MAKING PUBLIC-PRIVATE PARTNERSHIPS WORK IN SMALLHOLDER INCLUSIVE AGRICULTURAL VALUE CHAINS

1. WHAT IS A PUBLIC-PRIVATE PARTNERSHIP?

The term public-private partnership (PPP) is used to describe a variety of informal and formalized arrangements between public and private sector entities to create shared value.

While there is a wide range of partnership options, one central element is the sharing of costs, risks, and other resources. PPPs are not limited to bilateral collaboration between a government agency and a private company, and they can include a range of both public sector and private sector entities. Public partners can include: central and decentralized government, state banks and rural finance corporations, state-owned enterprises, research institutions, universities, marketing boards and donors.

Private sector partners can include: global and domestic food companies, input supply and agro-processing companies, financial institutions, SMEs and producer associations, civil society (NGOs) and third-party contractors.

Where PPPs explicitly involve producers as a key component of the arrangement through the creation of smallholder-inclusive value chains, the partnerships can be known as public-private-producer partnerships (PPPPs). In the agricultural sector, combined investments can increase the profitability of smallholder-inclusive initiatives by agribusiness. They can also improve the way that agricultural markets work for small-scale farmers and rural communities and create sustained agricultural growth.
2. WHY ARE PPPS CHALLENGING?

Securing economic, social and environmental benefits from PPPs requires careful navigation of the inherent tensions between partners. Diverse institutions may want to achieve alignment but different and often divergent institutional cultures, internal processes and procedures make collaboration challenging. Differences around goals, perceived risk, planning, performance measurement and financial capacity, for instance, can be an obstacle to negotiate and resolve.

These differences are not only significant at the time a PPP is established, but evolve over time due to changes in the market, political influences, and so on. Balancing the various changing cultures and objectives of partners has impacts on a range of key factors, including the kind of contractual arrangement used (formal or flexible), the goals set (manageable or more ambitious), and the level of investment in communication between parties.

3. WHAT ARE THE DIFFERENT MODELS OF PPPS?

Different models of partnership include:

- **Company-led models** – companies are both collaborators and instigators of partnerships in order to secure the supply of commodities, ensure food safety standards are met, or as part of their corporate social responsibility. For example, the Cocoa Partnership was established to ensure Cadbury has a secure and sustainable supply of good quality cocoa from Ghana.

- **Coalition models** – multi-stakeholder initiatives often include developing country governments, donors, private sector, civil society organizations and research institutions. For example, the World Cocoa Foundation targets improvements along the entire value chain or at key levels (such as the producer level) to improve development outcomes and the environmental sustainability of business transactions (see Box 1).

- **Donor-led models** – donors increasingly want to engage the private sector in innovation and improvements to the effectiveness and value-for-money of development interventions. For example, the Coffee Farmer Resilience Fund is a partnership between USAID, Keurig Green Mountain Inc., Cooperative Coffees, Starbucks and Root Capital, to support 40,000 coffee farmers to combat the coffee rust outbreak in Latin America and the Caribbean.

- **Business-NGO alliance models** – where NGOs have sought out or been sought out by private sector actors to partner on development interventions. For example, TechnoServe, supported by the Bill & Melinda Gates Foundation, works with 50,000 smallholder fruit farmers in Kenya and Uganda to provide sustainable local sourcing for Coca-Cola.

- **NGO-led models** – NGO initiatives that lead to the creation of a viable social enterprise or for-profit company which exports goods to developed countries. For example, AgroFair, a producer co-owned organization, was established in 1996 to import sustainably produced Fairtrade bananas to the European market, and now produces and markets a range of tropical fruit and juices.
High finance, input and transport costs, and poor infrastructure make many low-income countries relatively uncompetitive for commercial agriculture. Securing commercial funding for businesses establishing new value chains is a challenge, particularly where weak legal and regulatory frameworks prevent local banks and other investors from investing in projects which require high upfront capital expenditure, have seasonal incomes, or take years to become profitable – as is the case with many agribusiness projects. Collaboration significantly alters the cost curve facing individual companies. As future growth targets require companies to move into lower income, difficult-to-reach segments to acquire new customers and sources of supply, pre-competitive collaborations are likely to become a new norm.

Pre-competitive costs often covered under a PPP include:

- **Infrastructure** – missing or unreliable communication infrastructure and transport systems present challenges for companies as they move into developing markets. Infrastructure is traditionally a challenge addressed by the public sector, but some companies are co-investing to overcome it.

