**

As a private equity firm, the focus of Abraaj is largely on maximising value for shareholders. Hence, any investments undertaken are based on this fundamental principle. In this regard, the agriculture sector will compete with other sectors for investment funds. Abraaj's key considerations of regarding FDI in the agriculture sector include:

- **Access and Availability of Water Resources:** Their focus is on water surplus countries, and it was acknowledged that there are very few water surplus countries in the world.
- **Land Ownership / Security of Tenure:** The minimum lease period that is considered by Abraaj is 25 years, and this should ideally be on a renewable basis. This will allow it sufficient time to increase the value of the investment, and sell to a third party who would have sufficient time (over 15 years lease remaining) to capitalise on the investment. Any shorter lease period would make exiting the investment with a suitable return more difficult.
- **Availability of Suitable Infrastructure:** Suitable road, electricity and telecommunications infrastructure are among the key elements considered from an infrastructure perspective.
- **Security of Personnel:** The safety and ease of movement of personnel outside the project area is of paramount importance for the investor to be in a position to attract skilled manpower from outside the recipient country.
- **Skilled Manpower:** The availability of appropriate human resources with experience in large scale commercial farming is also a key consideration. In many respects, semi-skilled manpower is available in potential recipient countries. However, expertise and experience in large scale mechanised commercial farming that is globally competitive is severely long.
- **Spreading of Risks / Risk Sharing:** The ability to attract other investors to the project also plays an important role in determining the investment destination. In order to spread risk there is a strong preference for equity participation from like-minded partners. In addition investing in several countries spread the geographic and political risk.
- **Overall Investment and Business Climate:** The extent of law and order, the legal and regulatory framework and ability to enforce contracts along with the business and investment climate are examined in order to ensure that the environment is conducive, and facilitates the achievement of the key objective of maximising shareholder value.



### **Al-Qudra Holdings**

Al-Qudra Holding is an Abu Dhabi based, private joint stock investment company focusing on strategic investments with a view to contributing to the sustainable development of the Middle East region. The company is involved in several key sectors including real estate, infrastructure development, utilities production and distribution, industrial production and agriculture. It is exploring various investment opportunities and has facilitated the development of various projects to meet local and regional market needs.

In order to devote sufficient attention to the agriculture sector, it established Al-Qudra Agriculture which is committed to meeting the higher demand for food and reducing the effects of rising food prices. In July 2008, the company announced its plan to acquire 400,000 hectares of farmlands in the Asia (Pakistan, Vietnam, Thailand and India), Middle East (Syria), and Africa (Sudan, Morocco, and Algeria). Its focus on FDI in agriculture stems from the recent crisis and the resultant higher prices along with expectations of lower levels of food supply from the West.<sup>2</sup> It is on this basis that strategic investments are being sought in the agriculture sector.

### **The Role of Al-Qudra in Agriculture**

Al-Qudra could best be classified as a “strategic semi-private investor”. Its focus is on exploring potential for investment in the agriculture sector from both the perspective of ensuring food security and obtaining a return on investment. Al-Qudra sees itself as undertaking assessments on a country-by-country basis to identify potentials, and acquiring appropriate agricultural land. It proposes using advanced technology to provide efficient solutions to the sector. Its investment time horizon is long-term and is in line with the timelines for investment in the agriculture sector.

Being semi-private, an additional constraint for Al-Qudra is the issue of outright purchase of land in host countries (as a result of sovereignty issues- there are political issues and considerations that arise when a company linked to a government tries to buy land in a third country). Hence, the preference and less problematic, cheaper alternative of long-term renewable leases (minimum 25 years) as opposed to out-right land acquisition.

It is envisaged that from a business perspective, it will function purely as a private investor that will operate on sound management principles. However, its focus will be on strategic crops that can firstly address the food requirements of the UAE, secondly the Muslim world, and then the rest of the world. Although Al-Qudra will function to a large extent as financier, and have equity participation, it will also be involved in the management of the projects. Given its strong linkages to the government of Abu Dhabi, its focus will be on strategic crops, and it will have upfront off-takes agreements with the government. Therefore, from the market perspective, the risk is minimised.

In light of the above, with the guaranteed markets and relatively lower risk, the focus for Al-Qudra is on strategic crops as opposed to high value crops (such as papino,

<sup>2</sup>In light of the recent financial crisis, access to credit from the banking and financial sectors will become more restrictive. In addition, the financial crisis resulted in governments re-focusing limited sources away from subsidising food production towards stemming the adverse impacts of the financial crisis. The potential net resultant affect would be lower levels of the production in the West, and further strain on limited supply of agriculture output for human consumption.

mangoes and vegetables) that have higher risk and markets that are not guaranteed. However, in instances where there is still surplus capacity to undertake high value crop production, these may be exploited.

