

## **Trends and Future Perspectives of Organized Farms in Japan**

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## Trends and Future Perspectives of Organized Farms in Japan

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This paper discussed the types of farm enterprises, recent trends of them entry into and establishment of farming business in Japan. The cooperative farm corporations (CFCs) that are controlled by the Agricultural Cooperatives Act have been distinguished from the enterprises that are controlled by the Code of Commerce. Distinctions and characteristics are evaluated along the historical backgrounds. Not many but young willing farmers are increasingly converting their business form into CFCs and expanding business size either by horizontal or vertical ways. Agribusiness enterprises are entering to include the production. However, their interest products are limited. Particularly staple food supply is entrusted much to CFCs and traditional family farms as usual. Emphasis must be placed to encourage CFCs since CFCs play important public roles in the rural community. One suggestion is to make arrangements so that CFCs can join enterprises and work together complementary.

### A. Objectives

The characteristics of Japanese agriculture can be briefly stated as follows:

(a) Characteristics common to Asian countries:

Japanese agriculture is small-scale, family farm managed agriculture, with emphasis laid on rice paddies.

(b) Characteristics of Japanese agriculture different from those of other Asian countries:

As a result of general economic growth, the percentage of part-time farmers has been increasing, and agricultural productivity did not increase significantly, resulting in loss of cost competitiveness with imported agricultural products. The Japanese agricultural sector has been declining.

To put it more detail, the delay in reforming the industrial structure of

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agricultural sector to correspond with the trends of the global market economy resulted in the persistence of part-time farming. The farmers grow older and there is a serious shortage of successors. The area of farmlands used for non-agricultural purposes or left unused has also been increasing, resulting in the deterioration of economic and social activities in the rural communities and a long-term downward tendency of the food self-sufficiency rate in Japan.

Under these circumstances, replacing conventional family farms with enterprise type farms has become an important theme after the WTO legislation has been put into effect. To facilitate this development, the Farmland Act was amended to allow companies to possess farmlands under certain conditions. This amendment was put into effect in April 2001.

This paper will discuss the following topics from the viewpoint of facilitating enterprise types of farm businesses to enter into and/or establish in the agricultural sector:

- (a) definition and types of farm enterprises in Japan,
- (b) recent trends of enterprises entry into and/or establishment in, and
- (c) imaging focal problems, which need to be resolved.

## **B. JSCs and cooperative farm corporations (CFCs): Definition, their roles, and significance in Japanese agriculture**

Why the title of this paper includes the term "organized farm business" must be explained first. In Japan, cooperative farm corporations (express as "CFCs" in short) have been traditionally distinguished from joint stock companies (express as "JSCs" in short) and limited responsibility companies, while the farm operated under either of these management forms has been called "organized farm". JSCs and limited responsibility companies are controlled by the Code of Commerce and have been viewed as the final goal of advances in the form of farm business. On the other hand, CFCs are a form of management, which is operated either by a single farm manager or a group of farmers, and are controlled by the Agricultural Cooperatives Act.

CFC can be characterized as follows:

- (a) it is a form of management organization evolved from the conventional family-based farms since farmers and their family are only eligible to be members, and

(b) there is always agricultural production division as a principal part of business activities which makes use of farmlands owned by the corporation or its members.

In contrast, enterprises are characterized by:

(a) new entry from the non-agricultural sector, and

(b) commonly specializing in livestock production or fresh vegetable and flower productions in facilities, which do not require farmlands.

It is well known that all farmers in Japan are members of multi-purposes agricultural cooperatives. The establishment of CFCs in various forms has been promoted in Japan to allow small-sized farmers to gain economics of scale [1]. The CFCs, jointly founded by farmers, are independent organizations dedicated to earning private profits. Therefore, CFC does not differ essentially from an enterprise on this view. Historically, mutually dependent relationships of the farm households, such as the share-use of machines and facilities among neighboring farms, and mutual assistance in farm tasks at peak farming season have been brought up as the rural community virtue. Such community's traditions were base of the CFCs. Thus the CFC has been viewed as a goal to be attained by these activities.