- **Research and development** – PPPs can support the private sector to make major investments in production areas where returns on investments have been quite low. The public sector can underwrite the risk that the private sector would face. Once those areas have been tested and developed, private companies can carry out the adoption throughout the whole region. For instance, the International Rice Research Institute in the Philippines tested and adapted flood-tolerant seed varieties to local conditions in India and Bangladesh before the private companies entered the market.

- **Technology and innovation** – PPPs in infrastructure such as irrigation offer a way of improving operational efficiency of public services by introducing private sector technology and innovation. Long-term value for money can be harnessed through risk transfer to the private sector over the lifespan of the project – from design/construction to operations/maintenance.

- **Extension** – in many countries, small-scale farmers need to be supported with extension services in order to reach a certain level of productivity and quality. The costs of extension services in many PPPs are shared between the public (donors) and private sector, as they are seen as initial investments to uplift the agricultural sector. For example, HEINEKEN has established a number of PPPs with the Dutch Ministry of Foreign Affairs, which enable the company to aggregate farmers and deliver extension services to them through partnerships with local NGOs and MFIs.

- **Storage** – some governments have responded to food price spikes by increasing strategic grain reserves. PPPs are used to support the private sector to build storage facilities at a competitive price using the most suitable technology to reduce post-harvest losses and transfer grain management knowledge to government.

**Box 1: Jointly meeting pre-competitive costs**

The World Cocoa Foundation’s Cocoa Livelihoods Program and the Roundtable on Sustainable Palm Oil are examples of successful pre-competitive activities among industry competitors:

- In the cocoa industry, 16 competitors came together to provide aggregation, training, inputs and credit to smallholders to ensure future supply across the industry.

- In palm oil, suppliers, traders, brands and retailers came together to certify the commodity sourced from shared origins. A shared distribution channel has been developed, including transport, warehousing and demand generation, to make rural distribution viable for retailers.

In the long term, however, government and donor support will likely be required to build enabling ecosystems. Even in many instances where there is a clear market opportunity, the risk of free-riders limits companies’ willingness to invest independently in the creation of “public goods” such as infrastructure and consumer education. Governments or donors could provide such goods outright, or facilitate pre-competitive or associative collaborations where market and infrastructure development would be advantageous to many competitors.
The private sector is seen as the engine of growth in developing countries, with successful businesses driving growth, creating jobs and paying the taxes that finance services and investment. Agriculture is recognized as an important driver of economic growth and rural poverty reduction, and has received significant levels of support through development finance. The recent engagement by donors with the private sector to meet economic development outcomes is mobilizing further resources in a range of sectors, including agriculture.

Donors are working with partners to tackle barriers to investment, and provide technical expertise and tools. These efforts can have a direct effect on the success of private sector initiatives by helping to overcome investment challenges and integrate development-focused approaches into investment strategies.

In agriculture and agribusiness, development finance is starting to support companies in developing or scaling up inclusive business models. Having a direct impact on poverty is a core objective of donor funding. From the private sector perspective, on the other hand, smallholder-inclusive business models pose additional challenges to competitiveness due to low quality product, insufficient and inconsistent supply, and issues of mutual mistrust.

Funds are therefore being made available to catalyze increased capital in the system in the short term, through giving confidence to co-investors via thorough due diligence of investees’ financial returns and development impact. Over the longer term, the objective is for funds to catalyze further capital through proving the financial viability of pro-poor business models and demonstrating the positive impact that this type of investment will deliver.

Companies are particularly attractive to donors when they propose activities in the following areas:

- When a company is interested in working in remote rural areas where there are very limited sources of income for the rural population
- When a company provides access to an export market, which brings in forex as well as increased incomes to farmers
- When a company creates additional employment opportunities through investment in communities, i.e. schools, local healthcare, etc.

See Box 2 for an example of the criteria to be met by agribusinesses to access development finance.