### **Factors Determining the Investment Destination**

The factors considered by Al-Qudra holdings prior to embarking on an investment in the agriculture sector is similar to that of Abraaj Capital. This is not surprising as both operate on private sector principles. Nonetheless, for the sake of completeness, the key factors considered prior to undertaking an investment in agriculture include:

- Resource availability (land and water);
- Availability of suitable infrastructure;
- Contractual laws to govern the investment from a long-term security perspective which will minimise the investment risk;
- Long-term land tenure guarantees / cover by international law;
- Ease of movement for personnel and investor both in and out of the country and within the country;
- Ease of doing business for foreign investment;
- Support from recipient government in addressing community-based issues,
- Securing land and water rights;
- Proximity to the Gulf region; and
- Level of inter-governmental relationships, bilateral agreements between governments, stability and security in host country government.

### **VIII. ENVISAGED ROLE FOR DEVELOPMENT PARTNERS AS IDENTIFIED BY THE PRIVATE SECTOR<sup>3</sup>**

Both Abraaj Capital and Al-Qudra Holdings highlighted that development partners including the IDB could play an important role in the stimulating of FDI in the agriculture sector. The MDBs could, among others, facilitate FDI in the agriculture sector by:

- Making available finance for:
  - Funding infrastructure projects that unlock key constraints inhibiting the development of the agriculture sector;
  - Equity participation in projects. By “putting their money where their mouths are”, development partners could take equity stakes in the potential investments. This would assist in reducing the risk exposure, and also increase confidence in the investment and business climate in the recipient country. It may also serve the dual purpose of marketing the country as an investment destination to other private sector investors;
- Providing advisory services by, among others, acting as an honest broker between the various parties to facilitate public-private dialogue, and ensure a level playing field.

<sup>3</sup> This section covers the considerations by both Abraaj Capital and Al-Qudra Holdings. Where the issue is relevant for only one of the investors, it is identified as such.

### **Investor Perspective on Key Impediments to Investment in Agriculture**

On the basis of details provided by KAI, Abraaj Capital, Al-Qudra Holdings, and the Abu Dhabi Fund for Development several constraints were identified with regard to investment in the agriculture sector. These include:

- Lack of access to information on specific investment opportunities and other key factors relating to specific potential projects. The requirement from the private sector is for clearly identifiable / identified opportunities in the form of bankable projects that have at the very least scoping / pre-feasibility undertaken by reputable independent third party; and
- Lack of professionalism by recipient governments in dealing with prospective investors. This is to a large extent due to a mismatch between the actual regulations and what is implemented. Also, investors (even where backed by their governments) find that the bureaucracy related to foreign investment is onerous. The lack of clear upfront commitment, clear channels of communication and single point of contact, long term-contractual guarantees, openness, good governance and transparency from recipient governments further compounds the problem.

## **IX. STIMULATING FDI IN AGRICULTURE**

There is significant potential for FDI in OIC member countries specifically in the agriculture sector. However, these potentials remain largely untapped. Issues considered by potential investors were highlighted earlier. Countries wishing to successfully attract FDI will have to take cognizance of these factors and create an environment that is conducive to FDI. In the case of Sudan, some of the key bottlenecks hampering FDI were discussed. Potential recipient countries along with their development partners will need to make a concerted effort if they aim at attracting large amounts of investment into their economies.

### **Potential Recipient Countries**

The changing environment warrants new directions to be explored, and special efforts made, to mobilise capital for sustainable agriculture by countries such as Pakistan who are rich in arable land. These countries need to exploit the potential investment opportunities available and ensure that they have a favourable investment climate to entice suitable investors.

The benefits would thus accrue both to the investor nation in the form of securing food supplies and reducing the price volatilities in their home countries, while the investment destination would benefit from the FDI (including assistance in its own endeavours at ensuring food security) and the corresponding job creation that would follow. Thus, it emerges as a “win-win scenario” for the host and investor nations. Hence, a shift from a protected and isolated approach to economic development in which international competitiveness, regional co-operation and a more diversified economic base is paramount. Potential recipient countries need to be cognizant that the opportunities to promote FDI in the agriculture sector need to be exploited as a matter of urgency since such investments could result in the “crowding-in” of other investors, with the resultant positive externalities to the domestic economy.

