

# INTERNATIONAL INVESTMENTS IN AGRICULTURAL PRODUCTION<sup>1</sup>

DAVID HALLAM<sup>2</sup>

## Introduction

There has been a recent resurgence of interest in international investment in agricultural land. Purchases and leasing of agricultural land in Africa by investors in various Gulf States for food production in support of their food security strategy have perhaps attracted most attention until now, although these are just one of a variety of actual or planned investment flows with different motivations. Other countries outside Africa are also being targeted and major investments have also been made or are being planned by Chinese and, rather controversially, South Korean investors. Investment companies in Europe and North America are also exploring opportunities motivated by potentially high expected returns on investment partly due to higher food prices and especially where biofuel feedstock production is a possibility.

The main driver for the recent spate of interest in international investment in food production appears to be food security and a fear arising from the recent high food prices and policy-induced supply shocks that dependence on world markets for food supplies or agricultural raw materials has become more risky. Investment in food production overseas is one possible strategic response among others. At the same time, a number of developing countries in Africa are making strenuous efforts to attract such investments to exploit “surplus” land, encouraging international access to land resources whose ownership and control in the past have typically been entirely national.

Not surprisingly, the apparently anomalous situation of food insecure, least developed countries in Africa selling their land assets to rich countries to produce food to be repatriated to feed their own wealthier people has attracted substantial media interest. It has also attracted international concern more generally, including at the recent G8 agricultural ministers’ meeting. Some argue that these investments could mark the beginning of a fundamental change in the geopolitics of international agriculture. Certainly, complex and controversial issues – economic, political, institutional, legal and ethical – are raised in relation to food security, poverty reduction, rural development, technology and access to resources, especially land. On the other hand, the low level of investment in developing country agriculture, especially in Sub-Saharan Africa, over decades has been highlighted as a matter of concern and the underlying root cause of the recent world food crisis so any possibility of additional investment resources cannot be dismissed out of hand. The focus needs to be on how these investments can be made “win-win” rather than “neo-colonialism”.

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<sup>2</sup> Deputy Director, Trade and Markets Division, United Nations Food and Agriculture Organisation.

## **AGRICULTURAL INVESTMENTS IN THE HEADLINES**

### **Saudi Investors to Put \$100m into Ethiopian Farm**

*(Fortune, 15.4.2009)*

### **Saudis Set Aside \$800m to Secure Overseas Food**

*(Financial Times, 15.4.2009)*

### **UAE Stepping Up Agricultural Investment in Sudan**

*(Sudan Tribune, 7.8.2008)*

### **Food Is Gold So Billions Invested in Farming**

*(New York Times, 5.6.2008)*

### **Land Leased to Secure Crops for South Korea**

*(Financial Times, 18.11.2008)*

### **Korea's Daewoo Logistics Leases Madagascar Land for Feed, Fuel**

*(Bloomberg, 18.11.2008)*

### **Short of Food? Rent Half a Country**

*(New York Times, 19.11.2008)*

### **Pakistan Offers Farmland to Foreign Investors**

*(Reuters, 20.4.2009)*

### **UN Warns Of Neo-Colonialism**

*(Financial Times, 19.8.2008)*

### **Manufactured Famine: A New Wave of Food Colonialism Is Snatching Food from the Mouths of The Poor**

*(Guardian, 26.8.2008)*

### **Dispute Erupts Over Plans to Invest Millions in Rice Farming**

*(Economist, 23.4.2009)*

## **Recent Investment Trends and Patterns**

There are no detailed data on the extent of such investments. Available foreign direct investment data is not sufficiently detailed to determine just how much investment in agriculture there has been and what forms it takes. It is therefore difficult to say with any precision whether the recent investments are a totally new development or a continuation of existing trends. UNCTAD's *World Investment Report* for 2009 will however have a focus on agriculture, and country case studies currently being conducted by FAO, UNCTAD and the World Bank should provide some more detailed information regarding the extent, nature and impacts of investments in particular countries. Anecdotal information is available from the media although the accuracy of much of this is questionable. Some information is available from the investors themselves and from those developing countries receiving inward

investment, although not too much detail is divulged given the sensitivity of the issues surrounding these investments and the need for confidentiality.

On the basis of the information available, a number of observations can be made regarding recent trends and patterns.

