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Policy Notes

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Dealing with the soaring price of rice

*Roehlano M. Briones
and Arsenio M. Balisacan*

Rice is the country's primary staple. It is a critical item in the diet of the poor, accounting for as much as a quarter of the incomes of the bottom 30 percent of households. Even in the countryside, which hosts two out of every three poor persons, most households remain net buyers of rice. In recent months, however, the price of rice has surged: the retail price rose from P25.84/kg in January to as high as P38.76/kg in July. While prices have gone down to P36.70/kg by August, the increase is still a huge 42 percent.¹ This bodes ill for the country's poor, whose ranks had already swollen to 33 percent of the population by 2006 (up from 30% in 2003). Due to rising food prices alone, poverty is expected to climb up to 35 percent (Figure 1).²

In response, the government has moved aggressively in the distribution of subsidized

National Food Authority (NFA) rice, cracked down on alleged rice "hoarders," increased purchases of foreign rice, budgeted massive outlays for rice production, and even imposed a temporary moratorium on the conversion of agricultural land.

This *Policy Notes* traces the root of this rice price situation, analyzes the way that the government has responded and is responding to it, and offers insights and suggestions on what should be done.

What got us into this?

There are two sides to the story of the rice

¹ Bureau of Agricultural Statistics (BAS), 2008. Updates on palay, rice and corn prices, August and February issues.

² National Statistical Coordination Board (NSCB). *Philippine poverty statistics*, various issues; Balisacan, A., 2008. Briefing on the rice crisis.

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The authors are Senior Research Fellow of the Institute and Director, Southeast Asian Regional Center for Graduate Studies and Research in Agriculture, respectively. The views expressed are those of the authors and do not necessarily reflect those of PIDS or any of the study's sponsors.

Figure 1. Official poverty incidence and estimated 2008 poverty (projected from food price increases)

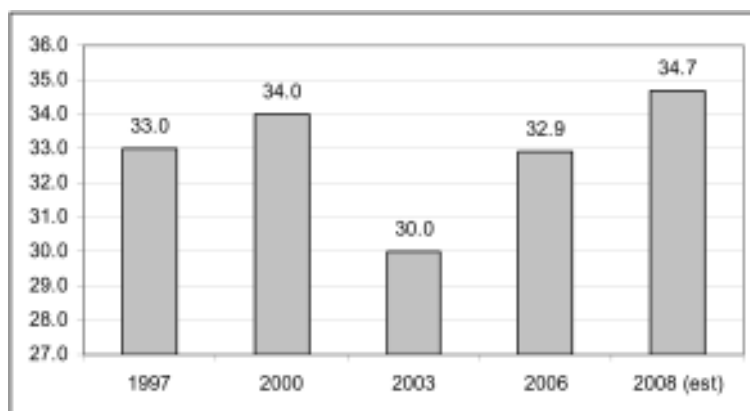
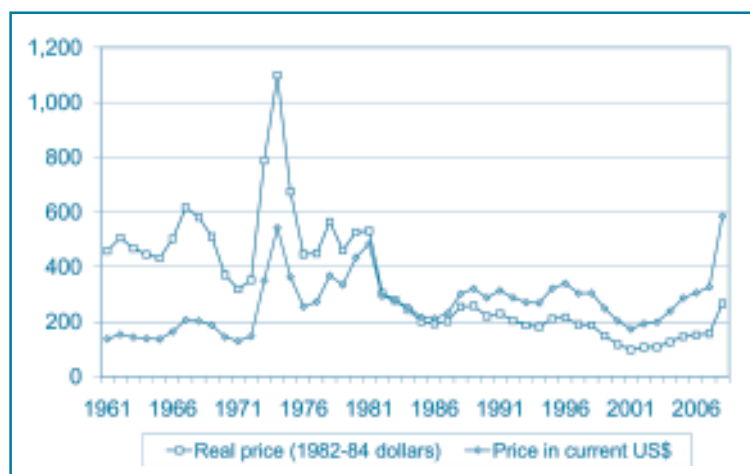


Figure 2. Real and nominal price of Thai rice (5% broken) in 1983 US dollars, 1961–April 2008



crisis. One side is foreign. From 2002 to 2006, imports averaged 14 percent of domestic consumption or about 1.3 million tons yearly, making the country one of the world's biggest rice importers.³ Unfortunately, world prices have soared in recent months. A benchmark Thai rice (25% broken) was selling for US\$869 as of May, about triple its level a year earlier, before easing somewhat in the succeeding months.⁴ As a result of these food price

spikes, mass demonstrations and even rioting had broken out in some poor countries such as Haiti, Egypt, Burkina Faso, Cameroon, Bangladesh, and Indonesia, arousing fears that a similar outbreak may happen here.⁵

Volatility in world markets is far from new. The current episode is a dim reminder of the severe food crisis in 1972 to 1974 (Figure 2).⁶ This was caused by supply shocks, as harvests were ravaged by El Niño while production costs were jacked up by rising oil prices. Normalization of weather, combined with production incentive from the high prices, led to a rebound of supplies, and a retreat of world prices. The ensuing decades have been called the era of "cheap rice."

