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# Policy Brief

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A closer look of policy “incentives and disincentives” for smallholders in the Philippines

## The Policy Environment of Vegetable-Agroforestry (VAF) System in the Philippines



Agriculture as a basis for rapid economic growth in the Philippines requires both productivity revolution in smallholder farming, innovative policies and political commitment. Vegetable-Agroforestry (VAF) system is a viable farming system that integrates vegetables in tree-based systems, and vice versa. The system provides multiple benefits, including provision of micronutrients to the diet of the rural community and enhancement of on-farm biodiversity and environmental sustainability. However, its viability is constrained by various factors, including farmers’ inability to invest in the system, inadequate institutional structures to facilitate information flow, and lack of market incentives. Policy incentives are thus, needed to stimulate smallholder investments in VAF system. This brief presents the policy incentives, disincentives and gaps in the context of smallholder investments in VAF system.



### Why smallholders?

Smallholders comprised a significant segment of the global farming population, and are most vulnerable to rapidly changing economic, social, political and environmental conditions. Often, national governments concentrate on large farmers for national food security and self-sufficiency issues because they have the operational resources, and are assumed to be easier to work with, and are more able to respond to suggestions. With this, assisting smallholders has become an effort for enhancing social welfare rather than substantially increasing national agricultural output.

In the Philippines, small farmers, including fisherfolks account to over 90% of all farmers and fisherfolks, which is around 21% of the total labor force in the country. There is ample scope for governments and other relevant sectors to pay attention to this important sector.

### What are incentives and disincentives?

In general, **incentives** contribute to, or serve as motivation to accomplish a task, which may lead to rewards. In contrast, **disincentives** refer to those that discourage, hinder, or deter positive responses or actions to occur. In this brief, incentives are considered elements of policy instruments that increase the comparative advantage of a VAF system and thus, stimulate investments among smallholders.



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**Republic Act (RA) 7607** provides the Magna Carta for small farmers, declaring that **smallholders** are to be regarded as equal partners in development, and therefore should be wholly supported in their economic endeavors. **Small farmers** are defined as natural persons dependent on small-scale subsistence farming as a primary source of income and whose sale, barter or exchange of agricultural products do not exceed a gross value of one hundred eighty thousand pesos (P180,000) per annum based on 1992 constant prices. Additionally, the Philippine Agrarian Law defines smallholders as those cultivating not more than 5 ha of land.

Small-farm families in less developed countries form about 80% of the world’s total farmer-groups.

# Policy Incentives and Disincentives

Since 1970s, government policy measures have “incentive” tendencies to encourage participation of the private sector and the civil society in any development undertaking. The succeeding sections present the incentives and disincentives of selected national policies relative to tree growing and vegetable production, in the context of small farmers.

## Tree Growing

The Forest Occupancy Program (1971) was launched to prevent the spread of swidden farming through controlled transfer of resource rights. Forest occupants were given lands not exceeding 7 hectares. The Family Approach to Reforestation Program (1971) was implemented to contract forest occupants for the establishment, maintenance and protection of forest plantations. The Communal Tree Farm Program (1974) was also launched, providing a 25-year lease agreement to families who wished to establish tree plantations and agroforestry farms within forestlands.

These programs led to the promulgation of Presidential Decree 705 (Revised Forestry Code of the Philippines). This law, among others, was a nationwide reforestation effort, in partnership with the private sector and civil society, which provided forest communities the right to develop forested areas and to receive government assistance. Although it provided several incentives, many farmers were still discouraged because of its disincentives. Small farmers lack the capacity to develop large forest areas (a minimum of 100 ha and 10 ha were allowed for lease to convert into agroforestry and tree farm, respectively). Even with credit assistance, lack of regular cash flow between planting and harvesting has led to problems in liquidating the investment. There were also uncertainties with the future prices of tree products at harvest time.

