FOREIGN DIRECT INVESTMENTS (FDI) IN AGRICULTURE IN EASTERN AFRICA: Report on Tanzania

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‘‘THE GAINS AND LOSSES OF FOREIGN DIRECT INVESTMENT IN AGRICULTURE; THE TANZANIA COUNTRY CASE’’

REPORT PREPARED

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1.0 INTRODUCTION

Tanzania offers tremendous opportunities for investors as it is endowed with abundance of natural resources such as arable land; a wide base for raw materials supply from local sources; political stability; good market policy such as privatisation, investment incentives, liberalized foreign exchange controls and the ongoing establishment of socially responsible economy. Other important attributes include excellent geographical location in the East African Region and excellent tourist attraction sites.

Agriculture is the foundation of the Tanzanian economy. It is the main source of food as it provides about 95 percent of the national food requirements and provides employment opportunities to about 77.5 percent of Tanzanians. It accounts for about 24.1 percent of the Gross Domestic Product (GDP) and contributes about 31 percent of the foreign exchange earnings. It has linkages with the non-farm sector through forward linkages to agro-processing, consumption and export; provides raw materials to industries and a market for manufactured goods.

Foreign direct investment (FDI) in agriculture has had notable positive impacts on food security and poverty reduction in terms of improved production and productivity, but also some negative effects particularly to communities directly affected by land transfers. FDI in agriculture has shown mixed trend with ups and downs in the last decade. The Government needs to prioritize interventions in order to attract more FDI inflows in agriculture.

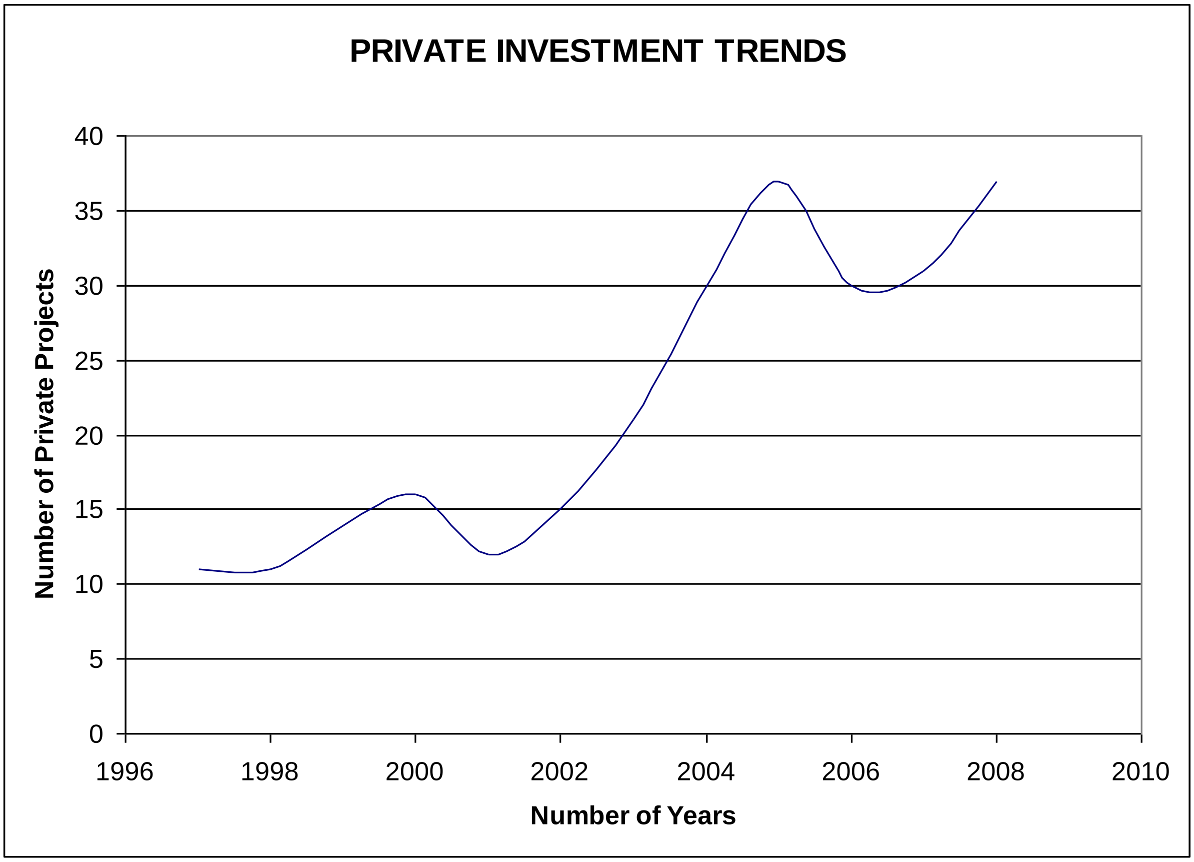
1.1 Foreign direct investment in agriculture

