

### AFRICA'S AGRICULTURAL POTENTIAL Lessons from African countries on private investment and value addition

*From the African Community of Practice on Managing for Development  
Results at the African Capacity Building Foundation (ACBF)*



Case Study  
N° 53

#### SYNOPSIS

Africa has enormous agricultural potential to eliminate hunger and poverty. This potential lies in the fertile land and abundant water, human, and natural resources as well as rapidly expanding markets. Historically, Africa's agricultural investment models have been based on harnessing small-scale indigenous farming, but output from these models are unlikely to increase production at the national level. However, many of the large scale private agricultural investments made by overseas operators have often been exploitative rather than cooperative. This paper examines Africa's agricultural potential and value largely based on secondary literature. The paper further highlights two contrasting case studies in Morocco and Ethiopia.

**Key findings:** Investments that combine a commercial farming approach underpinned by significant capital investment with local small-scale farming have the potential to develop African agriculture in a sustainable and profitable manner. Agricultural value chain including storage, processing and transportation can reduce the volatility of returns if all stakeholders have the required knowledge, capacities and tools. Thus, by adopting the value chain approach, private investments can increase productivity and profitability of Africa's agricultural industry. Additionally, private investments require sound regulatory and institutional frameworks to enable them take advantage of new opportunities including innovations in information, science and technologies that have several applications at different stages in the value chains.

**Main lessons:** The case studies revealed that integrating private investments to national objectives is an important determinant of success in commercially-oriented small-scale agriculture. Secondly, the effectiveness and sustainability of private agricultural investments depend not only on their economic viability but also their socio-cultural implications.

**Key recommendations:** Large scale private investments ought to ensure government buy-in for their success. Furthermore, it is important for government policies to aim at promotion of not only economically viable but also socially and culturally acceptable private sector investments in agriculture. Beside, such policies should incentivise private sector to include smallholders in value chains. Governments should also develop regional value chains for strategic agricultural commodities, especially those identified by the African Union Food Security Summit in Abuja, for African countries to enhance their agricultural transformation and global competitiveness. Finally, capacity building efforts are required especially in skills training. In particular, training on cost-benefit analysis and value chains management. Relatedly, support with agricultural research to inform policies as well as statistics availability (on land use for example) to guide investors is critical. Such capacity building efforts would complement the African governments' approach to develop competitive agricultural systems and related policies as necessary.

## Introduction

Africa has a promising agricultural potential in terms of fertile land and abundant water resources, human resources, natural resources and rapidly expanding markets (Africa Progress Panel, 2010). However, owing to the scarcity of capital and technology, majority of Africa's agricultural practitioners has land holding of less than two hectares and average farm size of one hectare (Eastwood et al., 2010). According to the Food and Agriculture Organization of the United Nations (FAO) (2011) up to 83 percent of rural households cultivate less than two hectares per household and 52 percent on less than one hectare. A report compiled by the Economic Commission for Africa, sub-Regional Office for West Africa (ECA/SRO-WA) (2012) indicates that despite its huge potential, agricultural productivity remains low in Africa compared to other regions. The low investment returns in African agriculture can be attributed to poorly developed business models combined with negative economic environments and weaknesses in commodity prices (FAO, 2004, World Bank, 2013).

Nonetheless, a structural transformation of Africa's agricultural sector can be achieved through efficient private investment strategically designed to ensure value addition. This can have higher multiplier effects on agricultural productivity and alleviate poverty ([www.undp.org](http://www.undp.org)).

The Africa Capacity Indicators Report on Capacity for Development for Agriculture Transformation and Food Security (2012)<sup>1</sup> noted that improving the productivity and the economic returns of agriculture has immediate effects on poverty and hunger, yet countries need capacities of all kinds to make this productivity improvement and secure the required economic returns.

Furthermore ECA/SRO-WA (2012) recommends a holistic transformation of the agricultural sector through research and development as well as development of infrastructure and markets in rural areas. Additionally, the report advocates skill training along the agricultural value chain, strengthening

policy frameworks for agriculture-specific programmes, and investment in modern technology including irrigation systems and water conservation technologies.

