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The potential of South–South investment for agricultural and economic development

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Introduction

1. The food crisis in recent years has given rise to the recognition that the agricultural sector in many developing countries is in need of significant additional investment to boost productivity and to support development of the rural economy. The Food and Agriculture Organization of the United Nations has recently estimated that developing countries will need upwards of \$80 billion a year in new investment to address existing problems of food insecurity and meet the growing demand for food crops that will arise from an expanding population. This amounts to a 50 per cent increase over current levels.
2. Investments will be needed in both the public and private sectors, with a particular focus on bolstering output in small farm holdings. However, though by no means a panacea, foreign participation can play a role in promoting agricultural development by bringing in financial resources, management skills and technical expertise.

I. Foreign participation in the agricultural sector

3. Foreign participation in agriculture refers to the involvement of a private or government entity in one country (hereafter referred to as the “home country”) in the agricultural sector of another country (“host country”), with the objective of exerting control over agricultural supply. Such participation principally takes two forms: (a) investment involving direct production through the acquisition (purchase or leasing) of land or investment in related industries, such as food processing and food retailing; and (b) the procurement of agricultural produce through contract farming or through traditional market relations.
4. Either form of participation may be undertaken in the pursuit of commercial interests or as part of a strategy to ensure food security for the home country. Food security-related investments are typically carried out by enterprises which are State-owned or closely associated with States.

5. UNCTAD's annual study of worldwide investment trends, the *World Investment Report*, finds that foreign participation in agriculture, though small, has been increasing. South–South investment has, in particular, risen sharply in this sector and is now significant compared to that by developed country transnational corporations (TNCs). For instance, the value of cross-border takeovers shows that net cross-border merger and acquisition purchases by investors from the South amounted to \$1.6 billion, accounting for over 40 per cent of the world's total M&A value in the sector in 2008 (\$3.6 billion).

6. As agriculture forms such a vital part of the economy in developing countries, in terms of output, employment and export earnings, especially in poorer countries, cross-border trade and investment involving the sector must be approached with care. Foreign participation could have far-reaching impacts on the sector, which gives rise to concerns about possible negative outcomes for farmers, the rural population and the wider economy. In recent years, concerns around the growing use of genetically modified organisms controlled by TNCs as well as the acquisition of land by foreign firms have been just two of the many issues that have attracted attention.

7. Although the global food business is very heavily dominated by TNCs from developed countries, such concerns can involve developing home countries as well, since firms from these countries have begun to acquire an international reach. Thus, there is a scope for South–South cooperation aimed at managing South–South investment in agriculture so as to improve food security and to facilitate rural development.

II. Trends in South–South investment in agriculture

8. The *World Investment Report 2009* lists the largest TNCs in agribusiness, subdivided into four industry categories: (a) agriculture-based (i.e. firms running farms or plantations); (b) input suppliers (e.g. of fertilizers or seed stock); (c) food and beverages; and (d) traders/retailers. When ranked by foreign assets, half of the top 25 TNCs in the “agriculture-based” category are headquartered in developing countries, although the presence of Southern TNCs in the other three categories is much less significant.

9. In addition to commercial expansion by Southern TNCs, food security has become a major driver of new investment in the wake of the food crisis. Though it is still difficult to assess the scale of South–South foreign direct investment (FDI) driven by food security concerns, the largest sources (developing home countries) of food security-related investment from the South include Bahrain, China, Qatar, Kuwait, the Libyan Arab Jamahiriya, Saudi Arabia, the Republic of Korea and the United Arab Emirates. The most important developing host countries are in Africa, with Ethiopia, Sudan, and the United Republic of Tanzania among the foremost food security-related FDI recipients.

10. A recent example of South–South investment in plantations is the \$800 million investment in a plantation in Liberia by Sime Darby (Malaysia) in 2009. Examples of investment by food processors and retailers include (a) the expansion of Zambeef (Zambia) into Ghana and Nigeria; (b) the retail network of Shoprite (South Africa) in a number of countries on the continent; (c) contracting farming arrangements throughout the Greater Mekong subregion by the CP group (Thailand); and (d) the expansion by Grupo Bimbo (Mexico) across Latin America and the Caribbean.

III. Potential benefits and risks

11. The potential benefits of foreign participation in agriculture are clear conceptually, but not necessarily as evident in practice. In the case of investment involving acquisition of land, in addition to the injection of funds resulting from sale or lease of the land, the

investor typically offers auxiliary investment such as the development of transport infrastructure. In the case of contract farming, retailers and food processors often provide financial and technical assistance to contracted farmers. For the farmer, such a contract represents a promise of a stable income stream, which may even be used as collateral for obtaining a loan. From the macroeconomic perspective, as transnational food processor and retail chains often procure agricultural produce for export, contract farming can also establish a source of foreign exchange.

