PAKISTAN

ANALYSIS OF CORPORATE SECTOR CONSTRAINTS IN AGRICULTURE

Assessment of the Existing National Agribusiness Environment

Findings and Conclusions

(DRAFT)

RONCO Consulting Corporation
in collaboration with
AGRI-BI-CON International (PVT) Ltd.

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Foreword

In January 1989, at the request of the Government of Pakistan, the United States Agency for International Development (USAID) entered into a contract with the RONCO Consulting Corporation, in collaboration with a Pakistan consulting firm, Agri-Bi-Con International (Pvt) Limited, to carry out an analysis of corporate sector constraints in agriculture (ACSCA). The purpose of ACSCA is to identify constraints, capabilities and opportunities to stimulate the growth of private sector agribusiness operations in Pakistan. The results of the analysis will be used to prepare a National Agribusiness Action Plan for the consideration of the Government of Pakistan, the Pakistan private sector and USAID. The plan will focus on policy and economic incentives required to increase private sector participation in agribusiness investment and development.

This report describes the approach to the analysis and summarizes the findings and conclusions. The challenge during the next few months will be to define an action plan with discreet, attainable steps designed to achieve an improved climate for agribusiness, or agro-industrial, investment. The process is substantially enriched by what is being learned through agro-industry case study research which is being carried out as a part of ACSCA, in parallel with the national assessment.

One of the main purposes of this report is to give readers an opportunity to critique both the approach and the findings and conclusions. Comments will be welcomed by the ACSCA team and will be seriously taken into account.

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Chief of Party

SUMMARY OF FINDINGS AND CONCLUSIONS

Based on work to date, the ACSCA team puts forward the following as a summary of findings and conclusions regarding the constraints to increased private-sector investment in agribusiness in Pakistan.

1. Public-Sector Domination of Agro-Industry

During the past two decades in Pakistan, much effort has gone into building public sector support services for agriculture, including agricultural research and extension, at both the federal and provincial levels. This is commendable. At the same time, rather than to encourage private-sector investment in agro-industries, public-sector agribusiness enterprises have been fostered, nurtured and subsidized. ACSCA case study analyses reveal a pervasive pattern of public-sector enterprise domination of the key agribusiness industries of fertilizer, farm machinery, edible oils and seeds. For example, the fertilizer industry constitutes a classical, government-managed ologopoly situation. The National Fertilizer Corporation (NFC), a fully-owned state holding company with five fertilizer plants, owns 53 percent of the nation's fertilizer production capacity. The Fauji Foundation, a quazi-state holding company, has two factories with another 24 percent of capacity. Two private companies, Exxon Chemical and Dawood-Hercules, have a combined total of 23 percent of production capacity. Fertilizer imports are through a governmental agency; the private companies are not allowed to import fertilizer. One of the most important conclusions is that public-sector enterprise control of agribusiness impedes growth of the agricultural economy, and diminishes the value and impact of GOP investment policies and incentives for the private sector. Without a drastic change in policy to reduce public-sector investment and control over agro-industry, broad-based private-sector investment and participation in agribusiness development are unlikely to occur.

2. The Limits of Deregulation

The Government deregulation of agribusiness, including the removal of price controls, is often cited as a factor favorable to private-sector agribusiness development, investment and competition. Our analysis of business practices in several key agro-industries does not support the proposition that effective deregulation has, in fact, occurred. Through its companies, agencies, banks and political institutions, the GOP effectively controls many major agribusiness markets, commodity flows and business practices. These controls directly affect commodity imports and exports, physical distribution, base-line production, raw material procurement costs, consumer product pricing and market competition. Using the fertilizer example again, National Fertilizer Marketing Ltd. a subsidiary of NFC, has the responsibility of marketing the production of NFC plants plus the allocated share of imported fertilizer. Although nitrogen fertilizer is nominally "deregulated," NFC effectively sets fertilizer prices which the other producers essentially follow. Edible oil prices were "deregulated" in 1986. The Ghee Corporation of Pakistan (GCP), a government-owned holding corporation made up of 24 ghee mill units, produce some 37 percent of the country's output of vegetable ghee and acts as the industry's price leader. GCP ghee price increases averaged only 4 percent per annum from November 1983 through August 1989, which was less than the inflation rate. This pricing practice continued while GCP incurred cumulative operating losses of Rs 600 million. The Trading Corporation of Pakistan (TCP), another government-owned company, has the sole authority to import soybean oil, a crucial ingrediant used by GCP and private companies for manufacturing ghee and cooking oil. TCP determines the quantity and timing of soybean oil imports, the allocation to GCP and approved private ghee mills, and the price of the oil to ghee manufacturers. Other oils, notably palm oil, may be imported by ghee and cooking manufacturers, but custom duties are levied by the government to assure that the costs of such oils are at least equal to TCP soybean oil prices.

The combination of public sector corporations acting as commodity price leaders, and other GOP entities controling the importation and pricing of commodities such as fertilizer and edible oil, constitutes restraint of trade and price-setting. These practices belie efforts by the government to deregulate agribusiness industries and commodity markets. The historical condition that the health of the agricultural economy of Pakistan is determined largely by governmental policies and practices rather than by market forces is a continuing reality.

3. Agribusiness Investment Policy

Pakistan's resources dictate that agriculture will remain for many decades a leading sector in Pakistan's economy. Viable agriculturally related businesses are essential for the country to maximize the economic value of its agricultural resources. Yet, no deliberate national policy aimed at developing a strong and dynamic, market-driven private agribusiness sector has been formulated or pursued. Neither is there an agency with a mandate specifically to promote agribusiness development. Both are needed, even to stimulate domestic investment. If, in addition, significant foreign investment in agribusiness is to be solicited, the agribusiness investment policies of Pakistan must be at least as attractive as are those of other countries in the region which are competing for the relatively scarce foreign investment being made in agro-industry. Thailand, Malaysia, the Philippines and Turkey, for instance, are agressively promoting foreign investment to source both capital and agribusiness technology. The Government of Pakistan is also trying to increase foreign investment by offering what appear to be liberal incentives. However, these incentives are no substitute for the required pragmatic efforts to offer investment incentives and to set economic policies that are more competitive than those of other countries which are immediately attractive to foreign investors.

4. Investor Confidence

Private-sector confidence in the government's investment policies is diminished due to frequent changes in policy, withdrawal of incentives--sometimes retroactively--and the lack of effective investment implementation mechanisms. In addition, promotional efforts intended to stimulate private-sector investment tend to over-state the quality of supporting services and the commitment of governmental agencies to assist the implementation of private-sector ventures in a timely and economically viable manner. Investor perseverance, based largely on political access and availability of financial resources, remains an essential requirement for doing business in Pakistan.

5. Institutional Capability and Support

In both the private and public sectors, institutional capability and support for agribusiness are weak in terms of introducing improved technology; investment promotion and development; technical and managerial training; consulting services and investment analysis; market analysis and development; business conceptualization and legal organization; joint venturing and financial packaging.

6. Agribusiness Management

Many agribusinesses lack financial viability due as much to poor private-sector business practices, especially in marketing, as to the impact of government regulations and administrative practices and policies. Conversely, in the agribusiness industries analyzed to date, those companies which employ sound management practices tend to do exceedingly well financially, despite the constraints encountered in the policy and regulatory environment.

7. Rate of Investment

Given the weaknesses in Pakistan's domestic economy and the international balance of trade perceived by potential investors, and the untimely and ineffective implementation of espoused economic policies which support private-sector intervention in agribusiness development, both the rate and quality of private sector investment are very limited. In addition, sanctioned private-sector projects are slowly implemented and tend to be highly debt leveraged. Imvestment is also hampered by security problems in Sind and other areas, as well as a perceived political instability.

8. Investment Impact

The slow rate of private sector investment weakens the government's efforts to achieve the employment, production and income generating goals of the 7th Five Year Plan. It is instructive to compare with other developing Asian countries. In general, those countries which sustained higher average rates of private investment from 1970 to 1988 have higher percapita incomes:

Country	Average rates of private investment (1970-1988)	Percapita incomes (1987)
India	9.9%	$ 300
Pakistan	6.0%	$ 350
Sri Lanka	12.8%	$ 400
Indonesia	11.8%	$ 450
Philippines	15.7%	$ 590
Thailand	16.8%	$ 850
Malaysia	15.8%	$1,810
Korea	21.2%	$2.690

Pakistan's problem of slow rates of private-sector investment is probably worsened by the public sector's perceived need to invest directly in agribusiness (e.g., the government's announced intention to invest in some seven new public agribusiness ventures.)

Contents

The annexes are not attached, but can be made available to anyone who wishes them by calling or writing:

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Annexes

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I. INTRODUCTION

A. Role and Definition of the Agricultural Corporate Sector

In the present stage of development of Pakistan's economy, agriculture provides greater scope for increasing production, incomes and employment than any other sector, particularly in rural areas. To achieve the production potential of Pakistan's rich agricultural resource base, an effective infrastructure of public services is essential: research, education, utilities, and roads. Equally imperative is the need for strong private-sector services--provided by small businesses, corporations, and cooperatives--to support the farming community, to provide the necessary production inputs as well as to process, distribute and market the farm outputs. The development history of agriculturally advanced economies bears testimony to the key role played by private-sector agribusinesses in technology development and innovation and in the provision of services to farmers.

During the past two decades in Pakistan, much effort has gone into building public support services for agriculture, at both the federal and provincial levels. A deliberate national policy aimed at developing a strong and dynamic, market-driven private-sector agribusiness community has not been formulated or pursued. Statements from senior government officials on the importance of private-sector agro-industries have been made from time-to-time, but the pronouncements have not been followed up with concrete policies or an integrated set of measures to put them into action. A conscious policy of the government to create an environment conducive to the growth of private-sector agribusiness will not only help farmers to enhance productivity and incomes, but will also increase foreign exchange earnings through more efficient servicing of the highly competitive export markets for farm products.

