THE ROLE OF THE STATE IN THE PHILIPPINE RICE TRADE

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Most state-owned food agencies that we have studied thus far share price stabilization and ensuring food security as common objectives. Implicit in these objectives, though, is the principal focus on the rice consumer. The rice producer/farmer, on the other hand, appears to be given a secondary focus. In fact, there are instances wherein price stability and food security are achieved at the cost of deteriorating incomes of small rice farmers. This happens when massive importation is done to curb supply shortfalls, trimming whatever profit margins the rice farmer could have had had the domestic price been allowed to rise due to production shortfall.

The past years' operation of the National Food Authority (NFA) tend to show that rice farming is really a losing proposition. And the other countries' experiences tend to reinforce this. But there are a few exceptions like Malaysia's BERNAS which has taken an active role in ensuring rice that farmers' income remains stable, remaining food-secure while not necessarily food self-sufficient.

This paper is divided into four main parts. First, some basic discussion on the Philippine rice industry is presented. Second, we delve into the principal mode of government intervention in the industry which is through the NFA—presenting some findings and observations on how other countries with a similar food corporation have done it, and a review of proposals both from the legislature and private research institutions and our own observations. Third, the debate on the tariffs as against quantitative restrictions on rice is revisited, with the extension of Annex 5 of the AoA at the backdrop. Finally, the paper attempts to find some common ground on which NGOs and POs working on the rice issue can work together towards ensuring food security, raising productivity and incomes for the small rice farmers.

THE BASICS

Since the 1980s, the country's rice production has grown at an annual rate of 2.41 percent. On the other hand, rice use has grown annually at 3.4 percent or one percentage point higher.

This underproduction has naturally led to increasing imports and a decline in our level of rice self-sufficiency. From a 95.4 percent rice sufficiency level in 1995, it fell to 89 percent in 1998.

Except for Metro Manila, all regions produce palay but only 5 out of 15 regions are self-sufficient in rice. These are Ilocos Region (Region 1), Cagayan Valley (Region 2), Central Luzon (Region 3), Western Visayas (Region 6) and Central Mindanao (Region 12).

Despite this, the country has the potential to be self-sufficient in rice and once more be a net rice exporter similar to what happened between 1978 and 1983. In 1995 our productivity was at 2.8 MT per hectare. This went up to about 3.1 metric tons in 2000, and 3.43 MT by 2003 but, except for Cambodia and Thailand, this level is still way below the 2000 productivity of other countries and that of the average world productivity. It is also quite disheartening to note that almost two decades ago, China had already been producing at 5.25 MT per hectare.

Table 1. Comparative Rice Productivity, Selected Countries

	Paddy Yield (MT/hectare)				% Change		
	2003	2000	1995	1990	1985	1985-1995	1995-2000
Cambodia	2.15	2.12	1.79	1.35	1.25	8.0	20.1
Indonesia	4.54	4.40	4.35	4.30	3.94	9.1	4.4
Philippines	3.43	3.07	2.80	2.98	2.59	15.1	22.5
Thailand	2.46	2.61	2.42	1.96	2.06	-4.9	1.7
Vietnam	4.63	4.24	3.69	3.18	2.78	14.4	25.5
China	6.07	6.26	6.02	5.72	5.25	9.0	0.8
World	3.84	3.89	3.66	3.53	3.25	8.6	4.9

Source: Food and Agriculture Organization (FAO)

If we can increase our productivity to 3.5 MT per hectare and assume that the 3.8 million hectares devoted to palay production remains, then potential palay output wouldl be 13.3 million MT per year. A 65-percent milling recovery rate from palay to rice is equivalent to 8.64 million MT of rice per year. At an average rice consumption of 100 kg per person per year, this output can support 86.4 Filipinos. At a population growth rate of 2.1 percent annually, that level of production can adequately feed Filipinos up to 2005. Beyond that, though, greater productivity through expansion of irrigated areas, adequate inputs, access to post-harvest facilities among others, must be seen as we cannot expect land devoted to rice to further expand.

Filipinos spend an average of 17 percent of their budget on cereals. This proportion goes up to 25 percent for poor families.

Other Countries' NFA:
A look at Vietnam, Indonesia and Malaysia

VINAFOOD I & VINAFOOD II of Vietnam and BULOG of Indonesia approximate the role of the National Food Authority. Approximate but not necessarily replicate since the local conditions in these countries are quite different from that of the Philippines.

While Vietnam's state-owned enterprises still engage in some local trading, they are mostly concentrated in the export market. However, due to weak export prices, their capacity to stabilize domestic prices has been greatly compromised. Weak export prices cannot cover the costs of state-owned enterprises (SOEs) for buying rice at government's designated floor price. Private traders, especially women, have been more active in the local wholesale and retail rice business.

The decision as to the kind of domestic support extended to rice farmers by Vietnam's SOEs has been devolved to the local and provincial level. And this is not limited to price support but production inputs support as well.

Indonesia's BULOG, the other hand, initially actively intervened in the rice market for price stabilization and ensured that farm-gate prices would not go below that of the farmers' production cost. At the IMF's instance, though, the BULOG has started to move towards minimal government intervention in the rice market. What has principally remained are the targeted rice subsidy scheme (for consumers), stock management, distribution and price control. It will now be allowed to earn profits by managing the rice buffer stock and trade agricultural commodities other than rice. It will venture into corn, sugar and soybeans trade as well for profit.

Malaysia's BERNAS has an import monopoly, and controls prices at the farm gate and at the border. It has extensive control over processing and marketing channels through the issuance of licenses to millers, wholesalers, retailers, importers and exporters. While "privatized" in 1998, it remains essentially government-controlled because its leading shareholder, Budaya Generasi, is a government-controlled company. Malaysia has deliberately targeted a rice-self sufficiency level of 65% but is able to achieve food security through imports. The price of rice has remained constant over the past ten years regardless of supply and demand. This is attributed, apart from its original objective of price stability, to political reasons, with the Malay and Bumiputra class dominating small paddy producers. The level of subsidy remains high at 58% of total farm income and price support increasing output by 65.8%.

One area of intervention in Malaysia worth emulating is the linking of the sale of stocks with import quotas on rice importers. As a condition to obtain an import license, the purchase of rice from the stockpile, proportionate to the amount to be imported, is imposed. The stockpile is priced above the wholesale price. The loss of the importer is recovered from the profits made on imported rice. This seems to be a clever way of managing and financing the stockpiling operations of the BERNAS, as it is equivalent to a tariff on imported rice, the cost of which is borne by rice consumers.

