



Enabling environments for agribusiness and agro-industries development

*Regional and country
perspectives*



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Executive summary

The agribusiness sector, which comprises the business activities performed from farm to fork, is a major generator of employment and income worldwide. In recent years, the importance of the agribusiness sector has grown significantly, as agricultural development strategies shifted from a pure production-oriented approach to a broader systems perspective that emphasizes agrifood chain coordination, value creation and the institutional setting under which chains operate. Seen as an engine for growth, agribusiness and its related industries are receiving increased attention in policies and strategies that aim to promote investments in agro-enterprises and agro-based value chain development. This has prompted a need for deeper understanding of the elements that form a conducive business climate, or enabling environment, for the development of agribusinesses, agro-industries and agrifood value chains.

This document is intended as a contribution to advancing knowledge on enabling environments for the development of agrifood value chains. It draws primarily from workshops organized by FAO in collaboration with other United Nations agencies and development partners between 2006 and 2008. FAO workshops on enabling environments for agribusiness and agro-industrial development were held in four regions – Africa, Asia, Latin America, and Eastern Europe and Central Asia – with in-depth studies of 20 countries. The document also benefits from work undertaken by FAO and partners as part of the technical preparation for a series of global and regional agro-industry fora, held in India, China, Peru, Nigeria and Lebanon between 2008 and 2011. In all of these events, business climates were highlighted as an area of strong relevance for promoting investment and developing agro-enterprises.

Although the study of enabling environments is not new, significant peculiarities of agribusinesses and agro-industries warrant a fresh and comprehensive examination of the factors that are unique to these economic sectors. Agribusiness and agro-industries are characterized by raw materials that are usually perishable, variable in quality, and not regularly available throughout the year. These characteristics represent non-negligible and often uncontrollable sources of risk for most agro-based investments. The sectors are also subject to stringent public sector regulations, not only because of concerns about food product safety and quality, but also in view of their significance for food security and political stability.

While examining the elements that constitute a conducive business climate for agribusiness and agro-industries, this study recognizes that the components of enabling environments considered by traditional assessment frameworks are relevant and necessary, but not sufficient to cover the specificities of these sectors. The background materials and cross-country cases discussed at the workshops and fora provided insights into country and regional differences that help put into perspective factors that are relevant for specific stages of agribusiness development and/or country and regional contexts.

The general finding from the research is that enabling environments are forged by the traditional, broader macro-level forces (political, social and economic) that are relevant to other sectors of an economy. However, specific additional factors were also identified as essential for driving further development of the agribusiness and agro-industries sectors: efficient land markets and tenure systems; access to appropriate rural and agricultural finance and risk management products; specific regulatory provisions, consistent trade policies and access to global markets; availability of skilled human resources, improved technologies and adequate infrastructural facilities and utilities (particularly rural roads and storage facilities); and capacity for complying with food quality and safety standards. The priority ranking of these factors differs from region to region – reflecting each region's level of development and the critical bottlenecks facing its strategic commodities. To some extent, priorities also differ among countries in each region, emphasizing the relevance of the country context in creating an enabling environment.

This study also considers the roles of the public sector and international organizations in promoting business climate reforms, and discusses the possibility of developing specific country-level indicators for agribusiness and agro-industries enabling environments. It concludes by calling attention to the fact that although business climates that are conducive to investments in agribusiness and agro-industries are important, they cannot by themselves guarantee that such investments will be forthcoming. In addition to efforts to improve business climates, there is also need to ensure that returns on investments are sufficient to compensate for any perceived constraints on enabling environments that increase risks and add to the costs of doing business. In other words, policies and strategies that aim to increase agro-based investments must go beyond a pure emphasis on business climates, considering as well elements that affect profitability and, in consequence, investors' perceptions of risk/return ratios.

