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Palmed Off: Incentive Problems with Joint-Venture Schemes for Oil Palm Development on Customary Land

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Summary. — The oil palm boom has prompted governments and plantation companies to find ways to incorporate customary landholders in large-scale plantation developments. This paper examines the joint-venture model that has been widely promoted in Sarawak, Malaysia. Principal–agent theory is used to analyze the structural relations between the actors in joint-venture projects—the landholders, the government agency that acts as their trustee, and the private investor. The analysis shows that unequal access to information and influence has compromised the stated objectives of the joint-venture schemes, leaving customary landholders vulnerable to significant exploitation and losses. Thus there has been a systematic failure to achieve the anticipated developmental outcomes.
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Key words — customary tenure, joint ventures, oil palm, principal–agent problem, Malaysia, Southeast Asia

Palm off. Impose or thrust fraudulently on a person. Cause a person to accept unwillingly or unknowingly. [1]

1. INTRODUCTION

Among the tenets associated with the ascendancy of market liberalism in development policy in the 1980s was the belief that greater private sector involvement in rural development would reduce the waste and inefficiency associated with government-managed schemes, while injecting the capital and expertise needed to greatly accelerate the developmental process (Ellis & Biggs, 2001; Staatz & Eicher, 1998). This was a particular example of the general presumption in market liberalism of the greater efficiency of the private sector, criticized by Quiggin (2011) as one of a series of 'zombie hypotheses' that are seemingly immune to contrary evidence.

It is true that many of the integrated agricultural development projects of the 1970s were overly ambitious and expensive while having limited impact (Binswanger, 1998), and that the proliferation of new parastatal agencies charged with 'bringing development to the people' was as much about creating 'jobs for the boys', outside the strictures of the line departments inherited from the colonial era, as it was about lifting rural communities out of poverty. Nevertheless, the new faith in the potential of the private sector to help achieve development goals more efficiently gave rise to a wave of policy reforms including corporatization and privatization of state development agencies, outsourcing of development services, public–private partnerships to deliver development infrastructure, and other policies that favored the growth of the private sector.

In particular, land development schemes designed to help smallholders establish profitable tree crops such as rubber, coffee, cocoa, and oil palm, because of the obvious commonality with private-sector commercial plantation development, became a ready target for corporatization, privatization, and public–private partnerships of various forms (Cramb, 1992; King, 1986). For example, the rubber and oil palm schemes established by the Federal Land Development Authority (FELDA) in Peninsular Malaysia in the 1960s and 1970s are now operated by FELDA Holdings Berhad, a publicly listed company with a capital value of over MYR 5 billion. [2] In Indonesia, much of the oil palm expansion in the era of market liberalism has been undertaken in nucleus estate and smallholder (NES) schemes in which private or state-owned plantation companies gain access to land for the nucleus estate in return for providing services to surrounding smallholders (Barlow, Zen, & Gondowarsito, 2003; McCarthy & Cramb, 2009; Zen, Barlow, & Gondowarsito, 2005).

A perceived obstacle to private-sector involvement in tree-crop development has been that the property rights over of the suitable land are held by traditional entities such as kin groups or villages (Curry & Koczberski, 2009; Deininger, 2003). Such land is variously referred to as customary, traditional, or communal, the central feature being that it is subject to some form of community-based tenure (Cramb & Wills, 1990). It will be referred to here as customary land. Governments in many countries have experimented with a variety of institutional arrangements to combine the land, labor, capital, and management required for profitable tree-crop development on customary land (Baird, 2009; Barlow, 1986; Casson, 2000; Deininger, 2003; Hall, Hirsch, & Li, 2011; SPF, 2008; Wright, 2009; Zen *et al.*, 2005; Zola, 2009). The nucleus estate and smallholder schemes mentioned above constitute one important and long-standing example (McCarthy & Cramb, 2009; Zen *et al.*, 2005). McCarthy (2010) and McCarthy, Gillespie, and Zen (2012) have identified newer arrangements in Indonesia whereby customary landholders surrender an area of land to a plantation company and receive up to 80%

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of the land fully established with oil palm in return, though in practice the proportion returned is often considerably less. In Laos, Chinese investment in smallholder rubber planting in the northern provinces involves the so-called 2 + 3 contracts in which the customary landholder provides the land and labor while the investor provides the capital, technical expertise, and market. The two parties to the contract share the net revenue in proportion to their contribution once the rubber holdings are in production. However, in many cases, the absence of a cash flow in the years before rubber tapping commences has induced landholders to revert to a 1 + 4 contract, where the investor pays wages to the landholder and takes a larger share of the profits (Manivong & Cramb, 2008; Shi, 2008).

