AGRIBUSINESS AND COMPETITIVE AGRO-INDUSTRIES IN THE ASIA AND PACIFIC REGION

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INTRODUCTION

Food and agricultural systems in many countries in the Asia-Pacific region are moving rapidly towards market-driven systems, with a greater reliance on input markets and growth of post-production enterprises. The role of the private sector is becoming increasingly important, smallholder farming is becoming commercialized, and the impact of agribusiness and agro-industry on economic and social development is increasingly being felt. Many governments in the region are responding to these changes through policy and program reforms and increased investments designed to accelerate the pace of agribusiness and agro-industry development.

A large and growing number of governments within the region have reformed their policies, adjusted programmatic priorities, and increased investments in order to accelerate the pace of agribusiness and agro-industry development. An analysis of trends and challenges highlights the growing importance of agribusiness and agro-industries in developing regions; the crucial role agro-industries play in economic development and poverty reduction; and the urgent need to rebalance policies, institutions and services focusing on agribusiness and agro-industries development.

SECTOR TRENDS AND IMPACTS

Changes in the agri-food systems within the Asia-Pacific region are being driven by rising per capita incomes, technological changes, trade liberalization and urbanization. Higher incomes, changing diets and increasing numbers of women in wage employment are leading to greater demand for high-value commodities, processed products and pre-prepared foods.

Diets are changing and increasingly include more animal products, such as fish, meat and dairy products, as well as fruits and vegetables. Staple crops are still the source of agricultural value addition, but are increasingly being differentiated into a range of products and services in order to meet quality and delivery standards of agro-industries.

Soaring prices for many traditional agricultural commodities suggests that the long-term decline in agricultural commodity real prices has ended and that an agricultural growth strategy based on expanding primary commodity production is more viable now than it has been over the past two decades.

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The prospects in developing countries for further expansion of food manufacturing appear to be greater than for the supply of primary commodities. Over the past 25 years, global manufacturing value addition for food, beverages, tobacco, textiles and leather products – the main agro-industry manufacturing product categories tracked by UNIDO – generated by developing countries has nearly doubled. For cotton textiles, developing countries accounted for 22 percent of value addition in 1980 but more than 40 percent in 2005. Tobacco accounted for the largest increase, reaching 44 percent of global value addition in 2005. European Union countries collectively accounted for the largest share of manufacturing value addition for foods and beverages in 2005 – a share it has maintained since 1980; however, by 2005, developing countries together accounted for 23 percent of the share of manufacturing value addition, as compared to 21 percent from Japan and 19 percent from North America.

There are large regional disparities among developing regions in the distribution of formal sector agro-industry value addition. For food and beverages, Latin American and South and Southeast Asian countries respectively accounted for nearly 43 and 39 percent of value addition in 2003. In contrast, African countries contributed less than 10 percent of value addition. There are similar disparities and patterns in value addition for tobacco products, textiles and leather products, although South and Southeast Asian countries account for a higher share of value addition for these product categories than Latin American countries.

Substantial organizational and institutional changes have taken place in the agricultural sector of most developing countries. These changes include:

- Growing concentration at all levels, particularly in the retail and processing sectors;
- Agribusiness enterprises are getting larger as firms seek economies of scale in food manufacturing, marketing and distribution;
- Private sector standards for food quality and safety are proliferating;
- Transactions of foods are increasingly being arranged through the use of contracts;
- More large-scale retailers and manufacturers are relying on specialized procurement channels and dedicated wholesalers; and
- Food is increasingly being "pulled" into formal sector retail outlets, such as supermarkets, rather than grown for sale in local markets.

Food distribution systems in developing countries have seen some notable changes over the past two decades. The structural transformation of the retail sector took off in Central Europe, South America and East Asia (excluding China) in the early 1990s. The share of food retail sales of supermarkets grew from around 10 percent to 50 to 60 percent in these regions. By the mid- to late 1990s, the share of food retail sales in Central American and Southeast Asian supermarkets accounted for 30 to 50 percent of total food retail sales. Starting in the late 1990s and early 2000s, substantial structural changes occurred in Eastern Europe, South Asia and parts of Africa where the share of food retail sales in supermarkets rose from five to 10 percent in less than a decade, and is growing by 20 to 40 percent a year.