## Value Chain Approaches

Value chain is defined comprehensively as 'an interlinked value-adding activities that converts inputs which, in turn, add to the bottom line and help create competitive advantage' ([www.businessdictionary.com](http://www.businessdictionary.com)). A value chain typically encompasses inbound distribution or logistics, manufacturing operations, outbound distribution or logistics, marketing and selling and after-sales service. These activities are supported by purchasing or procurement, research and development, human resource development and corporate infrastructure.

In adopting the value chain approach and addressing the challenges thereof it is important to identify and assist investors to modify their operations to provide the necessary pull and transformation along the value chain especially the inclusion of smallholder operators. There is the urgent need to incentivize these investors by: a) assisting them to develop and implement growth strategies that will help them expand their brands, deepen market presence, enter new markets, diversify and expand product ranges; b) helping them develop rigorous risk mitigation plans and financial risk management and c) providing guarantees and enabling environment to encourage them to make the required investment for expansion and growth (UN, 2013)

Value addition in Africa's agricultural industry also requires that agricultural development challenges such as lack of capital and technology, lack of information and infrastructure, high perishability and variability of output be addressed. In this regard, investments are required to facilitate the establishment of industrial clusters with improved infrastructural facilities, exchange of knowledge and skills, and collaboration in raw materials sourcing or

<sup>1</sup> Published by the African Capacity Building Foundation

market outlets development for agricultural products ([www.undp.org](http://www.undp.org)).

However, weak integration of Africa's agricultural sector with other sectors of their economies limits value chain development. This lack of sectorial integration denies most African countries the opportunity to benefit from linkages among the different sectors which can greatly enhance job creation, agricultural transformation and broad-based growth (UNECA, 2013).

Therefore, for the agriculture sector to effectively drive economic growth and development in Africa, sectorial intervention by investors must go beyond production expansion to tackle the challenges of agribusiness and agro-industrial development. This will enable Africa to fully exploit the benefits offered by domestic, regional and international agro-food markets as well as the available opportunities associated with the rapid rate of urbanisation and international demand and opportunities such as Africa Growth Opportunity Act (AGOA).

Furthermore, better national planning is required to increase private investments and value addition efforts in African agriculture. Countries should critically review their own situations and identify investment opportunities with optimal impact and returns. Such investments must be globally competitive with well-structured operating plans and properly executed to generate maximum returns.

### Objective

This AfCoP knowledge product aims to discuss Africa's agricultural potential and the contribution of private investments and value addition to agricultural productivity and food security. Drawing lessons from case studies on Morocco and Ethiopia, the paper brings to the fore challenges and opportunities associated with private investment and value addition efforts in African agriculture. The paper concludes with lessons and recommendations that can inform actionable policy across the continent towards improving agricultural productivity to ensure food security in Africa.

### Methodology

The paper is largely a desk review of secondary data and documentation, focusing on lessons learned from case studies on Morocco and Ethiopia. The paper is drafted in simple, understandable language and presented in a user-friendly format for easy assimilation and customisation by AfCoP members and the broader development community.

### Private sector agriculture investments in sub-Saharan Africa

Private sector agriculture investment in Africa is low but has been increasing over time, particularly in value-adding processes (FAO, 2004). Private investments in the agriculture sector are mainly directed towards high-value crops and traditional export products such as cocoa, coffee, and cut flowers targeted for markets in industrialized countries (Borger, 2008; UNIDO, 2013). Also, private sector investment in the fruit and vegetable sectors, especially in East Africa, have seen relatively high growth (Koroma and Mosoti, 2009, Mlanga, 2010).

Furthermore, food processing, transport and marketing activities linked to agricultural production are also attracting foreign direct investments. Incidentally, the wave of interest in purchasing farmland in African countries, is reported to be driven largely by the emerging need of industrialized countries to ensure their long-term food and biofuel supply, given the suitable agricultural potential in African countries to satisfy these needs (Cortula et al., 2009; Alemu, 2013).