The year 2001, however, heralded the end of this era, as world prices started their upward trend. The current uptrend, unlike that of the 1970s, is being driven by demand growth, combined with slow growth in supplies. Nevertheless, the levels reached in recent months are abnormally high, and are probably due to short-run imbalances owing to depleted rice stocks, export restraints in major rice-exporting countries, and choices made by

³ Bureau of Agricultural Statistics, 2008. Cereals supply and utilization accounts [online, accessed 10 September]. <http://countrystat.bas.gov.ph>.

⁴ http://www.riceexporters.or.th/default_eng.htm. Accessed September 10, 2008.

⁵ http://www.atimes.com/atimes/Asian_Economy/JE14Dk01.html. Accessed May 15 2008.

⁶ Thai price data from International Rice Research Institute, World Rice Statistics, 2008. <http://www.irri.org/science/ricestat/index.asp>. Deflated by US Consumer Price Index available from the Bureau of Labor Statistics, <http://www.bls.gov/cpi/home.htm#data>, accessed September 10, 2008.

importing country governments (such as the Philippines) to maintain or expand reserves.⁷ One cannot also discount the spillover from financial market developments, given the depreciation of the US dollar and the movement of portfolio investors into commodity speculation.

The country's price stabilization policies allowed the government to protect rice consumers from price shocks in the 1970s; on the other hand, during the cheap price period, protectionist policies were put in place to achieve self-sufficiency and defend rice farmers. The result was a wedge between foreign prices and local prices, which widened in the 1990s. Since the 2000s, that wedge has been thinning as world prices climb. Under today's extraordinary world prices, domestic rice is now competitive with foreign rice (Figure 3).⁸

This brings us to the other side of the story, which is domestic. Reliance on world markets is fundamentally due to a lack of competitiveness of rice production. Rice experts have long been anticipating a food crisis if commodity prices were to rise sharply—an expectation which has sadly come true. There is no dearth of studies diagnosing the rice problem and prescribing policy remedies.⁹

The first set of reasons behind the lack of competitiveness is supply side in nature. The country's agricultural strat-

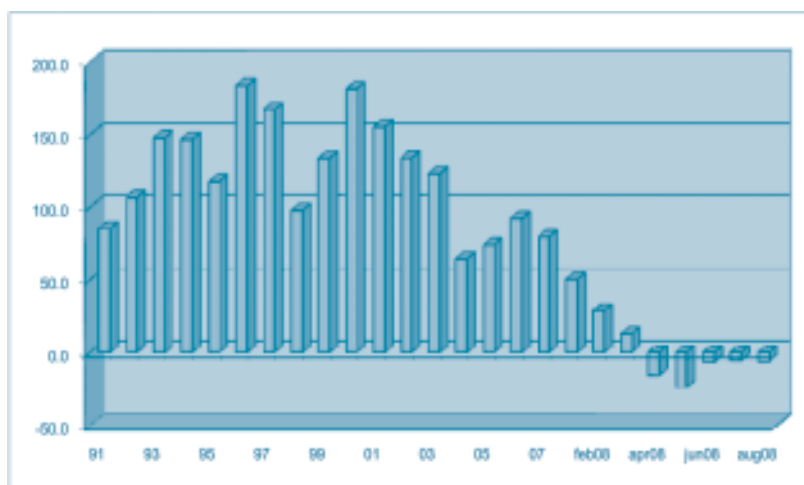
egy had failed to attend to the slowdown in productivity growth, which had been persistently observed from the 1980s and 1990s. This is in stark comparison to productivity improvements in the late 1960s and 1970s, which had led to the brief episode in which the country became a net exporter of rice. There remains a significant yield gap, i.e., shortfall from potential yield. Estimates of the yield gap range from 5 – 6 t/ha per season, attributable to climate, biological constraints

⁷ Food and Agriculture Organization, 2008. *Rice market monitor* XI No. 1. Commodity Markets, Policy Analysis and Projections Service, Trade and Markets Division, FAO.

⁸ Thai price is white broken A5 Super [online, accessed 11 September 2008]. <http://www.fao.org/es/esc/prices/PricesServlet.jsp?lang=en>. Domestic price is from BAS, Wholesale Prices of Cereals Monthly/Annual, <http://countrystat.bas.gov.ph>. Accessed September 11, 2008.