The changes in agri-food systems have significant implications for growth, poverty and food security. On the positive side, there is a rapid increase of value addition opportunities through agribusiness relative to primary production. Agro-processing enterprises are stimulating demand and the effective market size for farmers' products. Exporters and agro-processing enterprises are providing crucial inputs and services to the farm sector for those with access to such inputs. This is encouraging productivity and product quality improvements. Agro-industries are also stimulating market-induced innovation through value chains and networks, and domestic and export systems are increasingly becoming more mutually supportive.

While agribusiness and agro-industry development can increase competitiveness in international and domestic markets, the benefits are not automatic and will certainly not be shared by all.[2] Changes in agri-food systems pose particular risks for smallholder farmers, traders, processors, wholesale markets and retailers. Smallholder farmers are experiencing short-term difficulties in meeting agro-industry standards and contractual requirements; small-scale processors have increasingly to compete with larger scale food manufacturers that can benefit from economies of scale in processing technologies; and traders in local markets will be squeezed by the growing importance of specialized procurement practices and certified products.

There is no broad agreement on how the changes in agri-food systems will influence traditional players (i.e. wholesale markets, small traders and small businesses) in the long run. Current indications suggest that some sectors will experience significant impacts while other sectors will see more limited impacts from these changes. There is, however, agreement that the development of agribusiness and agro-industries will be context-specific and will be dependent on the product sector, market requirements, the development stage of a particular country or area, agricultural sector policies, institutions and services, as well as government actions to promote agro-industries and agricultural value chains.

If agribusiness development is to play a key role in reducing rural poverty in the Asia-Pacific region, then governments will need to create enabling conditions for agribusiness, while monitoring and taking the necessary steps to protect and enhance the livelihoods of smallholder farmers and other members of rural and urban communities most likely to be affected by agribusiness and agro-industry development.

ENABLING POLICIES AND INSTITUTIONS

The business environment represents one of the most important drivers of competitiveness for domestic and export-oriented agro-enterprises and agro-industries. Although many countries in the region have implemented major policy reforms over the past two decades, the business environment is still far from being conducive for agribusiness and agro-industries. Many countries continue to have complex laws and regulations governing business activities, ineffective systems for enforcing intellectual property rights, inadequate commercial services, lack of infrastructure, ineffective local government, and weak information and communication technology systems.

There are large and growing disparities both within and between regions in the creation of enabling business environments. The World Bank's "Doing Business 2008" shows a

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[2] Unfortunately, it is not possible to quantitatively characterize the impacts of agribusiness development on employment, value addition and rural incomes because national statistical surveys do not collect or report the necessary data on the informal and formal sectors, as well as on small, medium-sized and large entreprises.

continuing large gap between OECD countries and countries in the Asia-Pacific region with respect to procedures, time required and costs for enforcing contracts, starting a business, dealing with licenses and trading across borders. Consequently, farms and firms have to be much more efficient and better managed than their counterparts in other regions just to overcome the extra costs involved in operating in contexts with poor business investment policies and measures.

Cross-regional appraisals and country case studies focusing on issues, such as farm-agribusiness linkages, contract farming, farm commercialization, small enterprise development and changing retail procurement practices, a number of priorities for policy reform and institutional strengthening have been identified, these include:

- Legal and regulatory frameworks for resources, assets and business operations;
- Public sector cooperation with the private sector;
- Development of industry and producer organizations; and
- Clarification of institutional mandates for supporting investment in agribusiness and agro-industries.

Legal and regulatory frameworks that define rules and determine rights and obligations with respect to resources, assets and business operations are particularly important. For example, domestic and international investors are likely to expect protection of intellectual property rights (e.g. brands, genetic materials), and will also consider the extent to which they may be disadvantaged by legal or procedural preferences favoring government-owned or assisted enterprises. The rules and regulations under which commodity markets, exchanges and auctions operate also impact heavily on agribusiness investment. The regulatory framework is also crucially important as it establishes rules relating to employment conditions and contracting that affect agribusiness profitability, as well as the distribution of benefits from agribusiness development.

For example, the government in Myanmar is establishing grades and standards for edible oil production and trade, privatizing state-owned processing facilities and enhancing the roles of the private sector and commodity associations in promoting the development of the edible oil sector.

Strengthening public sector cooperation with the private sector merits particular attention. Strong communication and cooperation between the public and private sectors are essential because agro-industry development is generally driven by the private sector. The public sector can, for example, direct its science and technology investments to support private sector innovation and product development and, in doing so, also mobilize the assets, specialized knowledge, and capacities of agribusiness firms. Policy initiatives to attract foreign direct investments can improve national access to new technologies, as well as the introduction of new management methods and new agricultural business models. As another example, public-private sector cooperation can enhance the effectiveness of regulatory frameworks and private sector compliance.