THE NATIONAL FOOD AUTHORITY

The NFA has two mandated functions. One, it must ensure food security in staple cereals in times of calamity or emergency; and two, it is tasked to ensure stable supply and prices of staple cereals both at the farm gate and consumer levels, influencing prices at the farm gate such that farmers profit from their farm operations and similarly influencing prices at the retail level to ensure affordability to the consumers.

To do the above, the NFA engages in the following[1]:

1. **Buffer stocking.** It maintains at any time a minimum volume of stocks for distribution during emergency and/or relief operations. During normal times, the rice stock (household, commercial, government) must have a 120-day consumption requirement at the beginning of the year (January 1) and 90-day consumption requirement at the middle of the year (1 July). Any shortage in the total stocks held is used as basis for importation.
2. **Emergency/Relief Operations.** NFA provides rice supply to relief agencies such as the Department of Social Welfare and Development

1. "Reforming the NFA," Mitch Gustillo, Policy Brief, Congressional Planning and Budget Office, July 1999.

(DSWD) and the National Disaster Coordinating Council (NDCC). It may also release rice to local government units (LGUs) and other sectors participating in relief operations.

3. **Stabilization of farm gate prices.** Due to the seasonality of rice production and the concomitant price instability because of this seasonality, the NFA does most of its domestic procurement during the peak harvest months (October to December), when farm gate prices reach their lowest levels. Farmers who opt to sell their output to the NFA are paid a support price which guarantees a 30–35 percent return on investment to the farmers.
4. **Stabilization of Consumer Prices.** NFA's role is to ensure that the price of rice is affordable to the consumers. The volume and price of rice injected by the Authority into the market, whether sourced domestically or imported, are intended to forestall any attempt by the private sector to sell rice at unreasonable prices. A release price of NFA rice is considered a bench mark within which consumer prices are derived. It is calibrated such that it will not settle to a level so low, prompting traders to buy at lower prices to the detriment of the farmers, nor so high as to make it unaffordable to ordinary consumers.

The Issues

Many studies on the NFA and the stakeholders in the rice industry have already been done. While there are several points of agreement on the NFA's problems, there are instances where divergence on observations and analyses arise.

NFA's Urban Bias

A common observation among the many studies encountered is that NFA has stabilized rice prices for the consumer but has not influenced farm gate prices. In short, it has a strong consumer or urban bias. This is very much evidentin how subsidies from NFA are shared by consumers and producers. According to a Congressional Planning and Budget Office (CPBO) study, from 1992 to 1996, farmers got about 8 percent of NFA subsidies compared to the 92 percent received by the consumers.

Of late, consumer prices have been stabilized by an increasing volume of imports to compensate for the gap in supply. Importation has therefore rendered the already minuscule level (less than one percent of total supply) of NFA procurement futile. (See Table 2) To affect prices

Table 2. NFA Palay Procurements, 1975-1995

Year	Palay Procurements (in '000 MT)	Percent of Total Production
1975	233	3.6
1976	274	4.1
1977	649	8.9
1978	518	7.1
1979	757	9.8
1980	551	7.1
1981	580	7.5
1982	649	7.7
1983	533	7.3
1984	297	3.8
1985	401	4.5
1986	422	4.5
1987	572	6.6
1988	264	2.9
1989	207	2.1
1990	572	6.1
1991	555	5.9
1992	419	4.5
1993	155	1.6
1994	60	0.6
1995	5	0.04
1996	124	0.1
1997	101	0.9
1998	62	0.72
1999	560	4.75
2000	663	5.35
2001	474	3.66
2002	300	2.36
2003	296	2.19
2004 1st sem	88	1.47

Source: Bureau of Agricultural Statistics (BAS) & NFA at the farmgate, several studies show that NFA would need to procure about 25% of total production.

Worse, NFA's active intervention in the rice market has exerted downward pressures on farm-gate prices, resulting in losses in farm incomes. By ordering the sale of government rice at reduced prices during the last quarter of 1999, government unwittingly depressed palay prices at the farm gate as traders continued quoting lower buying prices for palay to be able to compete with the NFA's reduced prices for milled rice. Estimates of rice farmers' losses ran up to as high as P4 billion because of this policy.[2]

Subsidy to the Consumer has High Leakage to the Non-Poor

This observation remains uncontested. The people living in posh villages have as much access to the subsidized NFA rice as those living in the slums. As such, it is not difficult to see common calls to have targeted consumer subsidies such that the poor would be the ones that benefit from the subsidy.

Are Traders Really That Bad?

In 1990, the Senate Committee on Blue Ribbon Report established the existence of a rice cartel in trading. Known as the Big 7, this cartel was said to be capable of influencing the price of rice in Metro Manila by creating shortages and hoarding during lean months. That was fifteen years ago.

A study of the Management Organization and for Development and Empowerment (MODE) posits that the sweeping indictment of the private rice-marketing system as monopolistic may be unfounded. Monopolistic tendencies only happen in areas where infrastructure bottlenecks exist. The study even asserts that intense competition among millers across provinces is apparent. And while the rice cartel was pretty much blamed for the 1995 rice crisis, much of it was really due to the ill-timing of imports, the ill quality of its supply forecast, and finally, the ill monitoring of buffer stock levels.[3] Coupled with the cumbersome procedures inherent in bureaucratic processes, farmers' insiginificant access to NFA's palay price support has somehow strengthened the traders' role in local rice trade.

2. "Enhancing Food Security in the Philippines," Dr. Ramon Clarete, AGILE, Annex 7 of the Joint Report of the GOP and World Bank, 2 May 2000.
3. "State Intervention and Private Sector Participation in Philippine Rice Marketing," Charmaine G. Ramos, (Quezon City, Philippines: MODE and SEACON, 2000), p. 82.

