



Accelerating reform in Africa: Mobilising investment in infrastructure and agriculture

Africa Investment Initiative

Draft Policy Framework for Investment in Agriculture

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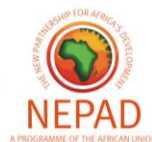


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DRAFT POLICY FRAMEWORK FOR INVESTMENT IN AGRICULTURE:

REAPING THE BENEFITS OF INVESTMENT IN AFRICA'S AGRICULTURE THROUGH AN INTEGRATED POLICY FRAMEWORK

INTRODUCTION

New investment challenges facing Africa's agriculture

1. World population is expected to grow by 2.3 billion between 2009 and 2050. Against a background of increasing land and water scarcity, as well as climate change, feeding a larger urban population while also adopting more sustainable production methods will become a challenge.¹ In Africa, where it is predicted that population levels will double over the same period, the challenge will be even more acute.

2. For decades, the continent has suffered from under-investment in agriculture, leading to stagnant productivity and poor growth in the sector. On average, African countries allocate only 4% of their budgetary expenditures to agriculture, compared with up to 14% in Asia.² In addition, Foreign Direct Investment (FDI) and Official Development Assistance (ODA) for the sector have long remained very low.

3. However, with 60% of the world's remaining uncultivated farmland,³ Africa has recently started to attract large-scale foreign investments geared towards new "frontier territories" for agricultural production. This trend has been driven mainly by emerging markets with increasing food needs, land and water shortages, and growing demand for biofuel. These new investments have also included land acquisition deals, which are commonly referred to in the media as "land-grabs".

¹ OECD-FAO Agricultural Outlook 2010-2019

² Exceptions in Africa include Mali, Burkina Faso and Ethiopia. See High-Level Meeting on African agriculture: http://www.un.org/esa/desa/ousg/statements/2009/20090210_african_agriculture.html

³ McKinsey Global Institute (2010), *Lions on the move: The progress and potential of African economies*, p. 7
http://www.mckinsey.com/mgi/publications/progress_and_potential_of_african_economies/pdfs/MGI_african_economies_full_report.pdf

4. As it is caught between rapidly rising regional and global demand and limited supply capacity, Africa's agriculture needs to make the most of these new opportunities and mitigate their possible adverse effects. On the one hand, such large-scale international investments can supply infrastructure, create employment, increase public revenues, and bring technology and skills to local farmers. On the other hand, they can also threaten food security, lead to the eviction of local land users and loss of access to land for indigenous groups, as well as generate competition for vital resources among local populations.⁴

5. African governments are fully aware of the importance of enhancing both the quantity and quality of agricultural investment throughout the continent to improve food security. Among the ambitious goals established by the New Partnership for Africa's Development (NEPAD) in its Comprehensive Africa Agriculture Development Programme (CAADP), is a commitment to raise agricultural productivity by at least 6% per year.⁵ Achieving this goal would require a massive increase in the current levels of public and private investment. In order to attract private investment while also meeting national development goals, African governments need to consider a whole set of measures in a wide range of policy areas. This may necessitate a well-coordinated approach that could take advantage of an integrated policy framework for investment in agriculture.

A policy framework for sustainable private investment in agriculture

6. The Policy Framework for Investment (PFI) – developed at the OECD in 2006 by 60 OECD and non-OECD countries – aims to support countries in mobilising private investment for steady economic growth and sustainable development. The PFI is a tool, providing a checklist of policy issues to be considered by any government interested in creating an environment that is attractive to all investors and in enhancing the development benefits of investment to society, especially the poor. In this way, the PFI aims to advance the implementation of the United Nations Monterrey Consensus, which emphasised the vital role of private investment in effective development strategies.

7. As a flexible instrument, the PFI can be adapted and applied to specific sectors. Given the importance of the agriculture sector for Africa's development, the NEPAD-OECD Africa Investment Initiative, the OECD Sahel and West Africa Club (SWAC) and the Office of the Special Adviser on Africa (OSAA) of the UN Secretary General have thus started to develop a draft policy framework for investment in agriculture. Following a request from the Government of Burkina Faso to the OECD, a first draft was prepared for consultation in this country and then substantially revised. It is now used by the Government of Burkina Faso for assessing its policies for agriculture investment. The Burkina Faso project and the participation of the national task force have greatly enhanced the present draft. It also benefited from the discussions on Responsible Investment in Agriculture held at the OECD within the framework of the Freedom of Investment Process.⁶

8. The purpose of this document is therefore to initiate discussion on a draft policy framework for investment in agriculture in order to improve and refine it into a final version. Such a policy framework

⁴ Press Release, 11 June 2009, The UN Special Rapporteur on the right to food recommends principles and measures to discipline "land grabbing".

<http://www.ohchr.org/EN/NewsEvents/Pages/DisplayNews.aspx?NewsID=8708&LangID=E>

⁵ See CAADP website: <http://www.nepad-caadp.net/about-caadp.php>

⁶ *Responsible Investment in Agriculture*, Note by the Secretariat in support of discussions for the "Freedom of Investment" Roundtable 12 [DAF/INV/WD(2010)3/REV1]

would be intended as a flexible instrument that governments can use in evaluating and designing policies for agricultural investment in Africa. It could assist African governments in their efforts to attract more and better quality investment in support of national development objectives, including through the elaboration of actionable and time-bound policy measures.

9. By focusing on host-country perspectives, it would serve as a complement to international initiatives, such as the “Principles for Responsible Agricultural Investment that Respects Rights, Livelihoods and Resources” promoted by the Food and Agriculture Organisation (FAO), the International Fund for Agricultural Development (IFAD), the World Bank Group and the United Nations Conference on Trade and Development (UNCTAD). The draft policy framework for investment in agriculture could also contribute to achieving CAADP objectives through supporting the design and implementation of regional and national plans for agricultural investment. In addition, it could provide the Global Donor Platform on Rural Development (GDPRD) and the ‘Alliance for a Green Revolution in Africa (AGRA)’ with an instrument to facilitate donor dialogue, harmonisation and alignment around African countries’ priorities for agricultural investment.

10. As ODA can play an important role in supporting African governments to address policy issues that hamper agricultural investment, the draft policy framework for investment in agriculture also highlights the positive contribution of new ODA instruments such as insurance mechanisms (like weather insurance), financial guarantees for smallholder farmers or initiatives to harness the potential of rural communities for innovation.

11. Sustainable growth in agriculture relies on a wide set of policies that go beyond strict agricultural policies *per se*. The draft PFI in agriculture proposes guidance, in the form of questions for governments’ consideration (Part I) and annotations (Part II) in nine policy areas for improving the quality of a country’s environment for investment in the sector:

- Investment policy
- Investment promotion and facilitation
- Human resource and skills development
- Trade policy
- Environment
- Responsible business conduct
- Infrastructure development
- Financial sector development
- Taxation

12. Given the range and variety of relevant measures involved, the draft PFI in agriculture calls for policy co-ordination at the host country level, both in the design and implementation phases.

PART I. DRAFT POLICY FRAMEWORK FOR INVESTMENT IN AGRICULTURE

1. Investment Policy

13. The quality of investment policies directly influences the decisions of all investors, be they small or large, domestic or foreign. These policies form the basis of a healthy and attractive business climate. Through the promotion of transparency, non-discrimination and property rights, they can lead to increased investment in the agriculture sector. At the same time, reaping the full benefits of investment in agriculture requires responsible behaviour by both government and investors and effective co-ordination between them. To ensure these benefits, and as part of creating a favourable climate for investment, governments should improve regulatory quality and public sector integrity. This will also boost investor confidence, facilitate business operations and support development efforts.

1.1 What measures has the Government taken to ensure that regulations, legislation and government policies for agricultural investment are transparent, accessible and clear for both foreign and domestic investors?

1.2. To what extent are the administrative requirements for investors in agriculture measured and quantified? What government procedures exist to identify and reduce unnecessary administrative burdens on investors?