Recipient countries need to pursue an industrial strategy that is directed at both a sectoral (industrial clusters specifically agriculture) and spatial level (to exploit the under-utilised potential in terms of arable land, water resources, etc.). This form of “targeting” is particularly appropriate in the current environment of readily available markets. However, due to lack of financing specifically in LDMCs, huge tracts of arable land remain un-exploited.

Although it is important for these economies to attract such investments, it is important that such FDI also meet objectives of the recipient country which should include:

- Addressing its own food security needs;
- Generating economic growth and development in underdeveloped areas;
- Mobilising foreign (and domestic) private sector investment;
- Generating long-term and sustainable employment;
- Exploiting the spin-off opportunities that arise from this relative crowding-in of private and public sector investments for the development of SMEs and the empowerment of the local communities;
- Taking advantage of under-utilised locational and economic advantages for export orientated growth; and
- Attracting modern technology into the agriculture sector.

On the basis of the above-mentioned objectives, it is proposed that the potential recipient countries embark on an exercise that allows for potential projects to be identified along with undertaking the basic pre-feasibility of such potentials with a view to marketing these potentials to the investor countries. Such an exercise could be undertaken with the assistance of experts and technical assistance from MDBs such as the IDB.

In this context, recipient governments will have three key strategic roles that could be played namely: (i) interventionist, (ii) catalytic, and (iii) facilitator. At the interventionist level, it would be to identify the potential areas of un-utilised potential, map the area, identify suitable projects, undertake pre-feasibility studies, arrange investor conferences, and undertake strategic investments in de-bottlenecking projects etc.

The catalytic role will, to a large extent, follow the investment where government could play an indirect, supporting role. In this regard, governments should attempt to facilitate the further development of agriculture clusters/hubs by encouraging private sector efforts and ensuring an environment that is conducive for these developments.

Recipient governments may also need to undertake local skills audits. Importantly, the identification of potential demand levels and skills determinations will have to be undertaken with key stakeholders involvement. Moreover, mechanisms to ensure effective skills transfer from foreign companies to form competent local farmers will need to be explored and agreed upon.

As a facilitator, governments could play a proactive role in stimulating the agriculture sector by creating a conducive environment for agriculture development. In this regard, a key role would be to assist in resolving land issues, and facilitating dialogue between the investors and local communities to ensure community buy-in and participation on the project. This could assist in mitigating some of the political risks on the project (see Box 1 where lack of such consultations resulted in the project being cancelled).

Investments in transport infrastructure, agriculture research and related infrastructure could also contribute towards these efforts. From the financial perspective, access to finance is still a key stumbling block for the farming communities. Innovative financing solutions that are not overly burdensome on small scale farmers needs to be devised and effectively implemented.

### Box 1

#### Daewoo's Experience of FDI in Agriculture in Madagascar

Madagascar is the fourth largest island located in the Indian Ocean and East of Mozambique, with population of 19.7 million, of which 71 percent lives in rural areas. The country's economy is highly dependent on agriculture with it contributing 26.5 percent of the GDP. Out of a total land area of 582 thousand square kilometers, 2.95 million hectares are arable land. Similar to many African economies, the agriculture sector in Madagascar has is under-developed and exhibits significant potential. Daewoo (Korea) sought to secure food supplies for Korea by undertaking FDI in the agriculture sector in Madagascar. In November 2008, Daewoo secured a lease on 1.3 million hectares of arable land for 99 years at a nominal cost in remote Western Madagascar to grow corn for export to South Korea. The investment was anticipated at US\$ 6 billion (the biggest agriculture FDI in the history) over a 25 year period, and could potentially create between 45,000 and 70,000 new jobs. Unfortunately, civil society including rural communities and farmers were not consulted. The resultant public outcry and subsequent violent protests claimed at least 100 lives. This coupled with the negative public sentiment lead to the collapse of the government. The deal was cancelled by the new government who claimed that it was unconstitutional and the people were not consulted. There are key lessons that OIC member countries seeking to undertake FDI in the agriculture sector can learn. These include:

- Recipient countries and investors must ensure that communities are widely consulted and receive tangible benefits from the project via either being part of the overall project, or benefiting from extension services and technical support from the investment.
- Countries must undertake detailed feasibility studies and ensure that the land tenure system meets the community concerns and investor requirements considering the political history of the country and social justice.
- In the case of large-scale agriculture investment land lease, failure to have balanced deal and proper consultation with the concerned communities will lead to many disappointments in both parties, particularly the host country.
- The investment should be of a reasonable size suitable for large-scale commercial farming (and not excessive as in the case of Daewoo).
- The cost of the lease should be realistic and not merely a nominal fee as it contributes to negative perceptions that the "country is being given away" to foreigners.