NFA is a Losing Proposition

No doubt about it. NFA's policy to buy high and sell low is a sure-fire formula for bankruptcy. Ever since NFA let go of its other revenue-raising activities (such as its monopoly in wheat importation) and concentrated on the rice and corn sector, the agency has been getting a lot of financial support from government. (See Table 3)

Table 3. NFA PROFIT (LOSSES), 1986 to 2003 (in billion pesos)

Year	From Operations	Before Gov't Subsidy	Gov't Subsidy	After Gov't Subsidy
1986	(0.826)	(1.583)	-	(1.598)
1987	(1.258)	(2.483)	-	(2.497)
1988	(1.079)	(1.779)	1.100	(0.679)
1989	(0.952)	(1.785)	1.720	(0.065)
1990	(0.386)	(1.026)	0.900	(0.126)
1991	(1.664)	(2.761)	0.996	(1.765)
1992	(2.351)	(3.940)	1.530	(2.410)
1993	(0.689)	(1.379)	1.760	0.381
1994	(1.105)	(1.226)	1.249	0.023
1995	(0.944)	(0.955)	0.955	0.000
1996	1.260	1.277	0.923	2.200
1997	0.060	(0.938)	1.500	0.562
1998	(1.213)	(2.245)	1.223	(1.022)
1999	(2.217)	(3.605)	1.193	(2.413)
2000	(4.216)	(5.453)	1.171	(4.282)
2001	(0.529)	(1.847)	0.090	(1.757)
2002	(3.765)	(5.023)	0.902	(4.121)
2003	(5.465)	(7.585)	0.922	(6.663)
Total	(27.340)	(44.340)	18.134	(26.230)

Source: Bureau of Agricultural Statistics (BAS) & NFA

The NFA's net worth has been decreasing. From 1998's P5.15 billion, its 2002 estimated networh is a negative P8.67 billion.

But other quarters justify that this should be viewed as a social cost that should be absorbed by the government for the country's food security. Privatizing it would leave the rice market in the hands of profit-hungry traders and seriously threaten our food security.[4] "Re-engineering" NFA would be the better approach. Without selling its assets but

4. "Strategic Re-organization of the NFA for the New Millennium," AGILE. 25 February 2000.

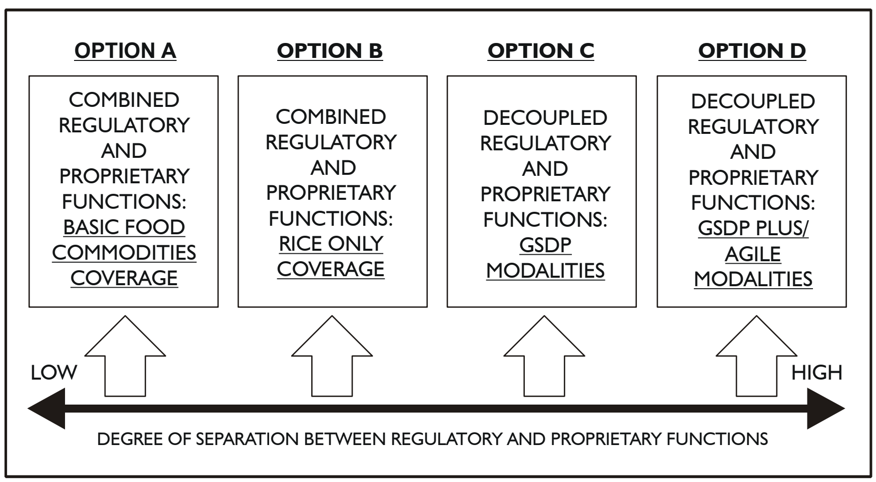
making some changes in its operations to make it more cost-efficient, NFA can fulfill its mandate minus the red ink in its balances.

HOW DO YOU SOLVE A PROBLEM LIKE NFA: A SPECTRUM OF PROPOSALS

Decoupling vs. Status Quo

An AGILE paper entitled "Strategic Reorganization of the NFA for the New Millenium," has neatly presented a framework of classifying the spectrum of proposals on what to do with the NFA. Basically, it lines up the proposals from left to right depending on the degree of separation between NFA's regulatory and proprietary functions. (See Figure 1)

FIGURE 1. SPECTRUM OF ALTERNATIVE OPTIONS FOR REORGANIZING THE NFA



Conflict is apparent when we see NFA as a party to determining the volume of rice imports, and at the same time, serving as the sole importer of the commodity, where of late, it has been deriving revenues. Further, it sets its buying and selling prices to influence the rice market and implements its pricing strategy with little regard for the adverse consequences this strategy has on other market players.

Essentially, decoupling would entail creating a government regulatory agency under the Department of Agriculture (DA) that will set the government release price for rice, decide on the volume of imports required to stabilize prices, among others, and allow the private sector to take over the marketing and trading functions of the agency.

For clarity, let us extensively use AGILE's presentation on how the decoupling concept is operationalized compared with other "status quo" proposals. The driving forces behind AGILE's proposal are two factors: greater faith that the private sector will deliver what government has failed to do and more important, minimizing agency cost while at the same time ensuring the country's food security.

Status Quo Options for Reorganizing the NFA: Options A and B

Option A- Combined Regulatory and Proprietary Functions: BasicFood Commodities Coverage proposes the retention of the current structure and combined functions of the NFA, as recently amended by Executive Order 22 (September 1998), which authorized its intervention in stabilizing the prices and supply of basic food items—including nongrains commodities. Thus, other than regulating the rice industry and being the country's exclusive importer of rice, the NFA has been tasked to stabilize the prices of corn, sugar, and fertilizer. Operational and financial improvements within the agency's current structure also form part of this option.

Critics of the NFA's expansion to other nongrains food items, particularly those who are acutely concerned about the country's budget deficit spending and the inefficiencies of government intervention systems, argue that its operations should be limited to the rice market. Supporters of this move also point out that the markets for other commodities have already been liberalized, and therefore, do not need government intervention. These are the basic justifications for **Option B - Combined Regulatory and Proprietary Functions:** Rice Only Coverage. As with Option A, operational and financial improvements are expected to accompany the proposed policy change limiting the NFA's intervention to the rice market.

Decoupling Options for Reorganizing the NFA: Options C and D

The decoupling of the NFA's regulatory functions from its marketing functions is one of the major reforms proposed under the Grains Sector Development Program ((GSDP), essentially to institutionalize a more transparent process for food security policy formulation and implementation that is more cost-efficient for the Philippine Government. The features of **Option C - Decoupled Regulatory and Proprietary Functions: GSDP Modalities** include:

- *Creating a Government Regulatory Agency under the Department of Agriculture to Assume Functions Associated with Ensuring Food Security.* The functions will include: (i) setting the government release price for rice; (ii) deciding on the volume of rice imports required to stabilize rice prices; (iii) moving rice stocks into areas hit by natural disasters; (iv) stabilizing palay prices in the event of a bumper crop; and (v) establishing other policy parameters that the Philippine Government may see fit to attain food security.