For example, the government in China is encouraging the establishment of "leading enterprises" as a link between farmers and local markets. "Leading enterprises" are privately owned companies that have been selected by local authorities to invest in village assets of land and labour by building infrastructure, and provide training and extension services to farmers in close collaboration with local authorities.

Commodity, regional, industrial and/or professionally-based associations, including producer organizations and cooperatives, have valuable roles to play in connecting producers and clients, crystallizing and expressing the viewpoints of similar groups, taking collective action, networking among themselves, facilitating linkages with other enterprises and organizations, and providing training, information, technology and legal support.

For example, Chambers of Commerce in the Philippines, composed of producers, traders, input suppliers, exporters or processors and key ministry officials, are actively encouraged to facilitate dialogue between the government and various value-chain participants.

Trade-offs between the pace and nature of agro-industrial development and poverty and food security objectives need to be identified and addressed. Rapid agro-industrial development could displace small farmers, processors, stores and traders who depend on traditional marketing and distribution channels at a pace which does not allow enough time to create alternative opportunities. Moreover, it is unlikely that policies aimed at agribusiness and agro-industrial development can by themselves address food insecurity and poverty.

For example, the government in Viet Nam is actively encouraging the development of industries related to agricultural raw products in rural areas in order to complement existing agricultural activities, thus following a policy example set by Taiwan Province of China. Land reforms and the strengthening of farmers' associations have also helped preserve agriculture and populations in rural areas. The government has also promoted private sector activities in rural areas, thereby encouraging rising agricultural productivity and incomes, while at the same time investing in rural infrastructure in order to provide easier access to markets and social services and attract industries.

Review of institutional mandates for influencing, regulating and supporting private sector investment in agribusiness and agro-industry is required. Ministries of agriculture operate under specific mandates and few – if any – ministries have mandates over all the different issues that enable or inhibit agribusiness and agro-industry development. Mechanisms are needed to strengthen linkages among public agencies responsible for policies, institutions and services impacting on agribusiness and agro-industry.

For example, a project co-funded by the Canadian International Development Agency, the Ministry of Agriculture and the Ministry of Commerce of the People's Republic of China, aims to assist smallholder farmers to adapt to global markets. High-level representatives from eight different ministries and state administrations sit as members on the project's board of directors. The project thus fosters interministerial dialogue and discussions on issues related to smallholder farmers and global markets.

AGRO-INDUSTRY AND VALUE CHAIN PROGRAMS

There is an increasing need for value chain programs that seek to improve the delivery of services to agro-industries, create value addition for small farmers and help farmers respond to changing markets and consumer requirements. Many countries have launched programs to support the development of specific agro-industries and value chains. In most cases, these programs have complemented agribusiness-related policy reforms and institutional strengthening. Particular attention has been given to strengthening business linkages, reducing transactions costs, fostering a better alignment of the capacities of farms and firms to collaborate on meeting requirements, ensuring fair governance within chains, improving market intelligence, improving management practices, strengthening producer organizations and upgrading technologies.

For example, between 1993 and 2003 World Bank projects have encouraged the establishment of Agribusiness Development Centres (ADCs) in order to provide advisory and analytical services to private sector agro-enterprises in a number of countries in the Asia-Pacific region. Since 2000, the Asian Development Bank has provided support for agribusiness and agro-industry projects to more than 10 countries in the Asia-Pacific region. FAO also provides support for the development of specific agro-industries and value chains in all agricultural sectors (crop, livestock, forestry and fishery) and reviews, appraises and applies value chain concepts and methods systematically.