Foreign Direct investment has the potential to generate employment, raise productivity, transfer skills and technology, enhance exports and contribute to the long- term economic development of the world's developing countries. However, there is a keen competition among developed and developing countries to attract FDI in their countries. This drive to lure investment often extends to the national level with different regional authorities pursuing their own strategies and assembling their own baskets of incentives to attract new investments.

Tanzania like other developing countries has implemented various reforms and active FDI promotion policies that have evolved over the years. However, given the large potential opportunities in the sector, FDI inflows in agriculture are still low compared to other sectors, due to various binding constraints such as inadequate agricultural support services, transportation infrastructure, marketing infrastructure, irrigation infrastructure and rural energy supply.

The Government of Tanzania is fully aware of the importance of FDI contribution to the economic growth. FDI can spur growth by facilitating technology transfer, expanding market access and competition, financing physical capital formation, and developing human capabilities (REPOA 2010). For the period 2000 to 2008, FDI in Tanzania has averaged USD 485.6 million annually, and has increased every year since 2003 as reflected in the increasing number of private projects in the agricultural sector (Figure 1). The exception is 2008-2009 when the country experienced effects of the global financial crisis that contributed to slow inflows of FDI. In general, FDI flows into the agricultural sector have remained relatively small and erratic in Tanzania due to the fact that agriculture is faced with a number of persistent challenges which include dependence on rain fed and poor infrastructure. Thus, financial institutions are reluctant to finance the sector due to the associated risks.