1.3 What steps has the Government taken towards the establishment of timely, secure and effective methods of ownership registration for land and other forms of agricultural property like farming equipment?

1.4 Does the level of intellectual property (IP) protection and enforcement mechanisms for developing farming implements like seeds encourage innovation and investment by domestic and foreign firms, including Small and Medium Enterprises (SMEs)?

1.5 Is the system of contract enforcement effective and widely accessible to all investors? What mechanisms for dispute settlement has the Government established to ensure the widest possible scope of investor protection at reasonable cost? Does the Government maintain a policy of timely, adequate, and effective compensation for expropriation consistent with international law?

1.6 Has the Government taken steps to strengthen domestic law covering land and water rights? What are the measures in place to improve the capacity of national and provincial authorities for negotiating contracts and to help them understand the legal provisions embedded in domestic law and the country's rights and obligations under international agreements?

1.7 What public consultation mechanisms and procedures, including prior notification, have been established to improve regulatory quality, thereby enhancing the investment environment? Are consultation mechanisms open to all concerned stakeholders? What mechanisms exist to involve the local communities in negotiating contracts, in particular those related to land leasing and access to natural resources like water?

2. Investment promotion and facilitation

14. Effective investment promotion can serve to highlight profitable investment opportunities, including by identifying relevant local partners and by raising the positive image of the agriculture sector as an investment target.

2.1 What policy strategy has the Government adopted to promote investment in agriculture and supporting industries? Is there a defined strategy to position the country into global agriculture value chains?

2.2. What institution is in charge of investment promotion and facilitation? Has the Government established an investment promotion agency (IPA)? Does the IPA include the agriculture sector in its promotion activities? Is the agency adequately funded, staffed and capable of delivering its mandate?

2.3 What specific measures are applied to promote investment in agriculture? Has the Government identified local value chains with growth potential and has it defined measures to promote these? Does the Government undertake cost-benefit analysis to assess the impact of investment incentives in the sector? Does the IPA have an investor targeting strategy?

2.4 What type of investor-state dialogue mechanism is in place? Does the IPA fulfill any policy advocacy role?

2.5 What steps has the Government taken to promote investment linkages to foster technology and knowledge transfer from investors to local producers and farmers?

Issues addressed:

- *Promoting agriculture as a key sector for domestic and foreign investment*
- *Targeting and attracting responsible investors*
- *Creating and maintaining an effective public-private dialogue*
- *Promoting technology and knowledge transfer to local producers and farmers*

3. Human resource and skills development

15. Education and skills are central to an attractive business environment. Human resource development can make the agriculture sector more attractive for investment, while increasing the ability of local communities to derive the benefits from investment – such as through an increased absorptive capacity of small-scale farmers and local SMEs for new technology and knowledge. A whole array of co-ordinated policies is needed to build a strong human capital base. These range from measures aimed at improving primary and secondary school education, business development service (BDS) provision and vocational as well as technical training, to reforms targeting the tertiary education and research/innovation systems.

3.1 Has the Government established a coherent and comprehensive human resource development (HRD) framework that meets the needs of the agriculture sector and takes into account global value chains as part of its broader development and investment strategies?

3.2 How are the needs of the agricultural sector identified and translated into HRD actions? Are there measures in place to understand the needs of investors for HRD and skills-upgrading?

3.3 What are the provisions for continued learning and vocational training tailored to the needs of the agriculture sector? How does the Government promote training programmes for farmers and local producers? What type of extension services exist for the local producers and farmers?

3.4 Are there special standards, R&D, and metrology institutes? What are their capacities to improve the qualifications of local farmers and producers, with the aim of increasing production for local markets, as well as boosting exports and sales to other countries? Do farmers and companies have easy access to standardization agencies and their services at reasonable costs?

3.5 What measures exist to promote training and mentoring of local farmers and suppliers by investors in agriculture?

Issues addressed:

- *Strengthening the absorptive capacity for technologies and know-how*
- *Improving access to and quality of vocational training, and strengthening local R&D capacity*
- *Promoting skills and technology transfer to local producers and farmers*
- *Improving the attractiveness of studying and working in the agriculture sector*

4. Trade policy

16. Policies relating to trade in goods and services can support more and better quality agricultural investment by expanding opportunities to reap scale economies and by facilitating integration into global supply chains, boosting productivity and rates of return on investment.

4.1 What recent efforts has the Government undertaken in terms of trade facilitation to reduce the compliance costs of customs, as well as regulatory and administrative procedures at the border?

4.2 To what extent do trade and trade-related policies raise the cost of inputs required by agricultural production (including machinery)?

4.3 How does trade policy support and attract investment through measures such as export promotion and export financing?

4.4 Has the Government entered regional trade agreements? What are the most prominent arrangements and how effective are they in increasing market size and access? How does the Government implement its World Trade Organisation (WTO) commitments?

Issues addressed:

- *Access to new technology*
- *Increased market size*
- *Addressing bureaucratic hurdles*
- *Export promotion*

5. Environment

17. While the development of a country's agriculture sector has a strong impact on the environment, good environmental policies contribute to both attracting responsible investors and developing a sustainable agriculture sector. They can help improve not only large-scale farming operations, but also small-scale production methods. Also, given that much of the increase in agriculture-related GHG emissions over the next decades is projected to take place in Africa,⁷ environmental policies will have to factor climate change mitigation and adaptation efforts in the sector.

5.1 How is the interaction between environmental policy and other policy areas framed and co-ordinated? Does the Government, in its quest to boost the competitiveness of the agriculture sector, manifest commitment to environment-friendly production? How is the capacity to manage natural resources at government level strengthened?

5.2 What are the policies to promote access to cleaner technologies for agricultural enterprises in general and small-scale farmers in particular? What are the implementation and support mechanisms?

5.3 How are R&D policies and institutions integrated in the environmental policy of the country?

5.4 How does the Government take into consideration the needs of the agriculture sector in the elaboration of its energy policy?

5.5 Are there any existing mechanisms to mitigate extreme weather events?

Issues addressed:

- *Global environmental challenges, including climate change*
- *Natural resource management*
- *Competitiveness and technological upgrading of small-scale farmers' production methods*
- *Access to markets and clean technologies*
- *Energy policy*

⁷ P.158 , OECD-FAO Agricultural Outlook 2010-2019

6. Responsible business conduct

18. Policies that promote recognised principles for responsible business conduct, such as those recommended in the OECD Guidelines for Multinational Enterprises (MNEs), help attract investments that contribute to sustainable development. This is particularly important in the agriculture sector, which is socially sensitive and plays a central role in allowing governments to fulfil their development objectives.

6.1 What mechanisms are being put in place to promote and enforce core labour standards in agriculture?

6.2 How does the Government make clear for investors the distinction between its own role and responsibilities and those ascribed to the business sector? Does it actively assume its responsibilities (e.g. by effectively enforcing laws on respecting human rights, environmental protection, labour relations and financial accountability)?

6.3 How does the Government communicate expected responsible business conduct in the agriculture sector to investors? How can the Government support companies' efforts to comply with the law?

6.4 Does the Government participate in inter-governmental co-operation in order to promote agreed concepts and principles for responsible business conduct, such as the OECD Guidelines for Multinational Enterprises.

Issues addressed:

- *Strengthening the legal and institutional framework*
- *Promoting good corporate citizenship and responsible business conduct*
- *Protecting fundamental rights and ensuring social as well as economic progress*

7. Infrastructure development

19. Developing agriculture-related infrastructure is an indispensable way to boost productivity, improve incomes and ensure food security. Such infrastructure includes irrigation, used directly in the production process; information communication technology to support farmers' commercial operations; and transportation and storage for the post-harvest phase. However, many African countries face a serious infrastructure deficit in agriculture. Only 3.5% of Africa's agricultural land is equipped for irrigation, which is equivalent to 7 million hectares in only a handful of countries. As a result, cash crops and high-value food crops, which are dependent on irrigation, are not developed to their potential.