- *Establishing One or More Trading Corporation(s), with not more than 49 percent Government Equity in Each.* The private sector will be given the option to invest at least 51 percent in the equity of each corporation. While the government regulatory agency will receive regular budgetary appropriations from Congress, the corporation (s) will not be subsidized and are expected to generate net profits from their grains trading activities.
- *Contracting the Services of the Trading Corporation(s) and other Private Sector Grains Traders for Food Security.* The proposed regulatory agency will contract the services of the newly formed trading corporation(s) and other private sector grains traders to implement the food security program. The process will be competitive and will enable society to benefit from the more effective and efficient provision of food security services.
- *Adoption and Implemention of Related Policy and Institutional Reforms.* On a much broader level, the GSDP also seeks to introduce NFA-related reforms that will improve the design and effectiveness of the country's food security program. These reforms include:
  * Stabilizing rice prices at market levels and implementing a separate targeted food safety net program for the poor;
  * Applying a seasonal price premium to the NFA's palay procurement at a level that reflects local production costs, productivity, and the world price of rice;
  * Setting the procurement volume to no more than the NFA's strategic 30-day rice buffer stock;
  * Institutionalizing a transparent and timely rice import policy formulation; and
  * Enabling private sector importation of rice, if it is determined that the country needs to import rice.

Option D - Decoupled Regulatory and Proprietary Functions: GSDP Plus/AGILE Modalities was formulated by AGILE's consultants after a careful review of (i) external factors influencing the development and sustained growth of the Philippine grains sector, (ii) lessons learned from the experience of other countries, and (iii) the current structure, operations, and impact of the NFA. **Option D**, as envisioned, has five major components.

Component 1: Implementation of a Rice Price Stabilization Scheme Without Buffer Stocks. The recommended scheme will restrict the fluctuations of domestic rice prices around a target price. While most price stabilization schemes for commodities around the world, including the NFA's intervention system, are typically supported by publicly held buffer stocks, this scheme significantly reduces the large fiscal burden associated with buffer stocking and enables the private sector to import the rice volume deemed necessary to maintain the target price (Box 2).

Component 2: Creation of a National Rice Board. In accordance with the DBM's reorganization principles, the AGILE consultants have designed a rice board

BOX 2. AGILE'S PROPOSED PRICE STABILIZATION SCHEME FOR RICE WITHOUT BUFFER STOCKS

Objective: To restrict the fluctuations of domestic rice prices around a target price using rice imports, thereby reducing the inefficiencies stemming from the NFA's current pricing policy, and addressing the heavy fiscal burden associated with buffer stocking.

Structure of the Proposed Price Band:

- Target Price: World price of rice, adjusted for the cost of freight, insurance, and transport from the port to the first warehouse, plus the calculated average implicit protection rate of 50 percent
- Upper and Lower Limits of the Band: $\pm$ 5 percent from the target price (to ensure that the resulting prices are tolerable to the buying public, based on analysis of wholesale rice prices in the Philippines from 1988–1998)
- Changes in the Target Price: $\pm$ 10 percent from the previous year's target price (to maintain the acceptability of the inter-period changes in the target price to the buying public, based on an analysis of changes in monthly retail rice prices from 1995–1999)

Implementation of the Price Band:

AGILE's proposed National Rice Board will be responsible for setting the price band and for correcting deviations from the rice band through in-quota rice imports or rice minimum access volumes (MAVs). Changes in the target price will be confined to $\pm$ 10 percent, by varying the implicit protection rate incorporated in the calculation of the target price.

to undertake the rice regulatory functions of the government. The National Rice Board (NRB), which will be attached to the DA, will have both regular and emergency powers. Its regular functions will include:

- Setting the parameters of the rice price stabilization band;
- Determining and announcing the rice import or export volumes required to maintain domestic rice prices within the band;
- Formulating and implementing a system for enabling the transparent and competitive participation of the private sector in rice imports;
- In the event rice trade is liberalized, developing and facilitating the implementation of the mechanics for the rice minimum access volume (MAV) (and whenever necessary, the expanded MAV) in a manner consistent with the government's WTO commitments; and
- Monitoring the actual volumes of rice imports and exports, palay and rice prices, and the performance of the private sector participating in rice importation.

The proposed rice board will also be vested with powers to deal with emergency situations-defined as cases when the prevailing retail price moves outside the targeted price band for rice. As warranted by the cause of the outward movement of the domestic rice retail price from the band being defended, the NRB will have powers to:

- Allocate the rice import quota to private sector groups, subject to WTO-consistent increased or reduced tariffs, in order to reduce the cost of imported rice; and
- Cause the procurement of palay at a predetermined support price through a purchase scheme requiring private sector participation.

Component 3: Transfer of the NFA's Duplicative Functions to Appropriate Government Units. Consistent with the principle of horizontal compartmentalization under the DBM's government reorganization paradigm, NFA functions not covered by the NRB, but which can be or are being undertaken by other government units at no additional cost, will be transferred to the agencies concerned. Based on AGILE's analysis of the NFA's functions, some of the functions proposed for transfer include:

- Coordination of research and development activities on grains, to the Bureau of Agricultural Research and the Philippine Council for Agriculture, Forestry and Natural Resources Research and Development (PCCARD) of the Department of Sicence and Technlogy (DOST);
- Introduction of more efficient post-harvest system and technologies, to the Bureau of Post-Harvest Research and Extension and the Philippine Rice Research Institute (PhilRice);
- Registration and licensing of persons and entities involved in the grains business, including their facilities and equipment, to the LGUs; and
- Inspection of grains stored in private warehouses for purposes of taking inventory, to the Bureau of Agricultural Statistics.

Component 4: Full Privatization of the NFA's Proprietary Functions, including the Unrestricted Sale of its Bundled Assets to the Private Sector. Lessons learned from international experience indicate that the private sector can be relied upon for agricultural trading activities, even for commodities with food security implications. Discussions with prospective private sector investors, particularly those groups currently involved in grains trading, suggest that a privatization scheme with the least government ownership and control will be the most attractive and viable modality. Thus, to reduce the rice market inefficiencies and the fiscal burden caused by its inherently conflicting mandate, the NFA's proprietary functions should be fully privatized.