**Box 2: Criteria for applications to the CDC DFID Impact Fund**

Successful applications must:

- Aim to achieve positive impact on the bottom-of-the-pyramid population in the target geographies as consumers, producers or employees
- Have potential to invest in sectors or enterprises that target poor women and girls as suppliers, producers or consumers of essential goods or businesses for the poor
- Focus on sectors or pro-poor businesses that are otherwise unable to attract commercial investment and hence require early-stage patient capital and technical support
- Be from sectors with a significant unmet need for investment to achieve impact, including businesses providing access to food, housing, energy, water, sanitation, health, education, financial services and livelihoods for the bottom of the pyramid
- Raise as much private investment as possible to match the Fund’s commitment
- Focus on making investments in low income countries to deliver higher potential impact
There are many demonstrated benefits for agribusiness from working through PPPs, including:

- Sustainable supply of inputs, including the ability to market the company as socially conscious
- Access to new markets
- Investment returns
- “Buying down” transactions costs and financial risks for companies who want to invest in poor communities but can’t bear the full burden of investment
- The potential to improve the overall business climate in low-income countries.

While partnerships can generate substantial benefits, formalized, multi-stakeholder arrangements also carry real costs. These can include:

- The slow pace of setting up a partnership, particularly given the different speed of decisionmaking between the public and private sectors
- Creating and maintaining administrative systems and structures to service the partnership, including those to report on development as well as commercial outcomes
- Delays inherent in decision-making and coordination between multiple partners
- Time and resources required from all partners to learn how to work together and understand each other's priorities

When choosing a suitable partner or partners, factors to consider include:

- **Type of partner** – the aim is to compose a PPP with the maximum complementary skills and resources likely to generate the greatest possible output. Selection should start with a realistic assessment of one’s own strengths and weaknesses. The next step is to invest considerable research to identify organizations most likely to benefit from and contribute to this profile.

- **Willingness to partner** – finding a particular skill set is not enough on its own: the relevant organization must be willing, as well as able.

- **Matching goals** – it is often easiest to determine the degree to which organizations’ goals and vision match each other. For example: a project that solely benefits Tanzanian smallholders rather than large-scale farming operations in the USA may not fully address every private company’s commercial growth aspirations. Where current goals clearly do match, it can still be difficult to assess long-term commitment to them, and to a possible PPP. This is especially true if there are setbacks along the way, or if a party believes the benefits to be unfairly distributed.
8. HOW TO STRUCTURE A PPP?

Priority setting

All potential partners should be open about where they see the priorities in the intended joint project, including the main goals and milestones within the project, the order in which they are to be tackled, and their position on each organization’s own internal priority list.

Each partner’s ability to make the success of the joint project a high priority within its own organization is also important. Each party needs high-ranking sponsors of the PPP, and should make work on the project an explicit part of key employees’ job descriptions and/or annual targets. Parties should openly discuss the similarities and differences in their operational culture and values, as they can profoundly affect a partnership’s productivity.

Contractual arrangements

Participants in successful PPPs repeatedly emphasize the importance of clear and detailed contracts. Contracts can be structured in a loose way that allows for a high degree of flexibility, or they can have a more formal, legal structure.

Contracts should unambiguously determine the division of tasks, as well as the distribution and use of any commercial rights in connection with the project. Topics such as liability and intellectual property also require careful attention.

The contract draft must reflect the principles already agreed during initial meetings and not use standard templates from legal departments. Partners must discuss any major “blockers” as early as possible – for example, an existing contractual arrangement between one of the PPP parties and another organization outside the new partnership.

Each PPP has an individual identity and contains unique elements. Negotiations should therefore be on a case-by-case basis, and parties must allocate resources accordingly.

Realism about the necessary timeframes is equally important: parties frequently have widely differing internal processes, often simply as a result of their size. Each organization needs to respect partners’ ways of working. Creating realistic expectations about the time needed for responses to proposals will help prevent frustration.

9. WHAT ARE THE CHALLENGES AND RISKS INVOLVED?

The challenges of entering into a PPP include:

- **Value creation** – public, private, and non-profit actors often have contradictory value creation reasoning, partly because they support different expectations and partly due to distinct identities and organizational and sectoral backgrounds.

- **Reachable targets** – public sector poverty reduction targets can be out of sync with the profit-making imperative fundamental to private business. Donors should therefore agree with private sector partners on reachable targets.

- **Binding contracts** – agribusiness PPPs face risks which are difficult to explicitly specify before signing contracts, which often leads to non-binding contracts. These risks include: supply risks, demand risks, payment mechanisms (in terms of regularity and price stability) and compensation risks (for example, in the case of product loss or market rejection). Plans change during implementation and companies tend to utilize a flexible approach that can adapt to circumstances, whereas donors prefer to use a log-frame approach that is harder to adjust.