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Acronyms

AgCLIR	Agriculture-Commercial Legal and Institutional Reform
AGS	Rural Infrastructure and Agro-industries Division (FAO)
AGSF	Agricultural Management, Marketing and Finance Services (FAO)
DCED	Donor Committee for Enterprise Development
EU	European Union
FAO	Food and Agriculture Organization of the United Nations
FDI	foreign direct investment
GDP	gross domestic product
GTZ	German Agency for Technical Cooperation (now GIZ – German Agency for International Cooperation)
IFAD	International Fund for Agricultural Development
NGO	non-governmental organization
OECD	Organisation for Economic Co-operation and Development
PPP	public-private partnership
R&D	research and development
SPS	sanitary and phyto-sanitary
TNC	transnational corporation
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNECA	United Nations Economic Commission for Africa
UNIDO	United Nations Industrial Development Organization
USAID	United States Agency for International Development
USDA	United States Department of Agriculture
VAT	value-added tax
WTO	World Trade Organization

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Chapter 1

Introduction

The agribusiness sector, which comprises the collective business activities performed from farm to fork, is an important generator of employment and income worldwide. Agribusinesses and agro-industries are a principal source of value addition for primary agricultural products, a catalyst for the development of efficient value chains, a contributor to improved product quality and safety, and a provider of services that allow food to flow from production to consumption. Modernization of food systems and globalization of their downstream segments, including processing and retailing, has led to substantial changes in the organization and performance of agrifood chains, particularly in the developing world. As observed by Vorley *et al.* (2007), such changes affect smallholder agriculture and rural livelihoods globally, challenging farmers and policy-makers to adapt to the new demands that food processors and retailers are making on their supply chains. In recent years, the importance of the agribusiness sector has grown significantly, as agricultural development strategies shift their focus from a production-oriented approach to a broader systems view that emphasizes agrifood chain coordination, value creation and the institutional setting under which chains operate. Seen as an engine for growth, agribusiness and its related industries are receiving increased attention in policies and strategies that aim to promote investments in agro-enterprises and develop agro-based value chains. This has prompted a need for deeper understanding of the elements that constitute a conducive business climate, or enabling environment, for the development of agribusinesses, agro-industries and agrifood value chains.

This document contributes to advancing the knowledge on what constitutes an enabling environment for the development of agribusiness, agro-industries and agrifood value chains. It draws heavily from multi-stakeholder workshops organized by FAO in collaboration with other United Nations (UN) agencies and development partners between 2006 and 2008. These workshops on enabling environments for agribusiness and agro-industrial development were undertaken in four regions – Africa, Asia, Latin America, and Eastern Europe and Central Asia – with in-depth studies from 20 countries.¹ The objectives of the assessments were to identify, characterize and appraise the set of policies, institutions, and support services that form the agro-based business climate in each of the selected countries; and to identify lessons learned and best practices from changes in policies, institutions and support services that have led to increased investments and improved competitive performance in specific agribusiness and agro-industry sub-sectors. The document

¹ The Gambia, Ghana, Kenya, Mozambique and the United Republic of Tanzania in Africa; India, Indonesia, Nepal, the Philippines and Thailand in Asia; Argentina, Chile, Costa Rica, El Salvador and Peru in Latin America; and Armenia, Croatia, Hungary, Serbia and Ukraine in Eastern Europe and Central Asia.

benefits from work undertaken by FAO and partners as part of the technical preparations for a series of global and regional agro-industry fora, held in India, China, Peru, Nigeria and Lebanon between 2008 and 2011. In all of these events, business climates were highlighted as an area of strong relevance for promoting investment and developing agro-enterprises.

This work is part of FAO's Agribusiness Development Programme, which addresses issues central to agribusiness development in developing countries, and advises on policies and strategies for improving agribusiness competitiveness, including fostering better coordination and linkages among business partners.

Proper understanding of the business climate is considered a fundamental step towards the design of policies and strategies that can reduce the costs of doing business, and thus increase the investment attractiveness and competitiveness of a particular economy. Although the study of enabling environments is not new, most work in this area has taken a broad, economy-wide view of factors that affect the costs of doing business and thus inhibit or facilitate entrepreneurship, investment attraction and economic growth.

However, an argument can be made for the need to consider business climates from a sector-based perspective, as the conditions that favour or hamper the investment attractiveness of a particular economic sector – such as telecommunications or financial services – in a given economy may not be similar to those that are important for other sectors, such as tourism or civil construction. Some factors and conditions are cross-cutting and thus relevant for any economic sector, but others are relevant to only one or a few specific sectors, and should not be neglected when enabling environments are being considered from a sector-based perspective. This argument is particularly strong in the case of the agribusiness and agro-industries, which have particular characteristics that warrant a fresh and comprehensive examination of what constitutes an enabling environment in their regard.