Factors such as promoting greater competition in the economy and maximizing the government's privatization proceeds likewise prompt the sale of the NFA's bundled assets to the private sector. Selling all the assets to one group will not only require a significant amount of financing: it will also mean that monopolistic powers over the market will be transferred from the public to the private sector. Dividing the assets into 6-10 bundles with no specifications from the government on how the assets will eventually be used will facilitate sale, maximize government privatization proceeds, and adress anti-monopoly concerns.

Component 5: Adoption and Implementation of Complementary Grains and Policy Institutional Reforms. There are three other equally important policy and institutional changes deemed critical to a more efficient and effective food security program in the Philippines.

- Targeted Food Assistance: Providing safety nets to the poor will always be essential to a developing economy like the Philippines, which must pursue structural and macroeconomic adjustment reforms in order to achieve a more sustained pace of growth. Towards this end, a tight budgetary situation, such as the one confronting the Philippines today, does not allow for a generous amount of food subsidies. This calls for a more targeted approach to providing food subsidies, in contrast to the general consumer subsidies currently being implemented by the NFA.
- Rural Infrastructure Support: An accelerated program of providing rural infrastructure will undoubtedly lead to production and productivity gains in the rice sector and consequently, increased farm incomes. Farm-to-market roads and irrigation facilities-such as those provided for under the GSDP-will enhance producer welfare, and pave the way for more gains to be realized under a more liberalized rice trade regime in the country.
- Technological Improvements & Market Development: Promoting technological improvements and market development will be vital to the sustained development of the Philippine grains sector. In this regard, the campaign for more rewarding partnerships between the public and private sectors in research and development, and for the development of information networks that facilitate market transactions, will have to be intensified.

A Re-engineered NFA

In his University of Asia and the Pacific (UAP) masteral thesis, former NFA Administrator Romeo G. David suggests a re-engineered NFA where the agency retains its assets, regulatory and marketing functions. Apart from having a targeted consumer subsidy, which is a common recommendation, he proposes changes in the following:

- Stabilization of farm gate prices. The NFA will offer its warehouses for grains storage by the farmers who can enjoy the option of selling it to any buyer within a six-month period. The farmer who deposits his palay can immediately get the equivalent of 80 percent of the total value of his stocks based on the support price from which he could settle his obligations and wait for better prices. Within the six-month period, the farmer may opt to sell his produce to private traders at a price higher than the government support price. He will pay back NFA the amount previously paid him plus storage and shrinkage allowance. However, if he chooses to finally sell to NFA his stocks, the NFA pays him the balance of 20 percent based on the support price without charging any additional cost.

- Buffer stocking. The NFA can provide the national government the buffer stocking service to be treated as food security reserve and bill the national government accordingly.
- Emergency/Relief Operations. The present arrangement entitles the LGUs, DSWD and PNRC to immediately withdraw from any NFA warehouse in calamity areas rice for immediate relief on a credit line. This set-up is retained and further expanded to include other groups or agencies such as congressional districts. Legislators can allocate a part of their countryside development fund (CDF) to secure rice for relief purposes. In calamity-declared areas where government's buffer stock is depleted but farmers' stocks are available, the NFA shall invoke the power of the state to expropriate private property with just compensation.

One comment on this proposal is that in terms of maintaining buffer stocks, it becomes a mere accounting exercise where instead of NFA directly being credited with the expense, it shall be the national government which carry it. So rather than the expense appearing in NFA's books, it will the national government, through the Department of Agriculture, perhaps, which will be billed for the expense. Thus, it will not have an impact on our consolidated public sector deficit (CPSD) position.

FDC Proposal[5]

The Freedom from Debt Coalition (FDC) published a paper which, among others, bats for :

- Targeted procurement. While targeted subsidies for consumer price stabilization appears to be a commonly accepted proposition, targeted procurement that favors small farmers who do not have the capacity to dry their palay and meet the stringent quality requirements of the NFA, should be considered. The agency must likewise have access to adequate financial resources to pay farmers in cash rather than in checks since the poorest farmers usually cannot afford to wait for a check to be cashed.

5. "A New Lease on Life for the NFA: Affirming state intervention in the food market," by Pablo Medina, Freedom from Debt Coalition Policy Studies, November 1999.

- Retention of quantitative trade controls but the right to import will be bid out. A "simultaneous-buy-sell system" (SBS), a system used with some success in Japan, may be established. Here, buyers and sellers negotiate to determine the conditions of a sale and propose a quantity and price to be exchanged. The food agency then studies all bids and chooses those that have the widest margin between the proposed selling and buying prices. This margin will be kept by the agency and can be utilized for domestic procurement.

A flexible rice inventory target for buffer stocking. For times of bountiful harvest, a ten-day equivalent of national rice consumption is recommended; for low production years, 35 days. This policy would reduce the cost of maintaining unnecessarily high public stocks in years of plentiful output.

Proposals from the Legislature

Reorganizing the NFA by overhauling its charter (the legal basis of which is a Marcosian Decree, PD No. 4) is not a new legislative proposal. As early as the 11th Congress, proposals to that effect emanating from then Cong. Roxas, Sarmiento, Alvarez, among others, wanted to establish a new food authority which could effectively intervene in the rice market. However, most of the proposals then carried budgetary support and it would have been difficult then, and even now, to carry the bill (s) through the legislative mill without looking at the implications on government's fiscal position.

It is worth mentioning that the Asian Development Bank, through its so-called Grains Sector Development Program (GSDP) has been pushing for the "privatization" of NFA and the tariffication of rice imports. It is composed to a $100 million policy loan and $75 million investment loan. Privatization of NFA's importation has been a standing call from some quarters, as it is viewed as non-transparent and often seen as marred by corruption from NFA officials themselves. But the loan did not prosper, because one of the conditionalities was the presidential certification of the two bills pertaining to NFA's reorganization and the removal of the quantitative restrictions on rice imports. Faced with piling bills on loan commitment fees, government opted to cancel the loan altogether.