### Factors affecting agribusiness investments

Private sector investments are often motivated by expected returns relative to perceived risk and uncertainty, which in turn are shaped by both external and internal factors (World Bank, 2005. World Bank, 2013). Again, private sector agriculture investments in many Africa countries are responsive to most of the factors that drive investments in other sectors of their economies. This is because the critical components of a supportive agriculture environment

such as access to markets and natural resources, good infrastructure, and a stable macro-economic and political environment are similar to those of other sectors of the economy (UNIDO, 2007; World Bank, 2013).

In recent times, the global surge in food prices has stimulated private sector interest in Africa's agricultural sector, in anticipation of higher returns on their investment. In spite of the general increase in agriculture sector investment by the private sector, factors such as risk management and supply chain coordination, specialized infrastructure and support services related to compliance to international food safety and standards can affect the extent of such investments (OECD, 2008; Grow Africa Secretariat, 2013). According to OECD (2008) sector-specific factors such as the interdependence of businesses along the supply chain and the need for specialized infrastructure such as cold storage facilities also affect private sector investments in Africa's agriculture. External factors such as trade protectionist measures, commodity price trends and market volatility also influence private sector participation in Africa agriculture.

### Role of the public sector in private investments in Agriculture

The public sector, through its policies and programmes, plays an important role in shaping market conditions and prospects for private sector investment in African agriculture. At the regional level, African Heads of State and Governments have made commitments to increase budgetary resources to promote development of agriculture through programmes such as the African Union's New Partnership for Africa's Development (NEPAD), the Comprehensive Africa Agriculture Development Programme (CAADP) and the Alliance for a Green Revolution in Africa (AGRA) (UN, 2013).

These efforts notwithstanding, the potential of private investment in agriculture remains to be fully

unleashed because most African governments have not adequately focused on infrastructure development to help meet the needs of the agricultural sector.

At the national level, some countries have adopted proactive strategies to attract private sector agribusiness investments by offering various incentives such as tax holidays within the first few years of an agribusiness establishment (Nigeria) and zero duty on agricultural machinery (Ghana, Nigeria) (FAO, 2008; UN, 2013). However, there is still a greater need to strengthen collaboration between the public and the private sector geared towards development of the agriculture sector. It is also instructive for the governments to realize that, it is not just the numbers of initiatives, but the effectiveness of mobilizing local and international funding supported by a pragmatic policy frameworks that will assure increased private investment in agriculture.

At the local level, agriculture relies on public goods and services such as extension services, agricultural information and plant protection services. Where such services are lacking, private investment has been severely constrained. Furthermore, the high risk associated with rain-fed agriculture, creates a demand for crop or weather insurance, but the absence of such risk-mitigating mechanisms in most countries in Africa, prevent some entrepreneurs from investing in the sector.

### Case study 1: Integrated Agriculture and Agribusiness Project (IAA): A private sector investment to mitigate rural poverty in Morocco.<sup>2</sup>

The proximity of Morocco to Europe offers excellent marketing opportunities for fruits and berries, many of which are permitted into Europe under seasonally adjusted duty. Additionally, Morocco has been exploring the United States market with substantial

<sup>2</sup> Source: Moroccan IAA Evaluation (2012). Development and Training Services, Inc. (dTS), the United States Agency for International Development.

shipments of clementine, olives, and olive oil. As the provisions of free trade agreements with Europe and America gradually phased in, and new export opportunities and competitive challenges emerged, Morocco, buttressed by funding from International fund for Agricultural Development (IFAD), sought to promote agriculture development through a variety of private investment projects.

The Integrated Agriculture and Agribusiness Project (IAA) is one such project that had a significantly positive impact on Morocco's agriculture industry. The \$14.8 million IAA intervention was implemented between 2005 and 2008 by Chemonics.

The main objectives of the project were to (i) improve public policies and institutions in support of more competitive agriculture and agribusiness (ii) increase productivity and variety in agriculture including livestock production (iii) increase competitiveness of agro-processing industries and (iv) enhance the capacity of agribusinesses, firms, and institutions to support competitive value chains. The IAA focused on five main value chains (sheep, olives, aromatic and medicinal plants, capers, berries) mostly in three regions of the country. During the project implementation, government officials complimented the IAA training, through development of web sites, generation and dissemination of market information, work on value chains, and cost-benefit analysis.