- There does appear to have been an increase in international investments in agriculture in developing countries although the number of actual implemented investments appears to be less than the number being planned or discussed or reported in the media.
- Land under foreign control remains a relatively small proportion of total land areas in most cases.
- The main form of investment is in purchase or long-term leasing of agricultural land for food production.
- Major investors in current investment flows are the Gulf States but also China and South Korea.
- The main targets for investment are countries in Africa but there are also investments in Pakistan, Kazakhstan, Cambodia, and Brazil for example.
- Investors are primarily private sector but governments and sovereign wealth funds are also involved.
- Private sector investors are often investment or holding companies rather than agro-food specialists which means that necessary expertise for managing complex large-scale agricultural investments needs to be acquired.
- Private sector investors are often funded by government or sovereign wealth funds, making it difficult to separate them out and judge the extent of public sector involvement.
- Sovereign wealth funds seem to be playing a lesser role than had originally been thought although they do appear to have been diversifying their portfolios to include developing country investments and in agriculture.
- In host countries it is governments who are engaged in formulating investment deals.
- Recent investments emphasise production of basic foods, unlike foreign direct investment (FDI) in agriculture in the past.
- Investments include production of animal feed to meet the rising demand for livestock products.
- More traditional FDI continues – in horticulture and flowers in East Africa, for example – but emphasising various forms of joint ventures.
- The recent investments involving acquisition of land and actual production are against the trends in FDI more generally.
- There may be some signs of a shift away from Africa and a search for greater local involvement through joint ventures as with FDI in the past.

### **Investor motivations**

The motivation for these investments depends on the investor – whether private sector or government. Private sector investments can represent portfolio diversification for financial returns. Biofuel production is also an important objective. However, the main reason for the recent spate of interest and which differentiates it from more previous international investments is food security. This reflects a fear arising from the recent high food prices and

policy-induced supply shocks that dependence on world markets for food supplies has become more risky. Investors seek enhanced food security through investment in countries where the land and water constraints faced domestically are not present. However, they also require security of their investments. While the current preoccupation is to buy land since titled ownership of assets is seen as most secure, there are many arguments against this from the point of view of the receiving country. It is also not clear that it is necessary or desirable even for the investing country. Acquisition of land does not necessarily provide immunity to sovereign risk and can provoke political and economic conflict. Other forms of investment such as contract farming and out-grower schemes can offer just as much security of supply.

In any case, land investments are only one strategic response to the food security problems of countries with limited land and water resources and discussion of these investments needs to be set in the wider context of broader strategic discussions of food security problems. There are a variety of other mechanisms, including creation of regional food reserves, financial instruments to manage risk, bilateral agreements including counter-trade and improvement of international food market information systems, which are under active discussion. In the limit, investment might be simply in much-needed infrastructure and institutions which currently constrain much developing country agriculture especially in Sub-Saharan Africa. This, together with efforts to improve the efficiency and reliability of world markets as sources of food might raise food security for all concerned more generally through expanding production and trade possibilities.

In some cases where governments are involved, these investments can be similar to official development assistance. Japan is planning to invest in projects to increase food production in developing countries, especially in Latin America, but which might indirectly benefit Japan through increased export availability.

### **Host country motivations**

Lack of investment has been identified as a fundamental cause of the continuing low productivity and stagnant production of developing country agriculture. FAO estimates that developing countries need an additional \$30 billion per year investment to double food production by 2050 (needed to feed growing populations and ensure basic right to food). Most recent estimates are even higher. Public investment resources are limited by budgetary pressures and official development assistance to agriculture has been declining over many years. The private sector in developing countries has tended to have little capacity to fund investment. International investments therefore have a potentially important role to play.

Some countries are making strenuous efforts to attract such investments to exploit “surplus” land currently unused or under-utilised. Selling, leasing or providing concessional access to land raises the questions of how the land concerned was previously being utilised, by whom and on what tenurial basis. In many cases, the situation is unclear due to ill-defined property rights, with informal land rights based on tradition and culture. While it is true that much land in Sub-Saharan Africa is currently not utilised to its full potential, apparently “surplus” land overall does not mean land is unused or unoccupied. Its exploitation under new investments involves reconciling different claims. Change of use and access may involve potentially negative effects on food security and raise complex economic, social and cultural issues. There is substantial evidence of such negative effects arising in other contexts – large-scale biofuel feedstock production, for example. Such difficulties at least demand consultation with

those with traditional rights to land, and favour alternative arrangements for investments. More generally, issues are raised by the shift in the terms of access to land from traditional and historical to market-based.