20. Disseminating knowledge is another important way of enhancing agricultural growth. Farmers need to be able to access market information and negotiate with suppliers and buyers, making access to information and communication services, such as mobile phones, a necessity. Moreover, all-weather roads are needed to facilitate access to fertile farmlands and forests, link farms to markets, and feed into cross-border corridors and ports to facilitate exports. Improved transport networks like these would make it easier for small-scale subsistence farmers to move into commercial farming and boost their incomes as a result. In the post-harvest stage, adequate systems for storing agricultural produce are essential to avoid losses and waste due to insects, rodents, fires and theft. Such systems should include granaries, silos, pesticides and fumigants from the small-scale farm-level up to national level where grain marketing boards manage the national output. Together, these infrastructure components – irrigation, telecommunications, transportation and storage – can facilitate production and mitigate obstacles that undermine agriculture. Lastly, a sound investment policy for agriculture must consider ways not only to boost physical infrastructure, but also to provide farmers with the requisite skills and tools to make the most of it.

7.1. What measures are in place to ensure coherence across infrastructure, rural development and agricultural policies?

7.2. Does the Government have clear guidelines and transparent procedures for the disbursement of public monies for funding agriculture projects and, if so, do they make provisions for agriculture-related infrastructure?

7.3. How is the Government developing information technology and communications systems to support farming activities?

7.4. What incentives has the Government considered for attracting private investors to develop secondary roads? Are the requirements for all modes of transport regularly reviewed, taking into consideration investor needs and the links between different modes of transport infrastructure?

7.5. Is there an institutional framework for managing water resources, including irrigation systems, and water harvesting and storage technologies?

7.6. What measures has the Government put in place to build storage facilities for agriculture produce? Are there measures to promote private storage activities?

Issues Addressed

- *Public administration's support mechanisms for infrastructure development*
- *Natural resource management*

8. Financial sector development

21. Financial markets contribute to improved economic outcomes by channelling resources to appropriate projects, stimulating savings and investment and minimizing transaction costs. With regard to the development of agricultural activities, a solid financial sector can contribute to providing financial services for agricultural production, targeting large investors as well as local farmers and smaller entrepreneurs through specific agricultural credits.

8.1 How does the regulatory framework contribute to a well functioning financial market for the agriculture sector? What is the current situation regarding collateral requirements? Are the following systems in place: an efficient local cadastre system; a credit information system; a registration system for movable assets?

8.2 What is the state of competition in the banking sector? What are the possibilities for local financing and access to credit?

8.3 Do national and regional capital markets play a role in channelling investment and facilitating the efforts of large and medium-size agribusiness corporations to raise capital? Are there financial instruments for raising funds and mitigating risks?

8.4 Are there geographical differences in terms of access to credit for local farmers and SMEs? How is access to financial services provided for isolated groups in the agriculture sector and what is the role of the microfinance and leasing industries?

8.5 What are the available guarantees and insurances to support local farmers in accessing credits (credit & mutual guarantee schemes)? What models have proven successful in providing guarantees? Are there any instruments (such as export credit guarantee schemes) available to support farmers to enter new regional/international markets?

8.6 What support and business development service (BDS) measures are available to local farmers when applying for credit? Is there any training provision in place and, if so, how is it spread among different towns and regions? Are there any agreements established between public authorities, enterprises and NGOs to develop management skills for local farmers?

Issues addressed:

- *Local financial sector development*
- *Strategies and tools to improve access to finance for local farmers and SMEs*
- *Initiatives to strengthen local farmers and SMEs' capacity in accessing and managing credit*

9. Taxation

21. The 2002 UN Monterrey Consensus recognized taxation's key role in domestic resource mobilisation, an acknowledgement also echoed at the 2008 United Nations Doha Conference on Financing for Development.⁸ It is the main avenue for generating resources for public goods provision, such as infrastructure. Taxation provides a predictable and stable flow of revenue to finance development objectives. At the same time, it is an integral part of any country's investment policy framework, having a direct impact on profits while also providing backbone infrastructure for business development. Governments thus face the challenge of striking the optimal balance between a tax regime that is business and investment friendly, while at the same time leveraging enough revenue for public service delivery – which, in turn, makes economies more attractive to investors. In Africa, agriculture has traditionally been used to generate resources to be transferred to industry, with an adverse effect on agricultural growth. Issues such as import tariffs need to be considered, especially in a context of reliance on foreign inputs, including fertilizers and machinery. Access to such inputs is crucial for local producers' competitiveness. The same applies to export taxes affecting access to regional and global markets. Finally, tax incentives for agricultural investment have to be considered with caution, as the effect of tax breaks and holidays rarely translate to increased investment and technology and knowledge transfer down the agriculture value chain if not accompanied by other reforms to improve the business climate.⁹

9.1 Are the tax policy and administration in line with the Government's agricultural investment objectives? Is the tax burden on agri-business appropriate for these objectives?

9.2 Does the Government have sufficient capacity to develop and implement a transparent and efficient tax policy and administration system? Do tax officials support tax payers, including small-scale producers, in meeting the tax requirements, thereby strengthening the Government's accountability to the community?

9.3 How is taxation administered and co-ordinated between the federal/central and state/local levels? Do the taxes paid by entrepreneurs, producers and investors accrue to local government so as to fund the provision of local public goods – such as basic infrastructure needed for agricultural development?

Issues addressed:

- *Good governance, efficiency, transparency and co-ordination in tax policy and administration*
- *Infrastructure development and public services provision*
- *Domestic resource mobilisation*

⁸ p. 2, http://www.un.org/esa/ffd/doha/draftoutcome/DraftOutcomeDoc_English.pdf

⁹ Chai and Goyal, 2008, <http://www.imf.org/external/pubs/ft/wp/2008/wp08257.pdf>

PART II. ANNOTATIONS TO THE POLICY FRAMEWORK FOR INVESTMENT IN AGRICULTURE

1. Investment policy

1.1 What measures has the Government taken to ensure that regulations, legislation and government policies for agricultural investment are transparent, accessible and clear for both foreign and domestic investors?

22. Transparency and predictability of investment policies are not only important to foreign investors, who are accustomed to dealing with different types of legal systems and therefore value clear-cut policy frameworks. They are also crucial for SMEs in the agriculture sector, as they often face difficulties in tapping into the financial opportunities available through the formal sector of the economy. Also, well-formulated investment policies and measures can reduce transaction costs and make it easier for investors to manage their risks. Some of the ways in which transparency and predictability can be promoted include: government consultations with local and foreign investors; simplification and revision of administrative processes; and publication and dissemination of investment policies.

1.2. To what extent are the administrative requirements for investors in agriculture measured and quantified? What government procedures exist to identify and reduce unnecessary administrative burdens on investors?

23. Results of the “Doing Business” project of the World Bank demonstrate that heavier regulation and excessive “red tape” are associated with higher costs and delays for investors and are also linked to higher levels of corruption among public officials. Yet simplifying rules and procedures is challenging when rapidly evolving environmental conditions (in relation to climate change for instance) or new market trends (such as the arrival of new investors from emerging economies) may call for an update of regulations and more thorough consultation processes. Regulatory Impact Assessments (RIA), which examine the likely benefits, costs and effects of new or changed regulations, including the social and environmental consequences, can also help to pinpoint administrative burdens that might arise, while other investment policy tools can improve coherence and help determine priorities for action. However, in order to achieve the necessary harmony between reform and simplicity, institutional capacity in government agencies at both the national and sub-national levels is vital, as are incentives and standards for good conduct and appropriate enforcement mechanisms. When this harmony is not achieved, the consequences for investment are negative, ranging from decreased respect for the rule of law, misallocation of resources, increased corruption, and uncertainty for investors.

1.3 What steps has the Government taken towards the establishment of timely, secure and effective methods of ownership registration for land and other forms of property like farming equipment?