This Analysis of Corporate Sector Constraints in Agriculture (ACSCA) is intended to identify opportunities and to outline an integrated set of policies and measures that will help to strengthen private-sector agribusiness so that the inherent potential of Pakistan's agriculture can be achieved.

To help clarify the scope of the analysis, some definitions are in order. Agricultural production encompasses the production and harvesting of crops and livestock--the output of farming. (Agriculture is normally defined to include forestry and fishing as well as crop and livestock farming.) Sometimes the term "agriculture" is used broadly to include the activities of supplying the inputs for farming and of marketing and processing the products, or outputs, from farming. Also, the term "agribusiness" is often defined to include all three functions: the supply of farm inputs, farm production, and marketing and processing of farm products.

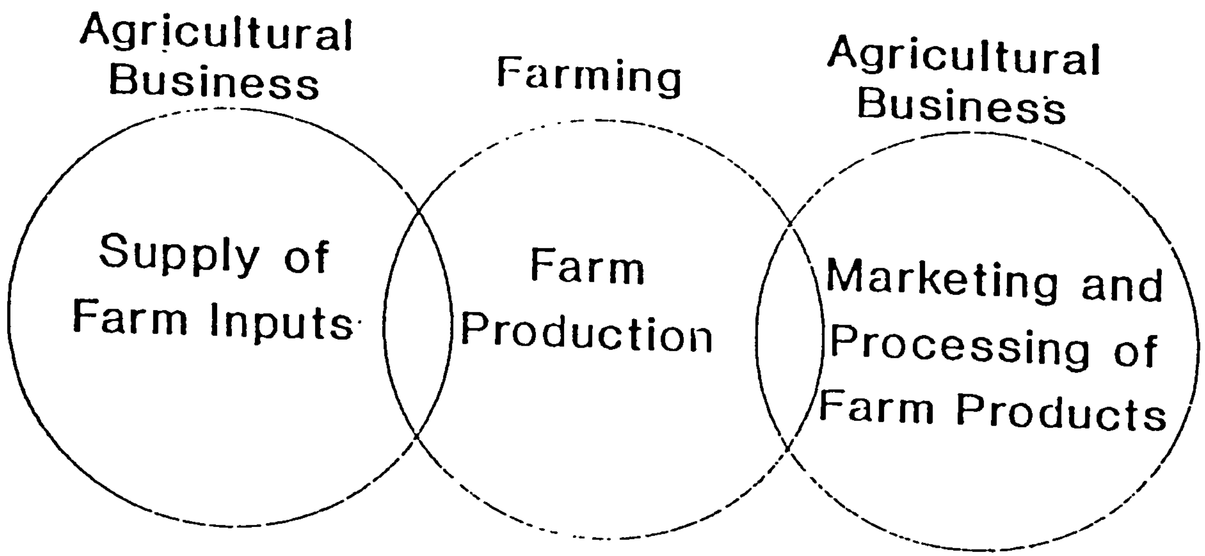
Figure 1 is a schematic of these three functions. In this analysis of corporate sector constraints, the "corporate sector" generally refers to the two outer rings, designated as Agricultural Business in Figure 1. Agricultural Business includes the collection, storage, manufacture and distribution of food and fibre products and farm inputs. In this analysis, the terms corporate sector, agricultural business and agribusiness are used interchangably.

The analysis is concerned with the investment climate for those businesses in the two outer circles which either produce farm inputs, such as seed, fertilizer and farm machinery, or which process and market the output of farms. The analysis is concerned with policies which influence activities in the middle circle--farm production--only to the extent that the effects of those policies influence the financial viability of businesses in the two outer circles, due to backward and forward linkages to and from farm production. For example, government price policy relating to a particular farm commodity, such as oilseeds, is considered in the analysis only to the extent that the effect of that policy has a significant influence on the financial viability of the agribusinesses serving oilseed producers.

B. Purpose of the Analysis

The purpose of the analysis of corporate sector constraints in agriculture is to identify the constraints to and opportunities for increasing private sector investment and participation in agribusiness development in Pakistan. The results of the analysis will be used to prepare a National Agribusiness Action Plan for consideration by the Government of Pakistan. The Action Plan will focus on policies and economic incentives required to stimulate the growth of private sector agribusiness operations. The underlying assumption based on examples from other countries is that a dynamic and growing agribusiness sector will have a positive effect on the overall growth and development of Pakistan.

Figure 1: Schematic of the Concept of Agribusiness



C. The Importance of Agriculture and Agribusiness

The combined economic impact of agricultural production and agribusiness activity is illustrated in the following table:

The Agricultural Economy of Pakistan

Economic Indicator	Economic Impact
Employment to total employment	70%
Contribution to total Gross Domestic Product	50%
Exports to total exports	50%
Household consumption to total consumption	60%
Energy consumption (1984-85)	40%
Consumption of imports (1984-85)	45%
Food/Fibre manufacturing tax revenue (1984-85)	26%
Capital investment to total investment (1984-85)	36%
Agricultural capital formation (1986-87)	Rs. 7,661 million
Agricultural credit (1986-87)	Rs.15,158 million

At the time of Independence in 1947, Pakistan had an extremely limited industrial base: a few small-scale agro-based units, three textile mills and one cement plant. Today, although there are few large ones, the formal agribusiness sector includes hundreds of firms. (Annex A gives a partial picture of changes in the number of agribusinesses). In addition, thousands of informal, unorganized enterprises outside the statutory framework of laws, regulations, and taxation are engaged in wholesale and retail marketing of various agricultural commodities and farm production inputs. While this latter group of enterprises forms a sizable and dynamic sector of the economy, it is outside the scope of direct investigation in the ACSCA study. To the extent that policy reforms result from the study, the informal agribusiness sector should benefit.

D. Methodology of the Analysis

Data collection for the Analysis of Corporate Sector Constraints in Agriculture (ACSCA) follows two main paths: (a) a national assessment, based mainly on secondary data, and (b) case study research in six agro-based industries.

1. The National Assessment

Analytical methods used in the National Assessment include qualitative and quantitative analyses of data and information assembled by ACSCA professional staff.

Qualitative Assessment: Annex B contains a list of the sources of information and data that were drawn upon for the assessment. Those secondary sources were supplemented by personal interviews with key persons involved in agribusiness operations and development, either as entrepreneurs, as policymakers, as financiers, or as officers in agencies responsible for implementing official policies, regulations and administrative actions. A list of those interviewed is included in Annex C. Finally, a series of seminars was held to draw out from the participants what they perceive to be the main constraints which inhibit agribusiness investment. The seminars included a mix of private business people, representatives of financial institutions, and government officials. They were held under the auspices of Chambers of Commerce and Industry and local governments, in Karachi, Lahore, Peshawar, Quetta and Multan.

This report of findings and conclusions is, in effect, a description of the main conceptual points stemming from the above sources of data and information.

Quantitative Assessment: The conceptual framework for the quantitative assessment builds on previous quantitative work carried out in Pakistan. The PAKSIM Model is being modified to apply more specifically to the agribusiness sector in Pakistan. Intensive runs of the models will take place during the summer of 1990, using data from the case studies and other sources (e.g., EAN) to supplement secondary sources. The ACSCA team will strive for maximum interaction with Pakistani counterpart institutions and professionals in running the simulations. The models will help to show the effects on the general economy of alternative policies with respect to agribusiness investment, development and trade.

2. Subsector Case Study Research

Six major agribusiness industries, or subsectors, are being analyzed to determine the constraints to and opportunities for private sector participation in agribusiness development:

- Fertilizer and Farm Chemicals
- Farm Machinery and Implements
- Seed Production
- Edible Oils
- Fruit and Vegetable Processing
- Animal and Poultry Feed

Research reports about each of these subsectors will be used to prepare a composite agribusiness industry case study report.

The case study methodology focuses on three facets of agribusiness activity:

a. input agribusiness industries;

b. output agribusiness industries; and

c. in-depth analysis and comparison of the viability and capability of specific corporate agribusiness operations within a given sub-sector as well as the overall agribusiness sector of Pakistan.

The integrated analysis of those six subsectors will demonstrate the interdependence inherent in the business relationships in the wider agribusiness sector. This research focus will help to isolate the most important policy issues affecting private sector investment and participation in agro-industry development, as well as the problems and limitations that arise when policy formation is based on narrow sub-sector issues or specific commodity objectives.

The data and information asembled about each subsector follows a research format and process intended to provide:

a. a clear profile of the industry in terms of its market, products and services, the impact on the economy and the interaction between companies in the industry;

b. an in-depth funtional analysis, on site, of the business practices, viability and capability of selected companies in each industry;

c. a sharply focused summary of the opportunities and constraints affecting the specific agribusiness industry; and

d. a presentation of findings, conclusions and recommendations focused on the current and potential role of:

-- private-sector investment in the industry;

-- public policy to stimulate greater private-sector investment in the industry; and

-- foreign assistance to foster development of private-sector agribusiness activity.

The results of the case study research will provide data and information which:

a. empirically demonstrate the importance of understanding the forward and backward linkages of agribusiness activity to guide public policy formation and to suggest investment incentives to stimulate agribusiness development;

b. clearly identify constraints and bottlenecks to agribusiness development which in turn impede growth in agricultural productivity, markets and incomes;

c. sharply focus on key agribusiness priorities, sectors and opportunities to be addressed by the government, the private sector and foreign donors; and

d. contribute directly to the findings and recommendations to be presented in the National Assessment report and the proposals for change and development to be presented in the National Agribusiness Action Plan.