There are a number of reasons why some governments in the Asia-Pacific region are supporting the development of specific agro-industries and value chains, most of which relate to public sector developmental objectives, or which have public-goods characteristics. These reasons include:

- Progress being made in one part of the value chain should not be negated by poor performance in other parts of the chain. For example, when farm productivity is increased complementary attention must be given to agro-enterprises responsible for post-production product handling, processing and distribution.
- Public sector facilitation and information provision can help in developing productive partnerships among firms in value chains. Although collaboration between firms is increasingly important, developing the trust and commitment that is crucial to achieve partnerships and chain integration is neither easy nor without costs. The public sector can absorb some of the high transaction and information costs, as well as the risks that often discourage potential lead firms from developing value chains.
- When governments participate in value chain development, they can help ensure fair governance in value chains. There is concern that if agribusiness and agro-industry development is left entirely to the private sector, the larger scale and more powerful participants will capture most of the benefits leaving disproportionately small gains for the farmers and smaller agro-enterprises that might participate in the chains. Governments can, for example, provide advisory support to producer organizations on contracts negotiation and compliance. Ancillary development of financial institutions, products and services to fund agribusiness undertakings can help to level negotiating positions and equities among chain participants.
- Governments can provide support to improve the performance of domestic market value chains that may not be able to attract private investment by themselves. Multinational firms and large-scale national firms can and do invest in establishing global value chains, but agro-industry and value chain promotion is seen in many countries as not simply a trade competitiveness issue. There is in particular an interest in reinforcing value chains for products based on local and traditional crops, where small-farmers may have some comparative advantage and specialized knowledge.

FAO regional appraisals, case studies and country experiences point to **several key lessons** on strategies and interventions for promoting specific agro-industries and value chains, while ensuring that smallholder farmers and small agro-enterprises can benefit from agribusiness and agro-industry development:

- The public sector can use public-private partnerships to ensure that the **specialized management competencies and technical expertise of private sector firms are directed at benefiting small farmers and processors**. As one example, public-private partnership in research and dissemination of results can improve the technologies available to small scale producers and processors.
- The public sector, in partnership with chain partners, needs to **strengthen the entrepreneurial capacities of farmers** to understand and meet the timing, quality and safety requirements of processors, exporters, importers and retailers. Capacity-building should also address the start-up financing and development of small- and medium-sized agro-processing enterprises.
- Value chain programs should **facilitate and support farmer organizations and producer alliances**. By consolidating their interests, small producers can achieve economies of scale in buying inputs and selling products. Producer associations and cooperatives can provide a platform for small farmers to do business with larger-scale input suppliers, traders, agro-processors and retailers. Such associations need to be profitable in order to be sustainable in the long run: business management capacities and governance issues are therefore important in this respect.
- Specific attention is needed to **reinforce financial and business services to small farmers and processors**. Business services that help firms to improve the quality and efficiency of their processes, reduce their costs and expand their operations are important to all firms and especially critical to smallholder farmers, small firms and new start-ups whose transaction costs are large in relation to the size of their output. Services can and often are embedded in the contracts established between producers, agro-processors, exporters and other firms.
- It is important to anticipate future vulnerabilities and **build the capacities of chain participants to innovate, diversify or exit as markets change**. Just as is the case for enterprise development programs, support for specific value chains can increase vulnerability if incentives induce farmers and firms to develop skills and assets that are specific to products and services susceptible to large shifts in demand and prices.
- The potential of value chain programs for improving livelihoods, but also for increasing vulnerability puts a premium on appraisals of comparative advantage and investment requirements in the exploratory and diagnostics phase before intervention. During programme implementation, attention is needed to **monitor and assess impacts and the distribution of benefits**.
- **Public sector engagement with the private sector** to support specific agro-industries and value chains can be an important dimension of the global partnership for development envisaged in Goal 8 of the Millennium Development Goals. The above public sector actions will help ensure that agro-industries are rules-based and non-discriminatory, and include a commitment to good governance, development and poverty reduction. Proactive support for specific agro-industries is particularly needed to address the constraints faced by least developed and landlocked countries, as well as small island developing states.

- **Support for specific agro-industries and value chains** can also help reduce the cost of food, increase employment opportunities, and provide incentives for sound environmental management practices, thereby also contribute to alleviating extreme hunger and poverty and ensuring environmental sustainability.

INDUSTRY STANDARDS AND QUALITY REQUIREMENTS

One of the most significant challenges faced by the public sector in relation to agribusiness development is the rapid proliferation of industry standards and quality requirements. Many agribusiness firms, industry organizations and consortia have over the past decade developed their own standards and quality requirements, which often surpass public standards. The main objective of most industry standards and requirements is to manage risks relating to product safety and quality, improve consistency of food quality and safety, enable the comparison of prices between suppliers, reduce transaction costs and strengthen consumer confidence and loyalty.