One reason land may not be used to its full potential is that the infrastructural investments needed to bring it into production are so significant as to be beyond the budgetary resources of the country. International investments might bring much-needed infrastructural investments from which all can benefit, but at the same time are deterred by inadequate infrastructure.

The financial benefits of asset transfers to host countries may be small, but international investments are seen as potentially providing developmental benefits through technology transfer, employment creation, infrastructural provisions, production increases, food security and export earnings. Whether these potential developmental benefits are actually likely to be realised is a key concern in the current discussion.

### **Impacts of international investments**

Benefits to the receiving country are a major concern. The key question concerns the extent to which benefits from the investment spillover into the domestic sector in a synergistic relationship including with existing smallholder production systems. Benefits should arise from capital inflows, technology transfer leading to innovation and productivity increase, upgrading domestic production, quality improvement, employment creation, backward and forward linkages and multiplier effects through local sourcing of labour and other inputs and processing of outputs and possibly an increase in food supplies for the domestic market and for export. However, these benefits will not flow if investment results in the creation of an enclave of advanced agriculture in a dualistic system with traditional smallholder agriculture and which smallholders cannot emulate.

While international land acquisitions have been relatively little-studied and information on them is scarce there is a lot of knowledge and research on FDI more generally in agriculture. In spite of the particular economic and political dimensions of land acquisitions, the general FDI experience can provide some guidance not only on the likely benefits and pitfalls of land acquisitions but also the pros and cons of different forms of FDI. It is interesting to note that some of the features of the current round of investment in land appear to be contrary to trends in FDI more generally which seems to be favouring various looser contractual arrangements rather than actual acquisition of major assets. Studies of the effects of FDI in agriculture show that the claimed benefits do not always materialise and catalogue concerns over highly mechanised production technologies with limited employment creation effects; dependence on imported inputs and hence limited domestic multiplier effects; adverse environmental impacts of production practices such as chemical contamination, land degradation and depletion of water resources; and limited labour rights and poor working conditions. At the same time, there is also evidence of longer-run benefits in terms of improved technology, products quality and sanitary and phytosanitary standards, for example. In considering the question of the benefits or otherwise it is therefore important to take a dynamic perspective.

Additional political and ethical concerns are raised where the receiving country is food insecure. While there is a presumption that investments will increase aggregate food supplies this does not imply that domestic food availability will increase, notably where food produced is repatriated to the investing country. It could even decrease where land and water resources

are commandeered by the international investment project at the expense of domestic smallholders. Extensive control of land by other countries can also raise questions of political interference and influence.

The impacts of such investments are not necessarily confined to the two parties involved. Third countries may also be impacted through any resulting changes in international trade volumes and price variability where, for example a major importer secures food supplies outside the market.

Whether or not international investments lead to broader developmental benefits for developing countries depends crucially on the terms and conditions of the investment agreements and the effectiveness of the policy and legislative frameworks in minimising risks.

### **Alternative business models**

Most of the recent investments, actual or planned, have involved purchase or long-term leasing of land. However, there are a number of alternatives which might achieve or even better achieve food security objectives of the investing countries. Alternative business models – various contractual arrangements, for example - can offer just as much security of supply. It is interesting to note that in other contexts, vertical integration tends to be based much more on such arrangements than the traditional acquisition and operation of upstream and downstream assets and activities. The development of East African horticultural production for export by European supermarkets is a case in point. Such looser arrangements are likely to be more conducive to the interests of the receiving country. However, even here, there are likely to be questions as to the compatibility of the needs of the investors with small-holder agriculture and this in turn raises questions about the poverty reduction potential.

What business model is appropriate depends to some extent on what products the investment is intended to produce, the production system and what collateral investments - in infrastructure, for example - are also needed. Investors may favour land purchase or long-term leasing where economies of scale are significant or major infrastructural investments such as roads and ports are needed. Where economies of scale are not significant, contractual arrangements such as out-grower schemes may be just as acceptable to investors and possibly more capable of generating developmental benefits for local producers.