Extensive operational data and empirical information are being provided for the case study by private and public sector companies, trade and professional associations and entrepreneurs engaged in each of the targeted agribusiness industries. While the results of subsector research will be presented in individual research reports, the key policy, regulatory and operational constraints identified will be presented in an integrated manner in one Case Study Report. The case study results will be incorporated in the final National Assessment report. A draft summary of case study data and information is included in Annex E.

3. Public Forums

As indicated above, a series of seminars was held in 1989 under auspices of the ACSCA Project to get suggestions and input from participants on the main constraints to private-sector investment in agribusiness in Pakistan. Those meetings contributed many of the ideas contained in this draft Assessment Report. During 1990, a series of workshops, seminars and symposiums is being sponsored under the project to get public reaction to the major findings of the study team. A Workshop to be held in early April will set the context of the study and describe its main findings and conclusions. The organizers will seek the counsel of participants in sharpening (or perhaps in some cases discarding) individual findings, so that a more solid basis the final draft Assessment is planned for August 1990.

In addition to the public sessions on the National Assessment, a three-day workshop will be held in October 1990 on results of the Case Studies, and a three-day symosium will be held in early December 1990 on the draft National Agribusiness Action Plan. Following these workshops and symposiums, the respective documents will be prepared in final copy.

II. GOVERNMENT INVESTMENT AND INDUSTRIAL POLICY

A. The Current Policy Stance

1. The Climate for Investment

An Industrial Policy Package issued by the Federal Ministry of Industries in July 1989 recognizes that the climate for investment in the past has not been as favorable as the Government would like. The Minister's foreword to the Industrial Policy Package document states that:

> there is a need for greater efforts in mobilising our resources through a more confident atmosphere for capital investment and induction of modern technology. . . . Previous industrial policies could not be effectively implemented . . . in an atmosphere of uncertainties of policies, precedural delays in the approval of projects and inadequacy of infrastructure facilities.
>
> The fundamental approach of the new policy is to liberalize investment opportunities for entrepreneurs in selected industries. . . For meeting these objectives, the policy has removed impediments in the way of the clearance of an imvestment proposal by creating a high-powered sanctioning authority, viz. Board of Investment (BOI) to be chaired by the Prime Minister. . . Efforts have also been made in this policy to streamline the procedural matters in minimizing the areas of investment where Government sanction would be required, One Window Operation in sanctioned industrial estates and ensuring provision of required facilities for implementation of the project within 60 days of sanction/approval of an industrial project. . . To make the policy more attractive, fiscal, monetary and trade policies have been attuned to the needs. . .

Since it was formed in April 1989, the BOI has been meeting once each month under chairmanship of the Prime Minister. Reports of the meetings suggest that the BOI is seriously and deliberately attempting to speed up both the sanctioning and implementation processes, although a greater degree of success is achieved in sanctioning than in implementation.

One indication of degregulation, or liberalization in investment policy, is that the list of industries--the Specified List--for which the private sector is required to seek permission from the GOP in order to establish new industrial units has been reduced from 12 to 7. The new Specified List includes:

- arms and ammunition;
- security printing, currency and mint;
- high explosives;
- radio-active substances;
- alcohol and beverage industry based on imported concentrates;
- manufacturers of automobiles, tractors and farm machinery; or
- petroleum blending plants;

The only agro-industry dropped from the Specified List was the vegetable ghee/cooking oil industry based on imported seed oil. The other industries dropped were manufacturers of air-conditioners, refrigerators and deepfreezers, of drugs and pharmaceuticals, of motorcycles and scooters, and of TV, radios, tape recorders, VCRs, VCR cassettes, and tapes.

2. Government Policy Regarding Agribusiness Development

Tractors and Farm Machinery are the only agro-industry on the Specified List. All other agribusinesses do not require government sanction unless the size of investment exceeds Rs. 1 billion or "major policy decisions" are involved.

The July 1989 Industrial Policy Package states that:

> Emphasis will continue to be placed on development of export-oriented and import-substitution agro-based, engineering, electronic and high-tech industries. . . For realisation of the twin objectives of the development of agro-based industry in the rural economy and creation of employment in these areas, an amount of Rs. 1.2 billion has been allocated in the budget of 1988-89. The amount will be disbursed through the Agricultural Development Bank of Pakistan and the nationalized banks; thus removing impediment of finances in the much needed development of agro-based industry. . . Greater reliance will continue to be placed on the private sector to achieve the objectives of the new industrial policy. . . Allocated share for private

sector (in the 7th Five Year Plan) is over 90 per cent of the total investment. To make this possible, effective monetary and fiscal incentives have been given to attract private investment.

The present Government is of the view that in order to attract private investment, specially from abroad, guarantees shall have to be extended against policy of nationalization. Moreover, to rationalise the investment strategy, a policy of privatisation is being gradually introduced in order to cohibit both the public and private sectors in the national development process. It has been categorically declared by the Prime Minister that there will be no nationalization of industry in future.

The Pakistan Investment Guide (July 1989) issued by the Ministry of Industries contains a list of "investment priority areas" which is "indicative and not exhaustive." The list includes the following types of businesses which are agro-based or which support agriculture:

- Feeding and fattening ingredients for livestock;
- By-products of sugarcane/sugar;
- Processing, canning and preservation of fruits and vegetables;
- Fertilizer;
- Basic manufacture of insecticides and pesticides;
- Tannery chemicals;
- Textile weaving; and
- Newsprint and craft paper.

Pakistan's stated policy is to encourage foreign investment in setting up industrial undertakings. Private investment, both local and foreign, is to be promoted and channeled into priority sectors. Foreign private investment is preferred in industries which are either capital intensive, involve sophisticated technology, bring managerial and technical skills or marketing expertise, or break new grounds in promotion of industry not set up in the past in Pakistan. Foreign private investment is classified as either "prohibited" or "allowed, subject to normal restrictions." The prohibited list includes ownership of real estate, including agricultural land and forests, and irrigation systems. The "allowed" list includes livestock, seed, dairy, and poultry farming; deep-sea, coastal and inland fishing; and manufacturing (including most agribusiness.)

Government policy is to encourage and support the development of small-scale industries, which encompass a wide spectrum of agriculturally related businesses.

In short, while the various policies refer to and reflect the importance of agribusiness, there is not a defined agribusiness development policy.

B. Implementation of Policy, Regulations and Procedures

The implementation of Government policy for guiding investment in industrial activities, including agribusiness, involves subsidiary regulations and administrative practices and policies: sanctioning procedures for new enterprises; fiscal incentives or disincentives; deregulation; special treatment for key industries and underdeveloped, mainly rural and sub-urban geographic areas; credit policy; and policies regarding foreign investment.

The philosophy and approach of the Government toward industrial growth have shifted periodically during the history of Pakistan. More recently, in parallel with policies of many other countries of the world, pronouncements have shifted toward more reliance on private enterprise and less on direct public investment as an industrialization policy. However, at the same time, the Government has announced intentions to invest directly in a number of new business ventures, ostensibly "to create jobs." Official policy has also been directed toward liberalization of sanctioning procedures for new or expanded ventures. Annex F contains a brief on the evolution of sanctioning procedures.

1. Investment Promotion

The government has not had a comprehensive, proactive policy or program of investment promotion. The Investment Promotion Bureau (IPB) has operated more as a sanctioning authority than an investment promoting entity. However, to try to make it more effective, the IPB, which serves as the field arm of BOI, was reorganized in late 1989 into three divisions:

- Approval and Regulatory Division
- Monitoring Division
- Promotion, Publicity & Publications Division

There is a "key industries" list, which by implication suggests that the industries on the list are those for which the government wishes to encourage investment, but there are no known promotional activities aimed at stimulating investment in those industries. In addition, fertilizer is now the only agro-industry on the key industries list.

2. Sanctioning Procedures

The procedures for getting approval to start a new agribusiness or to expand an existing one are extremely tedious and time-consuming. For multinational companies attempting to register a business in Pakistan or to expand an existing one, the procedure is even more debilitating. The companies are often willing to invest, but the rules and regulations keep them from doing it. Sanctioning procedures must be markedly improved if substantially increased investment in agribusiness is to be realized.

The July 1989 Industrial Policy Package purports:

> to streamline the procedural matters in minimizing the areas of investment where Government sanction would be required. . . In order to alleviate the difficulties faced by the local as well as foreign entrepreneurs, in obtaining sanctions for the establishment of industrial units, the requirement of Government sanction has been dispensed with, to a large extent. . . The projects will now be sanctioned, depending on their size and type, by the Board of Investment (BOI) headed by the Prime Minister.

In the following cases, sanction by the BOI is required:

a. investment in the industrial unit exceeds Rs. 1 billion;

b. the unit involves one of the items on the Specified List (see page 9);

c. foreign equity participation is 50 percent or more (this requirement was dropped by the BOI at its meeting of February 28, 1990); or

d. major policy decisions are involved.

Except for the manufacture of tractors and farm machinery (the only agro-industry on the Specified List), agribusinesses with less than Rs. 1 billion of investment do not require BOI sanction unless "major policy decisions are involved." A key to the degree that sanctioning procedures will be liberalized under the new structure will be the extent to which sanctioning officials identify "major policy decisions" in potential agribusiness investments.

3. Locational Policy

In the past, Provincial Governments have required that a new business obtain from them a No Objection Certificate (NOC) which certifies that the location chosen by the entrepreneur for the plant is satisfactory to the Government. This has been a major source of delay, at best, and of unbridled frustration in many cases. During the past year or so, the Provincial Governments have apparently acquiesced to the suggestion from the Federal Government that instead they should each notify a "negative list" indicating areas in which the establishment of industries is not considered desirable. The Pakistan Investment Guide, July 1989, states that:

> Investors will thus be free to establish industries outside these areas without any requirement of NOC from the concerned Provincial Government. In case an entrepreneur wishes to establish any industry in the restricted areas, he will have to apply for an NOC from the Provincial Government and such applications will be considered on a case to case basis and NOC could be issued if the entrepreneur can establish merits of his case.