Agribusinesses and agro-industries are characterized by biological raw materials that are usually perishable, variable in quality, and not regularly available throughout the year. Mostly because of its biological nature, agricultural production is inherently risky. The biological process of agriculture and the seasonality of production impose strict schedules for all activities along agricultural value chains, implying the need for effective coordination among all agents. In addition, the agricultural production process depends on climatic factors over which there is little control. These two aspects are key to understanding investment climates for agribusinesses, as investors' success depends on the effective functioning of other agents in the chain (e.g., producer groups, intermediaries, service providers) over which they may have no control. Success also depends on investors' ability to cope with climatic shocks, as no matter where along the value chain the investor is participating, he/she can be affected by shocks in production (with coping strategies that include diversifying the sources of raw material, relying on commodity markets with efficient storage systems, and using insurance and futures/options products). These aspects also represent business entry barriers, especially for smallholders and micro-businesses that cannot offer what agents need, or cope with all the risks involved.

Because agriculture has a direct link to food security, it tends to be regarded as strategically important for countries. Thus, motivations other than purely economic ones often influence policies governing the sector and its related industries.

In addition, factors affecting the competitiveness of agribusinesses and agro-industries differ at different stages of the value chain, and among sub-sectors and commodities. In most developing countries, the breadth of the sector implies that it cuts across the mandate of more than one ministry, thus requiring coordination among different ministries, particularly those of agriculture, trade and industry.

This report discusses enabling environments from the specific perspective of agribusiness and agro-industries. It is organized in seven chapters. Following these introductory remarks, chapter 2 presents the conceptual framework and scope of the study, briefly analyses different approaches to assessing business climates, discusses their relevance for appraising agribusiness and agro-industries sectors, and identifies major stakeholders and their possible roles in and/or contributions to the creation of enabling environments for agribusiness development. Chapters 3 and 4 summarize key findings from the country studies and the multi-stakeholder regional workshops, identifying similarities and differences among them to generate a list of necessary but not sufficient factors for agribusiness development. These chapters also highlight best practices that have led to increased investment and greater competitiveness in specific agro-industrial sub-sectors, and lessons learned from these. Chapter 5 discusses enabling environment reforms, and chapter 6 proposes an agenda for improving enabling environments for agribusiness and agro-industries. Finally, chapter 7 sums up the key findings and presents recommendations for future action.

Chapter 2

Conceptual framework

DEFINITIONS OF KEY CONCEPTS AND ISSUES

Following Christy *et al.* (2009), “enabling business environments” are defined here as sets of policies, institutions, support services and other conditions that collectively improve or create a general business setting where enterprises and business activities can start, develop and thrive. The environment shapes the costs and risks of doing business, hence the competitiveness of an enterprise and its value creation abilities. The concept of a conducive enabling environment is thus associated with a situation in which domestic and foreign firms can operate and grow as a result of the presence, interaction and capacity of different institutions, policies and services.² Such an environment boosts the competitiveness of a business within its market. An enabling environment where enterprises can thrive is therefore an essential prerequisite for economic development.

Countries that create conducive business climates employ sound policies, institutions and services to promote investment, attract capital and engender economic growth. The term “enabling environments”, although often imprecisely defined, is increasingly used by a number of institutions in reference to an array of factors external to an enterprise. For instance, the Organisation for Economic Co-operation and Development (OECD) refers to an enabling environment as one of the main incentives for foreign direct investment (FDI) (see, for example, OECD, 2003). The United States Department of Agriculture’s (USDA) Economic Research Service and the World Bank Group also widely use the term “enabling environment” in their literature, but do not define it precisely (Landes, 2008; World Bank, 2004).

Several definitions of the term “agribusiness” exist in the literature. *Encyclopaedia Britannica* defines agribusiness broadly as “agriculture operated by business; specifically, a part of a modern economy devoted to the production, processing and distribution of food, fibre products and by-products including the financial institutions that fund these activities” (Encyclopaedia Britannica Inc., 2011). A simplistic definition states that agribusiness refers to any business related to agriculture, including farming, processing, exporting, input suppliers, trading and retailing (USAID, 2008). The term *agribusiness* is often used to convey an aggregate view of agriculture and business-related activities, covering the multiple functions and processes involved in modern food production and distribution. For the purposes of this study, agribusiness denotes the collective business activities that are performed from farm to table. It covers agricultural input suppliers, producers, agroprocessors, distributors, traders, exporters, retailers and consumers.

² The term “enabling environment” is used interchangeably with the term “conducive/favourable business climate”.