24. Secure and transferable property rights, especially rights to land, are an important pre-requisite for a healthy investment environment. Well-defined and secure ownership, including effective registration of public and private properties, encourages new investment and makes it more likely that land-owners will maintain and improve their investments. For example, land titles give an incentive to owners to promote

investments that enhance productivity. Property rights, moreover, entitle the investor to participate in the eventual profits that derive from an investment and reduce the risk of fraudulent transactions. Reliable land titling and property registration systems also help individuals and businesses to seek legal redress in cases of violation of property rights and offer a form of collateral that investors can use to access credit (see chapter on financial sector development). Increased access to credit in turn enables informal entrepreneurs to shift to the formal sector.

1.4 Does the level of intellectual property (IP) protection and enforcement mechanisms for developing farming implements like drought-resistant seeds encourage innovation and investment by domestic and foreign firms, including Small and Medium Enterprises (SMEs)?

25. Well-defined IP protection and enforcement mechanisms can encourage innovation derived from agro-research. For example, innovative products, such as new forms of seeds to increase productivity, can only be developed in a context of strict IP protection. Not only would such a protection framework favor local R&D by foreign investors, but it would also provide local businesses with a secure environment to invest in innovation and thus contribute to local entrepreneurship and competitiveness.

1.5 Is the system of contract enforcement effective and widely accessible to all investors? What mechanisms for dispute settlement has the Government established to ensure the widest possible scope of protection at reasonable cost? Does the Government maintain a policy of timely, adequate, and effective compensation for expropriation consistent with international law?

26. Investors' trust in the integrity of the markets is critical because ultimately, it is the possibility of buying and selling assets through market transactions that reveals the value of an asset. To gain investors' trust, there needs to be a legal framework capable of ensuring the enforcement of contracts, the protection of property rights and the fair resolution of disputes – all hallmarks of an efficient market. Confidence in the integrity of markets can also be promoted through the development of alternative dispute settlement procedures, such as arbitration, mediation and conciliation hearings organized by industry bodies or specialised agencies. These are particularly useful options for settling disagreements between transacting parties at a reasonable cost because in many cases, recourse to the judiciary system can be slow and expensive, thereby discouraging potential investors.

27. One of the challenges for governments is balancing expropriation with investor interests. All bilateral investment treaties and recent regional agreements dealing with investment recognise the need for compensation when a government expropriates property.

28. Yet despite the widespread acceptance of the need for timely, adequate and effective compensation, the power of government to expropriate has a negative impact on the investment climate and requires a careful balancing of interests and judgment on the part of policy makers. If a government decides to expropriate land or other agricultural property, this decision ought to serve a public purpose; observe due process of law; be non-discriminatory; and follow transparent rules that define the situations in which expropriations are justified and the process by which the compensation is to be determined.

1.6 Has the Government taken steps to strengthen domestic law covering land and water rights? What are the measures in place to improve the capacity of national and provincial authorities for negotiating contracts as well as understanding the legal provisions embedded in domestic law and the country's rights and obligations under international agreements)?

29. Host governments need to be able to assess the legal implications and development impacts of contracts and agreements that touch upon access to land, water and food. When a country has a weak domestic legal framework covering land and water rights in agriculture, it makes investors' business plans more complicated and investments riskier and may possibly impair a country's development efforts. The international legal framework, through International Investment Agreements (IIAs) for example, provides protection to foreign investors which host country authorities need to be aware of when negotiating contracts. In case of a dispute, the enforcement of the contract rights could be treated as treaty rights, so that should an investment treaty contain an umbrella clause covering contractual obligations, the host state would also have an international obligation to abide by its contractual obligations, the violation of which could substantiate a claim brought by the investor against the state before an international arbitral tribunal.¹⁰ These aspects need to be evaluated carefully by governments, especially in land-leasing contract negotiations. At the same time, investors should comply with application law and participate in good faith in any contracts they sign, such as by disavowing bribery and other corrupt practices. Similarly, they should engage in dialogue with affected communities, thereby avoiding possible implementation disputes and social hostility.

1.7 What public consultation procedures, including prior notification, have been established to improve regulatory quality, thereby enhancing the investment environment? Are consultation mechanisms open to all concerned stakeholders? What mechanisms exist to involve the local communities in negotiating contracts, particularly those related to land leasing and access to natural resources like water?

30. Laws and regulations should be developed in an open and transparent fashion, with appropriate legislative controls and procedures for effective and timely inputs from national and foreign parties. The challenge is often to put in place a regulatory framework that strikes the right balance between promoting business growth, investor confidence and competitiveness on the one hand, while addressing concerns about food security and environmental sustainability on the other hand. Achieving this balance requires consultation between public and private stakeholders, as well as freedom of the media to scrutinise these processes. Other stakeholders could include potential domestic and foreign investors; relevant businesses; farmers; agricultural workers; trade unions; other civil society organisations; wider interest groups; and other parts of government. In order to improve clarity and representativeness in the consultative process, it may be helpful to consult with umbrella organisations and find innovative fora for their participation in decision-making processes (such as mobile communication technologies). However it is also important to consider how those affected by decisions on investment in agriculture (for example, subsistence farmers, processing workers and women) might actively participate in these processes and maximise their benefits while protecting their rights.

¹⁰ The issue of umbrella clauses is discussed in "Interpretation of the Umbrella Clause in Investment Agreements" in *International Investment Law, Understanding Concepts and Tracking Innovations*, OECD (2009).

2. Investment promotion and facilitation

2.1 What policy strategy has the Government adopted to promote investment in agriculture and supporting industries? Is there a defined strategy to position the country into global agriculture value chains?

31. Assigning the agricultural sector a central role in the development agenda is a necessary step towards designing measures that can successfully attract investment in agriculture. Some Asian economies have shown that making agriculture a priority sector (for example through modernising farming and improving access to finance) can boost economic and social development. India's successful cotton-wheat production system is one of many examples of how this kind of prioritisation can work.¹¹ Prioritising agriculture, while positioning the country in a global value chain context, can channel resources into strategic areas and demonstrate commitment to existing and potential investors.

2.2. What institution is in charge of investment promotion and facilitation? Has the Government established an investment promotion agency (IPA)? Does the IPA include the agriculture sector in its promotion activities? Is the agency adequately funded, staffed and capable of delivering its mandate?

32. The establishment of Investment Promotion Agencies (IPAs) can provide a cost-effective opportunity to highlight a country's attractiveness as an investment destination. Also, an IPA can focus on specific priority areas and sectors, such as agriculture, and can act as a liaison between different government actors, concerned institutions and interested investors.

33. There is well documented best practice for IPA activities that governments can consult to boost their investment promotion activities. This helps governments target effective measures while avoiding costly mistakes.

2.3 What specific measures are applied to promote investment in agriculture? Has the Government identified local value chains with growth potential and has it defined measures to promote these? Does the Government undertake cost-benefit analysis to assess the impact of investment incentives in the sector? Does the IPA have an investor targeting strategy?

34. Measures to promote investment in agriculture can include specific incentives, such as tax holidays, to encourage investors to target the agricultural sector. However, the effectiveness of such measures in attracting investment has not been conclusively demonstrated. They can also reduce the government's ability to mobilize domestic resources for development purposes, while their implementation raises administrative costs. Governments should thus carry out regular impact assessments of investment incentives to evaluate their actual social and economic benefits. They might conclude that modern, well-run infrastructure, strong intellectual property rights and business-friendly regulations have a stronger impact on investment attractiveness.

¹¹ http://www.apaari.org/wp-content/uploads/2009/05/ss_2008_02.pdf

35. Certain governments can also target – notably through IPAs – specific investors that they consider valuable for their development objectives. This could be a relevant strategy for the agriculture sector, where certain companies have operational profiles that fit a country’s development agenda. IPAs can pay special attention to investors involved in mutually beneficial partnerships with small-scale farmers, which can take the form of out-grower schemes, contract farming or joint share equity schemes. Through such partnerships, investors can provide expertise and support to agro-processing as well as access to markets.¹²

2.4 What type of investor-state dialogue mechanism is in place? Does the IPA fulfill any policy advocacy role?

36. One important aspect of developing a sound and business-friendly investment climate in order to attract investors is to receive regular feedback from investors and to provide quick and accurate responses to their queries. Active communication channels can be key inputs for a healthy investment environment in agriculture.

