UNDERSTANDING LAND INVESTMENT DEALS IN AFRICA

THE MYTH OF ECONOMIC DEVELOPMENT

LAND DEAL BRIEF | DECEMBER 2011

Overview

The belief that large-scale land investment in Africa will result in much needed economic development is strongly promoted by foreign investors, government officials, and international institutions. As a result, many African governments fervently encourage foreign investment in agricultural land and offer what some have called "mouthwatering"[1] incentives to investors. Officials trust that land deals will spur growth with incoming capital, assist with infrastructure, and create employment for local people. On their part, investors reinforce these ideas with bold promises of economic development, "modernization" and numerous jobs. AgriSol Energy Tanzania LLC,[2] for instance, claims they will transform Tanzania into a "regional agricultural powerhouse" using genetically modified crops and other technologies to increase yields.[3]

The World Bank Group describes the exchange between developing countries and foreign investors as having enormous potential – a "win-win" situation – and over the past two decades, has established a host of pro-investment structures in African countries to promote private sector development, improve countries' investment climates, and remove barriers to foreign investment in agriculture and other sectors.[4]

Despite widespread claims, the Oakland Institute's (OI) field research and analysis of more than 30 land deals across 7 countries has found that promises of economic development through land and agro-investment are often overstated. As it happens, large-scale land investment may improve some macroeconomic indicators of development, but actually result in undermined public resources, environmental and social costs to the host country, and loss of livelihoods or lost economic opportunities for citizens. Analysis of various economic issues related to foreign investment in land demonstrates that opportunity for economic development is, in fact, limited.

Investor Incentives

African governments are offering a wide range of incentives to attract foreign investment. These include fiscal incentives, such as duty exemptions, full or partial tax holidays, or tax rate reductions for specific types of activities, as well as non-fiscal incentives including allowance of expatriate employment and remittance of profits and other benefits to foreign personnel. Some countries even offer the right to develop, produce, and exploit, without limits, all resources on leased land (see Table 1 for examples of incentives). Corporate executives readily admit the importance of incentives for investment decisions.[5] Moreover, econometric studies on the effects of fiscal incentives suggest that they have become significant determinants of international direct investment flows.[6]

Forgone Public Revenue

By providing fiscal incentives, governments lose out on opportunities for direct fiscal support to local taxpayers or for domestically financed investment. Public resources forgone due to investor incentives can severely undermine a country's tax base. Import duties, for example, represent approximately 15 percent of the total government revenue in Mozambique[7] and 45 percent in Sierra Leone.[8]

This notion is supported by findings from the Stockholm School of Economics, which suggest that the use of investment incentives focusing exclusively on foreign firms is generally not an efficient way to raise national welfare.[9] Researchers conclude that the main theoretical motive for financial subsidies – spillovers of foreign technology and skills to local industry – is, in fact, not an automatic consequence of foreign investment.

Similar evidence from an International Monetary Fund (IMF) study shows that tax incentives merely reduce much-needed tax revenues without promoting growth.[10] The study finds evidence that lower corporate income tax rates and longer tax holidays are effective in attracting investment,

Table 1. Examples of Investor Incentives by Land Deal/Country

Investor/Deal Name	Country	Investor Incentives
Addax Bioenergy	Sierra Leone	• 10-year tax holiday on agricultural investments in tree crops and rice • Exemption from import duties • Allows 100% foreign ownership of land • Allows full repatriation of profits • No restrictions on expatriate employees
EmVest Limpopo	Mozambique	• Exemption from customs duties on capital inputs • Exemption from VAT • Exemption from income tax for five years from the start of operations • Reduced profit tax — 80% until 2015 and 50% from 2016 to 2025 • Profit repatriation for a base period of 25 years, renewable for 10 year periods • Optional repatriation of the investment's total equity
Malibya	Mali	• Right to transfer (out of the country) all dividends and proceeds of any kind as well as proceeds of liquidation or sale of their belongings • No land fees, no limits on water use • Total exemption from all duties and taxes related to Malibya activities for 30 years • Exemption for the first 8 years from company tax, corporation tax, and license • Exemption for the duration of the construction for 3 years of import taxes and duties on equipment, machinery, tools, spare parts and building materials required for the project
Nile Trading and Development, Inc.	South Sudan	• Right to develop, produce and exploit timber/forestry resources on the leased land • Right to trade and profit from any resulting carbon credits from timber on the leased land • Right to engage in agricultural activities, and to exploit petroleum, natural gas, as well as other minerals • Right to sublease any portion or all of the leased land to third parties

but not in boosting gross private fixed capital formation or growth.[11] Indeed, Sierra Leone's Minister of Finance and Economic Development, in a 2011 budget speech, admitted, "the existing regimes and volume of requests for duty and other tax exemptions have tended to severely erode our tax base and undermine the effective progressivity, fairness, and efficiency of the tax system."[12] According to an IMF economist, generous tax incentives on offer in Sierra Leone should be minimized and the country should work to develop infrastructure that would appeal to foreign investors instead of granting them tax holidays.[13]