### Box 1. Some incentives under PD 705

- Ownership rights to planted trees & other products
- Rights to sell, contract, convey or dispose planted trees & products
- Discounted fees, rentals & forest charges
- Tax exemptions & tax credits
- Free government technical assistance
- Assured credit assistance & use of facilities
- Exemption from export log ban
- Market assurance for timber products
- Unrestricted export of plantation products

The Integrated Social Forestry (ISF) program (1982) was implemented to provide land tenure to forest occupants through a Certificate of Steward Contract (CSC). CSC provided land use rights over a certain forest area for 25 years, renewable for another 25 years. In return, farmers were obliged to plant trees, at least 20% of the area, and are allowed to convert it into more productive farms. They were also encouraged to form local groups and cooperatives. With DAO 04 (1991), additional incentives were given to encourage farmer participation.

### Box 2. Incentives under the ISFP

- Grant & land tenure
- Priority for wage-based employment
- Settler census to control migration
- Extension & information activities
- Community organizing to ensure participation
- Research & development support
- All incomes derived from the land are given to the participant
- Forest products are exempted from forest charges
- Provision of technical, legal, financial, marketing, credit & other assistance
- Assistance from government agencies, NGOs & private organizations
- Compensation for permanent investments
- Retention of rights to avail subsequent arrangements over the land.

Republic Act 7160 (Local Government Code of 1991) was aimed to strengthen the capacity of local government units (LGUs) to share with the national government, the responsibility in maintaining ecological balance within their political jurisdiction. In effect, projects were devolved to LGUs, except for model ISF sites and communal forest areas exceeding 50 square kilometers, which remained under DENR’s supervision.

In the 1990 Philippine Master Plan for Forestry Development, the Community-Based Forest Management (CBFM) was adopted as a national strategy to ensure sustainable development of forest resources. It unified the various forestry programs and projects implemented in the past 2 decades. However, many of the CBFM areas were either logged-over areas, grasslands, or relatively forested, which require huge capital to develop. The disincentive to small farmers was that, the initial technical and financial support provided by the government was largely inadequate to make them self-sufficient.

### Box 3. Incentives under the CBFMP

- Security of tenure
- Right to use & manage the resources
- Exemption from land use rental
- Exemption from forest charges
- Right to be consulted on government projects in the area
- Authority to enter into contracts or agreements
- Preferential access to assistance & information
- Right to receive all income & proceeds of the area
- Right to contract with private entities
- Right to contract with government entities

The Upland Agroforestry Program (2005) was launched to promote equitable distribution of opportunities, income and wealth in developing agroforestry systems. However, the disincentive is that the smallest area that can be applied should not be smaller than 50 hectares. Farmers are also required to submit proofs of financial and technical capability to undertake agroforestry development, and will have to incur the cost of surveys, mapping and in formulating agroforestry development plans. DENR was entitled to a share of the gross revenue and other benefits from the farm. Given these requirements, it is unlikely that small farmers can benefit from this program. The intention of promoting widespread implementation of agroforestry under this program is thus, selective.

Policy incentives to tree growing had evolved from direct to indirect. The provision of direct incentives was common from 1970s to 1980s but beginning in late 1990s, the notion of incentive gradually shifted to more indirect ones, such as comprehensive land and resource use rights through various land tenure instruments. Security of tenure is perhaps the most significant incentive provided to smallholder farmers.

## Vegetable Farming

The **Crop Insurance Law (PD 1467)** (1989) was enacted to protect agricultural producers against loss of agricultural assets due to natural calamities, diseases and other hazards. This policy embodies direct incentives to vegetable growers, but the disincentive remains in the inability of farmers to cash-out the premium payment, and because of limited funding available to the Philippine Crop Insurance Corporation, it only focused on farmers patronizing formal credits with financing institutions (e.g. Land Bank of the Philippines). In effect, both the crop insurance and government's credit program is selectively serving richer farmers because small farmers do not have the capacity to comply with credit requirements and procedures.