12. If the potential benefits of foreign participation are promising, their ultimate value to the host economy depends on the bargaining strength and strategic vision of domestic policy makers. As widely recognized, the risks from such partnerships are all too evident. For instance, investment in large farm land has been criticized for aggravating food shortages in the host country. In some cases, the agreement between the investor and the host country government for leasing land has not sufficiently taken into account the existing usage of the land by the local people. Such problems are all the more likely in countries where land ownership is not clearly defined.

13. More generally, concerns have been raised about the potential tension between certain forms of export-oriented FDI and food security. If foreign acquisition of land results in diverting food production from supplying the domestic to export markets, it may create disruption in the local food supply system. Less directly, the cultivation or procurement of cash crops for export may constrain the availability of land for production of staple crops for the domestic market. As emphasized elsewhere, food security is often an issue of affordability rather than availability. Thus, to the extent that exporting agricultural produce can bring in much-needed foreign exchange, it could contribute to improving food security in the host country. However, a full assessment, in this regard, would also have to take in to account the import content of such agricultural production, the extent of repatriated profits, etc. The task for policymakers therefore is to manage foreign participation in such a way that it does not disrupt the local food supply system (e.g. through output sharing agreements), is consistent with macroeconomic goals and ensures that, in the longer term, it contributes to sustainable growth in the agricultural sector.

14. Particularly with respect to the last of these challenges, contract farming has given rise to concerns about its exclusive nature and the detrimental effects on the livelihood of poorer, small-scale farmers. Food processors and retailers typically require their contracted farmers meet stringent safety and quality standards. Despite the offer of technical and financial assistance, farmers are unlikely to be able to meet the requirements except for the few who run larger-scale, capital-intensive operations in areas where infrastructure is well developed. Thus, small-scale farmers are not only left out of the new income opportunities, but are also likely to be marginalized as the market evolves in such a way as to favour large scale agriculture.

15. The consequences of exclusivity with regard to the beneficiaries of foreign participation may arise at the country or even regional level. Smaller economies may offer too little in terms of the size of the markets or productive capacity to potential investors and thus struggle to attract foreign investment.

IV. Policy responses

16. To meet rising food requirements and to revitalize agriculture in poor countries, policymakers need to promote investment. Notwithstanding existing concerns about foreign participation, host countries should not underestimate the potential gains. However, the potential benefits do not arise automatically and the key challenge is to ensure that foreign participation generates development benefits in the host country and that the possible risks

are effectively mitigated through appropriate policy action. To this end, social and environmental concerns have to be addressed, particularly with regard to possible long-term implications for economic development and food security. Governments therefore need to devise well-coordinated strategies aimed at long-term agricultural development. In this context, South–South cooperation has a role to play for three reasons:

(a) Countries with fast-growing food demand and countries with large potential for expanding agricultural output are both to be found among developing countries. Therefore, food security-related investment often has a South–South character. Among possible future initiatives, the *World Investment Report*, for example, recommends that consideration be given to developing a set of internationally agreed core principles for large-scale acquisitions of agricultural land by foreign investors. This is not a South–South issue *per se*, but given the prominent roles of developing countries both as investor and recipient in this regard, their contributions would be vitally important.

(b) The creation of a regional market with respect to the agricultural sector addresses the problem of limited market size and offers investors opportunities for establishing regional value chains. Such a regional market also provides a context for governments to jointly address institutional and other constraints to regional investment and trade (including infrastructural ones);

(c) Finally, as emphasized in the first session of this expert meeting, the strength of South–South cooperation is, among others, in the geographical proximity and cultural affinity among developing countries. This aspect is also true of the agricultural industry. The sharing of experience and policy lessons would be an important contribution of South–South cooperation in enhancing the performance of the industry and improving food security in the developing world.

V. Issues for discussion

A. The role of regional integration

- (a) How can regional integration facilitate cross-border investment in agriculture?
- (b) What specific measures, including in other industries, could lead to increased investment?
- (c) What are the pitfalls and potential negative impacts policy makers need to take into account at the regional level?

B. Home and host country policies

- (a) What home and host country policies could encourage sustainable and socially desirable cross-border investment in agriculture?
- (b) What constitutes a “business friendly” environment in the case of agriculture, given the need to mitigate the negative impact of (foreign) investment in the industry?

C. Food security-related investment

- (a) What are the factors that could give rise to tensions over leasing of land?
- (b) What are the issues that need to be considered to address concerns over “land grab”?

(c) Is a set of internationally agreed core principles for (foreign) investment in agriculture desirable? What elements should such principles include?