The government of Mozambique offers various fiscal incentives to EmVest Asset Management, a firm that intends to use 2,000 hectares[14] in the Chokwe District for crop and livestock production. The exemption from income tax for 5 years (2010-2015) means that Mozambique forgoes nearly $1 million of public revenue a year during that period. Exemption from Customs Duties (5% capital goods) and from VAT (17%

capital goods) further erodes the potential for the investment to bring income to the country.[15]

Similar fiscal incentives are being negotiated between the government of Tanzania and AgriSol, for a 325,000 hectare project for corn, soybean, sorghum, and sugarcane cultivation. These incentives may imply substantial unattained revenue for the government, as they include exemption from customs duties on all agricultural inputs, exemption from value-added tax (VAT) on all imported inputs, as well as unprocessed agricultural produce, guaranteed transfer of net profits or dividends of the investment and remittance of net proceeds.[16] AgriSol will generate significant profits through its project. While it intends to invest $100 million over a 10 year period, if corn is cultivated on only 200,000 of these 325,000 hectares, net profits for the company could be $272 million a year, an amount which nearly equals the total budget of Tanzania's Ministry of Agriculture.[17] The investor is seeking the award of Strategic Investor Status that would include an exemption from the corporate tax, currently 30 percent of this amount.[18]

A report by Uwazi, an East African NGO, estimated that 2009/10 tax exemptions in Tanzania amounted to TZS 695 billion ($425 million), more than half the TZS 1.3 trillion ($795 million) the government planned to borrow from commercial sources for infrastructure financing in 2010/11. "Had it been collected, it would have provided 40 percent more resources for education or 72 percent more resources for health in 2009/10."[19]

No Limits on Profit Repatriation or Exports

Many African countries also allow foreign investors full repatriation of profits, forgoing another opportunity to boost public resources. In the case of Tanzania, under the *1997 Investment Act*, foreign investors are guaranteed the transfer of all net profits or dividends of their investment.

In addition to few limits on profit repatriation, little restriction is placed on the export of produce itself. Consequently, little investment occurs in local processing which would potentially increase employment opportunities within the host country. Land deal proponents often claim the benefits of added value to local markets, such as supporters of the Addax Bioenergy deal, who have argued that the company's ethanol production will provide a boost to Sierra Leone's energy market, greatly reducing its dependence on crude oil.[20] Yet multiple sources, including Addax's own Managing Director, Nikolai Germann, affirm that in reality there is no market for ethanol in Sierra Leone and that less than 10 percent of ethanol will stay for local use.[21] In most countries studied, land contracts do not require that the crops produced be sold within the country.[22]

Taking Advantage of Taxation Loopholes

Finally, by registering their company or fund in tax havens, such as Cayman Islands or Isle of Man, many foreign investors minimize taxes and potential for fiscal revenues that could be generated from their operations. Mauritius also offers a very favorable tax regime, which has attracted a number of companies that are investing in Africa. First, Mauritius has double-tax avoidance agreements (double-tax treaties) with a number of African countries, thereby preventing taxation of investments by two or more countries on the same income or asset.[23] The island also offers other benefits for offshore companies, including provision of lower tax rates on corporate incomes (15 percent), as well as exemption from stamp duty, land transfer tax, and capital gains tax.[24]

For these reasons, many foreign companies and institutional investors choose to incorporate in Mauritius and operate elsewhere. Emergent Asset Management, for example, has local holding companies for its assets in each African country where it does business, but the ownership of each holding company is located in Mauritius in order to benefit from "tax efficiency."[25] Emergent and other investors located in Mauritius, therefore, enjoy the levy of tax on capital gains in their countries of operation, and as no such tax on capital gains exists in Mauritius, they assume minimum taxation in Mauritius as well.

The island nation's financial regime thus represents a quasi tax haven, and has facilitated the incorporation of companies and funds who, for all practical purposes, are paper companies whose control and management is almost wholly outside Mauritius.[26]

Low Land Prices and Rental Fees

African land is readily offered in huge tracts and at extremely low prices or lease rates compared to other continents (see Tables 2 and 3).

Table 2. Sampling of Farmland Lease Fees by Land Deal

Location	Deal	Price $/ha/yr	Lease Terms
Ethiopia	Saudi Star	Free land rent	10,000 ha; 60-year lease
Mali	Malibya	Free land rent	100,000 ha; 50-year lease
Ethiopia	Karuturi	6.75*	300,000 ha; 99-year lease
Sudan	Nile Trading and Development	0.04	600,000 ha at $25,000; 49-year lease
Sierra Leone	Sierra Leone Agriculture	2	43,000 ha; 45-year lease
Sierra Leone	Quifel Agribusiness SL Limited	5	126,000 ha; 49-year lease

Source: Based on Oakland Institute field research, October 2010-June 2011

* Karuturi initially received their land for just $ 1.25/ha (20 birr/ha) but subsequent negotiation with the federal government has raised that price to $ 6.75/ha (111 birr/ha).

