

# CONTRACTING ARRANGEMENTS

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## INVESTMENT MODELS, INCLUSIVE DEVELOPMENT AND CONTRACT FARMING IN THE BEIRA CORRIDOR

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### 1. INTRODUCTION

*“The Beira Agricultural Growth Corridor seeks to stimulate a major increase in agricultural production in an area whose growth potential has not yet been realised. The Beira Corridor has 10 million hectare of arable land with good soils, good climate and reliable access to water, but despite the promising conditions, very little commercial agriculture is practiced”.* In addition, “the Beira Corridor project aims at drawing smallholder farmers out of the cycle of subsistence farming by providing the infrastructure, finance and training needed to improve their productivity. The project has followed a cluster approach whereby agriculture is developed around existing infrastructure, which provides easy access to electricity and water supplies, for irrigation, and road and rail networks for access to markets” (Beira Corridor, 2012).

Beyond questions of whether land is effectively available (Kaarhus, 2011) or the effectiveness of the Beira Agricultural Growth Corridor project (NEPAD/AU/World Economic Forum, 2012), agricultural initiatives and projects have mushroomed in the region. This policy brief details the different investment models being established and what this means for inclusive development and contract farming in the Beira corridor.

### 2. SEVEN INVESTMENT MODELS IN THE BEIRA CORRIDOR

Without claiming to be exhaustive, seven models of agricultural investments can be identified in the Beira corridor (Anseeuw and Boche, 2012):

#### 2.1 Independent Farmers

Although composed of different type of farmers engaging in diverse farming activities, the particularity of this group of investors relates mainly to the fact that they are settling as independent farmers, relying on their own funding. The model is based on the establishment of large independent family farms (mainly based on South Africa’s commercial farm model).

#### Characteristics:

- Less than 5 000 ha
- Various production patterns (mostly in fruits (mango, banana, citrus), grain production, cattle and game farming)
- Farmers realise all the activities on their own, with little contracting or partnerships
- There are few successful farmers in this model; most of them are struggling to establish (due to technical difficulties and institutional uncertainties)



#### Inclusiveness, local development and contract farming:

- Besides production for domestic markets in some cases, there is little inclusiveness with domestic farmers
- Since it often concerns individual cases, these investments have little leverage on broader developments such as infrastructure or social measures

## 2.2 Associative management model

Mushrooming from the previous one, this model consists of farmers establishing associations in order to overcome some of the obstacles encountered by the independent farmers. It overcomes these difficulties by reducing transaction costs and through economies of scale.

### Characteristics:

- Grouping of independent farmers (each of less than 5 000 ha)
- Engage in various production patterns
- Often informal, but the establishment of farmers' associations enables them to overcome some barriers of entry within the commercial agricultural sector (minimum level of production for commercialization, access to financial resources, etc.)



### Inclusiveness, local development and contract farming:

- More stable, do occur as autonomous and independent clusters, little interaction with local dynamics mushroom
- Opens up markets and creates an agrarian economy. Subsequently, indirect outcomes will, in time, lead to better infrastructure (roads, electricity grids, etc.)
- Some associative models were developed with local farmers, leading to more inclusive agricultural investment models and thus broader local benefits and development

## 2.3 Cooperative model

It concerns the establishment of cooperative structures of farmers in charge of developing farming operations in the host country. These cooperative structures are often based on a multi-level governance structure going from well-structured agricultural unions, established abroad at national level, to the development of several farmer cooperatives and the establishment of farmers with collective and individual operations.

### Characteristics:

- Size of projects depends on the number of farmers involved, generally cover 10 000 ha – 80 000 ha
- Large scale plantations (generally of basic commodities such as maize, at least in the early phase of the projects)
- Solid organisational base opens doors and possibilities, ranging from government support to possible contractual arrangements for farmers engaged
- Related to bilateral agreements, performance thresholds are established and conditionalities are agreed upon (production for local markets, inclusion of local farmers, etc.)



