Outsourcing's third wave

Buying farmland abroad

May 21st 2009
From *The Economist* print edition
http://www.economist.com/world/international/displayStory.cfm?story_id=13692889

Rich food importers are acquiring vast tracts of poor countries' farmland. Is this beneficial foreign investment or neocolonialism?

A: Other deals (area unknown)

Target	Investor	Deal type/value
Cambodia	Kuwait	Land for rice
China	United States *(Goldman Sachs)*	\$450m-500m, poultry and pigs
Ethiopia	India	\$4bn
	UK *(Sun Biofuels)*	Jatropha
	Saudi investors	\$100m
Malawi	Djibouti	unknown
Mozambique	UK *(Sun Biofuels)*	Jatropha
Sudan	Egypt	Wheat (2m tonnes pa)
	Kuwait	"Giant" strategic partnership
	Qatar	Joint holding firm
Turkey	Bahrain *(Agricapital)*	\$500m (may rise to \$3bn-6bn)

B: Failed deals

Target	Investor	Size of deal
Mozambique	China	\$800m
Philippines	China	1.24m ha
Indonesia	Saudi Arabia *(Saudi Binladin Group)*	0.50m ha
Madagascar	South Korea *(Daewoo)*	1.30m ha

EARLY this year, the king of Saudi Arabia held a ceremony to receive a batch of rice, part of the first crop to be produced under something called the King Abdullah initiative for Saudi agricultural investment abroad. It had been grown in Ethiopia, where a group of Saudi investors is spending \$100m to raise wheat, barley and rice on land leased to them by the government. The investors are exempt from tax in the first few years and may export the entire crop back home. Meanwhile, the World Food Programme (WFP) is spending almost the same amount as the investors (\$116m) providing 230,000 tonnes of food aid between 2007 and 2011 to the 4.6m Ethiopians it thinks are threatened by hunger and malnutrition.

The Saudi programme is an example of a powerful but contentious trend sweeping the poor world: countries that export capital but import food are outsourcing farm production to countries

that need capital but have land to spare. Instead of buying food on world markets, governments and politically influential companies buy or lease farmland abroad, grow the crops there and ship them back.

Supporters of such deals argue they provide new seeds, techniques and money for agriculture, the basis of poor countries' economies, which has suffered from disastrous underinvestment for decades. Opponents call the projects "land grabs", claim the farms will be insulated from host countries and argue that poor farmers will be pushed off land they have farmed for generations. What is unquestionable is that the projects are large, risky and controversial. In Madagascar they contributed to the overthrow of a government.

Investment in foreign farms is not new. After the collapse of the Soviet Union in 1991 foreign investors rushed to snap up former state-owned and collective farms. Before that there were famous—indeed notorious—examples of European attempts to set up flagship farms in ex-colonies, such as Britain's ill-fated attempt in the 1940s to turn tracts of southern Tanzania into a limitless peanut prairie (the southern Tanganyika groundnut scheme). The phrase "banana republics" originally referred to servile dictatorships running countries whose economies were dominated by foreign-owned fruit plantations.

But several things about the current fashion are new. One is its scale. A big land deal used to be around 100,000 hectares (240,000 acres). Now the largest ones are many times that. In Sudan alone, South Korea has signed deals for 690,000 hectares, the United Arab Emirates (UAE) for 400,000 hectares and Egypt has secured a similar deal to grow wheat. An official in Sudan says his country will set aside for Arab governments roughly a fifth of the cultivated land in Africa's largest country (traditionally known as the breadbasket of the Arab world).

It is not just Gulf states that are buying up farms. China secured the right to grow palm oil for biofuel on 2.8m hectares of Congo, which would be the world's largest palm-oil plantation. It is negotiating to grow biofuels on 2m hectares in Zambia, a country where Chinese farms are said to produce a quarter of the eggs sold in the capital, Lusaka. According to one estimate, 1m Chinese farm labourers will be working in Africa this year, a number one African leader called "catastrophic".

In total, says the International Food Policy Research Institute (IFPRI), a think-tank in Washington, DC, between 15m and 20m hectares of farmland in poor countries have been subject to transactions or talks involving foreigners since 2006. That is the size of France's agricultural land and a fifth of all the farmland of the European Union. Putting a conservative figure on the land's value, IFPRI calculates that these deals are worth $20 billion-30

billion—at least ten times as much as an emergency package for agriculture recently announced by the World Bank and 15 times more than the American administration's new fund for food security.

If you assume that the land, when developed, will yield roughly two tonnes of grain per hectare (which would be twice the African average but less than that of Europe, America and rich Asia), it would produce 30m-40m tonnes of cereals a year. That is a significant share of the world's cereals trade of roughly 220m tonnes a year and would be more than enough to meet the appetite for grain imports in the Middle East. What is happening, argues Richard Ferguson, an analyst for Nomura Securities, is outsourcing's third great wave, following that of manufacturing in the 1980s and information technology in the 1990s.