Table 3. Sampling of Average Farmland Prices by Country, 2010

Location	Average price $/ha/yr
New Zealand (dairy)	23,000
England (average all land types)	22,000
US (dryland in corn belt)	16,000
Poland	4,550-8,125
Brazil (Mato Grosso dryland)	7,000
Argentina (Central provinces)	5,000-10,000

Source: The Knight Frank Farmland Index 2010

Low prices are certainly attractive to foreign investors. According to Susan Payne, CEO of Emergent Asset Management,

> "In South Africa and Sub Saharan Africa the cost of agriland, arable, good agriland that we're buying is one-seventh of the price of similar land in Argentina, Brazil and America. That alone is an arbitrage opportunity. We could be moronic and not grow anything and we think we will make money over the next decade."[27]

The benefits of investment for host countries is undermined by these low prices. Payne alludes to the fact that, because of low land prices, it is perhaps in the investor's best interest to sit on the land and profit from arbitrage between low land acquisition prices compared to sales values as the market improves. While such speculation often entails higher risk, returns on speculative investments in African farmland have been reported to reach 25 percent.[28] Indeed, many of the land deals investigated by the Oakland Institute are not yet operational, indicating that investments may have been made solely for speculative rather than productive purposes.

Weak Environmental/Resource Use Regulation

In addition to low land prices, the lack of regulation surrounding land deals undermines the potential for host countries to economically benefit from their own natural wealth. Oakland Institute's investigations confirmed that for many land deals, resource use within lease areas is largely unregulated, and valuable natural resources are extracted and exported at will. For instance, South Sudan offered full rights to the Texas-based Nile Trading and Development, Inc.

("NTD") to lease, plant, extract, and export any resources within its 600,000 ha lease area (see Table 1). By granting foreign investors the right to exploit all timber and mineral resources on leased land and recoup the majority of the profits, South Sudan forgoes the opportunity to economically benefit from its own resource base.[29]

Similarly, water use by foreign investors is greatly under-regulated. In addition to land, arguably the most important resource for ensuring the long-term economic stability of African nations is access to water. Researchers have alluded to land grabs as "virtual water grabs," as not only land, but also water resources are being ceded to foreign entities for the duration of their leases, the majority of which are 50 to 99 years.[30]

The Malibya project, for instance, is charged negligible fees for unlimited water extraction from the Niger River for the next 50 years, while millions of people downstream are dependent on sustained river flows.[31] The Office du Niger constitutes one of the most important and biodiverse inland wetlands in West Africa. Despite being considered a "fragile zone" by Mali's Ministry of Environment and Sanitation, no studies have been undertaken to assess the environmental effects of large-scale agricultural investment in this region, including how much water can be extracted without negatively impacting populations downstream. Such large-scale environmental impacts have long-term economic consequences for the country, as reduction of water resources below critical levels will render surrounding land futile for agricultural purposes as well as devastate communities dependent on sustained flows.

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Job Creation

An expectation from agricultural investment is the prospect of employment creation. Investors claim that their projects are "socially responsible," as they promise to boost local income through new positions and contractual arrangements, such as farmer outgrower schemes. Yet, the majority of land deals investigated by OI offer basic wage labor employment, mostly low-paying laborer positions, which present a number of disadvantages. First, according to the World Bank, wage labor income by itself amounts to 2 to 10 times less than the income of the average smallholder.[32] Second, most agricultural wage labor positions are seasonal. Thus, the impressive number of positions to be created, such as the 20,000 to 30,000 employees to be hired by Karuturi in Ethiopia are misleading in terms of actual employment creation for local development.

Also, a large body of research backs the notion that small farms are more productive, biodiverse, and sustainable than large, industrial-style plantations, and in terms of local peoples' wellbeing, small-scale agriculture offers a number of benefits. In the first place, goods that come from small farms are relatively less capital-intensive than goods from large farms, meaning that more labor is used to produce each unit. Therefore, small farms employ relatively more labor, including rural unskilled laborers, than do large farms, providing more gainful livelihood options for locals. Secondly, small farms have higher output per land unit because they utilize their land more efficiently, growing multiple crops, thereby improving local food security. Small farms also are more productive because of their relatively high concentration of labor per hectare compared to larger farms.[33] Additionally, because the household is the main workforce, the costs of supervision are low[34] – household labor is generally self-supervising in effort and diligence.[35]