If the policy as stated in the above paragraph is effectively implemented by the Provincial Governments, then this will have been a most positive step and the issue should essentially disappear. The Provincial Governments are issuing a negative list for the sugar industry. The ACSCA team intends to follow developments over the next few months to see whether notable issues remain in the implementation of locational policy.

4. Taxation Policies and Incentives

The Income Tax Ordinance contains several measures which are intended to be incentives for investment. These include investment allowances, tax holidays for selected industries and underdeveloped areas, and various kinds of tax credits and tax exemptions. Annex G discusses these and identifies some of the issues for further investigation. While the ACSCA team is not yet ready to make recommendations, one of the issues of concern to agribusinessmen is the removal from the key industries list, except for fertilizer, of all those agribusinesses which formerly qualified based on their using 70 percent or more of locally produced raw materials. Removal from the key industries list means that they do not qualify for a tax holiday (unless the industry is located in an area designated as "underdeveloped.") The Trade Policy section of Annex G discusses import and export regulations and some of the changes which have taken place in recent years.

5. Key Industries

Key industries for adding higher value and acquiring sophisticated technology are identified in the Industrial Policy Package, July 1989. The six so designated are:

- Biotechnology
- Fibre optics
- Solar energy equipment
- Computers and software
- Electronic equipment
- Fertilizers

A four-year tax holiday is to be granted to businesses set up in these key industries up to June 30, 1993.

6. Indigenization Policy

An objective of the GOP is to attain self-reliance in the engineering and technical industries. The indigenization, or "deletion," policy is intended to help achieve the objective. The policy offers rewards to certain industries for timely deletion of imported items in favor of locally manufactured ones; on the other hand, a "penal duty of 100% over and above the industrial rate or the full commercial rate of duty, whichever is higher, is levied if any item is not deleted as scheduled."

7. Geographic Preferences

To help develop "backward areas," special concessions are given to businesses which agree to set up operations in those areas. The designated areas include NWFP, Baluchistan (except Hub Chowki areas), FATA, Northern areas, and Azad Kashmir. In these areas, the income tax holiday is for eight years for new businesses which will have been established up to June 30, 1993. The businesses are also exempt from customs duties on all machinery not manufactured in Pakistan and from import surcharges and sales taxes.

Experience to date indicates that only in minor cases do the investment incentives offset the disadvantage of lack of infrastructure in the underdeveloped areas.

8. Foreign Investment

As a part of this study, a member of the ACSCA team held discussions in the U.S. and the U.K. with senior officers of 11 U.S. and 4 U.K. multinational companies on their operations in Pakistan and their attitudes about doing business in Pakistan. Contacts were initiated with either the Chairman or President of each company. The survey was conducted with the person contacted or with one of the senior officers of the company (i.e., Executive Vice President International, Group Vice President responsible for the area which includes Pakistan, or Vice President/Director of Planning.) In some cases, follow-up interviews or correspondence were held with additional senior officers of a company. Among the U.S. companies were Castle and Cook (Dole), Central Soya, General Mills, International Multi Foods, Land O'Lakes, Pillsbury, Proctor & Gamble, Quaker Oats, and United Brands (Chiqita). The U.K. companies were BAT (British American Tobacco), RHM (Rank Hovis McDougall), Unilever and United Biscuits. In brief, of the 15 companies:

a. two companies which have operations in Pakistan are "generally positive" on conducting business in Pakistan;

b. two companies which have operations in Pakistan are considering or are proceeding to expand operations despite their concerns on the overall economic/political/business climate in Pakistan;

c. one company is considering establishing operations in Pakistan if the overall economic/political/business climate in Pakistan continues to improve;

d. three companies might be interested in establishing operations in Pakistan if the overall economic/political/business climate were better in Pakistan;

e. seven companies are not considering establishing operations in Pakistan, for three basic reasons:

    (1) they feel Pakistan is an unstable economic and political area;

    (2) there is "insufficient information" available to them on the opportunities in Pakistan (i.e., they do not know if there is a market for their products in Pakistan or if there are raw materials they would use in an economic way to market internationally); and

    (3) there has been "no cooperation" from the Pakistan banks and government sources that they have contacted over the years.

In short, the results of this informal survey suggest that Pakistan needs more "corporate supporters" in the multinational agribusiness community and, therefore, must make changes in the economic/political/business climate if multinational agribusiness firms are to be attracted to Pakistan. This will require an investment of both time and money to provide relevant information and to promote the country.

A press release (Dawn, Aug 30, 1989) suggests that the Government is aware of the need:

> The Advisor to the Ministry of Finance . . . invited the foreign investors who are already in Pakistan to give suggestions which can attract fresh foreign investment into the country . . . (and is) preparing a report in this regard for the Prime Minister. . . (The Advisor) has conducted a study of the countries which are attracting massive foreign investment these days.

Regarding repatriation of capital by foreign investors, the announced policy of the Government of Pakistan (as attributed to the Minister of Industries by The Pakistan Times, Aug 25, 1989) is that:

> foreign investors could easily transfer their profit and capital to their respective countries. Their foreign national employees could send 50 percent of their income abroad and also transfer their savings on returning to their countries. (Further), if a project costs (less than) one billion rupees or had (not more than) 49 percent foreign equity, there was no need even to seek any formal permission for it.

III. THE MAIN CONSTRAINTS

A. Public-Sector Domination of Agro-Industry

During the past two decades in Pakistan, much effort has gone into building public sector support services for agriculture, including agricultural research and extension, at both the federal and provincial levels. This is commendable. At the same time, rather than to encourage private sector investment in agro-industries, public sector agribusiness enterprises have been fostered, nurtured and subsidized. ACSCA case study analyses reveal a pervasive pattern of public sector enterprise domination of the key agribusiness industries of fertilizer, farm machinery, edible oils and seeds. One of the most important conclusions is that public sector enterprise control of agribusiness impedes growth of the agricultural economy, and diminishes the value and impact of GOP investment policies and incentives for the private sector. Serious constraints to agribusiness investment and to economic efficiency in Pakistan arise in these "mixed" agro-industries due to the controlling GOP organizational (ologopoly) structures and the associated trade restraints and product pricing practices that are common in those industries. Without a drastic change in policy to reduce public sector investment and control over agro-industry, broad-based private sector investment and participation in agribusiness development are unlikely to occur.

A prime example is the fertilizer industry. The National Fertilizer Corporation (NFC), a fully-owned state holding company with five fertilizer factories, owns 53 percent of the nation's fertilizer production capacity. The Fauji Foundation, a quazi-state institution, has two factories with another 24 percent of capacity. (Under a standing agreement with the Government of Pakistan, Fauji Fertilizer Company is assured of a fixed rate of return of 20 percent for 10 years.) At the moment, there are two private-sector fertilizer companies--Exxon Chemical and Dawood-Hercules, with a combined total of 23 percent of total fertilizer production capacity. With respect to marketing, National Fertilizer Marketing Ltd., a susbsidiary of NFC, has the responsibility of marketing the production of NFC plants plus a 40 percent share of imported fertilizer. Furthermore, imports of fertilizer are controlled by the Ministry of Agriculture through the Department of Fertilizer Imports. The private companies are allocated a 60 percent share of the imported fertilizer to market in addition to their own production, but they are not allowed to import fertilizer. This constitutes a classical ologopoly situation--though nitrogen fertilizer is nominally "deregulated," the NFC effectively sets prices which the other producers essentially adhere to.

In addition to the fertilizer example, other case studies, especially those of Edible Oil, Farm Machinery, and to a lesser extent the Seed Industry, also demonstrate widespread Government control--and associated inefficiencies--in the industries. In the case of edible oils, the Ghee Corporation of Pakistan (GCP), a government holding company with 24 ghee mill units, produced in 1989 about 54 percent of the country's output of vegetable ghee/cooking oil. The remainder is produced by about 50 private-sector units, about 20 of which have started operations since the 1986 deregulation. One objective of the deregulation was to reduce GCP's share of the ghee market as a percentage of the total ghee market. In practice, the deregulation measures have fallen short of expectations. GCP still acts as the "price leader" and the price does not reflect market conditions. In addition, the sole authority to import soybean oil is with the Trading Corporation of Pakistan. The private sector can import other edible oils, subject to import licensing. Notwithstanding the shortcommings, deregulation has somewhat improved the environment in which oil producers and processors operate, but the industry has not developed in a manner that stimulates local production of non-traditional oilseeds for edible oil and livestock feed. Current use of foreign exchange for the importation of edible oil and feed cake is in excess of $350 million per year.

In the case of farm machinery, two tractor companies of the public conglomerate, Pakistan Automobile Corporation Limited, account for a market share of 95 percent of tractors sold:

- Millat Tractors Limited 66 percent
- Al-Ghazi Tractors Limited 29 percent

The tractor manufacturing industry is "vertically integrated" in the sense that the GOP owns and controls, in addition to the two major tractor companies, most of the raw material (steel) and manufacturing concerns which make the subassemblies for the tractor companies and, through Government-owned financial institutions, supplies virtually all of the credit for tractor purchases. The deletion (indigenization) program, while it has fostered the establishment of companies to supply parts for the tractor manufacturers, constitutes a major barrier to entry of new firms and, therefore, competition in the tractor industry. On the other hand, the implement industry is characterized by a large number of small businesses, generally poorly equipped, and there is a dearth of durable, broad-spectrum implements.