A distinguishing feature of industry standards and quality requirement programs is the existence of some type of branding or labeling along with certification. Private sector retailers and food manufacturers initially took the lead in developing branding, labeling and certification capacities in their supply chains in response to consumer. In some cases, brands and labels are used to differentiate specific products to consumers, in other cases certification is carried out on a business-to-business basis and consumers are informed about supply chain practices but not on a product specific basis.

More recently, several inter-professional organizations have been driving development of process, as well as product industry standards and requirements. Some of the better known organizations working on certification programs are: Fairtrade Labeling Organizations International (FLO); Social Accountability International (SAI); Sustainable Agriculture Network/Rainforest Alliance; the Sustainable Food Laboratory (SFL); and the International Federation of Organic Agriculture Movements (IFOAM). Perhaps the best known is the GLOBALGAP consortium, developed by selected European retailers, that now includes partners in more than 70 countries worldwide.

As is the case for international standards and frameworks, **industry standards and requirements can make a significant contribution to agribusiness and agro-industries development**. By establishing standards, the agro-food industry ensures consumer protection and provides both incentives and sanctions for improvement of product quality and safety. Quality assurance and control systems are put in place, and inspections and controls are enforced. The proliferation of industry standards has resulted in a number of positive, as well as negative impacts for agribusinesses in the Asia-Pacific region.

As product specifications and certification requirements advance, it is unlikely that poorer countries will be able to keep up and benefit from their lower labor. Many industry standards and requirements cannot be met, or if they can only at very high cost in countries that lack access to sophisticated technologies, efficient and low-cost communication and information systems, adequate infrastructure, and supportive institutions and services.

Governments can play a role in optimizing the impacts and improving the fairness of industry standards and requirements, including by initiating a dialogue on standards between the public and private sectors. Several measures can strengthen capacity for compliance and certification while reducing costs, including: reform of institutions and legal frameworks; investments in physical facilities, laboratories, equipment and other kinds of infrastructure; reinforcement of institutions charged with responsibility for food safety, control of frauds, animal and plant health; strengthening of applied science capacity and facilities; provision of technical assistance to build capabilities at different levels; public-private alliances to strengthen participation of small-scale producers; and market feasibility and impact studies.

RESPONDING TO THE CHALLENGES

The trends toward **increasing concentration, vertical coordination and contracting** in agricultural sectors within the Asia-Pacific region will certainly continue. A rebalancing of agricultural policies, institutions and services that focus on agribusiness and agro-industry development will be required sooner or later. Deliberate and strategic interventions by governments can play an important role in fostering the development of agro-industries and value chains. However, few governments have developed a coherent vision for agribusiness development. Moreover, coping with the complex challenges of agribusiness and agro-industries development exceeds the capacity of most public sector agencies. Responding to the challenges of agribusiness and agro-industries development will require increased attention to, and enhanced capacity for, the following public sector actions relating to:

Information and analysis

- Analysis of country, regional and global trends, changes and factors affecting the transformation of agri-food systems;
- Characterization and appraisal of the structure of agro-industries and value chains linking input suppliers and producers through to final retail markets;
- Diagnostic analysis and benchmarking of agro-industries and value chains to identify strategies for agro-industry and value chain development; and
- Development of information and knowledge management systems for agribusiness as well as small-scale producers and processors, and inter-professional organizations.

Enabling policies, institutions and services

- Formulation and implementation of strategies for improving agribusiness and agro-industry policies, legal and regulatory frameworks, institutions and services;
- Incorporation of agribusiness and agro-industry development strategies and actions into country-level programme frameworks and strategic plans for agricultural development;
- Reinforcement of communication and cooperation with private sector firms, foundations and NGOs active in agribusiness and agro-industry development;
- Reinforcement of compliance and certification systems for food safety standards and industry quality requirements;

- Reinforcement of market information services and financial institutions and services for market-oriented farmers and agro-enterprises; and
- Provision of basic infrastructure to improve market access and reduce business costs.

Support for specific agro-industries and value chains

- Appraisal of market and agribusiness opportunities and sound methods for prioritizing specific agro-industries and value chains;
- Facilitation of innovative arrangements linking smallholder farmers with commercial farmers, exporters or agro-processing firms in long-term relationships combining cooperation, coordination and services provision;
- Identification of innovative micro-financing products that facilitate the participation of small farmers in agribusiness ventures;
- Design and implementation of initiatives that improve entrepreneurial capacities of smallholder farmers and small agro-enterprises to participate in value chains for high-value products, including branded and certified products; and
- Identification and use of innovative mechanisms to link public funding with private sector resources.