Lastly, small farms' utilization of relatively more labor per land unit naturally distributes a relatively larger portion of their profits, revenues, and output to their laborers. The average farm size for crop-based farming in Mali is just 4.7 ha, and one third of the 805,000 farm households cultivate less than 1 ha.[36] To put in perspective the recent large land deals identified by OI research in Mali, the area they cover could sustain conservatively 112,537 farm families,[37] well over half a million people (686,478).[38] Instead, that land is now concentrated in the hands of 22 investors, who are planning to employ a few thousand plantation workers.[39]

Infrastructure Development

Investors promise infrastructure, such as roads, canals, and irrigation systems, as a key development benefit to host countries. Constructing roads may be valuable to improve farmers' access to markets and ease the movement of food between food surplus and food deficit areas. Yet, such projects can lead to undesirable outcomes, such as internal displacement and disruption of cattle and people's movements. In Mali, the construction of a 40-kilometer irrigation canal and adjacent road by the Malibya company resulted in massive disruption in the region of Kolongo, as houses and farms were destroyed and feeding grounds obstructed.[40] Also, because canals and other infrastructural projects are built for the sole use of investors, and because their leases typically entail holdings of between 50 and 99 years, such infrastructure will prove useless to local communities for the duration of these leases.

Furthermore, the development of land for large-scale agricultural operations oftentimes disrupts or destroys local livelihood patterns, which poses a major hindrance to economic opportunity at the local level. Construction of the canal for the Malibya project in 2009 in Mali closed the small irrigation channels that were watering the market gardens of the women farmers' groups in that area. The AgriSol deal in Tanzania requires the removal of 162,000 people who have been farming on the land for several decades.[41] The development of plantations in the South Omo region of Ethiopia threatens the lives of half a million agro-pastoralists who will lose access to grazing lands, areas of wild food harvest, loss of the ability to grow food along the Omo River, and water sources.[42]

In all 7 countries studied, OI researchers found an alarming pattern of loss of important natural resources and displacement of small farmers by foreign land investment projects.[43] Small farmers and pastoralists have been hit hard by the loss of livelihoods and economic independence as their lands are given away with little compensation and/or job replacement in exchange. The OI research thus demonstrates that for local people, there is a deep downside to large-scale agricultural investment.

The views and conclusions expressed in this publication are opinions of the Oakland Institute alone.

ENDNOTES

1 Sai Ramakrishna Karuturi, CEO of Karuturi Global Ltd, conversation regarding Ethiopian investment with Oakland Institute researcher Felix Horne, November 2010.

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10 See: Alexander Klemm and Stefan Van Parys, "Empirical evidence on the effects of tax incentives," IMF Working Paper 09/136, Washington, DC: IMF, 1 July 2009, www.imf.org/external/pubs/ft/wp/2009/wp09136.pdf (accessed 21 January 2011).

11 Ibid.

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13 IMF economist, Freetown, Sierra Leone, direct communication, 12 October 2011.

14 EmVest provides conflicting reports of the extent of its land concessions as it describes a 2,000-ha lease whereas government legal documents mention only 1,000 ha.

15 Source: based on data from EmVest Investment Proposal and Rep. of Mozambique EmVest Authorization document. Such incentives are compounded through other provisions including cheap irrigation which is facilitated by unlimited access to water charged by surface irrigated rather than total volume used.

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19 *Uwasi,* "Tanzania's Tax Exemptions: Are they too high and making us too dependent on foreign aid?" October 2010.

20 *Sierra Express Media*, "President Koroma hails Addax Groups multi-million dollar Bio-fuel investment in Sierra Leone," 11 February 2010, http://www.sierraexpressmedia.com/archives/5834 (accessed 18 April 2011).

21 *Sierra Express Media*, "Down With Addax's $200M 'Investment.' It's not good for Sierra Leone!" 3 March 2010, http://www.sierraexpressmedia.com/archives/6236 (accessed 18 April 2011).

22 See the different Oakland Institute country reports in the series "Understanding Land Investment Deals in Africa" at www.oaklandinstitute.org.

23 LowTax Global Tax and Business Portal, "Mauritius: Double Tax Treaties," available at: http://www.lowtax.net/lowtax/html/jm2tax.html (accessed 19 July 2011). It is not unusual for a business or individual who is resident in one country to make a taxable gain in another. This person may find that he is obliged by domestic laws to pay tax on that gain locally and pay again in the country in which the gain was made. Many nations thus make bilateral double taxation agreements with each other. In some cases, this requires that tax be paid in the country of residence and be exempt in the country in which it arises. In the remaining cases, the country where the gain arises deducts taxation at source ("withholding tax") and the taxpayer receives a compensating foreign tax credit in the country of residence to reflect the fact that tax has already been paid.

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43 See the different Oakland Institute country reports and briefs that detail the issue of displacing smallholder farmers in the series "Understanding Land Investment Deals in Africa" at www.oaklandinstitute.org.

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