The announced policy of the present, democratically elected government is for the private sector to play a greater role in business and in economic development. An integral part of this policy was a decision in early 1989 to "privatize" some businesses that are now government owned and operated. A Disinvestment Cell was set up in the Ministry of Finance, with an Additional Secretary in charge. In phase one, the announced plan was to privatize some profitable enterprises; a part of this plan is to offer (not to exceed 49 percent of) shares to "members of the working class," to encourage their participation in strengthening the economy and to broaden the base of the stock exchange. The Government would retain at least 51 percent of shares. In the second phase, the shares of unprofitable public sector units would be offered to the private sector "after making them commercially viable." As one might expect, this kind of "privatization," which keeps management of the enterprises effectively under control of the Government, is not generally attractive to private investors. To date, the plan has not been implemented.

A paradox in the Government's plan to privatize is that the Ministry of Production has announced plans for the Government to invest in a number of new production enterprises, including four new fertilizer plants under auspices of NFC. One likely detrimental effect of this is that Exxon and Dawood-Hercules, which had both expressed intentions to build new plants, may find it prudent to delay or cancel their proposed investments (estimated at $300 to $500 million.) If NFC goes ahead, the industry will retain an ologopoly dominated by both the NFC, the market price leader, and the GOP, which controls the purchase, storage, distribution and pricing of imported fertilizer.

With these kinds of conflicting policies, the potential impact, breadth and depth of private-sector investment in agribusiness industries in Pakistan is likely to remain very limited and imbalanced unless and until the GOP:

- fosters real privatization of public-sector enterprises;
- stops investing (with foreign donor support) in more public-sector enterprises; and
- designs, implements, and promotes policies and incentives seriously intended to increase private-sector participation and investment in competitive, market-driven agribusiness industries.

B. Over-Regulation of Trade and Commerce

The Government deregulation of agribusiness, including the removal of price controls, is often cited as a factor favorable to private sector agribusiness development, investment and competition. The ACSCA analysis of business practices in several key agro-industries does not support the proposition that effective deregulation has, in fact, occurred. As indicated above, even though locally-produced nitrogen fertilizer prices have been "deregulated," effective price setting by GOP entities remains. The two private-sector fertilizer companies which, because of better management, are more efficient, are able to take advantage of the price-protected situation and to make handsome returns on their investments, while some of the state-owned enterprises are subsidized directly by the GOP. If the industry were truly opened up exclusively to private investment, average costs of fertilizer production and therefore prices would decline due to both a higher degree of competition and increased efficiency. In a competitive environment, the private firms would also work harder at marketing, including more agressive farmer education and extension programs.

Through its companies, agencies, banks and political institutions, the GOP effectively controls many major agribusiness markets, commodity flows and business practices. These controls directly affect commodity imports and exports, physical distribution, base-line production, raw material procurement costs, consumer product pricing and market competition. Restrictions and regulations which affect exports include taxes and duties, quotas and bans, and licensing. Details of these phenomena will be presented in the forthcoming series of Case Study research reports.

C. Sluggish Implementation of Investment Policy

1. Investment Incentives

Pakistan's resources dictate that agriculture will remain for many decades a leading sector in Pakistan's economy. Viable agriculturally related businesses are essential for the country to maximize the economic value of its agricultural resources. Yet, no deliberate national policy aimed at developing a strong and dynamic, market-driven private agribusiness sector has been formulated or pursued. Neither is there an agency with a mandate specifically to promote agribusiness development. Both are needed, even to stimulate domestic investment. If, in addition, significant foreign investment in agribusiness is to be solicited, the agribusiness investment policies of Pakistan must be at least as attractive as are those of other countries in the region which are competing for the relatively scarce foreign investment being made in agro-industry.

Private sector confidence in the Government's investment policies is diminished due to frequent changes in policy, withdrawal of incentives--sometimes retroactively--and the lack of effective investment implementation mechanisms. In addition, promotional efforts intended to stimulate private sector investment tend to over-state the quality of supporting services and the commitment of governmental agencies to assist the implementation of private sector ventures in a timely and economically viable manner. Investor perseverance, based largely on political access and availability of financial resources, remains an essential requirement for doing business in Pakistan.

2. Sanctioning Procedures

Historically, the Investment Promotion Bureau has been a bottleneck, often fatal, to serious potential investors, rather than an agency which has tried to encourage and assist entrepreneurs. Amazingly consistent negative stories about experiences with IPB were relayed to the ACSCA team in 1989 by Pakistani business people, foreign business concerns which considered coming to Pakistan to do business but ultimately decided not to, and even by a number of government officials. Several people indicated that the IPB would be more appropriately named the Investment Prevention Bureau. ACSCA team members who visited in May 1989 with a senior official of IPB were unable to obtain any kind of promotional materials, nor even positive verbal expressions indicating that agribusiness investment was desired. In fairness to IPB, the exact stance of the new government regarding industrial policy had not yet been articulated publicly, which may account to some degree for the reticence of the IPB representative. Since then, in July 1989, an attractive promotional brochure--Industrial Policy Package--and a more detailed Pakistan Investment Guide were issued by the Ministry of Industries.

As indicated under the heading, The Climate for Investment, in Section II of this report, the Board of Investment is apparently taking a special interest in improving both the sanctioning and post-sanctioning procedures. This includes a major revamping of the IPB. The Asian Development Bank announced on January 30, 1990 that it had approved a $350,000 technical assistance grant to Pakistan for restructuring and reorienting the role and functions of the IPB toward industrial promotion.

3. Post-sanctioning Procedures

Post-sanctioning procedures include: (a) getting approval of the Controller of Capital Issues to issue share capital; (b) getting approval for financing from development finance institutions or nationalized banks; (c) obtaining licenses or permits for import of plant and machinery from the Chief Controller of Imports and Exports (CCI&E); (d) obtaining licenses for import of raw materials and spares, from the regional Imports and Exports Office; (e) applying to the Provincial Chief Inspector of Factories (if 10 or more persons are to be employed) to be registered under the Factories Act; (f) registering the business as either a sole proprietorship, a partnership or a limited company; (g) obtaining assurance from the relevant Provincial Government that it has no objection to the site chosen for plant location; and (h) arranging infrastructure facilities: telecommunications, gas, power, water and sewerage.

Evidence accumulating from the case studies and from other sources suggests that the delays and frustrations associated with post-sanctioning procedures are frequently more debilitating than are those associated with sanctioning.

A Pakistan press article ("Changing Gear," The Herald, Dr. Shahid Zahid, May 1989) describes the problem succinctly:

> Because of bureaucratic controls and corruption, foreign investment, even where desirable, has shied away. . . some serious thought has to be given to reducing the bureaucratic hurdles and procedures

> involved in setting up industries. Any opposition from vested interests within the bureaucracy must be challenged if progress is to be encouraged.

Another article (Dawn, Aug. 31, 1989: Foreign Capital as Tool of Growth) provides evidence that the rate of industrial expansion in Pakistan is less than desirable and that other Asian countries are obtaining more foreign investment than is Pakistan, and then goes on to state:

> The reasons are not difficult to explain. In the area of foreign investment, as in many other areas, there has been a large gap between our policy pronouncement and practice, between what the men at the top desire and the small men at the bottom devise. Bureaucratic obstruction or footdragging has been a major deterrent to rapid industrial expansion. Too often our economic officials feel the authority and discretionary powers vested in them are meant to be exhibited or demonstrated rather than used for promotion of the goals they are meant for.

The above statements capsulize what have been oft-repeated statements to ACSCA team members about how post-sanctioning procedures are implemented. To a large extent, the attitude characterized above is a carryover from the days when colonial administrators used the bureaucracy to control the populace. To change those attitudes to reflect a mandate to serve rather than to control represents a tremendous challenge. In addition, a prejudice exists among much of the bureaucracy against the private sector. Because of the prejudice, the translation of policy into action takes a long time. As it relates specifically to agribusiness investment, the ACSCA team will define in the Action Plan some specific measures designed to speed up the procedures, ideally in ways that will give the participants a positive feeling about their ability to facilitate advancement of their country's goals for investment and employment.

4. Frequency of Policy Changes

One cause for concern among business people is the frequency with which policy changes are made, sometimes even retroactively. Some businessmen refer to this as the ad hoc approach to policy. Occasionally, a policy will be changed or dropped even though it had been announced as one which would apply until a certain date still in the future. As a case in point, under the Income Tax Ordinance, a policy had been announced that a tax credit of 15 percent of the amount invested up to June 30, 1991 would be allowed to companies investing in industrial plant and machinery for balancing, modernization and replacement (BMR); in mid-1989, this concession was withdrawn retroactively from July 1, 1988.

In July 1989, a new system to limit certain vegetable exports was introduced. A ban was placed on exports of chillies (the ban was altered in January 1990 to become a 5,000 MT quota). The ban caused defaults on exporter contracts, with the result that the purchaser has gone to other country sources which are considered to be more reliable suppliers.

Another example includes having dropped in 1989 without advance notice the horticulture processing industry from the key industries list. Potential investors who were counting on the fiscal incentives associated with the list have expressed concern that horticulture was dropped from the list.

D. Weak Supporting Institutions

In both the private and public sectors, institutional capability and support for agribusiness are weak in terms of introducing improved technology; investment promotion and development; technical and managerial training; consulting services and investment analysis; market analysis and development; business conceptualization and legal organization; joint venturing and financial packaging.

1. Agro-Industrial Technology Development & Transfer

Evidence obtained in the case studies indicates that the technology being used in many of Pakistan's agribusinesses is inadequate, at best. In the handling of fruits and vegetables, there is hardly even rudimentary technology being used for removing field heat, in cooling and storage or for trucking. Cans used in food preservation are still made by the old lead solder method and would not be permitted in most western countries. Most fertilizer plants are not state-of-the-art. The technology used in the pesticides industry is woefully inadequate. Edible oil extractors are obsolete. The techniques used to manufacture farm implements and some sub-assemblies and parts for tractors are sub-standard. In those cases in which the technology in agribusiness is good, there are too few trained people to use it properly. Unless they are tied with multinational companies, Pakistan's food companies do not have the capability to conduct research and development.