Agro-industry refers to the establishment of linkages between enterprises and supply chains for developing, transforming and distributing specific inputs and products in the agriculture sector. Consequently, agro-industries are a subset of the agribusiness sector. Agribusiness and agro-industry both involve commercialization and value addition of agricultural and post-production enterprises, and the building of linkages among agricultural enterprises (FAO, 2007b). The terms agribusiness and agro-industries are often associated with large-scale farming enterprises or enterprises involved in large-scale food production, processing, distribution and quality control of agricultural products. Smaller agriculture-related entities (farms, processors, etc.) are less often thought of as agribusinesses or agro-industries, but strictly they should also be part of the definition, as considered in this report.

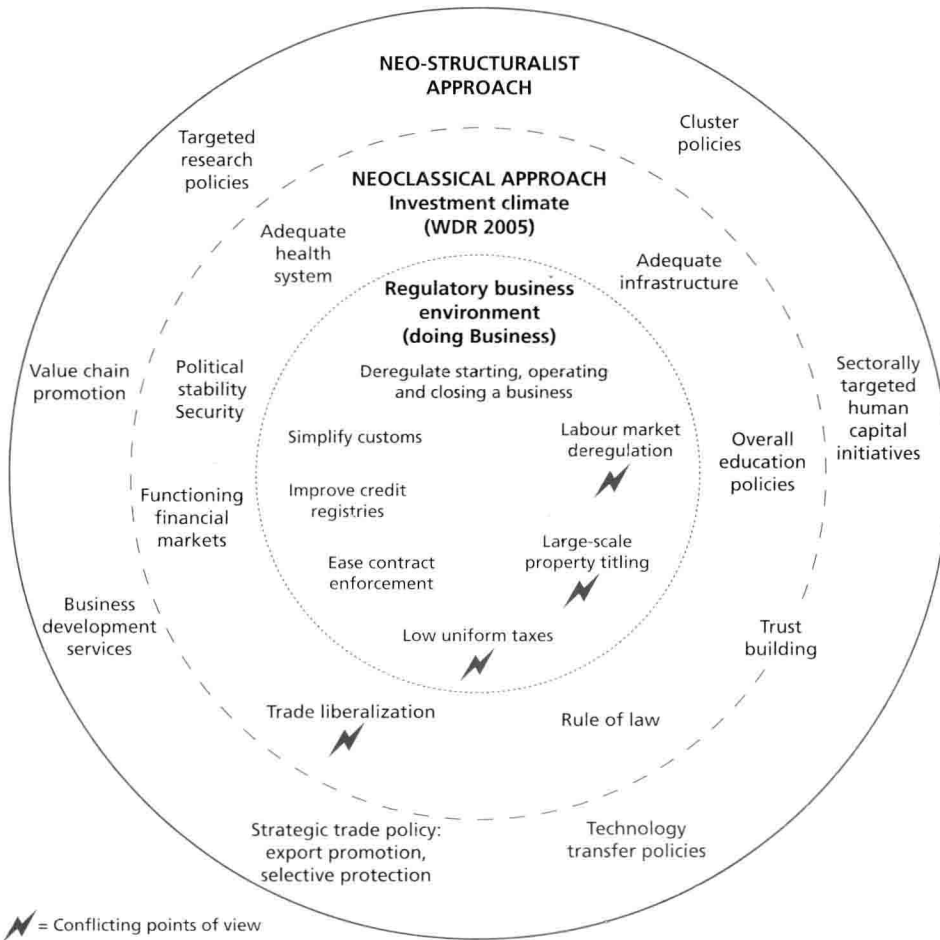
ENABLING ENVIRONMENTS: CONCEPTUAL ISSUES

The concept of an enabling environment is closely associated with private sector development and generally refers to the business-friendly conditions that must be in place to propel private sector dynamism. A joint study by the United Nations Industrial Development Organization (UNIDO) and the German Agency for Technical Cooperation (GTZ)³ distinguishes two approaches to understanding the concept of a business-enabling environment: the neoclassical and the neo-structuralist approaches (UNIDO, GTZ and German Federal Ministry for Economic Cooperation and Development, 2008). As depicted in Figure 1, the neoclassical approach is embedded within the neo-structuralist approach, which addresses a wider spectrum of elements. According to this typology, the regulatory business environment is a subset of both approaches and forms the inner circle of Figure 1.