*Source:* [www.africanagriculture.blogspot.com](http://www.africanagriculture.blogspot.com); [www.en.afrik.com](http://www.en.afrik.com); [www.bloomberg.com](http://www.bloomberg.com); [www.rjkoehler.com](http://www.rjkoehler.com)

Access to appropriate technology, technical support and new crop varieties could also be made available to small scale agriculture enterprises via public private partnerships. Arguably a most important element is security of investment through land ownership and property rights. This would encourage farmers to take risk and the land could be used as security in accessing finance.

In order to attract investors, the possibilities of preferential agreements regarding wages, labour flexibility, subcontracting and training to assist with the development of these labour intensive industries could be explored. The recipient government could also examine the possibility of giving the investors “tax holidays” / “tax breaks” on condition that they will provide extension services to the local farmers, and help with skills transfer and technology diffusion.

In addition, from the perspective of investors, there are several areas in which the host country government could play an important facilitatory role. These include:

- Providing access to suitable water resources;
- Identification of suitable large tracks of land;
- Providing security of tenure;
- Good governance and transparency;
- Facilitating discussions with local communities;
- Ensuring microeconomic stability; and
- Provision of key infrastructure.

If the above areas related to general enabling environment are addressed, then investment opportunities could potentially be exploited. Countries are competing for FDI with the rest of the world. If they cannot provide a business and investment climate that is at the very least as good as the rest of the world, they will not be in a position to attract investors. Investment funds will flow to those countries that offer the best overall package. As such, in the case of Sudan, the specific issues identified earlier and those highlighted by potential investors will have to be addressed. This will require commitment from local, provincial and national governments and coordinated efforts to ensure the success of such endeavours.

### **Role of Development Partners**

Multilateral Development Banks including the IDB have viewed the support and financing to the agriculture sector as an integral element of their efforts at moving people out of poverty. With approximately 75 percent of the Worlds residing in rural areas, the sector is crucial to addressing this key challenge. Since inception, at the sectoral level, 11 percent of IDB financing, 6 of World Bank financing between 1990 and 2008 and 17 percent African Development Bank went to the agriculture sector. Given the importance of this sector, it was expected that it would receive a significantly higher percentage of these development institutions financing allocations. However, many infrastructure projects funded by these institutions may assist in addressing some of the constraints in this sector. In order to provide more effective development assistance to the agriculture (and rural sector), strategic priorities were identified by these institutions.

There has been a global response to prevent a catastrophe arising out of the higher food prices and supply shortages. Notably, the World Bank launched its initiative the “New Deal for Global Food Policy” wherein it will provide cash transfers, food-for-work programmes and assist with measures to increase agriculture productivity. It has also stated that it will double its agriculture financing to Africa to US\$800 million per annum. The International Fund for Agriculture Development (IFAD), the African Development Bank (AfDB) and the Asian Development Bank (AsDB) have also announced similar initiatives. Moreover, many donors have pledged support to the most severely affected countries.

The IDB has also launched its own initiative commonly known as the “Jeddah Declaration” wherein its assistance package of US\$1.5 billion to be financed over a period of 5 years was approved in May 2008. It is intended to cater for both the urgent and medium to long term needs. The programme aims at regenerating the agriculture sector in the IDB member countries by supporting agriculture to become more productive and commercially oriented so as to increase the income level of the farmers and livestock raiser, and promote economic growth. In terms of the Jeddah Declaration, it is apparent that all private sector entities in the IDB Group have an important role to play albeit for different activities. Under the Jeddah Declaration, both recipient and investor countries could potentially benefit from the IDB Group initiative. Investor nations could be assisted by the financing activities, whilst recipient countries could also obtain short-term assistance specifically with regards to meeting immediate food security needs.

It was highlighted earlier that development partners are key to fostering FDI in the agriculture sector. The nature of the interventions by development partners would be to create the appropriate enabling environment to attract FDI in the agriculture sector. Their role would be at three levels namely, (i) provision of technical assistance; (ii) advisory services (acting as an “honest broker”); and (iii) financing. These three roles are within the expertise of the MDBs including the IDB and could complement existing activities and operations. In this regard, it is proposed that development partners may consider:

- **Provision of *Technical Assistance* to:**

- Build domestic capacity in the agriculture sector;
- Assist recipient countries by provision of information/undertaking appropriate studies and project appraisals;
- Fund skills development programmes in the agriculture sector using their technical assistance budgets. In this regard, the focus should not be on establishing/maintaining large training centres on site, rather on on-the job training (both theoretical and practical) and the utilisation of outside training providers for basic/generic training; and
- Strengthen relevant institutions; and Establish centres of research similar to International Centre for Biosaline Agriculture (ICBA) that could undertake strategic research in the agriculture sector.