Figure 1: **Private Investment Trends in Agricultural Sector**

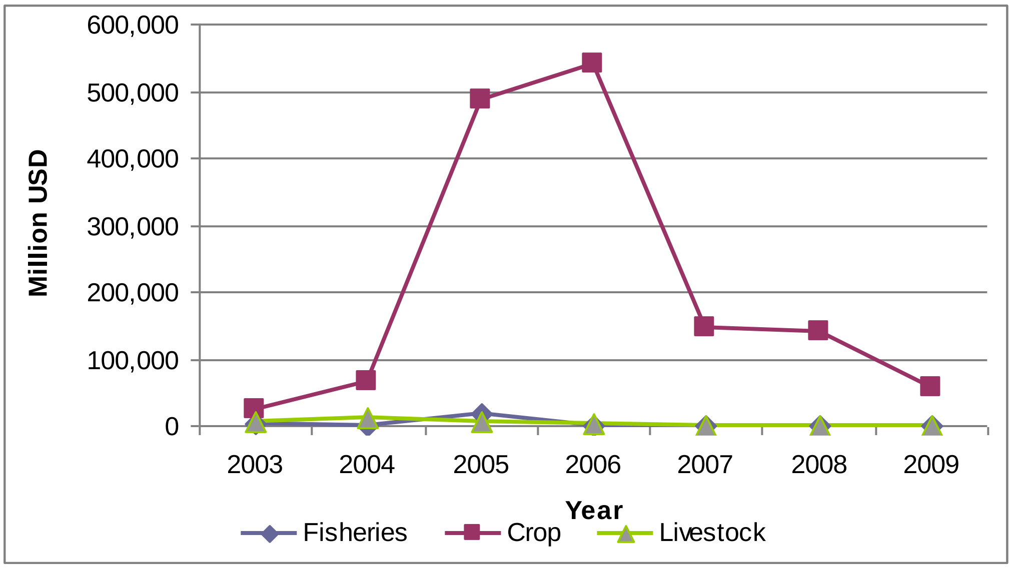


Source: Tanzania Investment Centre report, 2009.

2.0 CONTRIBUTION OF FDI IN AGRICULTURE SUB-SECTORS

Private sector investment in agriculture remained low between 1997 and 2004. Remarkable improvements were however registered in the crop subsector between 2004 and 2006, followed by a decline between 2008 and 2009. Livestock and fisheries sub-sectors abruptly grew in 2004 and 2005 respectively but remained constant most of the years (Figure 2). The improvement is attributed to the formation and the operation of Tanzania Investment Centre (TIC), established in 1998. The Centre promoted the trade policy of 2003 which offered opportunities and investment incentives for both domestic and foreign investors. Other contributory factors included investment incentive packages in agriculture, zero-rating of capital goods and all farm inputs including fertilizer, pesticides and herbicides; reduced import tariff on project capital items to 0% for investors with TIC Certificate of Incentive; deferment of VAT payment on project capital goods; VAT exemption on agricultural exports and for domestically produced agricultural inputs. Apparently, the drop up of investment in 2008 and 2009 was attributed to the global economic crunch and adverse weather especially in northern Tanzania.

Figure 2: **Private sector investment in agriculture sub-sectors**.