37. IPAs can play an important role in facilitating effective communication between investors and the government. As the interlocutor between the government and investors, the IPA is often the main source of feedback to policymakers on the concerns of investors. Conversely, through its regular contacts with government agencies, the IPA can be an effective communication channel for investors on government activities that have an impact on the business climate.

38. Such interactions can take many forms. For instance, an IPA can act as a useful facilitator, by matching foreign investors with local entrepreneurs, hosting a database of business opportunities, and advocating policies. All of these functions require in-house technical and managerial capacity, including a qualified staff with relevant business experience in sector specific activities.

39. In some cases, IPAs themselves can have a more sector-oriented focus. For agriculture, one example is the Tunisian Agricultural Investment Promotion Agency.¹³

2.5 What steps has the Government taken to promote investment linkages to foster technology and knowledge transfer from investors to local producers and farmers?

40. The recognized benefits from investment, especially FDI, include technology and knowledge transfer to the local economy. However, these benefits do not materialize automatically. Certain measures have to be in place to motivate the investors to involve local partners and suppliers, while ensuring that the local suppliers – often SMEs – are partnership ready. SME promotion measures for technical upgrading and access to finance can help local suppliers to embark on larger projects and innovate. Hence, investor-SME linkages can only be an avenue for technology and knowledge transfer if the SMEs have sufficient absorptive capacity. This issue will be analysed in more detail in the following chapter on human resources and skills development.

41. An IPA can be well-placed to promote such linkages. For example, an IPA can help investors find suitable partners, while also transmitting local suppliers’ needs to relevant public authorities and institutions.

¹² <http://ifad-un.blogspot.com/2010/06/responding-to-land-grabbing-and.html>

¹³ <http://www.tunisie.com/APIA/>

3. Human resource and skills development

3.1 Has the Government established a coherent and comprehensive human resource development (HRD) framework that meets the needs of the agriculture sector and takes into account global value chains as part of its broader development and investment strategies?

42. HRD policies cover numerous dimensions, from general education and professional skills to health. These policies should be closely aligned with the investment and development strategies at national level (see the chapter on investment policy), and thus need to be addressed through a coherent and comprehensive strategy that takes full account of the policy linkages and national implementation capacity.

3.2 How are the needs of the agricultural sector identified and translated into HRD actions? Are there measures in place to understand the needs of investors for HRD and skills-upgrading?

43. The obstacles to sustainable development through investment in agriculture have to be carefully identified before HRD measures can be developed to tackle them. For example, a group of farmers may be skilled and able to produce according to certain standards requested by investors. Yet, if they are unaware of what investors need, because of poor business development services (BDS), then their skills will not be used effectively. It is also important to identify investors' needs for local sourcing: for example, this might allow farmers to obtain the necessary training and upgrading from specialised BDS providers, or simply apply the right type of inputs (such as phytosanitary products) in their production processes and eventually become suppliers.

3.3 What are the provisions for continued learning and vocational training tailored to the needs of the agriculture sector? How does the Government promote training programmes for farmers and local producers? What type of extension services exist for the local producers and farmers?

44. Training and skills improvement efforts can include measures such as creating or strengthening training institutes for agriculture, developing extension services to farmers for specific needs, as well as providing farmers with valuable market information. For instance, there are documented cases where small-scale farmers are not aware of the final price of their products once they reach local or export markets. Such information is crucial for farmers' associations and co-operatives in strengthening their bargaining positions vis-à-vis buyers and investors. For example, in Uganda, it is estimated that a training project on ICT use increased farmers' rates of return by 5-15% through allowing them to better access prices and other key market information.¹⁴

3.4 Are there special standards, R&D, and metrology institutes? What are their capacities to improve the qualifications of local farmers and producers, with the aim of increasing production for local markets, as well as to boosting exports and sales to other countries? Do farmers and companies have easy access to standardization agencies and their services at reasonable costs?

¹⁴ P.62, "If words were food, nobody would go hungry", The Economist, Nov. 21-27th edition, 2009

45. Specialised institutes have an important role in filling the R&D and innovation gaps in the agriculture sector. The Tea Research Institute in Sri Lanka is one example of a well-staffed institute that provides the needed technical inputs for Sri Lanka's tea production, which has successfully established its brand in the global product market.¹⁵ In terms of standards, specialised services are needed to train farmers in global standards that are required to enter and remain competitive in global markets.¹⁶

3.5 What measures exist to promote training and mentoring of local farmers and suppliers by investors in agriculture?

46. In order to ensure quality inputs into their supply chains, investors often have to undertake training and mentoring activities for their supplying farmers and SMEs. This also includes assisting them in acquiring new technology to be able to comply with sanitary-phytosanitary standards (SPS), fertilisation methods, and sometimes financing requirements. In addition, global reputational pressure on investors has led to responsible corporate behaviour and attention to local communities' well-being as a key dimension of global competitiveness.¹⁷ Many Multi-National Enterprises (MNEs) support their suppliers – in this case farmers – through different training schemes, driven by the importance of maintaining a positive image while maximising profits. Government policies can play an important role in promoting measures, such as out-grower schemes, which present strong incentives for investors to endow their suppliers with new skills and technology, resulting in more competitive local partners.

4. Trade policy

4.1 What recent efforts has the Government undertaken in terms of trade facilitation to reduce the compliance costs of customs, as well as regulatory and administrative procedures at the border?

47. When custom procedures do not conform to internationally recognized standards, it can lead to delays in cross-border deliveries and increased business costs. These problems make it harder to harness efficiency gains from global supply chains, lowering rates of return and discouraging investment. Border delays become even more crucial in the agriculture sector where products are perishable (see the chapter on infrastructure development). Custom delays, moreover, have an overall negative impact on the business climate.

4.2 To what extent do trade policies and trade-related raise the cost of inputs required by agricultural production (including machinery)?

¹⁵ Ceylon tea and its Lion logo were developed by the Sri Lanka tea board.

¹⁶ OECD (2004), *Addressing market access concerns of developing countries arising from environmental and health requirements*, Paris.

¹⁷ Industry Canada, http://www.ic.gc.ca/eic/site/csr-rse.nsf/eng/h_rs00100.html

48. A large proportion of international trade involves business to business transactions. Modern supply chains involve hundreds of domestic and international producers. Trade policies that hinder access to intermediate goods and services, and which raise their cost, can hold back this process. This hindrance becomes even more important in the context of the WTO obligations from the Agreement on Trade-Related Investment Measures (TRIMs), which prohibit government measures that oblige local sourcing. Machinery and other inputs (see the chapter on human resources development) must also be imported at reasonable cost – necessitating an efficient tariff regime.

4.3 How does trade policy support and attract investment through measures such as export promotion and export financing?

49. While home countries (origin of foreign investment) can promote trade in case of market failures at the host country level, such as through export credit guarantees, host governments have a number of policy options available. For instance, the promotion of exports through export financing and technical assistance for local suppliers to meet global standards can prove to be useful measures. These are not only important to increase the attractiveness of the host country as an investment destination (by strengthening the agricultural supply base – see the chapters on investment promotion and human resource development), but also to strengthen the trading capacity of local farmers and entrepreneurs.

4.4 Has the Government entered regional trade agreements? What are the most prominent arrangements and how effective are they in increasing market size and access? How does the Government implement its WTO commitments?

50. Developing regional markets is a vital element in increasing trade in Africa's agriculture sector. Numerous regional initiatives have been able to open opportunities in this regard, such as the East African Community and the common external tariff of the West African Economic and Monetary Union.¹⁸ Such arrangements can increase intra-African trading – which today accounts for less than 10% of African countries' external trade – and can thus contribute to boosting investments.