Reasons for these deficiencies, in many cases, appear to be:

a. lack of market competition to force greater efficiency and quality production;

b. lack of mandatory or enforced standards for safety, production or product quality; and

c. lack of information and training to stimulate improved technology development and adoption by agribusinesses.

The lack of modern technology is in some cases related to a curious import policy: "For the last few years, the import policy has been so designed that no foreign company can now import any item which it did not import before 1972 and so they cannot take advantage of the rapid improvement in technology which has taken place during the last 17 years. That means that old companies have perforce to be content with their ancient technology instead of opting for the latest and most economical." (Attributed to Dr. Habib, President of Overseas Investors Chamber, Dawn, Aug. 31, 1989)

2. Agribusiness Promotion and Development

Various business and development activities are carried out by Chambers of Commerce and Industry, the Federation of Chambers of Commerce and Industry, the Overseas Investors Chamber, and other entities such as the American Business Council. The ACSCA team has identified no agency that focuses especially on agribusiness promotion and development.

3. Industrial and Managerial Training

The Lahore University of Management Sciences (LUMS), a private-sector initiative, offers a two-year course leading to an MBA degree. The 15-member Faculty is mostly trained abroad at the PhD level. Rigid criteria are used to select about 60 students per class from among many hundreds of applicants. Graduates are "picked up like hot cakes" upon completion of their degrees. LUMS also offers one-week short courses in Executive Development, which are well-subscribed.

Other institutions provide MBAs and other kinds of industrial and business management training. The preliminary conclusion is that substantial scope exists for cost-effective additional kinds of training programs designed to improve the performance of agribusinesses. In particular, good MBA (Agribusiness) training programs, either at LUMS or abroad, would help to fill a great need.

4. Investment Analysis and Financing

At this juncture in the Analysis, the ACSCA team concludes that virtually no entity exists in Pakistan which serves agribusiness and has the capability to do independent, rigorous technical and financial feasibility studies as a basis for potential investors and financiers to decide with confidence whether the ventures will be viable. Some of the development finance institutions (DFI's) do "appraisals" or "feasibility studies" for clients, with some hesitation, because the clients are unable to engage professional consultants or institutions to help them do a rigorous, independent analysis. The hesitation of the DFI's hinges on their preference not to do the feasibility studies because if they do and the business later turns sour, the client will blame the DFI for a faulty feasibility study. Banks and DFI's generally prefer that feasibility studies be done independently, leaving them with the role of appraising the studies as a basis for deciding whether on not to support the ventures.

The Investment Advisory Center of Pakistan (IACP) is reported to do well at representing Pakistan to potential outside investors. It claims to do project identification, investment analysis, and feasibility studies. Samples of IACP analyses available to the ACSCA team are typical of such work by other parastatal organizations--they are not impressive. This judgment is consistent with that reflected by a previous team whose report:

> shows a summary of the agro-industry profiles as presented by the Investment Advisory Center of Pakistan (IACP). Unfortunately, the various analyses do not follow a standard format, which makes comparisons between them sometimes difficult. . . IACP's analyses are, by and large, incomplete, and are done unsystematically. With particular reference to agro-industries there is no systematic treatment of agricultural production, processing, and marketing as the three building blocks of any agro-industry. Occasionally, comments are made about agricultural production or about marketing, incidental to the major emphasis on processing proper. As a result, most of the identified agro-industrial opportunities are rather unconvincing. (Pakistan: Prospects for Non-Traditional Agricultural and Agro-Industrial Exports, AMEC, Inc., April 1984)

Financial and Management Services (Pvt.) Limited (FMS), a Karachi-based company, was formed in 1985 by the Pakistan Banking Council, Bankers Equity Limited, Industrial Development Bank of Pakistan, Investment Corporation of Pakistan, National Development Finance Corporation and Pakistan Industrial Credit and Investment Corporation, plus a group of private sector businessmen. FMS engaged Booz Allen & Hamilton, an international consulting firm, to assist with start-up and to provide specialized consultants. According to a recent brochure, FMS has done studies and analyses for the World Bank (110 person-months), the Asian Development Bank (12 person-months), the Pakistan Banking Council, nationalized banks, and DFIs (46 person-months), public-sector clients (14 person-months), and private-sector clients (26 person-months). Work for the private-sector clients was essentially all industry (non-agribusiness) related.

5. Market Analysis and Development

One of the main shortcomings in agribusiness in Pakistan is the lack of appreciation of the importance of market analysis. The tendency is to figure out what can be produced and then to see if the product can be sold, either in the domestic market or by exporting it. More often than not, this approach is doomed to failure. The proliferation of UHT milk plants and juice plants which has resulted in gross excess capacity are cases in point--market analyses were either superficial or non-existent. The fault lies as much with the institutions which financed the plants as with the entrepreneurs. The answer lies in taking a "market-driven" approach by those who do the feasibility studies and by the financial institutions which appraise the feasibility studies. The capability to take this approach effectively needs to be developed. There is no institution in Pakistan which is strong in this area.

E. Corporate Business Operations

Many agribusinesses lack financial viability due as much to poor private-sector business practices, especially in marketing, as to the impact of government regulations and administrative practices and policies. Conversely, in the oligopolistic agribusiness industries analyzed, those companies which employ sound management practices tend to do exceedingly well financially, despite the constraints encountered in the policy and regulatory environment. Exxon Chemical is a prime example of the latter category of companies; several other multi-national companies, some foreign/local joint ventures and some Pakistani agribusiness companies also qualify, but these appear to be in the minority.

Information derived from the case studies and the ACSCA seminars is providing valuable insights about the strengths and limitations of the private sector's present and medium term participation in agribusiness. A few of the insights are:

1. Private-Sector Agribusiness Planning and Investment Perceptions

Established agribusinesses in Pakistan, foreign and/or locally owned, appear to have a sound basis on which to plan the expansion or diversification of their operations. From experience, they understand, often intuitively only, the scope of their markets and the investment opportunities available to them. Decisions to invest are taken slowly and with great caution in response to their perceptions of economic and political risk.

Capitalization of new activities tends to be highly debt oriented, despite complaints about interest rates. In many cases, business risk is avoided by:

a. following the "leadership" of public sector companies in a given industry (e.g., market pricing);

b. avoiding significant market confrontation with competitors by sticking with traditional product lines and geographic markets; and

c. sustained contact with public sector banks, companies and agencies in a political process that effectively secures significant support for companies on a case-by-case basis.

While these insights tend to indicate a "business as usual" status quo mentality--often demonstrated by oligopolistic business practices--there are some interesting though limited perceptions and innovative actions being taken by the established private sector. These include:

a. closely or family held companies making public offerings of shares to raise new equity capital on the one hand, or to increase personal cash liquidity on the other;

b. exploring joint venture opportunities with other companies, often foreign transnational corporations;

c. greater participation in trade associations and public forums both to understand and to play a role in GOP policy formation efforts which target private-sector initiative; and

d. increased awareness of the importance of new technology and employee training to improve the viability, quality and efficiency of production.

While new Pakistani entrants into agribusiness appear to be more risk-oriented, there is little indication in most cases that they understand how to plan and implement effective marketing strategies linked to production and management requirements and capability.

New foreign private sector intervention in agribusiness in Pakistan is promising but very limited. These include investments in improved seed development and marketing, food processing and distribution in domestic and foreign markets, and licensing arrangements in the manufacturing of equipment, spare parts and packaging. Foreign investors are being encouraged by the GOP and the private sector but the promotional efforts of both do not reflect an understanding of foreign investor requirements or how to target specific companies.

2. Economic and Financial Viability of Agribusiness Sectors

Many public and private sector agribusinesses are profitable because of direct and indirect government subsidies, lack of market competition due to monopolistic practices and depressed raw material commodity prices at the farm level. Equity investment in new activities tends to be less than the already highly leveraged development bank ratio of 30 percent. Private sector investors tend to seek a full return of original capital in three years or less.

Established companies tend to remove equity and retained earnings from their businesses and look to debt capital sources to meet their working capital or new fixed capital investment requirements. Debt repayment and collateral security requirements are often not adhered to, while foreclosure by the development banks is viewed to be unlikely.

Credit for most new agribusiness enterprises appears to be difficult to put in place, and relatively few applications are approved.

3. Management and Labor Issues

With a few notable exceptions, middle management and overall labor turnover in both public and private sector agribusinesses is extremely high. This appears to be due to a combination of factors including:

a. limited opportunity for advancement;

b. few, if any, training opportunities;

c. poor working conditions, working hours, work environment, and health and safety environment; and

d. low remuneration, benefits and incentives.

The exceptions to this include some public sector companies where job security is virtually assured, and several of the larger private-sector companies, especially those which are owned by or include foreign investors or foreign trained senior local managers.

There is great scope and need for human resource development and managerial training in Pakistani agribusinesses.

4. Market Competition

Very limited market research and testing takes place in the more open industries. Since most of the agro-industries are in a non-competitive environment, market competition is muted due to:

(a) regulatory practices of the GOP;

(b) public-sector domination of enterprises and operations;

(c) poor infrastructure development and maintenance; and

(d) poor management capabilities.