Source: TIC 2009

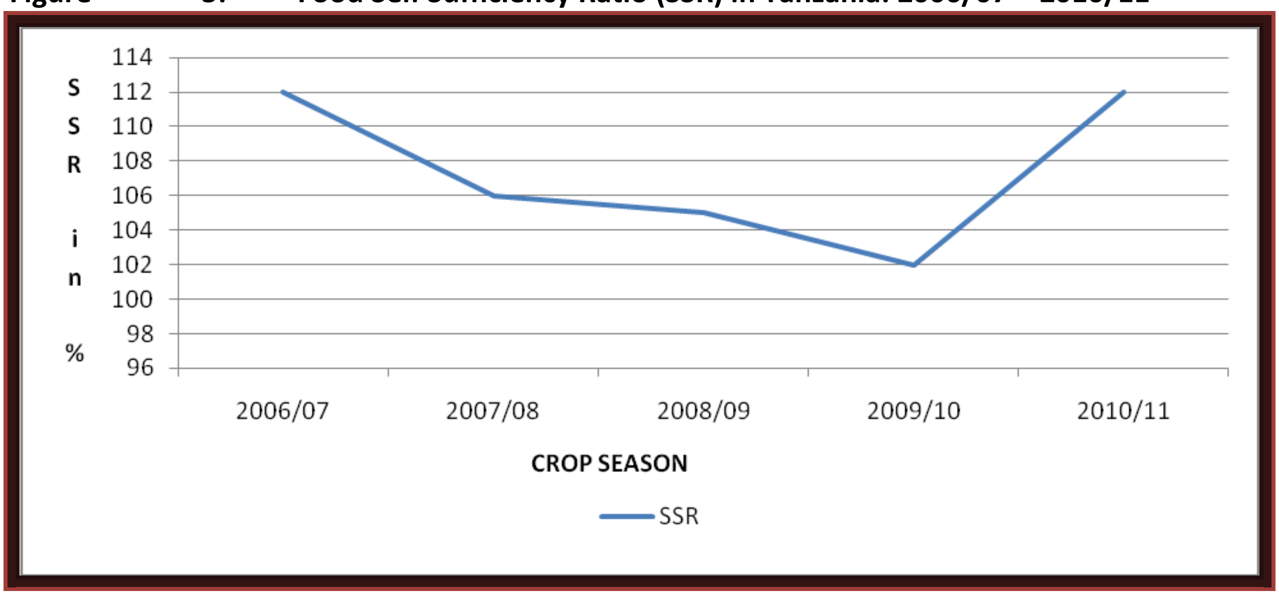
3.0 IMPACT OF FDI ON FOOD SECURITY AND POVERTY REDUCTION

Agriculture is the most efficient sector in creating employment and plays a pivotal role in addressing both urban and rural poverty. As growth is the single most important factor affecting poverty reduction, FDI flow into the sector is thus central to achieving that goal. FDI in the sector has remained very small (about 2.1% of total FDI inflow) despite the sector's impressive growth rate that has averaged 4.4 percent in the recent past.

Nonetheless, the impact of FDI on food security and poverty reduction can be assessed through gains in agricultural productivity and production. Several studies around the world have found that local firms' productivity increases with sales to multinational enterprises. Similar results have been recorded in Tanzania particularly in undertakings by estates or large commercial farms, which have been able to attract considerable FDI (Msuya, 2007). The crops sub sector attracts the bulk of FDI and the tea and sugar industries are good examples to illustrate gains from FDI. For instance the production of sugar cane in Mtibwa and Kilombero districts in Morogoro region and tea in Rungwe district in Mbeya region have demonstrated that through FDI has resulted into expanded area cultivated, increased production and productivity and improved quality. In Rungwe, through Wakulima Tea Company (WATCO) annual green leaf production increased fivefold from 3.77 million kilograms in 2000/01 to 15.28 million kilograms in 2004/05. Also, the average yield of green leaf from smallholders increased as well as quality above standards set by the company. The same is for sugar cane production in Mtibwa Sugar Estate (MSE) and Kilombero Sugar Company Ltd. (KSCL) whereby smallholders increased production from 907,000 tonnes in 1999/00 to 1,594,000 tonnes in 2004/05 accounting for about 68 percent of total production of sugar in 2004/05 season. The smallholders' income in these sugar cane and tea production areas had risen and contributed to reduction in income poverty. Therefore, in general, FDI in Tanzania has had a positive impact and especially for smallholder farmers who are linked to foreign invested enterprises (FIEs) through integrated producer schemes.

Likewise, even in food crop production gains have been recorded but not as much as in cash crops as cited above. It is hard to attribute this gain to FDI as the Government embarked on a targeted agricultural inputs support programme for many years. Nevertheless, by implication FDI has also contributed to this success. A good indicator of gains in food security is the food self sufficiency ratio. Overall, the trend in food Self Sufficiency Ratio (SSR) for Tanzania between 2005/06 and 2010/11 crop season has been between 100 and 120 percent. From 102 percent in 2005/06, SSR made a sharp increase to 112 percent in 2006/07, afterwards the SSR made a perpetual but gradual decline to 106 percent, 105 percent and 102 percent in 2007/08, 2008/09 and 2009/10 respectively; before rising to 112 percent again in 2010/11 (Figure 3.).

Figure 3: Food Self Sufficiency Ratio (SSR) in Tanzania: 2006/07 – 2010/11



Source: MAFC (2010)

Total crop production during 2009/10 crop season has been higher than the food requirement thus creating a surplus of 429,000 tonnes. This surplus is mainly maize.