5. Environment

5.1 How is the interaction between environmental policy and other policy areas framed and co-ordinated? Does the Government, in its quest to boost the competitiveness of the agriculture sector, manifest a strong commitment to environment-friendly production? How is the capacity to manage natural resources and prioritise decisions at government level strengthened?

51. Mainstreaming environmental issues in growth strategies for resource-intensive sectors, such as agriculture and fisheries, is key to not only protecting the environment, but also maximising economic returns on investment. Resource mismanagement has a cost to society and the economy as a whole and can even lead to the depletion of natural resources that play a pivotal role for the livelihoods of entire communities and, sometimes, countries. For this reason, natural resource management needs to be closely co-ordinated with policies aiming to increase investment in agriculture.

¹⁸ UEMOA-WAEMU

52. In addition, the effects of climate change on Africa's agriculture – from more erratic rainfall that adversely affects rain-fed farming¹⁹ to extreme weather events that can damage the agricultural produce – require adaptation efforts that concern several policy areas, including environmental, as well as investment and agricultural policies. Sustaining the growth potential of Africa's agriculture will also entail co-ordinating these efforts on the part of various policy communities.

5.2 What are the policies to promote access to cleaner technologies for agricultural enterprises in general and small-scale farmers in particular? What are the implementation and support mechanisms?

53. Bringing down trade barriers (see Chapter on trade policy) to allow access to cleaner technologies is an important challenge for governments to tackle, in order to increase local agriculture competitiveness and improve the environmental sustainability of productive activities. Attracting and promoting investors experienced in using cleaner technologies can also support governments' efforts in this regard (see the chapter on investment promotion). These efforts, however, need to be accompanied by measures to increase the capacity of small-scale farmers and SMEs to absorb the new technology (see the chapter on human resource development). They also need to be aligned with policies which take into account priorities for environmental resource management, so that crucial sectors, such as water, receive adequate attention.

5.3 How are R&D policies and institutions integrated in the environmental policy of the country?

54. For the above measures to be effective, R&D institutions need to be aligned with environmental policies, as these institutions are crucial for supporting local actors in adapting to cleaner production technologies. At the same time, they have a crucial role to play in the use of meteorology and rain-forecasting techniques for the development of the sector. Also, they can help in improving the extension services provided to farmers to promote multi-cropping (and to replace monoculture), thus contributing to more balanced ecological systems as well as reducing farmers' reliance on single crops.

5.4 How does the Government take into consideration the needs of the agriculture sector in the elaboration of its energy policy?

55. Strengthening the agriculture sector in a responsible and sustainable manner, especially in the areas of production, transformation and commercialisation, requires a coherent energy policy that takes the sector's needs into account. This is important because agriculture development relies heavily on storage, transport and trade in national, regional and global markets. The sustainable use of energy in cold chain systems, for example, is a recurrent topic in the debate on boosting the transformation and commercialisation of agricultural produce.

5.5 Are there existing mechanisms to mitigate extreme weather events?

¹⁹ Only 3.5% of African arable land is actually irrigated.

56. As African agriculture is mostly rain fed, it is also particularly vulnerable to environmental risks, from erratic rainfall to droughts and floods. Risk mitigation instruments can therefore play an important role in supporting farmers to address such risks. Business development services can direct them towards the instruments that are best suited to their needs. Development partners have created some products that are particularly suited to the needs of African small-scale farmers. The World Bank and the International Finance Corporation (IFC) pioneered weather insurance – insurance that makes payouts on the basis of objective indices such as rainfall or temperature. Since then, private and public insurance companies in India and Africa have insured more than 2 million farmers against weather risks.²⁰

6. Responsible business conduct

6.1 What mechanisms are being put in place to promote and enforce core labour standards in agriculture?

57. Core labour standards relate to fundamental principles and basic human rights in the workforce and are distinct from labour standards regarding work conditions and employment protection laws. Specifically, they aim to eliminate all forms of forced or compulsory labour, to abolish child labour, to uphold the principle of non-discrimination in respect of employment and occupation and to ensure the freedom of association and the right to collective bargaining. This is especially important in the context of farmers' co-operatives. These core labour standards are a key element in the healthy functioning of market economies and help to create a level playing field for all investors – foreign and domestic, small and large. They also improve economic performance, in part because they improve skills (as highlighted in the chapter on human resource development), as well as provide incentives for the younger generation to accumulate human capital. Most countries have ratified the ILO core labour standard conventions, but compliance with, and enforcement of, the standards is uneven across countries. In some cases, such as within special export processing zones, governments deliberately waive components of the core labour standards for fear that their existence may deter investment.

58. However, there is no unequivocal empirical support for this concern. Indeed, Multi-National Enterprises (MNEs) are more likely to invest in countries with stricter safeguards and enforcement of basic human and worker rights than in those countries where such rights are absent or poorly enforced. In short, there is a need to raise awareness of the problems associated with low compliance with core labour standards and to promote tools that foster responsible business practices, such as the *OECD Guidelines for Multinational Enterprises*.

6.2 How does the Government make clear for investors the distinction between its own role and responsibilities and those ascribed to the business sector? Does it actively assume its responsibilities (e.g. by effectively enforcing laws on respecting human rights, environmental protection, labour relations and financial accountability)?

59. The core mission of business is to identify and manage investment projects that yield competitive returns to suppliers of capital. In fulfilling this core function, business must however behave responsibly and comply with legal and regulatory requirements. In addition, it needs to be sensitive to societal expectations that might be communicated through channels other than the law. The role of governments is to look after the collective interests of their citizens. As part of this role, they work with companies, trade

²⁰ World Bank (2009), *Innovative Finance for Development Solutions*, Washington DC

unions and other civil society organisations to create enabling environments for responsible business conduct. This is especially important for the agriculture sector in Africa, which affects large proportions of the population and has important social implications.

60. Creating an enabling environment can include a clearly communicated distinction between the respective roles and responsibilities of government and business. This would reduce uncertainty over expectations concerning responsible business conduct, thus encouraging investment, and allowing private and public sector actors to play mutually-supportive roles in enhancing economic, social and environmental well-being.

6.3 How does the Government communicate expected responsible business conduct in the agriculture sector to investors? How can the Government support companies' efforts to comply with the law?

61. Law-making is the key channel for communicating societal expectations to companies, but it is not the only one. Communication on expectations about how companies should conduct themselves can also come from discussions and disputes within the workplace, consultations with local communities, negotiations with trade unions, as well as through discussions with investors, dialogue with civil society organisations, media reporting, and so forth.

62. Government-backed instruments for responsible business conduct are also important for communicating with business. Governments need to give special consideration to small- and medium-sized enterprises engaged in agriculture, as they may not have the same capacities as larger enterprises to adhere to certain policies but represent key drivers of responsible business conduct.

63. Governments can facilitate and motivate companies' efforts to comply with laws by seeking out companies' views on laws and enforcement practices. They can also provide conciliation and ombudsman facilities so that investors and others have the means to complain about government decisions that they believe are unjust. In the United States, for example, there are many examples of agriculture ombudsman programmes, which provide key liaison channels between government and the private sector.²¹ In addition, governments can acknowledge and support private initiatives to enhance compliance by providing guidance on appropriate compliance management practices.

6.4 Does the Government participate in inter-governmental co-operation in order to promote agreed concepts and principles for responsible business conduct, such as the OECD Guidelines for Multinational Enterprises?

64. Governments are co-operating with each other and with other actors to strengthen the international legal and policy framework in which business is conducted. Multilateral instruments dealing with responsible business conduct, such as the *OECD Guidelines for Multinational Enterprises*, the International Labour Organization (ILO) *Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policies* and the United Nations *Global Compact*, draw on a broader framework of international declarations and conventions. They communicate and promote agreed concepts and principles for appropriate business conduct. Increased global acceptance of common principles for business conduct also helps to reduce the likelihood that observing appropriate responsible business conduct principles could become a competitive disadvantage for investors.

