

Vulnerability of Agriculture to the Global Financial Crisis

Executive Summary

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Philippine agriculture is a vital cog of the Philippine economy. It comprises about 20% of the gross domestic product (GDP), some 37% of the labor force, and less than 10% of merchandise exports. The whole agri-food chain (agribusiness context) accounts for nearly half of GDP. This includes supply of industrial farm inputs and services, agri-food processing, packaging, logistics and financing.

Is Philippine agriculture¹, or the broader scope of agribusiness, vulnerable to the ongoing global financial crisis? Is its vulnerability a result of shrinking global demand and the resulting fall in commodity prices? Or is it the lack of competitiveness and preparedness to the global business cycle? This paper hopes to answer these questions.

There are about 10 million (M) hectares (ha) of farmland in the country scattered in 5 M farms, averaging only 2 ha. Some 12 M farm workers and fishers work in these farms and seas, plus another 4 M in non-farm enterprises.

Despite the notable growth, however, some experts have questioned why rural poverty still hovers at 50% in contrast to other countries like China, Indonesia and Vietnam which recorded significant falls in poverty incidence. Habito (2009) found that the growth of manufacturing jobs is one of the factors. This author opines that another factor is the country's poor performance in agri-food exports.

Five key industries are discussed in the paper. Proposals will be made in the short-term and medium-term to address key concerns. The five industries host nearly three quarters of the farmers and farmlands.

I. Impact of the Crisis on the Sector (highlighting the vulnerabilities)

Is Philippine agriculture vulnerable? In part, it is. Commodity export is always buffeted by global price cycles. The fall in world commodity prices from their peak in 2008 has dual effects: reduce output prices for exportables, and shrink input prices. Lower fertilizer and fuel prices in 2009 will have positive effects on farm bottom lines. In the policy front, a peso depreciation will have positive effects on exportables like coconut and banana. Currency depreciation has also the twin effect of added protection to local products as imports become more costly.

But the real story behind the *headlines* is that the *sector's coping mechanisms* are fragile because the country has long under invested in the sector's competitiveness. This has long weakened its defenses from external threats. The best defense is offense. And adequate investments of well-crafted strategies generate higher productivity and competitive advantage.

¹ Agriculture as defined in this paper includes fishery.

The ASEAN Free Trade Area (AFTA) 2010 is an example of an external threat looming for several years in the horizon. It will impact on corn, sugar, as well as feeds, chicken and pork. The entry of feeds and meat will ultimately reduce demand for corn. The industries were given a long lead time, but defenses have not been installed.

Given the differences in vulnerabilities of the five products, the most impacted region will be the coconut areas of Mindanao, Bicol, Eastern and Central Visayas, and Southern Tagalog (mainly Quezon). In 2010, corn (Cagayan Valley and Mindanao) and sugar (Western and Central Visayas and Mindanao) will be highly vulnerable.

Vulnerability Summary

Product/Area	Region(s)/areas	Vulnerability
Coconut (3.3 M ha)	Mindanao, Bicol, East Visayas, Central Visayas, S. Tagalog.	High
Sugarcane (~400,000 ha)	West Visayas, Central Visayas Mindanao *	Low High (with AFTA 2010)**
Corn (1.35 M ha)	Cagayan Valley, Mindanao Pangasinan	Low High (with AFTA 2010)**
Rice (2.47 M ha)	Cagayan Valley, Central Luzon, Western Visayas, Mindanao, Other regions	Low
Cavendish banana (50,000 ha)	Mindanao (S, C, N)	Low

* also Cagayan Valley, Central Luzon

** AFTA 2010 has been agreed by the ASEAN members for over five years.

II. Proposed Immediate/Actionable Measures (1 to 2 years)

For agriculture as a whole, emphasis should be given on the following:

- The budget for 2010 should reflect sound resource allocation in order to have a broad-based impact on farm incomes and poverty reduction.
- The increment should be proportionately more for the under-budgeted sectors in the past such as corn, coconut and other tree crops, fishery and livestock.
- A concerted effort should be made to craft an AFTA 2010 preparedness program.