Nevertheless, the push to reform the NFA is not lost. In fact, the legislative proposals that were introduced in the 12th Congress were filed at NFA's instance. Several bills along these lines were filed, among which are those of Cong. Nachura, Cua, Lacson and Espino. After a series of public consultations and technical working groups, the consolidated bill came out with these features:

1. NFA's function will be split into two: The trading and buffer stocking task will be undertaken by the National Food Corporation, while its regulatory function is delegated to the Food Development and Regulatory Administration, both institutions are attached to the Department of Agriculture (DA).
2. The National Food Corporation
   a. Will start with a clean slate and an authorized capitalization of P20 billion. P15 billion shall be in the form of assets from the defunct NFA and P5 billion shall be given in cash by the DBM over a period of no longer than ten years. Its liabilities will be passed on to the CB-BOL

   b. Shall maintain and manage the national strategic rice reserve (equivalent to 15 days of national consumption all year-round) and the government's rice buffer stock (equivalent to 30 days of national rice consumption by July 1 every year, inclusive of the 15-day strategic rice reserve) when commissioned by the FDRA

   c. Shall undertake the importation of rice for government duty/tariff free

   d. Its Board is empowered to fix renumeration and allowances, effectively exempting it from the Salary Standardization Law (SSL).
3. The Food Development and Regulatory Administration shall carry on the remaining functions of the defunct NFA such as licensing, collecting fees, inspection of warehouses, foodgrains research coordination and regulate the foodgrains quedan system.
4. The following NFA mandates are, however, transferred to the following agencies:
   a. Food subsidies to the poor, particularly the Targeted Rice Distribution Program and Coconut Farmers Food Access Program (CFFAP) to the Department of Social Welfare and Development

   b. Stabilization of prices and grains supply at the farm gate to the Department of Agriculture

   c. Stabilization of supply and prices of rice at the consumer level to the Department of Agriculture

5. During the three-year transition period, the DBM shall include yearly in the President's budget the amounts of P1 billion for DA farm-gate price and supply stabilization and P250 million for DA supply and price stabilization of rice at the consumer level and P500 million for DSWD.

Some Comments

Similar to Mr. David's proposal, the impact of the above initiative from the legislature is not really to immediately relieve government's fiscal deficit but merely transfer NFA's liabilities to the CB-BOL. It will not have an immediate positive effect on the government's consolidated public sector deficit. It is precisely because of the government's fiscal position that the Department of Budget and Management recommended that NFA's importation of grains be privatized. And the extent that the new National Food Corporation will be exempt from the SSL further aggravates the headaches that the DBM and even the DOF are now experiencing.

After a three-year transition period, grains procurement at the farm-gate which will be lodged in the Department of Agriculture will be phased out. Over the medium-term, therefore, we shall see a greatly diminished state intervention in seeing price stability at the producer level and of course, a decrease in its contribution to the public sector deficit.

What if money is no object?

While the fiscal burden that NFA imposes on government is, by now, widely recognized, it would be a useful exercise to find out how much it would actually cost the government to secure our staple. It takes off from the following premises:

- Past support and subsidies had a strong consumer bias. This time, and given the urgency to catch up, the producer must be supported;
- The Philippines is a calamity-prone area. We are visited by an average of 20 typhoons a year so there is a need to have buffer stocks not just in times of drought but for relief operations after a typhoon or any other calamity;
- The world's grains trade is not likely to expand;
- The peso is bound to further depreciate, which could exert pressures on our wage bill if we continue to be increasingly import-dependent; and

- Assuming rice imports are totally privatized and tariffs are lowered in 2005, given the structure of incentives, there is a big possibility that big trader-millers will cease milling and concentrate on trading imported rice. It will create a condition for the further depression of farm-gate prices, making rice farming totally unattractive.

Under the GATT-WTO, a developing country is allowed to spend up to 10 percent of its agriculture's gross value added as domestic support for its farmers. We are barely spending three percent. So, let's look at the numbers.

In 1999, our agriculture's gross value added in nominal terms was P447 billion. Ten percent of this amount is P44.7 billion. Note that this is already bigger than the proposed, or even any of the past years' budget for agriculture. Nevertheless, to proceed, several studies have indicated that for NFA to be effective in influencing farmgate prices, it must purchase 25 percent of the domestic supply. With total palay production of around 11.8 million metric tons for 1999, government must purchase 2.95 million MT. At NFA's palay procurement price of P9.50 per kilo, the amount needed to influence farm-gate price is around P28.025 billion.

Indeed, it would make more sense for government to spend this huge amount on palay procurement, irrigation, farm-to-market roads, post-harvest facilities—which would have greater impact on productivity—rather than solely on palay procurement. But the problem is irrigation, which is really the biggest factor in increasing our potential output, takes a while to set up. Further, we need time to identify water sources and perhaps greater time to rehabilitate existing watershed areas. In the meantime, what do we do with our palay farmers? Are we sure that once these dams and irrigation projects are built, we still have palay farmers to speak of?

Price support can actually be viewed as government's short-term solution to what it has failed to do for decades. And we have only up to 2005 to address something which can be viewed as a matter of national security.

The need for an active state role in rice trade

Yes, not just among farmers but among rice industry researchers, there is the persistent demand that government retain an active role in rice importation and buffer stocking. Indeed, such a strategic function cannot be left to the vagaries of the market and the whims of a profit-driven private sector.

As such, while AGILE's proposal for NFA's set-up appears to neatly fall in place under a tariffied rice importation regime and conforms with the basic tenets of ADB's Grains Sector Development Program, it does not directly provide us with a definite handle, should we choose to maintain the quantitative restrictions on rice imports and allow the state to control rice imports.

FDC's proposal is workable in certain localities where there is greater transparency and accountability of local executives who would identify small farmers deserving of targeted procurement. The simultaneous-buy-sell-system, though, might be difficult to implement without greater access to information by participating buyers and sellers. If anything, import quotas may still be cornered by those who are willing to pay the price for such access.

As far as the proposal from the legislature is concerned, the idea that the NFC should be truly a service corporation that earns a decent fee from its warehousing and storage facility and yet remain government-controlled is feasible. Combined with Mr. David's proposal of paying the farmer 80% of the value of his palay or rice stored in their facility and the Malaysian model of imposing an implicit tariff for those who would want to import, it can be supported and pushed by NGOs and POs who wish to see a strong government presence in the rice trade.

State presence in grains trade should be pushed until such time that we have reached an average productivity level of at least 5 metric tons per hectare, and when rice farmers are able to earn a decent income not just from sustainable rice farming technologies, but from alternative sources of income from agriculture.

QRs VS. TARIFFS ON RICE REVISITED

Food security, food self-sufficiency, increasing farmers' income are goals common to government and civil society. Yet, these goals are not mutually reinforcing. There are times when one goal can actually be achieved only at the expense of the other. Food security can actually take precedence over or even come in direct conflict with the goal of increasing farmers' income. Is it the consumer or the producer, which will be given priority?