- **Advisory Services**

- *Honest Broker*: In this context, the focus may be on facilitating policy dialogue between the private sector, public sector and other social partners; in promoting public private partnerships (specifically around infrastructure

development); and in communicating the concerns of key stakeholders and communities to project owners;

- Package projects for Investor Conferences and participate therein; and
- Facilitate implementation of projects, and the forging of strategic partnerships.

- **Financing**

- Take up equity in such projects.

## X. CONCLUSIONS

Despite the wide publicity in recent times about foreign direct investment in the agriculture sector following the food crisis, it is interesting to note that little real investment has been made on the ground. Investors have undertaken preliminary discussions with potential recipient countries, but these are still at the early stages. In order for investors to progress to the stage where actual investments occur, prefeasibility and feasibility studies, along with key infrastructure are pre-requisites. The current status of investments is not surprising given the time lag of approximately 2 years between identification of a specific new investment opportunity and the actual investment. Consequently, it is anticipated that it may take 2-3 years before the announced investments may come to fruition (if there are no additional investment constraints). However, the easing of commodity prices coupled with the financial crisis and subsequent recession, resulted in proponents of FDI in the agriculture sector taking a more pragmatic and cautious approach. It is therefore expected that this timeline might shift out with priorities shifting.

Although countries such as Pakistan, Turkey, Indonesia and Sudan, have a strong 'ability' to attract FDI into their agriculture sectors, 'ability' on its own is not sufficient to attract investors. Of paramount importance is the need for an appropriate business and investment climate ('suitability'). In terms of the enabling environment for the agriculture sector, Turkey emerged as a preferred destination given its very strong business climate and reasonable 'ability' for agriculture. This is regardless of the fact that it has less un-utilised agriculture land than countries such as Iran and Mozambique. In this regard, it is important to note that without an appropriate investment and business climate, foreign investors will be cautious.

The decision to invest in a country is a rational one, based on the risks and returns associated with the project. On the issue of risk, there are several constraints that may hamper the investment decision. As long as these constraints are not addressed, foreign direct investment in countries will remain elusive. In the agriculture sector, the investment time horizon is typically between 5 to 7 years in order to determine the ex-ante rate of return on the investment. Investors (specifically from the GCC region) are seeking short-term quick returns on investment while the agriculture sector tends to require a longer-term commitment.

Overall, it must be recognised that investment will flow to countries that offer good returns with lower associated risk. Therefore, potential recipient countries must ensure that the investment climate is at the very least as good as those offered in alternate investment destinations. If this externally imposed market discipline is not adhered to, countries may find it extremely difficult to attract FDI into the agriculture sector.



Assuming the enabling environment is suitable, the missing link would then be the technical and managerial expertise required to successfully undertake investments in the agriculture sector. This is as an important third ingredient to the potential investment funds from the GCC and the ability to undertake agriculture (abundant water and land resources) in some countries.

In addition, there is a need for partnerships between recipient governments, investors and development partners. These partnerships are required in order to increase risk adjusted returns on investment. Potential recipient countries along with their development partners will need to address the business and investment climate by rationalising procedures, building capacity at the institutional level, training the workforce, tackling governance issues, and building productive infrastructure. These will enable countries to provide a suitable business and investment climate that is attractive to foreign investors.

The experience of Sudan highlights some key lessons for countries wishing to attract FDI into their agriculture sectors. Firstly, they should adopt a holistic perspective of the investors and type of investments that they wish to attract to their economy specifically in the agriculture sector. There must be a coordinated approach to land allocation with clear performance and investment agreements included in any land allocated/sold to potential investors. Secondly, governments need to develop clear guidelines and mechanisms to handle unsolicited requests for land and other investments. Thirdly, development partners have an important role to play in fostering FDI in the agriculture sector.

It must be recognised that there are several constraining factors impeding investment in the agriculture sector. Countries and their development partners will need to address these as a matter of urgency. If the business and investment environment is not conducive, investors will go to other countries as they seek to maximise long-term profit and return on investment resulting in a lost opportunity.

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