The project conducted an in-depth study of the five value chains and the world-wide export market. Findings from the study were factored into policies in Morocco. For example, results from a study on aromatic and medicinal plants (AMP) enabled the development of a joint Investor-Ministry strategy framework for the sector. Findings from a study on the logistics of berries also contributed to the marketing policy changes that reduced delays for exporting highly perishable fresh berries. Furthermore, The IAA studied marketing activities and trends in Morocco, Europe and the USA, leading to expanded marketing contacts, identification of new partners, and improved understanding of how to access the export markets. The IAA's relationships with the private sector and academia, resulted in new

partnerships and business deals for production and exports.

Moreover, the IAA facilitated access to processing equipment and training in cooperative management, production and post-harvest handling of produce. These tools provided new perspectives and led to modifications in Moroccan agricultural policies and procedures.

Besides, IAA signed trade liberalization agreements and set up shipping connections with the United States and other countries, creating new trading and marketing opportunities, some of which resulted in new trade or investment, particularly in berries and in processed products. Additionally, the IAA ensured that certifications and quality control procedures were improved to enable Moroccan suppliers meet markets requirements in Europe and elsewhere.

The project facilitated training of 4,236 people, of which 953 were in various cross-cutting areas such as Ministry staff training and 3,283 in the five value chains (Ref). The IAA's value chains efforts resulted in new investments of \$27 million and additional sales of \$56 million.

An evaluation report by IFAD showed that IAA reinforced and influenced the development of the Green Morocco Plan for 2008-2020, which had principles that mirrored USAID value chain principles. In particular, the Green Morocco Plan identified and developed key players called aggregators in processing and /or trade in each value chain that has strong financial, marketing and technical expertise.

The IAA project achieved sustainable results particularly in cases where the project worked with aggregators such as the Marjane supermarket chain, which helped to create better market for sheep farmers. Similarly, an aggregator in the olive value chain advised farmers on quality control and achieved traceability back to the farms as required by European buyers. In terms of value addition, the project concentrated efforts on small cooperatives of small scale farmers such as those in the olive sector, focusing on improved techniques for pressing oil from olives, or with harvesters of wild products (capers and rosemary).

Owing to the effective collaboration the IAA had with the Moroccan government, the project accomplished the intended results.

### Case study 2: Agricultural commercialisation and the role of large-scale investment in Ethiopia<sup>3</sup>

The Ethiopian government adopted a dualist system of agricultural production in a bid to promote greater agricultural commercialisation (MoFED 2005), and as a compromise between political and economic priorities. Under this system, the government equipped the politically-sensitive smallholder sector for enhanced productivity and specialisation for the high-value export markets, and also facilitated the development of large-scale commercial agriculture by foreign and domestic investors (MoFED 2005). This approach was premised on the assumption that the two systems were entirely separate. The policy was also informed by the low success chalked by the smallholder sector over the years and the unsustainability of past policies. Moreover, pressure that was brought to bear on the Ethiopians from donors, particularly, from the World Bank in favour of agricultural commercialisation, coupled with the demonstrated impact of agricultural investment in horticultural projects in neighbouring Kenya (Amdissa, 2006) fuelled the decision to promote private investments Ethiopia's agriculture sector.

According to the Ethiopian constitution, land management is the responsibility of ethnically-delineated regions (FDRE, 2003), but, in 2009, the federal government re-centralised land administration, creating the Agricultural Investment Support Directorate (AISD) in the Ministry of Agriculture and Rural Development (MoARD) to allocate land to foreign and domestic investors who had capacity to operate on more than 5,000 hectares of 'unused' land (previously not under cultivation),

which the smallholders could not develop due to resource constraints. This decision was based on the conviction that private investors were more capable of expanding production and export, facilitate technology transfer to smallholders to address food security and contribute more significantly to foreign exchange earnings and job creation.