As such, one is caught with the dilemma of choosing policy instruments that would best push a goal without compromising the other.

The removal of quantitative restrictions, their replacement with tariffs and the eventual phasing down of tariffs altogether on all trade transactions is the basic trajectory that all WTO-member countries have pledged to take towards a liberalized global trading regime. Without doubt, this policy shift would, at least in the short-term, impact on those common goals. But setting aside one's ideological baggage, the basic premise for advocating for a shift from QRs to tariffs is easy to understand. Greater transparency and the removal of discretion from importing authorities are attractive reasons why tariffs should be preferred over quantitative restrictions, not just for rice but for other commodities as well. And the revenues that can be derived therein, while viewed as merely icing on the cake, can be a primary motive for most cash-strapped developing nations. Yet, if that is all there is to it, then the most logical conclusion would be to immediately tariffy all commodities. But when offers were laid on the table for the WTO ratification in 1994, government chose to maintain the quantitative restrictions on our staple for ten years, invoking Annex 5 of the Agreement on Agriculture. (AoA)

The Major Issues

Lower prices for the consumer

Indeed, the domestic price of rice is high compared to the global market. As such, even if we impose a 50% to 70% tariff on imported Vietnam or Thai rice, which is about the level allowed under WTO rules, it would still be cheaper compared to domestically produced rice. Of course, that would remain true if the exchange rate of the peso vis-à-vis other foreign currencies does not plummet.

What is further stunning is the argument that while there are 3 million rice farmers, there are more than 80 million Filipino rice consumers.

Add to that the 3 million farmers that eventually become consumers when their own consumption stocks dwindle and one might end up accepting the argument that it is economically rational for us to just import cheap rice than insist on producing it.

Yet, shifting to tariffs might not necessarily result in cheap rice if importation is left principally to those who are able to fulfill government's stringent requirements to import. While lately, not much has been heard of the rice cartel, there are key players in the industry that to this day exist, ready to capitalize and leverage on more profit opportunities within the rice sector. Granted that they are able to procure imported rice cheaply, it is doubtful if they would sell it at a tremendously lower cost than what is prevailing in the domestic market. The possibilities of and incentive for collusion abound which might not at all result in cheaper rice in the domestic market.

Tax Revenues vs. Quota Rents

Tariffs undoubtedly give government the much-needed revenues that could possibly augment its spending to raise productivity of the farmers and concomitantly raise their incomes, which an import quota would not be able to provide. Compared to a quantitative restriction, a tariff is more transparent and is therefore less prone to lobbying and corruption. Critical in this set-up, though, is the assumption that government is able to monitor all the possible ports of entry for imported rice and collect the revenues that are due therefrom. Further, a high tariff rate may, for all intents and purposes, act as a de-facto quantitative restriction and would, similar to a QR, encourage smuggling. At the end of the day, therefore, the question of whether it will be a tariff or quota boils down to government's capacity to enforce a policy it so chooses.

A Thin Global Rice Market

Perhaps one of the strongest arguments why a nation with rice as staple should strive for rice self-sufficiency and not just rice security, is the thinness of the global rice market. Despite trade liberalization, rice traded in the global market has not gone beyond five percent of total production. A shock from a major rice supplier, or a sudden spike in the demand of a major importer can trigger volatility in global supply as well as the price of rice. As it is, China has already reduced the land devoted to grains production from from 112.5 million hectares in 1996 to 99.4 million hectares in 2003, and has caused a rise in world rice prices. Coupled with a currency contagion similar to what happened in 1997, a small country such as ours would therefore be highly vulnerable to social unrest should the supply of a staple be highly dependent on imports.

Shifting to tariffs, which may be set at an initially high level, would have to be gradually lowered, according to WTO rules. Should tariffication be done without the necessary push to ensure the stability of rice farmers' income, then for sure, the already unprofitable rice farming activity would eventually be driven out of business. It would be good if we could always buy rice cheaply from the global market, but such might not always be the case, considering the thinness of the market. It is no wonder that even Malaysia, which is rice-secure, has set to maintain a rice self-sufficiency level of no less than 65%. And Vietnam, which is a major rice exporter, maintains the option to enforce an export quota should its domestic food security is threatened.

Impact on Poverty

Caesar Cororaton, a Senior Research Fellow at the Philippine Institute for Development Studies (PIDS), in his study entitled, "Can the poor benefit from the removal of QR on rice?" published in May 2004, argues that the "displacement effects of the expected surge in rice imports will translate into larger negative income effects for household groups where the problem of poverty is severe."[1] He attributes this to the fact that lower income groups rely heavily on agriculture, palay production in particular. Below is a summary of the effect of a total removal of the quota on rice coupled with a reduction of the tariff on rice based on his simulation:

- local price of rice imports : -64.2%
- consumer price for rice : -4.9%
- consumer price index : -0.65%
- imports of rice : 3,676%
- impact on domestic production
  - rice milling : -2.0%
  - irrigated palay : -1.93%
  - non-irrigated palay : -1.60%
- ave. agri wages : -1.70%
- ave. return to capital in irrigated palay : -7.3%
- ave. return to capital in non-irrigated palay : -5.7%
- employment in irrigated palay : -4.6%
- employment in non-irrigated palay : -3.3%

Mr. Cororaton recognizes the need for market reforms in the rice sector but cautions on the way the reform is carried out especially for a critical commodity such as rice. He proposes the provision of direct government transfers to those adversely affected household groups in the

1. *"Can the poor benefit from the removal of QR on rice?"* Caesar B. Cororaton, Policy Notes No. 2004-04. Philippine Institute for Development Studies. May 2004

short-term, to mitigate its immediate negative impact and strongly urges the implementation of measures that have long-run positive effect on the productivity at the farm level such as irrigation, better farm-to-market roads and post-harvest facilities.

The Philippine Notification of Extension of Annex 5

Government's decision to request an extension of Annex 5 of the AoA last March 29, 2004 was met with mixed reactions from civil society. While others welcomed the move, others were more skeptical, asking if it was for real.

Based on the above discussion, the maintenance of the QRs seems to be a logical move by the government for a number of reasons:

First, maintaining the QRs on rice appears to be the best protection that government can offer to our farmers against the uncontrolled influx of and unfair competition from cheap imported rice, especially from countries like the USA, that heavily subsidize rice production and export.