- **Oversight mechanism** – the regulator, coordinator, and leadership role is crucial for successful implementation, yet can sometimes be overlooked or be carried out by the financier rather than an independent oversight body.

- **Transparency** – ensuring full transparency and yet enabling collaborators to keep some competitive advantage from privileged knowledge is a recurring challenge. The private sector generally maintains a culture of privacy in research and development, in order to be first to the patent office and/or gain all the advantages of leading into a new market. Private sector interest is usually closely linked to commercialization rights, which need to be explicitly defined at the start of a PPP. Private companies mostly aim to retain free access to their knowledge, which has been expensive to generate. They also want to prevent its use by competitors. Public sector parties are not always comfortable with this aspect of deal-making.
9. WHAT ARE THE CHALLENGES AND RISKS INVOLVED?

The risks of entering into a PPP include:

- **Costs** – the transaction costs inherent in PPPs can frustrate or discourage certain partners – actual and potential – especially those in the private sector. Slow or time-intensive processes can be off-putting to busy executives and can dissuade new members from joining. Many business people also have a hard time adjusting to the public sector instinct for extensive consensus building.

- **Finance** – some projects are easier to finance than others (e.g. if there is proven technology involved and/or the extent of the private sectors obligations and liability is clearly identifiable); some projects (e.g. water projects) will generate revenue in local currency only; while other projects (e.g. ports and airports) will provide generate revenue in US dollars or other international currencies, so constraints of local finance markets may have less impact.

- **Risk bearing** – private firms (and their lenders) are cautious about accepting major risks beyond their control, such as exchange rate risks or risks of existing assets. If they bear these risks then their price for the service will reflect this. Private firms will also want to know that the rules of the game regarding undertakings to increase tariffs/fair regulation are to be respected by government. In turn, managing government expectations helps to develop and maintain a good working relationship, which can provide necessary support. Private firms will also expect a significant level of control over operations if they are to accept significant risks.

- **Long-term changes** – given the long-term nature of PPPs and the complexity associated with them, it is difficult to identify all possible contingencies during project development. Events and issues may arise that were not anticipated in the documents or by the parties at the time of the contract. It is more likely than not that the parties will need to renegotiate the contract to accommodate these contingencies.

- **Failure** – it is possible that some projects may fail or may be terminated prior to the projected term of the project. This could happen for a number of reasons, including changes in government policy, failure by the private operator or government to perform their obligations, or external circumstances such as force majeure. While some of these issues may be addressed in the PPP agreement, it is likely that some of them will need to be managed during the course of the project. Reputational risk for companies is a key risk.
How is evidence measured?
Donors feel under increasing pressure to prove that public funds given to private business are actually making a difference and are not just paying for something companies would have done or achieved anyway. Deciding on what constitutes “additionality” is not straightforward, and is arguably among the most challenging questions faced by funders of partnerships. In turn, companies can struggle to make a convincing case that their intentions to improve smallholder livelihoods are genuine, and that a partnership approach is affordable, credible and will lead to change.

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<th>Behavioral additionality</th>
<th>Output additionality</th>
<th>Development additionality</th>
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<td>Grant support helps businesses to implement the project at greater speed. Where similar companies would need five years to set up a business project, those that receive support only need one-two years. Many businesses would implement the project anyway, but are able to implement it at a larger scale due to grant support and advice. Donor support requires companies to comply with good practice principles in the context of labor rights, the environment, or similar.</td>
<td>Businesses may invest in better quality equipment as a result of donor support, which may help in terms of environmentally sustainable production or increased competitiveness. Businesses are able to pay for better quality advisory services, such as in market research or product development, or on ways to scale up their business model in the future.</td>
<td>The involvement of a donor increases the focus on achieving wider changes in the sector or market. Donor requirements, advice and larger project size mean that higher impacts on local populations/smallholder farmers can be achieved.</td>
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What is the evidence of success?
While the available evidence suggests that PPPs can deliver positive development outcomes, the jury is still out in terms of the long-term impacts on poverty and rural development. Only very few structured mechanisms for partnering with business have published actual evaluations or some form of review of their entire portfolios. In addition, many projects are not complete, and more information and clarity is needed around the approaches used in PPPs to measure results.