²¹ <http://www.agombudsman.com/>

7. Infrastructure development

7.1. What measures are in place to ensure coherence across infrastructure, rural development and agricultural policies?

65. Many African countries have policies in place for infrastructure, agriculture and rural development but they are not necessarily well-co-ordinated. Co-ordination is important because of the long value chain involved in agriculture, where farming takes place in rural areas but sales and distribution run the national gamut and even cross borders. It is therefore critical for all the institutions along this chain to co-ordinate their efforts, especially given cross-cutting policy efforts such as rural development and infrastructure building, which have direct impacts on agriculture.

7.2. Does the Government have clear guidelines and transparent procedures for the disbursement of public monies for funding agriculture projects and, if so, do they make provisions for agriculture-related infrastructure?

66. As a general trend, public investment in Africa's agriculture is quite low and public financial management is not necessarily efficient. Governments could increase their investment in the agriculture sector while also ensuring that public funds are disbursed efficiently to meet agriculture infrastructure needs.

67. In addition, during the signing of land deals (acquisitions or concessions), international investors sometimes commit to invest more broadly in the economy, through infrastructure development or employment creation. Governments should thus consider systematic procedures to ensure that public and private funds for agriculture are also ear-marked for its associated infrastructure.

7.3. How is the Government developing information technology and communications systems to support farming activities?

68. Information and communications technologies are an important component of farming activities. Mobile phones, for instance, support agriculture marketing by allowing farmers to find information about crop prices, make cashless transactions and conduct business that would otherwise have required them to travel long distances. Governments can work with private operators to provide handsets for farmers in rural areas, subsidise air-time, or revise regulations to ensure that phone operators charge fair tariffs. In addition, early warning systems, including crop forecasts and rainfall and other meteorological data, need to be developed so that agricultural production is not adversely affected by extreme weather events. This is especially important in Africa where 94% of the agriculture is rain-fed; and it becomes even more so as climate change threatens to lead to more erratic rainfall.

7.4. What incentives has the Government considered for attracting private investors to develop secondary roads? Are the requirements for all modes of transport regularly reviewed, taking into consideration investor needs and the links between different modes of transport infrastructure?

69. Agricultural produce makes up a significant portion of Africa's trade exports, making a good transport network an important part of supporting trade in agricultural goods. Secondary roads are important because agriculture takes place in remote, rural areas, which often are not connected to other transport nodes that facilitate trade and commerce, such as airports, international rail and road corridors, and seaports. Transport is also an important element in the value chain, allowing small- to middle-scale farmers in remote areas to transport their goods to processing plants in urban areas.

7.5. Is there an institutional framework for managing water resources, including irrigation systems and water harvesting and storage technologies?

70. Many African countries are dependent on rain-fed agriculture but face chronic water shortages due to droughts or geographical constraints, such as being land-locked. It is therefore important to have an agricultural water development strategy in place to develop irrigation schemes and water harvesting technologies. Because of weak resources for developing such infrastructure, governments should consider ways to make the most of private sector investment in agriculture, by offering incentives for investors to construct and maintain irrigation infrastructure as part of land acquisition deals or concessions, for example. Another option involves making use of existing water supplies by taking a portion of funds from water user charges to subsidise irrigation systems.

7.6. What measures has the Government put in place to build storage facilities for agriculture produce? Are there measures to promote private storage activities?

71. Small-scale farmers often use rudimentary storage facilities and equipment, leading to post-harvest losses and waste. More appropriate facilities include barns, silos, refrigeration units and warehouses on site, and strategic grain reserves at a bigger scale for national needs. Not only is storage a good tool to ensure food security in lean times, but it also has economic benefits because farmers can earn more through reduced losses and more systematic product delivery to markets.

8. Financial sector development

8.1 How does the regulatory framework contribute to a well functioning financial market for the agriculture sector? What is the current situation regarding collateral requirements? Are the following systems in place: an efficient local cadastre system; a credit information system; a registration system for movable assets?

72. Two major challenges must be addressed in order to make lending transactions function smoothly for the agriculture sector. The first concerns the role of information in facilitating transactions. More and better information about borrowers can diminish the risk of default by reducing information asymmetry between lender and borrower. The second draws on the importance of collateral and creditor rights in lending. On the supply side, reluctance to lend can be reduced if lenders have transparency on the type and value of collateral and the necessary legal security to seize it in case of default. On the demand side, clear rules for permissible types of collateral and an accessible registration system can also boost private credit by protecting borrowers from excessive red tape or legal requirements and by simplifying the rules for collateralizing assets. An accurate, comprehensive and accessible cadastre and land registration system is therefore critical for collateral and access to finance more broadly. In addition, while immovable assets – land and buildings – are the most common form of collateral, more loans might be secured by weaker

borrowers if movable assets are also an accepted form of collateral. One solution is to establish a registry for movable assets that provides the necessary transparency and legal security for the collateral offered by loan applicants.

8.2 What is the state of competition in the banking sector? What are the possibilities for local financing and access to credit?

73. The banking sector must improve the acquisition of financial information and lower transaction costs, as well as allocate credit efficiently. One key benchmark for measuring banks' efficiency is the status of competition in the sector. A highly concentrated banking sector might result in lack of competitive pressure to attract savings and channel them efficiently to investors. An additional and important measure of banking sector efficiency is the sector's outreach to different segments of the economy and the population. Since access to banking is difficult for remote and small-scale farmers, they may require specific financing schemes.

74. Common features of the African banking landscape are: the limited number of large commercial banks with high liquidity; a relatively high interest rate spread; and a general lack of customized and diversified financing schemes and products. Hence, there is often a lack of competition, and limited opportunities for local financing and access to capital. This hampers both large investors (foreign and local) who have to seek capital abroad to finance their operations, and medium-sized local enterprises in need of customized financing and credit lines. And it becomes even more complex for small-scale farmers, who are vital for the development of the sector. Enhancing the role of competition in the banking sector may thus be an important step towards removing barriers to the expansion of private credit for agricultural investment.²²

8.3 Do national and regional capital markets play a role in channelling investment and facilitating the efforts of large and medium-size agribusiness corporations to raise capital? Are there financial instruments for raising funds and mitigating risks?

75. Capital markets are the place where providers and users of funds interact without bank mediation. Transparent and liquid capital markets act as an important financing channel for both the corporate sector and governments by allowing institutional and retail investors to steer their funds to the use they deem most appropriate. With regard to the agricultural sector, there are obvious advantages that capital markets can offer such as: (i) mechanisms for listing and raising capital that may restructure and modernise agricultural enterprises and contribute to creating competitive value chains; (ii) trading products, such as futures and other derivatives, for capital management risk²³; and (iii) information tools providing commodities-specific information services that empower industry participants to manage their price risk. In Africa, stock markets are for the most part not sufficiently large or developed to cater to the region's financial needs. Moreover, many African markets are still immature and market capitalisation is mostly dominated by a few firms.

76. However, automation of trading systems, regional integration efforts (as evidenced by the existing West African Regional Stock Exchange and the future East Africa Stock Exchange) and increased primary market activity could boost the size and liquidity of capital markets in the near future.

²² P. 40, OECD Agricultural Policies in Emerging Economies: Monitoring and Evaluation

²³ Such as the unsubsidized index based weather insurance in Malawi.

8.4 Are there geographical differences in terms of access to credit for local farmers and SMEs? How is access to financial services provided for isolated groups in the agriculture sector and what is the role of the microfinance and leasing industries?

77. Extending financing opportunities to local farmers and SMEs, thus allowing them to produce, innovate and invest, is vital to the growth of the agriculture sector in Africa. Nevertheless, commercial banks tend to follow a profit model that implies tight ties to businesses and consumer groups, i.e. a stronger presence in urban areas (see question 8.2). As a result, physical access to banking services in rural areas is often hampered by long distances to the nearest bank outlet. One of the potential solutions to this problem is micro-finance, an increasingly important and growing sector targeting small business owners unable to access more institutionalised sources of finance. Micro-finance may be particularly important in rural areas where banking facilities are not widespread.