A study by the Institute for Agriculture and Trade Policy (IATP) based on data from the US Department of Agriculture (USDA) and the Organization for Economic Cooperation and Development (OECD) indicates that the US dumps rice at the average rate of 20% since 2001. (IATP 2003)

As Oxfam International has pointed out, the continuous subsidization by countries like the US of the production and export of rice in the form of export credits, loan deficiency payments, market price support, commodity loan interests, state credit programs, direct government payments, etc. renders a tariff regime that is bound to 50% useless. It is likewise difficult for countries like the Philippines to use other WTO mechanisms such as the special safeguard measures (SSM), anti-dumping duties (ADD), countervailing measures, or the dispute settlement body (DSB) to guard against possible dumping, since all these require hefty investments in technical and resource capacity.

Second, government's direct admission of lack of support for the industry in terms of infrastructure, post-harvest facilities, irrigation and technology is a major reason for the industry's uncompetitiveness. The Philippine Peasant Institute (PPI) pointed out in their position paper against tariffication that, "(E)ven if imported Vietnam rice is imposed a 100 percent tariff, it will remain cheaper than the cheapest available rice (i.e. NFA rice) in the market. Vietnam rice is priced at PhP6.50 and will retail for only PhP13.00 with a 100 percent import tariff while NFA rice sells at PhP14.00. Clearly, imposing tariffs will not protect domestic rice producers because they are not yet capable of competing with other rice-producing countries."[2]

Third, as NFA Deputy Administrator Gregorio Tan quipped, "It is better that we find out the concessions that other countries would ask for in exchange for the maintenance of the QRs. If we don't, then we will never know what the costs to us had we shifted to tariffs." On the other hand, if we let go of the QRs, we must also know the concessions that are due us.

Korea has earlier given out a similar notice of extension and nine countries signified their intention to engage it in negotiations: US, Argentina, Australia, Egypt, Canada, China, Thailand, India and Pakistan. Had Vietnam been a full-fledged WTO member, it is expected that it will similarly manifest its intention to engage.

At this writing, Australia, Argentina, Canada, China, India, Thailand, Pakistan and the US have been reported to have manifested their intention to engage the Philippines in its request for the extension of the maintenance of its QRs on rice.

Mere Leveraging?

Government's sincerity in pushing for Annex 5's extension on rice can be challenged, especially when several Arroyo administration-aligned legislators in the 12th Congress have sponsored bills removing the QR on rice and replacing it with tariff. Said bills also allow the private sector to import rice and removes NFA's monopoly on rice importation.

Of course, government also looks at the bottomlines. Should countries that wish to engage us push for an increase on the minimum access volume (MAV) over and above our projected import demand, we shall be swamped with surplus rice in the domestic market. Our DA sources intimated that based on initial discussions, the Federation of Free Farmers headed by Mr. Raul Montemayor think that a minimum access volume of 600,000 metric tons at a 25% in-quota tariff is workable. Note that currently, the Philippines imposes a 50% tariff whether or not imported rice is in or out-quota. Mr. Tan of the NFA cautioned that if our trading partners ask for concessions should we push for a higher MAV,

2. http://www.ppi.org.ph/agri_trade/position_papers/post_paper.htm

then the lowering of the in-quota tariff rate is expected to be pushed by them.

And should our trading partners ask for concessions in terms of further opening up of our markets in other commodities just so we can enjoy this privilege (e,g, Thailand for greater access of its sugar, or China, its shoes) then government will be confronted with a host of problems, since competing industry interests will set in. Without a clear agro-industrial plan for the country, it would not have any basis as to which sector it will use as a pawn in order to preserve another.

OPPORTUNE TIME

The NGOs and POs working around the rice issue should view government's notification of the extension of Annex 5 as a counter-leverage to demand clear and doable policies and utilize it to similarly strengthen networks among farmer organizations within the region for calls that preserve the livelihood of small rice farmers.

First, if government is indeed sincere about protecting the livelihood of small rice farmers and at the same time achieving a near 100% self-sufficiency in our staple, it should now be ready to offer concessions in other areas which it thinks it has adequately protected for quite sometime and can now be left to the vagaries of the world market. Sugar easily comes to mind. But while exposing protected sectors to competition is a quick way to scan which can be given out as a concession, forcing the government to really lay down a coherent agro-industrial plan should be the overriding parameter for any concession to be given out. Caution must be exercised, though, because as in any negotiation, one must not prematurely lay his cards on the table.

Second, serious effort in increasing the productivity and incomes of our rice farmers must be given. Irrigation, appropriate technological inputs, access to technologies that promote cost effectivity should be in place. While government's hybrid rice program might increase productivity, without the subsidy that it provides for the use of its seeds, as well as the much-needed agriculture infrastructure, what is its impact on farmers' income?

And while we are pushing for the retention of the QR, it will not be there forever as surely, we are expected to eventually phase it down. As such, should government have the political will to really work for Annex 5's extension, it should merely be viewed as breathing space for our rice farmers and for government itself to get its act together.

Third, this brings to fore the issue of enforcement. Government must be able to strictly enforce the quota and the concomitant in and out-quota tariff rate that goes with it. Smuggling remains as a major problem of the industry and this becomes more and more attractive if quotas and tariff rates are placed at very high levels.

On the international level, NGOs and POs must utilize this as a platform in forging areas of cooperation among their counterparts in the region in issuing common calls.

For one, the removal of export subsidies and export credits of developed nations on their rice industry is urgent, especially when they have a minuscule number of rice farmers to speak of.

Second, the expansion of the special and differential treatment for developing nations, especially the concept of having some permanent recognition within the WTO of strategic/special products of developing countries, must be pushed. The fight that was started by the so-called SP-SSM (Special Product-Special Safeguard Measures) group led by Indonesia and supported by the Philippines in Cancun must not come to naught. There must be some room within that advocacy to fight for tariff flexibility based on world rice prices and crop seasonality. Along these lines, we must likewise exploit the opening that Article 28 of the AoA offers, which would allow tariffs on certain products to go beyond the WTO-mandated levels should tariffs be used for rice, which is 50%.

Finally, linkages among farmer organizations across the regions must be strengthened. The fact that small Thai farmers are still debt-ridden is ironic given the much-touted success of Thai rice's export. And for Thailand to demand concessions in the name of its rice farmers when the benefits of its export policy has not trickled down to them should find some resonance among the regional network partners working on the issue.

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