Several other features of the process are also new. Unlike older projects, the current ones mostly focus on staples or biofuels—wheat, maize, rice, jatropha. The Egyptian and South Korean projects in Sudan are both for wheat. Libya has leased 100,000 hectares of Mali for rice. By contrast, farming ventures used to be about cash crops (coffee, tea, sugar or bananas).

In the past, foreign farming investment was usually private: private investors bought land from private owners. That process has continued, particularly the snapping up of privatised land in the former Soviet Union. Last year a Swedish company called Alpcot Agro bought 128,000 hectares of Russia; South Korea's Hyundai Heavy Industries paid $6.5m for a majority stake in Khorol Zerno, a company that owns 10,000 hectares of eastern Siberia; Morgan Stanley, an American bank, bought 40,000 hectares of Ukraine in March. And Pava, the first Russian grain processor to be floated, plans to sell 40% of its landowning division to investors in the Gulf, giving them access to 500,000 hectares. Thanks to rising land values and (until recently) rising commodity prices, farming has been one of the few sectors to remain attractive during the credit crunch.

The great government grab

But the majority of the new deals have been government-to-government. The acquirers are foreign regimes or companies closely tied to them, such as sovereign-wealth funds. The sellers are host governments dispensing land they nominally own. Cambodia leased land to Kuwaiti investors last August after mutual prime-ministerial visits. Last year the Sudanese and Qatari governments set up a joint venture to invest in Sudan; the Kuwaiti and Sudanese ministers of finance signed what they called a "giant" strategic partnership for the same purpose. Saudi officials have visited Australia, Brazil, Egypt, Ethiopia, Kazakhstan, the Philippines, South Africa, Sudan, Turkey, Ukraine and Vietnam to talk about land acquisitions. The balance between the state and private sectors is heavily skewed in favour of the state.

AP But where's it going?

That makes the current round of land acquisitions different in kind, as well as scale. When private investors put money into cash crops, they tended to boost world trade and international economic activity. At least in theory, they encourage farmers to switch from growing subsistence rice to harvesting rubber for cash; from growing rubber to working in a tyre factory; and from making tyres to making cars. But now, governments are investing in staple crops in a protectionist impulse to circumvent world markets. Why are they doing this and what are the effects?

"Food security is not just an issue for Abu Dhabi or the United Arab Emirates," says Eissa Mohamed Al Suwaidi of the Abu Dhabi Fund for Development. "Recently, it has become a hot issue everywhere." He is confirming what everyone knows: the land deals are responses to food-market turmoil.

Between the start of 2007 and the middle of 2008, *The Economist* index of food prices rose 78%; soyabeans and rice both soared more than 130%. Meanwhile, food stocks slumped. In the five largest grain exporters, the ratio of stocks to consumption-plus-exports fell to 11% in 2009, below its ten-year average of over 15%.

It was not just the price rises that rattled food importers. Some of them, especially Arab ones, are oil exporters and their revenues were booming. They could afford higher prices. What they could not afford, though, was the spate of trade bans that grain exporters large and small imposed to keep food prices from rising at home. Ukraine and India banned wheat exports for a while; Argentina increased export taxes sharply. Actions like these raised fears in the Gulf that one day importers might not be able to secure enough supplies at any price. They persuaded many food-importing countries that they could no longer rely on world food markets for basic supplies.

Panic buying

What to do instead? The obvious answer was: invest in domestic farming and build up your own stocks. Countries that could, did so. Spending on rural infrastructure is the third largest item in China's 4 trillion yuan ($585 billion) economic-stimulus plan. European leaders said high prices showed the protectionist common agricultural policy needed to be preserved.

But the richest oil exporters did not have that option. Saudi Arabia made itself self-sufficient in wheat by lavishing untold quantities of money to create grain fields in the desert. In 2008, however, it abandoned its self-sufficiency programme when it discovered that farmers were burning their way through water—which comes from a non-replenishable aquifer below the Arabian sands—at a catastrophic rate. But if Saudi Arabia was growing more food than it should, and if it did not trust world markets, the only solution was to find farmland abroad. Other Gulf states followed suit. So did China and South Korea, countries not usually associated with water shortages but where agricultural expansion has been draining dry breadbasket areas like the North China Plain.

Water shortages have provided the hidden impulse behind many land deals. Peter Brabeck-Letmathe, the chairman of Nestlé, claims: "The purchases weren't about land, but water. For with the land comes the right to withdraw the water linked to it, in most countries essentially a

freebie that increasingly could be the most valuable part of the deal." He calls it "the great water grab".

For the countries seeking land (or water), the attractions are clear. But what of those selling or leasing their resources? They are keen enough, even sending road shows to the Gulf. Sudan is letting investors export 70% of the crop, even though it is the recipient of the largest food-aid operation in the world. Pakistan is offering half a million hectares of land and promising Gulf investors that if they sign up, it will hire a security force of 100,000 to protect the assets. For poor countries land deals offer a chance to reverse decades of underinvestment in agriculture.