But in spite of the gains discussed above, there are also negative impacts associated with FDI in agriculture. There has been and still are conflicts and disputes between large commercial farm enterprises with surrounding communities, particularly with regards to land acquisition and management. A very recent case is of Kilombero district in Morogoro region. Residents of Namwawala village, for example, have, in recent years, been complaining that their has been land grabbing by investors for sugarcane farming. A fact-finding mission of the Legal and Human Rights Centre and HAKIARDHI in 2009 discovered that 10,000 villagers would be made landless when 9,272.54 hectares of their land would be given to a sugarcane investor. However, this assertion cannot be verified by the Government. But this just shows how FDI can bring about negative social and economic impacts. But what could be agreed between the aforementioned organizations and the Government is the need for more transparency in the process of establishing the said investment, and-participatory decision-making in matters affecting villagers' interest in land. This now brings us to discuss what efforts the Government is doing to improve FDI in Tanzania.

4.0 GOVERNMENT EFFORTS TO IMPROVE FDI IN AGRICULTURE

4.1 Establishment of Tanzania Agricultural Development Bank (TADB): The Government is in the process of establishing an Agricultural Development Bank which will be providing agricultural credits to both small and large scale investors in agriculture. In the mean time Tanzania Investment Bank (TIB) has established an Agricultural Window which caters for credits to investors in agriculture sector. Prior to the establishment of TADB, the Government has been implementing various policies and initiatives to ensure adequate credits to productive sectors including agriculture. Some commercial banks have started to earmark agriculture sector activities and projects especially in rural areas.

4.2 Policy Incentives: In view of establishment of Public Private Partnership Policy of 2010 in Tanzania, it has been possible to mobilize private sector investments and partnership to help achieve the goals of Tanzania's Kilimo Kwanza Resolve. Tanzania has started implementing a five years Agricultural Development Plan through corridor approach like Southern Agricultural Growth Corridor of Tanzania (SAGCOT) that encourages Partnership in many aspects including Agro-processing and Contract farming. SAGCOT is a unique and powerful public-private partnership capable of delivering sustainable agricultural growth in the southern corridor of Tanzania.

4.3 Investment incentives Package in agriculture sector (Tax incentives): Tanzanian agriculture offers a well-balanced and competitive package of fiscal incentives in comparison with other African countries, aiming at providing competitive fiscal regime for foreign trade

4.4 Business International Membership: Investments in Tanzania are guaranteed against nationalization and expropriation. Tanzania is signatory of several multilateral and bilateral agreements on protection and promotion of foreign investment. Among others international agreements and membership, Tanzania is a member of Multilateral Investment Guarantee Agency (MIGA) and International Centre for Settlement of Investment Disputes (ICSID). Tanzania has a stable fiscal regime with sustainable level of inflation. Under its economic recovery program, Tanzania increased revenue streams and substantially reduced spending.

4.5 The foreign Exchange Market: The foreign exchange market in Tanzania is composed of the wholesale and retail markets. The IFEM is the wholesale market, which plays an important role in the determination of the country's official exchange rate and the provision of funds for the accumulation of international reserves. Bureaux de change and banks cater for the retail market, in which individuals and businesses satisfy their foreign exchange requirements. Tanzania's trade and exchange system is now completely free of restrictions on making payments and transfers for current account transactions. The Government has already accepted the obligations of Article VIII of the IMF's Articles of Agreement, in order to boost the country's attractiveness for foreign investors.

5.0 INVESTMENT PRIORITIES FOR THE AGRICULTURAL SECTOR IN TANZANIA

5.1 Investment necessary for increasing productivity

i) Irrigation: Tanzania mainland has a total irrigation potential of 29.4 million hectares, but only about 310,745 hectares are currently under irrigation. Tanzania has a large potential of increasing maize production by increasing the area under irrigation.

ii) Mechanization: Given that cultivation of most of the priority crops is done predominantly by the hand hoe, significant growth cannot be achieved without increased mechanization. It is estimated that about 70% of farming is dependent on the hand hoe, 20% on ox-ploughs and 10% on tractors. The use of rudimentary technology, such as a hand hoe is one among reasons that account for low labour productivity in agriculture. A mechanization programme that enables small holder producers to use ox ploughs and tractors has been initiated but it needs more investment.