The **Seed Industry Development Act of 1992** encouraged the private sector to engage in research and development (R&D), and in mass production and distribution of quality seeds. Obviously, this policy is more applicable to richer farmers. The gap is that, the services did not trickle down to small farmers, and there was no incentive for using locally-innovated seed technologies, which is more applicable to smallholder farmers.

### Box 4. Incentives of Seed Industry Development Act

- Technical assistance in seed technology, procurement & access to research results
- Tax exemption for imported equipment
- 200% deduction of expenses from research, development & extension activities

The WTO-GATT aims to open up market access worldwide and reduce distortions in world commodity prices. For the Philippines, the major areas covered were the expansion on market access and harmonization of sanitary and phytosanitary (SPS). **Republic Act 8178 on Agricultural Tariffication** provided for the replacement of quantitative restrictions on agricultural products with tariffs. Although it provided multiple incentives (e.g. provision of irrigation, farm-to-market roads, post-harvest facilities, credit, training and extension services, etc.), it contradicted the Magna Carta of small farmers, which protects the products of small farmers. After 10 years of WTO-GATT, the Philippine agriculture sector is still stifling to increase its contribution to the national economy. The key challenge in the vegetable sector is in responding to non-tariff barriers in terms of environmental and health requirements and SPS measures, which are impeding local products to enter the international export market.

The **Agricultural and Fisheries Modernization Act (AFMA)** (1997) was enacted to promote modernization in agriculture and fishery towards global competitiveness. Many of the Strategic Agriculture and Fisheries Development Zones plans that LGUs developed, did not materialize due to insufficient stakeholder consultation, and were very expensive to implement. To encourage agricultural modernization through private investments, AFMA was amended through **RA 9281** (2004), providing an extension of tax incentives to producers importing agricultural inputs and equipments. The extent of its application remains to be seen, but definitely, small farmers did not benefit from the amended Law.

### Box 5. Major provisions in AFMA

- Credit assistance to small farmers & fisherfolks
- Promotes R&D, particularly on irrigation
- Extension services
- Information & marketing support services

**Republic Act 7900 on High Value Crops Development (HVCD)** promotes high value crop production and provides the market orientation of developing the industry. In support of HVCD and AFMA, Pres. Gloria Macapagal-Arroyo launched the "Gintong Ani-High Value Commercial Crops Program" (GA-HVCCP), which harmonizes local initiatives with international market opportunities. The program adopts a major shift towards market-oriented production systems by introducing the "Commodity Producers Linkages with Users" to address the gaps in the commodity marketing systems. It also adopts a "home consumption-led" strategy to promote backyard production of fruits and vegetables. The 5 program components of GA-HVCCP entail many forms of direct and indirect incentives to vegetable producers. However, it requires huge investments, and the only way to make this possible is to generate counter-part funds from LGUs.

### Box 6. 5-program components of GA-HVCCP

- Policy reform, market development & promotion
- Infrastructure support
- Investment & financing
- Technology development, training, extension, & communication support
- Program advocacy, information networking & dissemination

Moreover, the guidelines on **Good Agricultural Practices (GAP)** involve setting of standards on agricultural producers to promote sustainable agriculture based on environmental protection, improved food quality and safety, and improved production techniques. There are direct and indirect incentives attached to GAP, but there are also apprehensions that the newly set international guidelines will marginalize small producers

because of the high costs involved in meeting the standards (e.g. use of new production techniques and more expensive environment-friendly inputs, additional labor and record-keeping requirements, etc.). Documentation is also a problem because many small farmers are uneducated. Without a comprehensive support system, meeting GAP standards by small farmers will remain an exemption rather than a rule.