The variety of arrangements that have been officially promoted or that have emerged 'spontaneously' highlights the need for detailed empirical examination of individual cases to build up an understanding of the circumstances resulting in outcomes favorable to customary landholders through to those that constitute nothing more than a 'land grab', whether by domestic or international actors (Borras, Hall, Scoones, White, & Wolford, 2011; Deininger, 2011; Deininger & Byerlee, 2011; Hall *et al.*, 2011; McCarthy, Vel, & Afiff, 2012). In this paper I examine the joint-venture (JV) approach to oil palm development on customary land in Sarawak, Malaysia—a model that has been vigorously pursued since the mid-1990s and which is now ripe for reassessment. The research reported here is part of a larger project examining the nature of the 'oil palm complex' in Malaysia and Indonesia and its interaction with rural livelihoods and processes of agrarian change (Cramb & Curry, 2012; McCarthy & Cramb, 2009).

The oil palm (*Elaeis guineensis*), indigenous to West Africa, was introduced to Malaysia in 1875 and first planted commercially in 1917 (Cramb & Curry, 2012). The palm grows well in equatorial conditions and is the highest yielding of the oil-producing crops. The crop begins to bear fruit in the third year and has a productive lifespan of 25–30 years. Though production can be undertaken at various scales, there are economies of scale and a need for timeliness in the processing of harvested fruit into crude palm oil, hence an incentive to establish a substantial planted area within the vicinity of each palm oil mill with good road infrastructure throughout. Large-scale commercial planting of oil palm began in Peninsular Malaysia in the 1960s, both by private plantation companies and the Federal Land Development Authority (FELDA). With the surge in demand for vegetable oil in recent decades, driven primarily by population and economic growth in the large economies of South and East Asia, as well as the more recent growth in demand for biofuels, global palm oil production has increased from five million tons in 1980 to 44 million tons in 2010, an annual growth rate of 7%.[3] Forty-two percent of the world's palm oil is produced in Malaysia, including the Peninsula and the Borneo states (Sabah and Sarawak), derived from smallholdings, estates, and a variety of state-managed and state-brokered intermediate arrangements such as JV schemes.

It is my contention in this paper that unequal access to information and influence has compromised the stated objectives of the JV oil palm schemes in Sarawak, leaving customary landholders vulnerable to significant exploitation and losses. That is, there is a fundamental structural problem in the JV approach arising from the well-known principal–agent problem that pervades economic life. I draw on the concepts of principal–agent theory to analyze the structural relations between the actors or partners in the JV schemes in order to explain what appears to be a systematic failure to achieve the anticipated and much-vaunted developmental outcomes. Elsewhere I have drawn on the theory of patron–client relations to explain the underlying motivation for the persistent push for large-scale private development of customary land in Sarawak, despite landholder concerns and the steady accumulation of evidence that these concerns have been largely justified (Cramb, 2007, 2011). But that analysis does not fully explain the *mechanics* of the problems that have unfolded once the policy was decided and the schemes were rolled out. Augmenting the patron–client perspective with principal–agent analysis gives a more complete appreciation of the experience with JV schemes over the past 15 years, hence a better prospect of drawing some general conclusions about the JV approach that can be applied in other contexts.

The research in Sarawak was conducted independently but with support from the Ministry of Land Development. Fieldwork was conducted during six visits to Sarawak between November 2007 and June 2011. I used semi-structured interviews with key informants in government ministries, departments, and agencies, as well as farmers, private consultants, plantation managers, and lawyers. I relied initially on personal contacts from an earlier period of employment in Sarawak and used a snowball technique to locate additional informants. Due to the politically sensitive nature of the topic, in most cases I have concealed the identity of the informants when citing them in this paper and have only identified their status and role. I also made use of secondary materials such as feasibility studies, impact statements, financial reports, policy papers, company profiles, and official statistics. I visited several oil palm schemes and plantations, including the Kanowit Oil Palm Project, the earliest and largest of the JV schemes, that is analyzed here as a case study. Wherever possible, I cross-checked the evidence I obtained by using two or more sources and/or types of data. The resultant narrative is thus empirically grounded, even if not every assertion that follows can be explicitly linked to a single item of evidence.

The paper is organized as follows. The next section provides an overview of the JV approach as it has been implemented in Sarawak, then Section 3 analyses the approach within a principal–agent framework. This analysis shows that there are complex layers of principal–agent relations in a large JV scheme but that the central issue is the role of the plantation developer or investor acting as agent for the customary landholders; this role is examined in Section 4. The principal–agent framework is applied to a case study of the Kanowit Oil Palm Project in Section 5. The analysis is broadened in Section 6 to consider comparisons between the Kanowit project and other JV schemes in Sarawak and some of the compromises that have been proposed or recently introduced. In Section 7 some general conclusions are drawn.

2. THE JOINT-VENTURE APPROACH IN SARAWAK

The Malaysian state of Sarawak on the north-western coast of Borneo provides an excellent case study of private sector involvement in the large-scale development of customary land (Leigh, 2001; Figure 1). Around 20–25% of the total land area and 60–70% of agricultural land is claimed as Native Customary Land, derived from traditional modes of occupancy and land use, notably shifting or forest-fallow cultivation. Indigenous groups known collectively as Dayaks (such as the Iban, Bidayuh, and others), most of whom still live in communities of 20–30 households that reside in a 'longhouse' and occupy extensive territories of farmland and forest, are the principal claimants of this Native Customary Land (Cramb, 2007).[4]

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