Among the assumptions of the neoclassical framework, markets are considered to be well functioning if conditions such as the observation of property rights and the guarantee of competition exist. The neo-structuralist approach in turn emphasizes market failure and the need for corrective policies and an active role of government. Essentially, the neoclassical approach is equivalent to the concept of the investment climate advanced by the World Bank (2004). In addition to the business regulatory environment, the investment climate includes "...the quality of infrastructure, the health system, the overall level of education, the rule of law, political stability and security, functioning financial markets, trade liberalization and international rules and standards" (World Bank, 2004). Sound investment climates are expected to be beneficial to society as a whole and not to businesses only. Through conducive enabling environments, opportunities and incentives are expected to exist for firms and entrepreneurs to invest and thus contribute to employment generation and income growth. Competition is considered as playing a central role to foster innovation, efficiency and productivity. It also contributes to ensure sharing of benefits of productivity improvements with society as a whole. Policies should focus on creating the conditions for competitiveness. The policies and behaviours that governments adopt and implement play critical roles in shaping the investment climates of societies and inducing changes.

³ Now the German Agency for International Cooperation (GIZ).

FIGURE 1

The business-enabling environment: neoclassical and neo-structuralist approaches

WDR = World Development Report

Source: UNIDO, GTZ and German Federal Ministry for Economic Cooperation and Development, 2008.

The same report (UNIDO, GTZ and German Federal Ministry for Economic Cooperation and Development, 2008) contends that “...most of the elements of the inner circles in Figure 1 are generally recognized as important elements of the business-enabling environment.” Yet, the document calls attention to the fact that “...there is no consensus regarding the need for government engagement in the outer circle and in the design of some policies within the inner circle, such as regulation of land markets, labour laws and tax systems”.

Kuyvenhoven (2004) studied policy conditions that foster the development of less-favoured areas. He grouped different interventions into three broad categories:

1. price and market policies: trade and domestic policy reforms, output pricing and input delivery, market structure and channels, market failures, and environmental services;

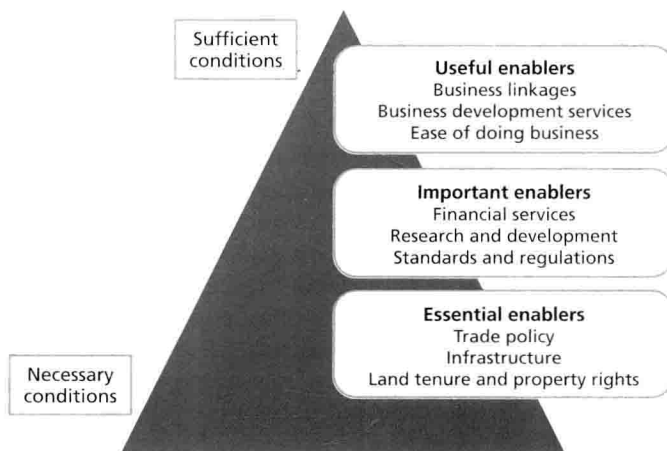
2. public services and investment: public investment, agricultural research, policy interaction, and diversification;
3. institutions and governance: including risk mitigation and safety nets.

Focusing on agribusinesses and agro-industries, Christy *et al.* (2009) called the ingredients of enabling environments the “enabling needs” (Figure 2). The nine enablers identified by these authors were derived from the proceedings of FAO’s regional workshops on enabling environments for agribusiness and agro-industrial development. At the base of the pyramid, the State must provide “essential enablers” that make possible the functioning of markets and enterprises. So-called “important enablers” are second-order activities that the State can and often does provide, such as finance, transportation and information. “Useful enablers” are defined as sufficient but not necessary conditions, including grades and standards, linking small farmers to formal markets, and business development services.

According to the World Bank, creating enabling environments is a key driver in attracting FDI and domestic investments (World Bank, 2004), while stimulation of investment is vital in reinforcing enabling environments. Investment brings structural changes to enabling environments, helps agribusinesses and agro-industries meet international market demands more effectively, and helps enabling environments transform into competitive markets. An enabling environment generally refers to creating conditions that attract investment, sometimes specifically FDI – creating a good investment climate. The investment climate reflects the array of local factors and conditions that create opportunities and incentives for businesses to invest and thrive. A large part of economic development policy is based on the principle that investment in general is a market-based solution, and on how specific firms’ strategies contribute to domestic economic growth. Economic development policy has therefore often centred on creating favourable conditions for attracting

FIGURE 2

Hierarchy of enabling needs for agro-industrial competitiveness



Source: Christy *et al.*, 2009.