Mixed models are also possible. There are instances of large-scale commercial units, often a privatised former state farm, owned and operated by an international investor with smallholders around it in a symbiotic relationship selling their output under contract to the central company while receiving support in the form of agreed sales, credit and technical assistance. Sugar investments in Tanzania are one example of such a development while the creation of a similar model based on so-called “farm blocks” is an objective of government policy in Zambia.

### **Some policy implications**

If it is acknowledged that international investment might make a positive contribution to raising productivity in developing country agriculture, the question arises as to what policies might help to maximise the positive contributions while minimising the associated risks. Investing countries can provide policy incentives to encourage and target outward investment. However, the onus to attract investments to where strategic needs are greatest and to ensure that those needs are met falls primarily on the host countries. They also need domestic policy measures to ensure that local agriculture is capable of capitalising on any spillover benefits of investments.

Host countries need to create an environment which is conducive to international investment and reduces the perceived risks. At the same time, national interests need to be preserved. Developing countries have made a great deal of progress in this respect in recent years, liberalising entry conditions and establishing investment promotion institutions to facilitate inward investment. Some participate in bilateral treaties and other international agreements and conventions for contract enforcement, arbitration and dispute settlements such as the Multilateral Investment Guarantee Agency. However, the lack of clear property rights, especially to land, remains a deterrent to investment in some countries. Lack of adequate infrastructure may also deter some investors although others see provision of infrastructure as a necessary component of their investments.

If the general developmental benefits of international investments are to be realised then appropriate policy, institutional and legislative frameworks need to be in place to guarantee them. Apart from the financial terms and conditions of the investment, provisions may be needed concerning *inter alia* local sourcing of inputs including labour, social and environmental standards, property rights and stakeholder involvement, food security concerns, distribution of food produced between export and local markets, and distribution of revenues. Trade policy is also involved where investors want to repatriate food produced and some countries have offered trade policy exceptions such as agreements not to impose export controls even in times of domestic food crises.

## **Conclusions and some outstanding issues**

Lack of investment in agriculture over decades has meant continuing low productivity and stagnant production in many developing countries. This lack of investment has been identified as an important underlying cause of the recent food crisis and the difficulties developing countries encountered in dealing with it. Additional investments of at least \$30 billion annually are needed in developing country agriculture. Developing countries' capacity to fill that gap is limited and the share of official development assistance going to agriculture has trended downwards over the years to as little as 5 percent. Foreign direct investment has an important potential role to play, therefore in financing agricultural investments in developing countries. In general terms, the apparent recent surge in interest in international investment in agriculture should be welcomed rather than condemned.

The motivation for the recent spate of interest is food security and a fear on the part of certain food importing countries arising from the recent high food prices and policy-induced supply shocks that dependence on world markets for food supplies has become more risky. The much-publicised "land grab" involving the purchase or leasing of agricultural land in developing countries for food production is just one form of investment. At the same time, a number of developing countries are making strenuous efforts to attract such investments to

exploit “surplus” land. Recent developments could mark the beginning of a profound change in the pattern and nature of global food production and land use.

While such investments should not be rejected in principle there are risks for the host developing country and they raise complex and controversial issues – economic, political, institutional, legal and ethical - in relation to food security, agricultural investment, agricultural development and land tenure and transfer. It is important that any international investment should bring development benefits to the receiving country in terms of technology transfer, employment creation, upstream and downstream linkages and so on. In this way, these investments can be “win-win” rather than “neo-colonialism”. However, these beneficial flows are not automatic: care must be taken in the formulation of investment contracts and appropriate legislative and policy frameworks need to be in place to ensure that development benefits are obtained. The case for an international code of conduct which highlighted the need for transparency, stakeholder involvement and sustainability and emphasised concerns for domestic food security and rural development needs to be explored.

There is an urgent need to monitor the extent, nature and impacts of international investments and to catalogue best practices in law and policy to better inform both host and investing countries. Detailed impact analysis is needed to assess whether an international code of conduct is desirable and what its content should be. The scope for forms of investment other than land acquisition – such as contract farming, out-grower schemes and other joint ventures - and which are more likely to yield development benefits to host countries needs to be evaluated and best practices promoted.

If foreign direct investment is to play an effective role in filling the investment gap facing developing country agriculture, there is a need to reconcile the investment objectives of investing countries with the investment needs of developing countries. Investment priorities need to be identified in a comprehensive and coherent investment strategy and efforts made to identify the most effective measures to promote the matching-up of capital to opportunities and needs.