### Inclusiveness, local development and contract farming:

- Through employment creation and enhanced infrastructure, an effective development, based on local dynamics, can be instigated
- As large scale plantations are the rule, few out-grower schemes are planned
- This being said, through bilateral agreements, projects can include significant range of benefits for local population (social infrastructure (schools, clinics, etc.), development of productive assets and infrastructure (preparing fields, delivering water, etc.), transfer of technologies, off-take from smallholder farmers, who can benefit from the establishment of marketing channels

## 2.4 The 1 000-day model

This model is based on the objective to make available on the international market, in approximately three years (hence the 1 000 day model), a ready-to-start large farm operating in food or biofuel production. The rationale of this hybrid model is based on two assumptions:

- An anticipation of a future demand for land for food and biofuel production
- The significant increase of land value at the time the farm is ready to produce (and can be sold to an agribusiness company or an investment fund. The 1 000-day model can be defined as “land speculation”

**Characteristics:**

- Average size: between 5 000 and 10 000 ha
- Objective of the investors is to raise on average a 30% return on investment after three years (i.e. 1 000 days)
- Many jatropha projects have been based on this model
- Little effective production in this model
- Most of these projects never really took off or collapsed



**Inclusiveness, local development and contract farming:**

- No prospects for local development, nor local farmer inclusion or contractual arrangements
- Activities are mainly mechanised, with few jobs being created (jobs created are short term as the project is supposed to be sold after three years)

**2.5 Asset Management Companies and Investment Fund model**

This model is characterised by the involvement of a new type of actor in the agricultural sector: financial actors and investment funds, aiming to diversify their portfolios. As a result of the widely held predictions, they perceive the agricultural sector as an investment for the future. The rationale on which these models are based is thus purely financial, with the investors anticipating a significant yearly return on investment, from the land and/or the production on the land.

**Characteristics:**

- Establish large-scale commercial and mechanised agricultural projects, covering between 5 000 and 10 000 ha
- Profit through technologically advanced contribution to agricultural operations (advanced financial tools, economies of scale (related to input purchases, etc.) and through advanced risk management)
- Lower than expected returns, often lead to loss of confidence in many asset management companies, withdrawal of funds, tighter control mechanisms, mainly through higher degree of coordination and vertical integration



**Inclusiveness, local development and contract farming:**

- Although the production can benefit domestic economies, the potential benefits for local communities are often limited
- Mainly large-scale, largely mechanised (and thus not labour intensive), risk-averse (hence no outsourcing or out-growers practices), focusing on most lucrative and well-established markets

**2.6 Nucleus-Estate Model**

This model is structured around agribusinesses that are integrating - at least partly - with primary production. When companies previously endeavoured to secure their primary needs (produced by independent farmers) through a diverse set of mechanisms such as contract farming and out-grower schemes (externalisation of activities), a reverse tendency of internalisation was identified. Two reasons explain this tendency: i) The high production risk environment related to the investment in less-established countries (requiring a more centralised control by the agribusiness); ii) The reversal of the risk/profit relationship appearing within the production chain (Vermeulen and Cotula, 2010). Whereas primary production constituted until now the main risk factor, with profits returning to downstream and particularly upstream actors; the increase in agricultural prices now tends to invert this relationship.

**Characteristics:**

- Large-scale (20 000 ha), mainly focusing on sugar, cotton and tobacco sectors, now expanding to other commodities such as fruits and vegetables and rice
- Includes three sections, functioning simultaneously: 1/3 own production; 1/3 contract farming; 1/3 market basis, giving the company flexibility for its activities



**Inclusiveness, local development and contract farming:**

- Facilitates inclusion of independent farmers (through contracting or spot market). Due to a problem of inconsistency, the latter might however not be through local farmers

**(continued)**

- Established by well-structured and developed agribusinesses (often multinationals), the model is generally stable
- Lately, engagement of non-agricultural businesses on the basis of similar models in agriculture (besides supermarkets, breweries, etc., also mining, marketing and transport companies)



**(continued)**

- Related to its centrally negotiated set-up, infrastructural development (i.e. road infrastructure, electricity, water, etc.) benefits to local development
- Through Corporate Social Responsibility (CSR) programs, can also engage in social infrastructure (schools, clinics, etc.)

## 2.7 Agri-business Estate

This model is characterised by the full vertical integration of the different segments of an agricultural value-chain, mainly through (general foreign) multinational enterprises. A recent tendency is indeed related to the decision of certain transformation industries to integrate the primary production, mainly with the aim to reduce costs and secure procurement (particularly since food price crisis in 2008-2009).

**Characteristics:**

- Very large projects (more than 20 000 ha) generally irrigated crops, highly mechanized and intensive in fertilizer farming systems
- Agricultural investment model based on high level of coordination, even a total integration of all activities



**Inclusiveness, local development and contract farming:**

- Because of the large amount invested in these projects and the risk of contracting with other farmers, agribusinesses prefer to rely mainly on their own production
- Due to the far-reaching vertical integration, few out-grower schemes with local farmers are developed
- Benefits mainly based on employment, even if governments promote partnerships between agribusiness and smallholder farmers

This policy brief can be downloaded on the NBF website [www.nepadbusinessfoundation.org](http://www.nepadbusinessfoundation.org)

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