In the government's drive to promote private investments, investors who exported more than half of their produce or provided 75 percent of such produce to exporters were allowed income tax holidays of up to five years. Those who operated in remote areas were eligible for an extra one year tax holiday. On the contrary, investors who produced mainly for the domestic market enjoyed income tax holidays for only two years. Apart from the tax holidays, investors who operated on 'unused'<sup>1</sup> were exempted from land use fees for five years, especially if they used improved seeds and irrigation, and when the holidays had expired, land fees were set low to encourage investment in target areas. Additionally, the state-owned, Development Bank of Ethiopia (DBE) offered concessional loans to large scale private investors.

As a result of these incentives, in 2006, some Israeli managers, with finance from European banks, invested in castor for bio-diesel, cosmetics and paints as demand for castor had risen due to high fuel prices, EU requirements for bio-fuel use and demand from rapidly growing economies like China. In 2007, 8,000 ha of 'unused' land in East Hararghe was leased to the company. As a considerable expanse of the land was already being used by smallholders and pastoralists, the investors adopted a production schemes based primarily on the land use history at the different sites. On pastoral lands they cropped directly with wage labourers and machinery; and on cultivated land out, grower schemes were negotiated with elders on behalf of the local smallholders.

<sup>3</sup> Source: **Tom Lavers** *The Role of Foreign Smallholder-focused Agricultural Development Strategy*. Paper presented at the International Conference on Global Land Grabbing 6-8 April 2011

Organised by the **Land Deals Politics Initiative (LDPI)** in collaboration with the **Journal of Peasant Studies** and hosted by the **Future Agricultures Consortium** at the **Institute of Development Studies**, University of Sussex

With a commitment by the government to provide up to 200,000 ha, and the optimism about the profit potential of the out grower schemes, the managers sourced more funding, raising €17m from European investment funds to massively expand their operations. The expansion received further government support as both the type of investment and the production system was in line with the government's development strategy (an agricultural project that provides industrial inputs and fuel for export or as substitute for imports). Consequently, traditional leaders signed contracts with the investors on behalf of the farmers and convinced their people to join the project.

By 2008 the project had covered 72,000 ha in East and West Hararghe, which had then become chronically food insecure as majority of the farmers, whose average land holding was less than 0.5 ha and who previously farmed maize, sorghum and some cash crops like chat and coffee, had been incentivised to switch to castor production. The company leased an additional 60,000 ha of 'unused' land<sup>1</sup> in West Hararghe, to establish a plantation although the out grower scheme was initially prioritised. They also built a bio-diesel processing factory; invested heavily in equipment including pesticide sprayers, peeling machines, motorbikes and cars and hired 5,000 staff, including agronomists, accountants and supervisors with a 30 m birr loan from an Ethiopian bank.

Not too long after the injection of huge sums of capital into the project, several challenges arose because castor yields fell short of the estimated yield targets. This occurred because the seeds had not been tested across the range of soils and rainfall conditions in the entire areas of production. In addition, sorghum price tripled just about the same time, and, given the fixed castor price, farmers expressed dissatisfaction with their incomes from the castor business.

This development led to decline in productivity as most farmers shifted from castor production to other crops, resulting in the investors incurring huge losses. Another challenge associated with the project implementation was the widespread adoption of mechanization in place of the outgrower schemes on

the 60,000 ha of land in West Hararghe, which had never been cleared.

Subsequently, the investors could not afford to pay wages or buy the remaining seeds from the outgrowers. The failure of the project created a major problem for the government, which was deeply involved in promoting the project.

Having switched from subsistence crops, and with no income as a replacement, the farmers lost up to half of their annual production. Additionally, the pesticides killed their bees, which had provided important extra income as honey. Eventually, some farmers had to sell cattle to buy food. Following the failure, the managers fled the country in April 2009 with the little funding left.

Unused land refers to land that has never been cultivated nor exploited by pastoralists due to financial constraints.

### Outcomes and overall assessment

The IAA project was implemented at a time when the Government of Morocco was re-evaluating and revising its agricultural policy priorities, reorganizing government services, and seeking to launch many new initiatives. Good timing therefore engendered the acceptance of the value chain model and cost-benefit analysis concepts.