F. Other Constraints

1. Infrastructure Development and Maintenance

The efficient operation of most agribusinesses requires access to infrastructure such as water, gas, electricity, roads and telecommunications facilities. A problem in almost any country is that in less developed regions infrastructure is expensive to develop and it requires allocating scarce governmental resources. Hard choices have to be made. Not all businesses can be provided all the infrastructure desired. One attempt to optimize the use of infrastructure facilities has been the development of industrial estates. A problem for some agribusinesses is that the estates may not provide a location near the farms with which the businesses interface. To deal with some of the difficult allocation issues, "High Powered Facilities Boards" and "One Window Facilities" have been set up, and managers of utilities are instructed to act expeditiously to provide the necessary facilities for industrial development. Following is a brief on some of the key areas of infrastructure.

Telecommunication Facilities: A representative of Pakistan Telegraph and Telephone (T&T) Department indicates that large industrial concerns are given Priority No. 2, following only hospitals and doctors. Out-of-turn connections are given on payment of Rs. 20,000. To provide telephone connections to a new industry in a rural area, T&T will expect the sponsor to contribute to line costs. A wireless connection with an effective range of 50 Km can be provided at a cost to be borne by the sponsor of Rs. 200,000. T&T has completely deregulated the provision and installation of FAX machines.

Export Transportation: One of the main constraints to exports of many agribusiness products is inadequate transportation infrastructure--by land, sea and air. For sea freight, this includes inadequate (or lack of) facilities at the ports for handling cooled or frozen products and insufficient shipping options for produce destined to the most desirable markets. For air freight, Pakistan International Airlines has had a monopoly on shipments out of the country. This has been a major constraint on shipment of fresh produce, in particular, but also on certain other types of agribusiness products. Participants at ACSCA's Seminar in Lahore reported that PIA reserves more than 90 percent of its cargo space for Karachi-based exports, even though the Punjab is the largest producer of citrus and mangoes, some of which could be exported. The air cargo constraint may be relieved sometime in the future, according to the Government's announcement that a new cargo air service is to be established. However, creating a cargo line will take time. Meanwhile, it would seem to be sensible policy to let potential exporters charter sufficient aircraft from any source, PIA or other, to meet their export needs.

Electricity: The Power Department of Pakistan's Water and Power Development Authority (WAPDA) reports that under the rural electrification scheme, WAPDA is extending power supply to villages within six kilometers of the main grid stations. Small industrial loads can be met from these extensions. Larger loads require extension of lines and transformers, the costs of which must be met by prospective industrial consumers. A new industrial connection within a reasonable distance of surplus capacity grid stations can be given in about four months. However, not all grid stations have surplus capacity. Power demand has been growing at 12 percent per year, which results in load shedding because power supply is lagging. WAPDA is apprehensive that load shedding will persist for several years because decisions on major generation capacity "have been held up."

Gas: Ministry of Petroleum and Natural Resources reports that industries must bear the cost of pipelines from the main distribution centers along the pipeline distribution network. (A 2" line for 5 miles may cost about Rs. 1.2 million.) The gas requirement is about five times greater in the winter season. Continuous supply is assured to industrial consumers only for the remaining 9 months. During winter, they have to make alternate arrangements, generally furnace oil. An assured supply of gas is a particular concern to the fertilizer manufacturing industry.

2. Banking, Credit Policy and Practices and Capital Markets

The financial system consists of the State Bank of Pakistan (the central bank); five large nationalized commercial banks; 17 foreign commercial banks; five industrial development finance institutions (Industrial Development Bank of Pakistan, Regional Development Finance Corporation, Agricultural Development Bank of Pakistan, House Building Finance Corporation, and the Small Business Finance Corporation); three investment companies (Pak-Saudi, Pak-Kuwait, and Pak-Libya); two stock exchanges (Karachi and Lahore); a cooperative bank; a number of leasing firms; two unit trust savings institutions (National Investment Trust and Investment Corporation of Pakistan); a government-owned life insurance company and several non-life insurance companies. The Government essentially owns and controls all financial institutions except for the foreign commercial banks, the non-life insurance companies and some of the leasing companies. The five nationalized commercial banks hold roughly two-thirds of the assets in the financial system.

With World Bank support, Pakistan is introducing reforms in the financial sector between 1989 and 1991 that include deregulation of financial markets (The World Bank News, March 30, 1989). The reform program is to promote growth of the country's financial markets, expansion of private investment and savings, and more efficient provision of services. The program includes measures to improve resource mobilization, allocation of credits and the profitability of Pakistan's banking system. The system will be strengthened through measures to give greater autonomy to nationalized commercial banks and make them more competitive with new private banks. Senior Government officials confirmed to the ACSCA team that a plan is underway to make the public sector commercial banks more autonomous, that measures to improve their profitability are being considered, and that the program to privatize the commercial banks is underway. The experiment will be started with Habib Bank Limited and one other bank, whose shares (which have been totally held by the Government) will be sold to the private sector. (It is not yet clear whether complete control will shift to the private sector or whether the Government will retain the majority shares.) The State Bank of Pakistan will continue to act as watchdog over credit ceilings within the framework of the Annual Credit Plan.

Annex J, written by an ACSCA team member with experience in banking and finance, discusses anticipated changes in international capital markets, interest rates and banking and how these may affect the climate for agribusiness development in Pakistan. The analysis is based on data from secondary sources and from discussions with bankers and investment bankers in the United States and the United Kingdom, with officials of the Asian Development Bank, the World Bank and the IMF, with representatives of various accounting firms and financial institutions in Pakistan, and with representatives of investment banking firms which expect to become operational in Pakistan in the near future. In short, the conclusion is that financing of agribusinesses in Pakistan will have to become more commercially oriented than has been the case. Sponsors will have to have more "at risk," so that if the project fails the sponsor will lose financially rather than the financing institution.

Investment Banks: Investment/merchant banking activities have not yet been fully developed in Pakistan. No financial institution in Pakistan has adequate expertise for corporate financial restructuring or for arranging take-overs, mergers, or the international syndication of the funding requirement of large private sector projects. However, there are some encouraging signs. Six private investment banks have been sanctioned. They will be able to negotiate loans from abroad or from within the country, against term deposits or certificates. Terms and conditions of foreign loans will need the clearance of the State Bank of Pakistan. While the State Bank will not guarantee repayment, the facility of payment of foreign exchange under the GOP policy of risk coverage will be available to private parties. It has also been announced (The Pakistan Times, August 25, 1989) that by December 1990, some foreign private investment banks will be authorized.

Securities Market: The securities market in Pakistan is underdeveloped and does not provide adequate funds for industrial development. The Karachi Stock Exchange started functioning in 1948 and the Lahore Stock Exchange was established in 1970. There were limited inducements for enterprises to be listed on the stock exchanges until mid-1986, when the Government introduced certain measures to strengthen the capital market. The corporate tax for listed companies was reduced from 50 to 40 percent while for unlisted companies it remained at 55 percent (a change was made recently?). Dividend income and capital gains from share transactions of listed companies were made tax exempt in the hands of shareholders, and an investment tax credit is available for purchase of primary shares of listed companies.

Venture Capital: There is no organized venture capital activity in Pakistan. Venture capital companies could help to mobilize both domestic and foreign resources for equity investments in potentially profitable businesses. An Asian Development Bank document for the Small-Scale Industry Project notes that a recent study financed by the ADB concludes that a venture capital company of moderate size would be feasible in Pakistan.

3. Government Role and Practice in Consumer Protection and Quality Control

Government has a legitimate role in protecting consumers against the possibility that goods which they purchase do not meet proper specifications. In agribusi. ess, cases in point would include processed foods and selected farm inputs, especially fertilizer, pesticides and seed.

Annex K includes a discussion of Pakistan's Pure Food Rules. The conclusion is that the rules are inadequate to protect consumers against aflatoxin, microbial maladies, heavy metal and pesticide contaminations, or from adulteration and inferior quality food products. The capability for testing and monitoring for compliance is very weak. One implication for agribusinesses in the food industry is that they tend to be lax about quality. While the businesses may survive in the domestic market, possibly at some harm to consumers, they most certainly cannot compete in international markets unless quality standards are substantially upgraded and adhered to.

Information obtained in the Fruit and Vegetable Processing case study points to two conclusions: (a) the presence or influence of food regulatory agencies in the food industry was not apparent, and (b) confusion exists as to which regulatory agency is responsible for the safety and quality of food products.

Fertilizer and pesticides must be labelled in the local language to indicate the active ingredients, which are not apparent from visual observation. Certified seeds must be labelled to "certify" that they are what they are claimed to be. Government's role is to spot check and test in laboratories sufficient samples of tagged goods to verify that the tags do represent the goods correctly. If adverse deviations are found, the manufacturer or merchant is liable for punishment. Annex L gives background on labeling requirements in the seed, fertilizer and pesticides industries and standards for the food processing industry. The issues being investigated by the ACSCA team are whether the rules are adequate and whether there appear to be abuses: (a) in the way governmental agencies implement the rules, which represent disincentives to agribusinesses, or (b) by agribusinesses in representing their goods to consumers. Evidence coming from the case studies suggests that abuses occur in both instances.

4. Policy Regarding Intellectual Property

Intellectual property is associated with innovation. It includes such intangibles as new or improved products or processes, new designs, or new trade marks. Several legally enforceable rights--patents, design registrations, copyright and trade marks--can be used to prevent others from obtaining the benefit of private creations. Annex I contains a description of the laws which regulate the use of intellectual property in Pakistan.

Agribusinesses are said to be disadvantaged occasionally by the administration of the laws intended to protect their rights, or by competitors having unjustly or unknowingly assumed the rights. Penalties for infringement are often described as too light to discourage the practice. The maximum fine for trade mark infringment is reported to be Rs. 5,000.

IV. SCOPE AND OPPORTUNITY FOR AGRIBUSINESS DEVELOPMENT

At this juncture, the ACSCA team is convinced that scope and opportunity exist for substantial agribusiness development, for both domestic purposes and exports, assuming that the policy environment fosters a supportive (non-business) role for the Government, and that the private sector takes a proactive approach to explore and develop opportunities in a deregulated economic environment. Implicit in the proactive approach is an underlying precept that the most fruitful efforts will be those which are **targeted at well-defined market opportunities** as opposed to trying to "sell what we produce."