### Box 7. Incentives under GAP

- Premium price
- Access to market/supply chain
- Product differentiation
- Stabilization of yield/revenue
- Reduction in storage losses
- Reduction in wastage
- Increased in farm assets
- Protection against market externalities
- Subsidies
- Skills improvement
- Recognition

In addition, **Organic Agriculture** was promoted to put premium-value to organically-produced agricultural exports and local consumption products. The potential economic and environmental benefits of organic farming are widely known to farmers, but generally, poor farmers are unwilling to lose their income when yields fall, during the initial adoption of organic farming techniques. Currently, the organic farming sector remains relatively small covering only 2000 hectares or 0.02% of the total agricultural area, making the country a net importer of organic products. An obvious gap of this policy is that, it did not provide direct incentives and support to promote wider adoption of organic farming techniques. Finally, the main disincentive to smallholder producers is the high costs across the market value chain. The main challenge is removing the policy barriers not only at the level of the producer, but within the whole vegetable enterprise.



## Major Policy Gaps

The policies governing the tree sector and vegetable industry are insufficient in stimulating smallholder investment in VAF system. Despite the on-going policy transformation, huge gap exist between the policy intention and the policy in practice. Often, national-level policies have unintended negative effects because their intentions are too general, if not ill-defined. On the one hand, they protect or provide incentives to one sector, but on the other hand, they restrict, undermine or create disincentives to another sector. The Magna Carta for smallholders is a classic example of inconsistencies in government policies. The policy instruments that followed the Magna Carta are partial to the needs and interests of smallholders; the issue is that, since the incentive provisions are not necessarily exclusive to the targeted sector, richer farmers or large holders tend to free-ride, and in the end, benefit more than the smallholders. Not surprisingly, without proper analysis of trade-off, national-level policies tend to undermine one sector over the other, promoting a form of selective development.

Several gaps also exist in policy implementation, in terms of communication, funding mechanism and operationalization. Many national-level policies are either not communicated or poorly disseminated at the local level. Policy implementation suffers from structural and funding constraints. For instance, the "Gintong Ani" program was implemented through the regional field offices of the Department of Agriculture with super-imposed structures, but was hampered with inadequate funding. Similarly, the performance of the Crop Insurance Program was fluctuating since it received limited funding than was promised by the national government — this defeated the purpose of serving small farmers in rural areas. Another issue is the weakness of national level policies in addressing local specificities. National level policies provide a general framework and enabling environment, but are not able to fully address the complex, diverse and unique conditions of smallholders. It was also surprising to find out a "low-level" awareness among government personnel about the Magna Carta for smallholders — very few at least have "heard" about it, while the majority has not heard about it at all.

At least in theory, the policy environment is supportive of VAF system, but is insufficient in stimulating smallholder investments. Incentives for smallholders, albeit limited exist; correspondingly, disincentives persist. Large holders tend to benefit more from national level policies than smallholders, because the former have more access to policy information and can leverage the associated costs of policy implementation. It is recognized that some issues are better resolved through national-level policies, while a number of issues can be effectively addressed by locally-formulated policies. For the vegetable sector, issues on **price regulation and control, commodity protection, reducing costs across the market value chain, non-tariff barriers, and global trade** require national-level policy interventions. Trade and price policies are particularly important because farmer decisions are commonly responsive to price variability. For the tree sector, issues regarding **restrictive policies, transaction costs, land tenure and resource rights, and domestic and international market incentives** are also to be addressed through national-level policies. At the local level, promoting smallholder investments in VAF system requires stronger policy action in terms of improving the **effectiveness of the extension system**, with emphasis on **improved technology provision and support for market linkages and infrastructure**. Where national-level policies do not effectively address the needs of smallholders, locally-crafted policies are needed to offset this gap. The potential of smallholder investments in VAF systems will likely depend on the essential fit between national and locally-crafted policies. Policy linkages between national and local levels need to be established, and policymakers need to mobilize adequate responses at both levels. Finally, the viability of VAF system depends on a whole set of policy environment that both national and local governments can provide. It is therefore a political imperative.

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