Rice. Low fertilizer usage, limited use of good seeds and the poor state of irrigation maintenance are among the causes of low productivity. The dominance of unorganized small farmers also makes formal farm credit intractable. Extension services have also suffered since the advent of the Local Government Code in 1991.

The national government (NG) and local government units (LGUs) must rally behind the imperative that the mayors and governors are the agriculture champions in their respective localities. Cluster farmers are convergence points for interventions in: (a) irrigation systems restoration; (b) certified and hybrid seeds use; (c) extension services; and (d) soil analysis and organic fertilizer development.

Meanwhile, the private sector, under a favorable business climate, can expand hybrid seed supply, and modernize their rice mills.

Corn. High post harvest losses, the poor farm-to-market roads, and upland soil degradation are among the challenges. Yields have fallen in many places despite similar levels of fertilizer inputs. Extension services have suffered as a result of the 1991 Local Government Code.

Under the AFTA, tariffs of the remaining tariff lines, except rice, will fall to zero to 5% in 2010. These include corn, feeds, chicken, and pork. Sadly, stakeholders' preparation to this strategic milestone falls short.

The tasks for the NG and LGUs are to: (a) construct rehabilitate and maintain farm-to-market roads; (b) build village level post harvest facilities; (c) promote *bacteria-primed* fertilization; and (d) prepare for AFTA 2010. By 2010, tariffs for corn, feeds, chicken and pork will fall to 5% from 30% to 40% today.

The private sector needs to: (a) expand hybrid seed supply; (b) invest in large PHF (for corn cobs); and (c) prepare for AFTA 2010.

Coconut. Low farm productivity and limited intercropping are the main causes of high poverty in coconut areas. The plantings of poor clones, the large area of senile trees due to limited replanting, and inadequate fertilization cause low yield.

The NG through the Philippine Coconut Authority (PCA) and LGUs must: (a) consider fertilization of strategic areas. There are reports that yield can increase by 50% in 24-36 months; and (b) there is need for urgent replanting with good clones some 30% of the area which are senile. Quick access to the levy money can help fund these projects, but this may be *hoping against hope*. Meanwhile, depreciating the peso will mitigate the collapse of farm incomes in the coconut areas.

The private sector should consider seed nuts multiplication as a potential project.

Sugarcane. Making the industry globally competitive involves solutions to high input costs, cane yield (tonnage and sugar content), logistics to mill, and mill efficiency. The advent of the agrarian reform program has severely curtailed land transactions that could have given land to the more efficient managers. Thus, economies of scale in plowing, irrigation and harvesting have been constrained. The Renewable Energy Act of 2008 will have positive impact on sugar mill rehabilitation.

The NG together with LGUs can consider the following: (a) improving key farm-mill roads; and (b) expanding irrigation access to sugar lands. The government financial institutions can promote contract plowing services.

The private sector needs to: (a) sustain research and development (R&D) by the Philsurin in cooperation with the Sugar Regulatory Administration; (b) improve mechanization rate; and (c) hone extension services through the mill district development council.

Banana is a globally competitive industry. The Government can provide the enabling environment by: (a) improving road networks to plantations and potential areas; (b)

restoring peace in Mindanao; and (c) marketing and farm rehabilitation support to independent small growers.

The role of the private sector: there is need to replicate the financing scheme of OneNetworkBank, Tagum Rural Bank and PenBank to individual small farmers with BPPA contracts² with big buyers. The Bangko Sentral ng Pilipinas and Land Bank's 5-7 year rediscounting plus technical assistance to bank's production technicians could be the key components.

III. Summary of Competitiveness Issues (vulnerabilities even prior to the crisis)

Low productivity and limited diversification are the general thread of Philippine agriculture. As a result, there is widespread rural poverty. The country is also not export competitive. *First*, Philippine agri-food export intensity is poor. In 2007, the Philippines had only 6.7% of its total merchandise exports coming from agri-food compared to 20% for the top 15 exporting countries, including its ASEAN neighbors. Most of its peers posted large surpluses while the Philippines had deficits. *Second*, relative to its ASEAN peers, the Philippine *export-to-farm land ratio* was only \$300 per ha in 2007 compared to \$2,710 for Malaysia, \$1,500 for Vietnam, and \$1,420 for Thailand. *Third*, in seafood export intensity, it only exported \$11 per kilometer of coastline as compared to \$1,918 for Thailand, and \$890 for Vietnam. *Lastly*, Philippine exports with high Revealed Comparative Advantage³ totaled only \$2.5 B in 2006. The Philippine export effort is only a third of Vietnam's, and one-seventh of Thailand's.