Considerable analysis will be needed to identify and verify potentially viable opportunities. Subject to such analyses being done, following are some agribusiness industries and ventures which may be promising in a deregulated, competitive operational and marketing environment.

A. Input Industries

1. **Fertilizer and Farm Chemicals**

2. **Basic Seed (certified and hybrid)**

3. **Farm Machinery and Implements**

B. Output Industries

1. **Edible Oils**

2. **Livestock Feed**

3. **Horticulture**

C. Service Industries

1. Marketing and Market Development

2. Transportation and Storage Services

3. Product Development, Packaging and Quality Control

4. Financial Services and Investment Banking

5. Management and Technical Training and Consulting

V. RECOMMENDATIONS

The global business economy is feverishly competitive. The key to Pakistan's economic viability in such a competitive world is a dynamic, innovative, market-driven private sector. The responsibility for achieving it belongs principally to the private sector itself. But the private sector will be successful only if a mutually cooperative and supportive relationship exists with government at all levels. Such is the context in which recommendations to encourage agribusiness development in Pakistan are proffered.

In formulating recommendations for both the final report and the National Agribusiness Action Plan, the ACSCA team will be cognizant that trade-offs exist in the policy arena. An attempt will be made to put forward recommendations which are consistent with the Nation's goals.

Within that context, following are the outlines of a few of the ideas which the ACSCA team is considering to develop into specific recommendations, each with a series of discrete action steps intended to facilitate implementation.

A. Fromulate and Adopt a National Agribusiness Development Policy

Following are the principles of a suggested national agribusiness development policy:

1. Private-Sector Agribusiness and Agro-Industry will be Given Special Emphasis in Overall Investment Policy

The formulation and over-seeing of the implementation of the Agribusiness Investment Policy should be an additional responsibility of the Federal Ministry of Food, Agriculture and Cooperatives, which should have a special cell for this purpose. This cell should have close formal links with the Ministries of Planning, Finance, Industries and Commerce, as well as the Board of Investment and the Economic Coordination

Committee, for effective implementation of the Agribusiness Investment Policy. A prime objective would be to maintain stability and predictability of policies.

2. The Environment for Private-Sector Agribusiness Investment will be Improved by Deregulating Agribusiness Trade and Commerce

A private sector can operate efficiently only if it works within the environment of a well-functioning market system. If the market environment is highly distorted--in the sense that there are great discrepancies between social and financial costs or benefits due to monopolies, externalities, or government intervention--the private sector is likely to act in an ineffecient way. Deregulating agribusiness trade and commerce is a prerequisite to efficient marketing in agribusiness activities.

3. Formulate and Begin to Implement a True Privatization Program for State-Owned Agribusiness Enterprises and Cease Public-Sector Investment in New Agribusinesses

Expansion of competitive markets and deregulation should go hand-in-hand with the transfer of ownership of state-owned agribusinesses. "Getting the prices right" will not be optimally efficient as long as much of the productive capacity in agribusiness is owned and run by the government.

Privatization of state-owned enterprises may take any of several forms. Among the most common forms used by other countries are:

- Divestiture, or selling the shares (at least a majority interest) to private investors;

- Liquidation, or selling the assets of the company and terminating the operation; this is the appropriate response in cases in which there is no economic or financial merit in continuing the business; or

- Other forms of Privatization, which may include leasing, management contracts, or concessions to private entrepreneurs.

To eliminate the economic inefficiencies of monopolies and ologopolies, and to capitalize on the economic efficiencies of private-sector competition, selected state-owned agribusinesses should be privatized (i.e., divested, liquidated or otherwise privatized).

Steps to be taken to implement an agribusiness privatization program include:

- Develop a Privatization Strategy

  --Define the objectives of the privatization program;
  --Foster transparency (openess) of the program;
  --Start first with smaller enterprises, so as to minimize the potential damage of mistakes;
  --Select initially about three agribusiness companies which appear to be good candidates for success;
  --Look for early, visible success; the "demonstration effect" is crucial; and
  --Build on the experience.

- Assign the Responsibility

  Appoint an individual, or organization, whose full responsibility will be to implement the program.

- Enact Authorizing Legislation

  Inter alia, the authorizing legislation should define the complex processes for: (a) valuation of enterprises; (b) public auctions; and (c) direct negotiation.

- Foster Public Awareness

  Plan and implement a public awareness campaign, including a major conference, on "Why Privatize."

- Prepare an Action Plan

  Formulate a detailed, time-phased action plan to begin to transfer selected holdings of (X holding company) to the private sector, or to dispose of the assets, or to carry out another mode of privatization.

- Build on the Initial Experience

B. Changes in Other Rules, Regulations & Policies

1. Need for an advocate of private-sector agribusiness in the cabinet.

-- Parastatal companies have an advocate in the Minister for Production;

-- The Minister of Industries should assume the role of advocate for private sector agribusiness, and should be routinely briefed by private-sector businessmen about policy and regulatory constraints so that these can be considered in the policy-making process.

2. **Need for investment sanctioning and post-sanctioning procedures which are streamlined, made positive and implemented congenially.**

3. **Need for intensive PROMOTION of agribusiness, to attract both local and foreign capital investment:**

   -- Techniques and incentives used by other countries can serve as models;

   -- This will require a sustained commitment of adequate resources, both time and money.

To learn what some other countries are doing to promote business development, the ACSCA team contacted all 50 state governments in the U.S., the U.K. county governments of Scotland and Wales, and the governments of Bahrain, India, Indonesia, Ireland, Malaysia, Nepal, Philippines, South Korea, Taiwan, Thailand and Turkey. The promotional materials, incentives and proactive development efforts of many of these governments are quite impressive and will be useful to the ACSCA team in helping to formulate specific suggestions to the Government of Pakistan on how to strengthen its investment promotional efforts in agribusiness. Following is a set of basic principles which seem to be common among the promotional programs of nearly all of those agencies:

a. A strong national economy is important to all facets of life, and all sectors--agriculture, education, health, religion, and social services--benefit from a strong economy.

b. A strong, market-driven private sector is fundamental in creating a strong economy.

c. A realistic vision of the nation's economic future and a conducive environment are prerequisites; to achieve this requires the judgment and involvement of responsible leaders to outline the economic strategy, to identify primary governmental actions, to give cohesion to the actions, and to avoid actions which may be harmful to the economy.

d. A governmental development agency (names among the governments solicited vary but include such titles as Development Authority, Industrial Development Authority, or Business Investment Bureau) which is responsible to a top governmental official, but takes counsel from both political and business spheres, must accept the responsibility to:

- o target and promote the development of specific businesses in the country;
- o assist ventures to obtain the necessary governmental approvals, to obtain financing and to help solve start-up problems; and
- o monitor the progress of the ventures and assist them as needed.

e. Adequate funds--ideally from govenment and business--must be provided to the agency for an extended period.

f. The agency must be staffed with high-calibre personnel who can effectively "market" the country and who can deal with business and political leaders as well as governmental officials.

g. Objectives of the agency must be quite specific, and the programs to achieve the objectives must be monitored and periodically evaluated to assure accountability and as a basis for making adjustments in programs.

h. The agency must be provided the tools to accomplish the objectives, and the means to coordinate with other public and private sector entities involved in economic development.

C. Recommended Institutional Support for Agribusiness Development

1. An Agribusiness Promotional Agency

A legitimate role exists for a governmental agency with a mandate and the resources to promote agribusiness investment. This entity could be an autonomous unit whose head would report directly to a Cabinet Minister, or the General Secretary or Chairman of the Board of Investment, who would be the spokesman for the agency in the policymaking arena. Alternatively, it might be a Division of the restructured Investment Promotion Bureau (although the latter would only be useful if the restructured IPB were truely given a charge, the right type of personnel and the resources to promote investment effectively.) The agribusiness promotional agency should be headed by a business-oriented Director. The functions of the agency would include:

a. Create a favorable environment for agribusiness investment.

b. Target and promote the development of specific agribusinesses in Pakistan.

c. Assist such ventures to obtain the necessary governmental approvals, to solve start-up problems and to obtain financing.

d. Assist and monitor the implementation and development of such ventures.

e. Coordinate with other public and private sector entities which foster agribusiness development and related policy and capital formation to sustain agribusiness development.

2. A Private Agribusiness Investment and Advisory Company

The functions of a private agribusiness investment advisory company would include:

a. Identify potential investment opportunities in agribusiness in Pakistan.

b. Do pre-feasibility studies on the most promising.

c. Identify potential investors, either local or foreign, or both.

d. Do full-fledged feasibility studies and business plans for those potential enterprises in which investors are seriously interested.

e. Assuming that the enterprise looks promising, assist clients to identify sources of financing and, if necessary, help with negotiations. Besides local DFI's, banks and (eventually) investment banks, sources may include OPIC, USAID's commodity import program (CIP), suppliers' credits, etc.

f. Invest directly in selected agribusiness enterprises (drawing on experience of aid-assisted private development banks and foundations in Jamaica and other countries).

g. Assist with sanctioning and post-sanctioning procedures.

h. Monitor progress of the enterprise and help to solve implementation problems.

i. Assist with "turn-arounds," mergers and improved management of existing agribusinesses.

3. An Agribusiness Marketing and Technology Center

Critical elements in private-sector agribusiness development are marketing and technological change. The temptation has been to get public agencies to take direct responsibility for the development and intermediation of technology, to the exclusion of other options.

4. Agribusiness Industrial and Managerial Training

(This concept will be developed over the next few months.)