In developing countries as a whole, the average growth in cereal yields has fallen from 3-6% a year in the 1960s to 1-2% a year now, says the World Bank. This reflects, among other things, a decline in public investment. In the 14 countries that depend most on farming, public spending on agriculture almost halved as a share of total public spending between 1980 and 2004. Foreign aid to farming also halved in real terms over the same period. Farming has done worst of all in Africa, where most of the largest land deals are taking place. There, agricultural output per farmworker was the lowest in the world during 1980-2004, growing by less than 1% a year, compared with over 3% a year in East Asia and the Middle East.

The investors promise a lot: new seeds, new marketing, better jobs, schools, clinics and roads. An official at Sudan's agriculture ministry said investment in farming in his country by Arab states would rise almost tenfold from $700m in 2007 to a forecast $7.5 billion in 2010. That would be half of all investment in the country, he said. In 2007, agricultural investment had been a mere 3% of the total.

China has set up 11 research stations in Africa to boost yields of staple crops. That is needed: sub-Saharan Africa spends much less than India on agricultural R&D. Even without new seed varieties or fancy drip-feed irrigation, investment should help farmers. One of the biggest constraints on African farming is the inability to borrow money for fertilisers. If new landlords just helped farmers get credit, it would make a big difference.

Yet a certain wariness ought to be maintained. Farming in Africa is hard. It breaks backs and the naive ambitions of outsiders. To judge by the scale of projects so far, the new investors seem to be pinning their hopes on creating technologically sophisticated large farms. These have worked well in Europe and the Americas. Paul Collier of Oxford University says Africa needs them too: "African peasant farming has fallen further and further behind the advancing commercial productivity frontier."

But alas, the record of large farms in Africa has been poor. Those that have done best are now moving away from staple crops to higher-value things such as flowers and fruit. Mechanised farming schemes that grow staples have often ended with abandoned machinery rusting in the returning bush. Moreover, large farmers are often well-connected and spend more time lobbying for special favours than doing the hard work.

Politics of a different sort poses more immediate problems. In Madagascar this year popular hostility to a deal that would have leased 1.3m hectares—half the island's arable land—to

Daewoo Logistics, a South Korean company, fanned the flames of opposition and contributed to the president's overthrow. In Zambia, the main opposition leader has come out against China's proposed 2m-hectare biofuels project—and China has threatened to pull out of Zambia if he ever came to power. The chairman of Cambodia's parliamentary foreign-affairs committee complains that no one has any idea what terms are being offered to Kuwait to lease rice paddies.

The head of the UN's Food and Agriculture Organisation, Jacques Diouf, dubs some projects "neocolonialist". Bowing before the wind, a Chinese agriculture-ministry official insists his country is not seeking to buy land abroad, though he adds that "if there are requests, we would like to assist." (On one estimate, China has signed 30 agricultural co-operation deals covering over 2m hectares since 2007.)

EPA Chinese neocolonialism going down well with Mozambique's elite

Objections to the projects are not simply Luddite. The deals produce losers as well as winners. Host governments usually claim that the land they are offering for sale or lease is vacant or owned by the state. That is not always true. "Empty" land often supports herders who graze animals on it. Land may be formally owned by the state but contain people who have farmed it for generations. Their customary rights are recognised locally, but often not accepted in law, or in the terms of a foreign-investment deal.

So the deals frequently set one group against another in host countries and the question is how those conflicts get resolved. "If you want people to invest in your country, you have to make concessions," says the spokesman for Kenya's president. (He was referring to a deal in which Qatar offered to build a new port in exchange for growing crops in the Tana river delta, something opposed by local farmers and conservationists.) The trouble is that the concessions are frequently one-sided. Customary owners are thrown off land they think of as theirs. Smallholders have their arms twisted to sign away their rights for a pittance.

This is worrying in itself. And it leads to so much local opposition that some deals cannot be implemented. The Saudi Binladin Group put on hold a $4.3 billion project to grow rice on 500,000 hectares of Indonesia. China postponed a 1.2m hectare deal in the Philippines.

Farms control

Joachim von Braun, the head of IFPRI, argues that the best way to resolve the conflicts and create "a win-win" is for foreign investors to sign a code of conduct to improve the terms of the deals for locals. Various international bodies have been working on their versions of such a code, including the African Union, which is due to ratify one at a summit in July.

Good practice would mean respecting customary rights; sharing benefits among locals (ie, not just bringing in your own workers), increasing transparency (current deals are shrouded in secrecy) and abiding by national trade policies (which means not exporting if the host country is suffering a famine). These sound well and good. But Sudan and Ethiopia have famines now: should they be declining to sign land deals altogether? Many of the worst abuses are committed by the foreign investors' local partners: will they be restrained by some international code?

There are plenty of reasons for scepticism about these deals. If they manage to reverse the long decline of farming in poor countries, they will have justified themselves. But like any big farming venture, they will take years to reveal their full impact. For the moment, the right response is to defer judgment and keep a watchful, hopeful but wary eye on their progress.