⁹ The most recent compilation of studies is: A. Balisacan, L. Sebastian, and Associates, 2007. *Securing rice, reducing poverty: challenges and policy directions*. Southeast Asian Regional Center for Graduate Studies and Research in Agriculture (SEARCA), Philippine Rice Research Institute (PhilRice), and Department of Agriculture – Bureau of Agricultural Statistics (DA-BAR), College, Los Baños, Laguna.

Figure 3. Difference between world and domestic prices of rice (as a proportion of world price), 1991–August 2008



(poor seeds, weeds, pests), physical constraints (soil nutrients, water management), and socioeconomic constraints (poor cultural practices). Overcoming these constraints can elevate yields by as much as 150 percent.

The second set of reasons is more structural and demand side in nature. Population is growing rapidly, causing demand for staples to outstrip the country's ability to produce at competitive cost, thus necessitating imports. However, purchasing power has stagnated, particularly in rural areas, due to the weak growth of employment and income opportunities both within and outside agriculture. These factors combine to make a significant subset of the poor vulnerable to rising world commodity prices.

Box 1: The FIELDS Program

Elements of the FIELDS program include:

1. expansion of areas planted with hybrid seeds and certified seeds, coupled with location-specific measures such as farm inputs like Bio-N, zinc sulfate, and other soil ameliorants;
2. restoration of irrigation facilities; provision of postharvest drying facilities;
3. planting of certified seeds in 600,000 hectares of rainfed lowlands and low-yielding irrigated areas, which will focus on the priority provinces covered by the President's Accelerated Hunger Mitigation Program (AHMP);
4. third cropping season under the Quick Turnaround (QTA) Program to cover 92,000-100,000 hectares of fully irrigated areas using hybrid and inbred certified seeds;
5. planting of hybrids and inbred certified seeds in restored and newly irrigated areas covering 60,000 hectares.

Source: http://www.da.gov.ph/wps/portal/da/news?%20WCM_GLOBAL_CONTEXT=/wps/wcm/connect/DA+Site/News. Accessed item for April 27, 2008.

Rather than addressing the underlying constraints to competitiveness, the policy framework has been oriented toward shielding the producer from foreign competition through a regime of trade interventions and subsidies. These interventions have "burned a hole" in the public coffers, compromised food affordability for the poor while failing to build a strong domestic production base as a hedge against world price volatility.

How are we dealing with it now?

The policy response to the present crisis may be characterized as a scaled-up version of "business as usual." Massive distribution of cheap NFA rice is focused on the twelve major population centers (Metro Manila, Baguio City, Lucena City, Legaspi City, Albay, Tacloban City, Bacolod City, Cebu City, Dumaguete City, Davao City, Cagayan de Oro, Zamboanga City, and General Santos City). Production support, totaling PHP43.7 billion, adopts the FIELDS strategy, i.e., Fertilizer, Irrigation and rural infrastructure, Extension and education, Loans, Dryers and other postharvest facilities, and Seeds of high-yielding varieties (Box 1). For rice, the plan entails essentially an enlargement of the GMA Rice Program, a program anchored on input subsidies rather than productivity growth.

Subsidies are a quick way to boost domestic production, but fail to address deep-seated productivity problems and impose a heavy fiscal burden. Even before the current spike, NFA had long been a black hole for taxpayer's money, absorbing PHP14 billion in 2007

alone. This year, its subsidy requirement would be much bigger, perhaps by 50 percent. Moreover, commodity-specific subsidies are not cost-effective, given their proneness to leakage and high distribution cost. Neither is targeting toward urban centers the appropriate way to reach the neediest, as incidence and severity of poverty in these centers tend to be far lower than in the countryside.

What is at stake?

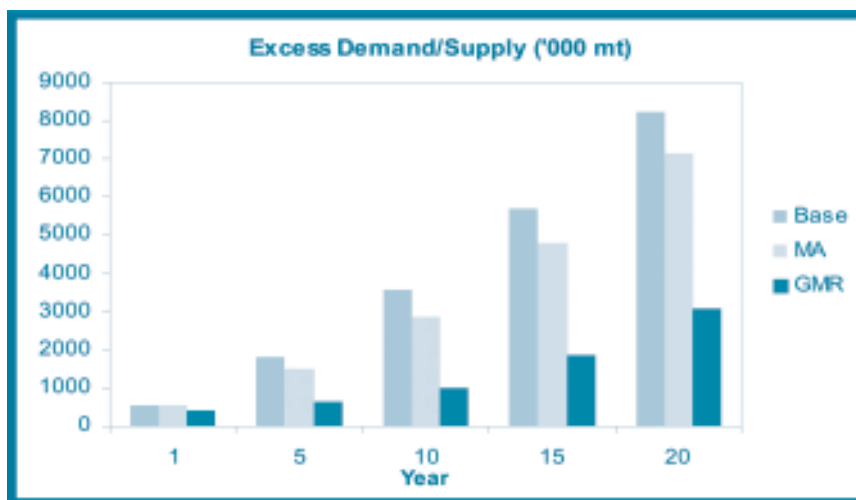
Philippine rice agriculture is at a crossroads, between maintaining “business as usual,” and alternative futures involving: a) a scenario with improved market access or MA (due to progress in international trade liberalization); and b) a scenario with improved market access combined with domestic reforms in governance and investment in agricultural productivity or GMR. A scenario analysis suggests the following:

- Yields, agricultural incomes, and agricultural employment are higher under MA and significantly higher under GMR, compared to business as usual.
- The country’s import requirements are biggest under business as usual but there is a dramatic shift toward self-sufficiency under GMR (Figure 4).¹⁰

What should be done?¹¹

In the short term, the paramount need is to protect food security which entails widening

Figure 4: Excess of demand over domestic supply for rice under alternative scenarios



access to affordable rice, whatever the source, but with funds carefully targeted to the poor. First, with regard to rice trade: high grain prices offer a rare opportunity to dismantle the expensive and inefficient regime of protection, widen access to more affordable rice while maintaining production incentives for farmers. Importation should be opened up to private traders. The rice tariff should be cut drastically, by 50 percent or more. It would also be timely to initiate NFA reform, not just at the operational level (though this is welcome), but more fundamentally, to lay the groundwork for a comprehensive review of its mandate and functions. Second, with

¹⁰ T. Paris and D. Antiporta, 2007. External environment, trade regimes, and policy options. In A. Balisacan, L. Sebastian, and Associates, *Securing rice, reducing poverty: challenges and policy directions*. SEARCA, PhilRice, and DABAR, College, Los Baños, Laguna.


¹¹ This section draws from A. Balisacan and L. Sebastian, 2007. Challenges and policy directions. In A. Balisacan, L. Sebastian, and Associates, *Securing rice, reducing poverty: challenges and policy directions*. SEARCA, PhilRice, and DABAR, College, Los Baños, Laguna.

regard to assistance, the delivery of welfare benefits should carefully be targeted. Existing welfare programs (e.g., conditional cash transfers) can be scaled up, with beneficiary selection incorporating criteria of food vulnerability (i.e., landless farm workers, households earning below subsistence, and so on). Site selection for subsidized rice distribution should be focused on depressed communities and conflict areas.

In the long term, food security should be achieved by addressing the underlying constraints to competitiveness. This involves, first, a set of reforms to create a favorable investment climate in rice trade and rural finance. The NFA should be moved out of active competition with the private sector, focusing instead on its core function of stabilizing food prices, mainly through maintaining buffer stocks. Second, governance should be improved, by rationalizing the national agricultural system as well as by empowering local government units (LGUs), private sector, and civil society in service delivery and monitoring. Third, the agricultural strategy should accelerate productivity growth by returning to the basics of R&D,

extension, and infrastructure. To develop and disseminate appropriate technologies, it is imperative to improve public sector R&D through human resource incentives, upgrading and maintenance of facilities, identification of research priorities and objectives, incorporation of impact assessment, and pursuance of adaptive and participatory approaches. Capacities of local extension personnel should be strengthened and oriented toward client-focused service delivery. Support for irrigation development should involve the rehabilitation of existing systems (rather than construction of new large-scale national systems), expansion of small-scale systems, facilitation of private systems (e.g., shallow tubewells), and institutional development of user associations toward maintenance and cost recovery.

The funding requirements for investing in productivity growth are manageable. Estimates for additional operations and maintenance expenses are about PhP1 billion annually. This is about 125 percent higher than the annual appropriation in 2000–2004, but a fraction of the food security budget being contemplated.

Measures to establish long-term competitiveness of the rice sector would not only boost domestic rice supplies. They would also go far in raising farm incomes, increasing purchasing power of farmers, and triggering a virtuous growth dynamic in the countryside. No less is required for a sustained end to the country's chronic problems of food insecurity and poverty. 

For further information, please contact

The Research Information Staff
 Philippine Institute for Development Studies
 NEDA sa Makati Building, 106 Amorsolo Street, Legaspi Village, 1229 Makati City
 Telephone Nos: (63-2) 894-2584 and 893-5705
 Fax Nos: (63-2) 893-9589 and 816-1091
 E-mail: rbriones@pids.gov.ph; jliguton@pids.gov.ph

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