Many of the criticisms of PPPs are linked to perceptions that claims of positive outcomes are not substantiated by the evidence. As a result, some business leaders have acknowledged the need for better and more consistent indicators of progress, as well as credible evidence of the results of inclusive business initiatives. A tool has been developed by the Sustainable Food Lab to offer a standard approach for businesses needing to measure and report on the impact of investments in smallholder value chains.
About the business

CB Farm Fresh is a smallholder-inclusive vegetable processor and distributor serving the extractives industry in Tete, Mozambique since 2009. It is one of only two companies in the country adding value to fresh vegetables through basic processing like washing, peeling, cutting and packaging.

About the Service Delivery Model

The most important component of the CB model is access to new, guaranteed markets. Without this, horticulture farmers struggle to sell any surplus, as the local market is too small and links too fragmented to absorb current production.

CB Farm Fresh has developed an end-to-end model centered on a core processing business. CB provides education, oversight and access to inputs for production-related activities. Having initially relied on imports from South Africa, the company is now able to source 80% of its produce locally to feed its 120 ton/month processing factory. As such, CB is on track to reach a target of 100% locally sourced produce by the end of 2015.

Unlike many outgrower programs that tend to work with one-hectare subsistence farmers, CB Farm Fresh works with farmers who are already on the road to semi-commercial status. CB farmers tend to be older, experienced farmers who have more than three hectares each and are producing above-average yields. To be considered for integration in the company’s sourcing model, CB looks for farmers’ commitment to further improving their yields, incomes and livelihoods, and as such increases the chance of success by selecting farmers with high potential. To do this, CB assesses their maize yields, as an indication of their potential for irrigated horticulture production.

To build a sustainable smallholder supply base, CB has invested in a model school to develop the capacity of farmers to feed its processing factory. CB provides a three-week, hands-on capacity building program where farmers are taught improved production techniques. The objective of the training is twofold: to teach farmers how to produce high-quality, high-yielding vegetables through provision of practical agricultural advice; and to screen and select the most promising farmers who will apply what they have learned to their own fields in the second week of training.

The best farmers will receive reimbursable, zero-interest irrigation installation on their lands, and CB will source vegetables directly from these high performers to feed the company’s processing factory. Demonstration farms, owned and tended by local farmers, incentivize farmers through tangible results.
11. THE CB FARM FRESH CASE – MOZAMBIQUE

About the PPP

The model school is aligned to the aims of the local government development agency, Agencia do Vale de Zambeze, which are to support social and economic development in the region through enabling private-sector growth with a focus on capacity building. The local government has committed to funding the cost of farmer training in the short to medium term ($100 per farmer).

In addition, Agencia do Vale de Zambeze has agreed to build five more model schools over the next five years, leasing tractors and irrigation to CB’s farmers as it scales up. Through regular advocacy work to keep the government aware of developments and progress, Agencia do Vale do Zambeze has invited CB to sit on an advisory panel for agribusiness developments in the region.

Risks and benefits

The preliminary results of the proof-of-concept are positive, and indicate that sourcing from local smallholder farmers is a viable alternative model, provided they receive support to produce the quality required by a high-end market.

On the processing side, CB’s 120-ton factory is operating at 80% capacity and has created around 50 local jobs. On the marketing side, CB has built a solid reputation for the quality and reliability of its service and now has an annual turnover of $6 million a year. On average, CB pays farmers a 15% markup on the local market price for fresh vegetables.

Over the next five years, CB will expand its operations, aiming to train up and source from around 200 irrigated vegetable farmers and create around 3,000 additional farm-laboring jobs.

Three potential risks and considerations have been identified, and will be monitored to sustain success:

- Ensuring financial sustainability by diversifying markets and funding streams
- Reinforcing back-office support to maximize efficiency
- Monitoring the introduction of new elements to the model and adjusting accordingly.

Future plans

- To complement the fresh vegetable product line, extend shelf life and absorb excess supply, CB is in the process of securing funding for a frozen product line, given rapidly rising demand of around 200% per year. To complement CB’s horticultural activities, the company aims to reach a further 20,000 dry-land farmers through support for maize and soy production and processing.

Challenges

- Financial sustainability of the model school, given unpredictable government funding streams
- Creating the right incentive structures to support repayment of loans
- Overcoming resistance among the older farming community to non-traditional techniques and technologies
12. KEY REFERENCES


IFC (2012) Food PPPs. Handshake IFC’s quarterly journal on public-private partnerships. Issue No. 5