Moving forward, the following competitiveness concerns should be addressed in the medium term. It can be started with the 2010 budget that will provide funding for industries which suffered discrimination in the past due to singular focus on rice self-sufficiency. There must be shift to ensuring income security and reducing poverty as a quantum leap from the past. First, implement the Agriculture and Fisheries Modernization Act (AFMA) by program elements, and with regional strategic perspective. Second, revisit the budget line by commodity (GMA⁴ rice, corn, high value crops, livestock, fisheries). At present, it lacks flexibility, and is biased against R&D and marketing support. Third, sound resource allocation criteria are imperative. About 70-80% of DA resources are allocated for rice. There is also more for production support, and less for R&D and marketing. Also, there are fewer resources for poverty-stricken sectors like coconut and fisheries.

IV. Proposed Medium-Term Measures (beyond 3 years)

Overall, there is need to sustain efforts geared towards sound budget and resource allocation to enhance farm incomes and reduce poverty. More budget should be allocated to sectors which have not received adequate support in the past.

Rice. There is need for the DA to address the following: (a) implementing a *rice master plan*; (b) R&D program into varieties with low water requirements; (c)

² For example banana production and purchase agreement (BPPA) is a long-term deal of 10 to 15 years to producers with fixed US\$ buying price.

³ An RCA greater than one means the product has comparative advantage. This is also called the Balassa Index.

⁴ Ginintuang Masaganang Ani Program - the banner program for agriculture

independent review of the social cost of rice self-sufficiency; (d) refining targeted rice subsidy; and (e) resource allocation based cost-benefits and regional strategy.

The Management Association of the Philippines (MAP) calls for the following: (a) drastic curtailment of the role of the National Food Authority; (b) promotion of non-rice sources of carbohydrates; and (c) encourage formation of rice growers associations to have a private sector lobby.

Corn. There is need to focus on corn value/supply chain improvements to make the industry an export player. In this regard, a critical mass of infrastructure in production zones is imperative from roads to postharvest facilities to bulk handling facilities (*end to end*) from Mindanao to Luzon and the Visayas.

In addition, the MAP recommendations must be considered. These include: (a) accelerating adoption of Bt corn; (b) enhancement of credit access to support investments on post-harvest facilities; and (c) establishing a corn growers' association (like the Sugar Alliance).

Coconut. It is time to craft a *strategic plan*. It will cover: (a) fertilization of 2 M ha; (b) replanting 1 M ha with good clones; (c) market-led intercropping of 1 M ha; (d) diversification of by-products; and (e) R&D for high value products. Coconut research must be separated from PCA following the Philippine Rice Research Institute model.

Further, there is need to (a) unlock the coconut levy; and (b) promote new products (like coconut flour and coconut sugar) as recommended by the MAP.

Sugar. It will entail supply chain improvements for a competitive export industry. This will include: (a) land consolidation to attain scale economies for farm mechanization; (b) freer land market (revisiting agrarian reform provisions on land eligibility and transferability)⁵; and (c) modernize the mills for power co-generation.

Banana. The road map is for Government to provide the infrastructure and business climate favorable for investments in Mindanao. Unilateral changes in policy (e.g. ban on aerial spraying) are not a positive signal of stable policy.

Altogether, it is highly imperative to craft regional agriculture strategies that capitalize on each region's competitive advantage. For example, there is need to pursue the food basket strategy in typhoon-free Mindanao. The strategies must also capture the vitality of marketing support and R&D, and not predominantly production support as has been the common practice.

The success of these strategies will be contingent on the absorptive capacity which, in many respect, is anchored on sustained human resource development at the national, regional and local levels.

⁵ A free land market will allow efficient managers to expand their holdings, and for the poor ones to move out of sugar farming.