78. The development of an active financial sector benefits from the presence of both banks and non-bank players as this allows for greater innovation and coverage. Regulation should therefore not favour the development of one sort of institution over the other. Moreover, as micro-finance institutions (MFIs) are often small, the cost of stringent regulatory standards can dramatically hamper their development. Therefore, policies should aim at ensuring that MFIs have sufficient capabilities and limiting systemic risk while keeping burdens on non-bank MFIs low and avoiding regulatory market distortions.

79. Leasing is another option to broaden access to finance for farmers while helping to mechanise agriculture in Africa. Leasing can ease access to finance since collateral is not necessary (because ownership remains with the lessor) and leasing contracts can be agreed to without considering credit histories. There are advantages on the supply side as well: asset ownership remains with lessors, and therefore problems with creditors' rights do not pose the same inconvenience as in the loan market. African governments may foster leasing markets not only through the design and implementation of a legal framework, but also by promoting capacity building and education in the leasing industry.

8.5 What are the available guarantees and insurances to support local farmers in accessing credits (credit & mutual guarantee schemes)? What models have proven successful in providing guarantees? Are there any instruments (such as export credit guarantee schemes) available to support farmers to enter new regional/international markets?

80. Small-scale farmers in Africa are perceived as risky clients by financial institutions for numerous reasons including their exposure to climate uncertainties that influence their production, and thus repayment rates of credit.

81. Guarantees and insurance are thus important parts of the credit cycle for farmers who cannot afford to provide the required collateral for obtaining credit. The term "guarantee schemes" refers to several different, but related, private sector arrangements and government institutions. Whatever their characteristics, all credit guarantee schemes are risk-mitigating tools, in which the bilateral relationship between lender and borrower is extended to include a third party, the guarantor.

82. The goal of guarantee schemes is to widen access to credit for small enterprises and export-oriented business, since they are considered particularly risky and therefore underserved. The case for risk-sharing mechanisms, backed by guarantee schemes, rests on two main arguments. First, depending on the

institutional setup of the schemes, they usually alleviate information asymmetry. By accepting to endorse a bank loan application, the guarantor signals confidence, presumably based on better knowledge of the project, about the risk of a proposed transaction. Therefore, by means of additional vetting, the guarantor helps redirect funds to market segments that are typically underserved by the lending industry.²⁴ Banks therefore might extend loans that they would not have granted otherwise. Second, since guarantee schemes do not replace the lender, they are a useful tool to increase market efficiency: with a relatively limited commitment of funds, a guarantee scheme can leverage a much larger amount of funds from credit institutions by modifying their lending decisions.

83. Compared to other parts of the world, including Asia and Latin America, African farmers find it difficult to obtain guarantees or insurance. Although traditional schemes have suffered weaknesses in the African context, different models have been developed to support farmers' access to credits. These include investors providing guarantees to banks for farmers who are part of their out-grower schemes. Another option is fostering the development of Mutual Guarantee Associations (MGAs) which have the same overall purpose as credit guarantee schemes. In order to widen access to finance, MGAs leverage the shared knowledge and peer pressure among entrepreneurs in a given industry or regional cluster. Members of an MGA collectively underwrite a loan by one of its members, which can have the following advantages: firstly, risk is spread among all member companies of an MGA; secondly, the borrower's peers may be able to assess the risk of a loan better than a bank given their proximity (regional or industry); and, thirdly, peer pressure may reinforce borrower discipline, since default has collective consequences for peers.

8.6 What support and business development service (BDS) measures are available to local farmers when applying for credit? Is there any training provision in place and, if so, how is it spread among different towns and regions? Are there any agreements established between public authorities, enterprise and NGOs to develop management skills for local farmers?

84. Difficulties of access to finance do not only represent a supply-side issue, but also include the demand-side of the market. In some cases, entrepreneurs and farmers could be reluctant to dilute their ownership or cede a share of control to equity investors (and instead try to borrow or accept limits to the firm's growth). But the most serious problem is the investment readiness of small entrepreneurs and farmers who are usually not able to evaluate the available funding options and to understand the concerns and needs of investors and bankers, which is essential to obtain credit or equity capital. Therefore, working on the demand-side through continuous upgrading of knowledge and skills, while improving conditions on the supply-side, is key to overall progress.

²⁴ That includes SMEs for public credit guarantees schemes and mutual guarantee associations and foreign clients or exporting businesses with high risk profiles.

9. Taxation

9.1 Are the tax policy and administration in line with the Government's agricultural investment objectives? Is the tax burden on agri-business appropriate for these objectives?

85. How much tax revenue governments raise depends on their broader objectives, including their investment promotion strategies (see chapters on investment policy and investment promotion). Establishing the right environment for business in any sector, including agriculture, to flourish will inevitably be achieved through a tax policy that results in an acceptable tax burden for businesses to operate. However, fiscal incentives for investors in agriculture have to be used carefully. In fact, investors are generally willing to accept a higher tax burden in exchange for more attractive risk/return opportunities. Governments should thus focus on certainty and consistency of tax treatment, the avoidance of double taxation, and efficient tax administration, all of which are important considerations for business.

86. These measures have to be considered against the backdrop of the Comprehensive Africa Agriculture Development Program (CAADP) directives, which include a commitment from African governments to increase their public investment in agriculture to 10% of their national budgets to reach an agricultural growth rate of 6% by 2015.²⁵ Governments thus have to find an optimal tax mix that minimises the tax burden, while providing the resources necessary to fund development objectives.

9.2 Does the Government have sufficient capacity to develop and implement a transparent and efficient tax policy and administration system? Do tax officials support tax payers, including small-scale producers, in meeting the tax requirements, thereby strengthening the Government's accountability to the community?

87. Taxation can act as a bridge between governments and their citizens, in that transparent implementation of a well-designed tax policy can enhance the credibility and accountability of the public sector vis-à-vis its citizens and the business community. However, achieving this result strongly depends on the Government's capacity to design and implement tax policies efficiently and in a transparent manner. Bribery and other corrupt tax practices are considered to be major impediments to generating a sound business climate, by increasing transaction costs and distorting competitive conditions.²⁶

88. To address these problems, the capacity for efficient tax collection should go beyond good governance standards to also supporting taxpayers with an aim to reduce the tax burden. Such measures involve simplification of tax payments, as well as instructing businesses on how to handle tax filing and documentation. For example, a major challenge for proper tax collection in agriculture in Africa is that small-scale producers often operate within the informal sector and sometimes lack the necessary records, such as documentation for their purchases of inputs.

²⁵ NEPAD-CAADP, <http://www.nepad-caadp.net/about-caadp.php>

²⁶ OECD, p. 5. OECD Bribery awareness handbook for tax examiners, www.oecd.org/dataoecd/20/20/37131825.pdf

9.3 How is taxation administered and co-ordinated between the federal/central and state/local levels? Do the taxes paid by entrepreneurs, producers and investors accrue to local government so as to fund the provision of local public goods – such as basic infrastructure needed for agricultural development?²⁷

89. Policy co-ordination between central/federal and state/local governments is crucial for efficient and transparent taxation. Local tax administrations need to be strengthened and their rights and obligations should be clearly stated by law. Policy co-ordination and harmonisation by the central tax administration and government clearly helps in avoiding inconsistencies and overlaps in the tax system.²⁸

90. At the same time, local government needs to be able to tap the national and local tax revenues pool in order to provide public goods and services at local level. This ability is crucial to develop infrastructure in rural areas, and thus improve the transport and transit conditions for agricultural produce for example. However, these elements need to be well co-ordinated, in addition to complementary policies aimed at strengthening local tax administrations' capacities, as well as local government's capacity for policy implementation.

²⁷ UNCTAD, http://www.unctad.org/en/docs/ciicrp3_en.pdf

²⁸ P.117, OECD, African Economic Outlook 2010

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