iii) Research and development and extension: Currently amount of resources allocated to research and development in the agricultural sector is 0.3% of the total government budget to the sector.

iv) Use of improved agricultural technologies: To bring about agricultural green revolution and transformation, access to and timely use of farm inputs is an important aspect.

v) Renewable energy sources and sustainable agricultural practices: Agricultural activities often cause environmental degradation through deforestation, soil degradation and soil erosion, which in turn lead to low productivity. The long term impact of environmental degradation has been climate change which has detrimental effects (for example, droughts and floods) on agriculture. Hence, there is a need for employing renewable energy and sustainable agricultural practices.

5.2 Investment necessary for market expansion

i) Rural infrastructure (roads, markets, storage facilities, electrification etc)

Investment in infrastructure is important for attracting private investment in agricultural related activities such as agro-processing, increasing producer prices and farmers' income.

ii) Agro-processing and value addition

The level of agro-processing infrastructure in Tanzania is very low. As a result, Tanzania is exporting unprocessed agro-products while the agro-processing industry cannot meet domestic demand. The low capacity in agro-processing is one of the main reasons for high post harvest losses. It is currently estimated that 30-70% of output of cereals, and fruits and vegetables, respectively, is lost post harvest due to inadequate agro-processing facilities.

In the fisheries sub-sector, 20% of output is lost post harvest due to lack of processing facilities. One of the major reasons for inadequate investment in agro-processing is poor physical infrastructure in rural areas.

Investment opportunities are available in setting up processing industries for various agricultural products and investment in the Export Processing Zones aimed for export. Since for along time Tanzania has been exporting raw products, efforts to increase investment in the agro-processing and value chain have been encouraged. Tanzania's food processing industry processes only about 1% of the available raw materials. This compares very poorly with 40-50% in Thailand, 78% in the Philippines, and 83% in Malaysia, which all fall under the category of developing countries. Unlike the other crops which are almost entirely processed for export, more than 90 per cent of the total cashew production is exported to India in the raw form. Through this form of trade Tanzania is known to lose billions of shillings every year.

5.3 Promotion of public-private sector partnership

Promotion of public-private partnership is critical for the sector development.

5.4 Capacity building at all levels

Investment in the sector should be accompanied by development of human capital and sustainable farming approaches.

6.0 CONCLUSION AND RECOMMENDATIONS

In Tanzania FDI in agriculture has had notable positive impacts in terms off improved production and productivity, but also some negative effects particularly to communities directly affected by land transfers. FDI in agriculture is still very low compared to other sectors and has shown mixed trend with ups and downs in the last decade. The Government has made serious efforts to attract more FDI in the agriculture sector owing the comparative advantage Tanzania has over other African Countries. The country is rich with diverse and extensive land; water resources; and climatic conditions. Its agro-climatic diversity provides the potential for a range of food staples, livestock and high value crops. In addition, the country has the opportunity to leverage its geographic position, having ocean access, port facilities and rapidly growing food markets in neighbouring countries. Tanzania’s political stability further fosters opportunities for long-term growth. A range of high value food and cash crops as well as livestock can be raised. The country can also take advantage of the rapidly growing food market in the region to advance her agricultural development agenda.

The initiation of ASDP and subsequently *Kilimo Kwanza* provides a framework for agricultural development in Tanzania and wide window for FDI. *Kilimo Kwanza* complements the ASDP by strategically positioning agriculture as a government priority with potential to achieve economic growth and food security. It also provides a call to action and collaboration among all stakeholders, recognizing the role of the private sector in meeting its goals.

In order to ensure improved and sustained FDI in the agricultural sector in Tanzania, the following are the priorities: improve and develop irrigation infrastructure; increase availability and utilization of agriculture and livestock inputs; increase use of mechanization; improve market access and agroprocessing; strengthen agriculture and livestock research, training and extension services; and enhance Public-Private partnership.

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