The project made important contributions, both conceptually at the Ministry level (supporting information management and outreach, value chain concepts, cost-benefit analysis, business promotion) and in the Ministry's interaction with the agricultural sector (demonstrating how the broad ideas of new policies could be adapted to specific value chain activities in five product areas).

Again, the case study on Morocco revealed that integrating private investments to national objectives is an important determinant of success. The introduction of the aggregator concept in the value chain and its incorporation into the Green Morocco plan proved to be prudent policy changes that focused on the well-being of farmers. Skills trainings provided by IAA, in particular the training on cost-

benefit analysis also complemented the government's approach to develop competitive agricultural systems and related policies.

The case on Ethiopia demonstrated how African governments can stimulate private investment in agriculture. Since major aspects of the project resonated with the government's development strategy, officials took huge risks with the welfare of smallholders and pastoralists. The case study also points out the need for private investors to have reliable information on land use, especially in remote areas, which are often the target of large scale agricultural investments. In this particular case, the pastoralists who were seen as merely passing through land were disregarded.

The study further showed that concentration of private investment in the remote, sparsely populated areas is likely to pose serious risks for smallholder and pastoralist populations, bringing the agricultural development strategy into direct conflict with the federal system which is founded on the principle of ethnic self-determination.

Moreover, the Ethiopian case study brings into sharp focus the conflict between the macro benefits of private investment, largely accruing from foreign exchange earnings, and the risks of investment borne at the micro level by pastoralists and smallholders in the vicinity of new investments.

### Conclusions/lessons learned/policy implications

The case studies clearly indicated that large scale private investments ought to ensure government and industry buy-in for their success, particularly, if they are aimed at policy change. Unpopular policy decisions can face resistance or apathy even when the changes are sensible. Furthermore, private investments and value addition can only be successful if there is an effective interaction among investors and policy makers. This interaction can be improved if appropriate research is done to establish production systems and value chains that are more profitable and socially acceptable by the people.

Government policy ought to aim at effectively supporting not only economically viable but also socially and culturally acceptable private sector agricultural investments. Beside, such policies should incentivise private sector to include smallholders in value chains. Finally, capacity building efforts should be deployed in the following areas: skills training, in particular, training on cost-benefit analysis and value chains management; agricultural research to inform policies; and statistics availability (on land use for example) to guide investors.

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## Acknowledgement

This knowledge series intends to summarize good practices and key policy findings on managing for development results (MfDR). African Community of Practice (AfCoP) knowledge products are widely disseminated and are available on the website of the Africa for Results initiative, at: [www.afrik4r.org/page/resources](http://www.afrik4r.org/page/resources).

This AfCoP-MfDR knowledge product is a joint work by the African Capacity Building Foundation (ACBF) and the African Development Bank (AfDB). This is one of the knowledge products produced by ACBF under the leadership of its Executive Secretary, Professor Emmanuel Nnadozie.

The product was prepared by a team led by the ACBF's Knowledge and Learning Department (K&L), under the overall supervision of its Director, Dr. Thomas Munthali. Within the KME Department, Ms. Aimtonga Makawia coordinated and managed production of the knowledge product while Dr Barassou Diawara, Mr. Kwabena Boakye, Mr. Frejus Thoto, Ms Anne Francois and other colleagues provided support with initial reviews of the manuscripts. Special thanks to colleagues from other departments of the Foundation who also supported and contributed to the production of this paper. ACBF is grateful to the Africa Development Bank which supported production of this MfDR case study under grant number 2100150023544.

The Foundation is also immensely grateful to Dr. Kwame Agyei Frimpong, the main contributor, for sharing the research work contributing to the development of this publication. We also thank Professor G. Nhamo, Dr. Lyimo, and Dr. A. Kirenga whose insightful external reviews enriched this knowledge product. The Foundation also wishes to express its appreciation to AfCoP members, ACBF partner institutions, and all individuals who provided inputs critical to completing this product. The views and opinions expressed in this publication do not necessarily reflect the official position of ACBF, its Board of Governors, its Executive Board, or that of the AfDB management or board.