However, two characteristics compared to enterprises must be stressed:

(a) Mutual trust, dependency relationships, equal participation principle in the village are still important base for rational scheduling of irrigation water delivering, sharing maintenance activities for levee of paddy fields, roads, irrigation facilities and so on. Therefore, rural cooperative spirits are dominating the management of CFCs.

(b) The other difference between them lies in that JSCs are not allowed to possess farmlands, while cooperative farm organizations composed of farmers possessing farmlands are allowed to own farmlands [2]. In April 2001, however, this regulation was amended to allow JSCs to possess farmlands under certain requirements. Thus, the distinction between enterprises and CFCs on this aspect had lost its significance.

Now, let's have a brief overview of the forms of farm organization as classified by the Japanese conventional definition. According to the Agricultural Census for 1995, there were about 6,500 organized farm business management bodies whose business was to sell agricultural products (the custom farm work services organizations were excluded). These organizations were:

- Joint-stock companies (JSCs): 1,000 (500)
- Limited responsibility companies: 2,000 (800)
- Cooperative farm corporation (CFCs): 1,500 (400)
- Agricultural cooperatives or other agricultural associations: 500 (100)
- Non-registered corporate organizations: 1,500 (30)

(Note: The figure in parentheses shows the numbers of organization with annual sales of farm products amounting to 100 million \ or more. 1 US\$=120 \.)

Although organized farm business management bodies have a larger volume of business than the individual farm households, the number of management bodies is much smaller than the number of so-called traditional commercial family farm households, 2.65 million households, (the total farms are accounted for 3.44 million households). Of the total farmland acreage in Japan (4.8 million ha), only about 1% is occupied by these organized farm business management bodies. In recent years, however, the trend has moved toward organized form of farm business management bodies, and the number of such bodies has been increasing gradually.

These trends may be conducted under the policy programs promoting the regeneration of agriculture. After the 1980s, the demands of foreign countries to open the Japanese market for agricultural products increased year after year. Japanese government gradually introduced market-oriented economy by withdrawing government's protective interventions, and began to make use of economic resources of the enterprises to evolve the international competitiveness of Japanese agriculture. Indeed, agricultural policy was changed completely to allow the acquisition of farmlands by JSCs in 2001.

However, it is an important to recognize that, instead of permitting full-scale entry of non-agricultural capital into the field of farmland cultivation based farming sector, the government is:

- (a) encouraging the conversion of CFCs and traditional family farms into JSCs,
- (b) arranging so that CFCs and farmers initiated JSCs can enjoy the following four types of supports or benefits from non-agricultural enterprises.

Four types of supports or benefits are:

- (a) supply of skilled human resource with high capabilities of management,
- (b) reputation, credibility, and funds for expanding business activities while mitigating management risk,
- (c) advanced technology, market information, and forming transaction network,

and

(d) opportunities for employing young personnel from the non-agricultural sector by offering improved working conditions.

Remarks

[1] After the World War II, Japanese government took three measures, the land reform, the enactment of the New Agricultural Cooperatives Act, and enactment of the Basic Agricultural Act of 1961. These measures were aimed at establishing family-oriented independent and stable farm management bodies whose standard of living would be comparable to that of non-agricultural households. Meanwhile, the entry of non-agricultural companies was strictly prohibited. Under this policy direction, JSCs were not allowed to own farmlands.

[2] The industrial sector had long demanded approval for JSCs to acquire farmlands. But the farmers' organizations had opposed for the following reasons:

(a) speculative acquisition of farmlands and uncontrolled use of farmlands for the purposes other than agricultural production might be prevailed, and

(b) it was highly probable that the allocation of irrigation water rights for the paddy fields and the utilization of farmlands within a village, which had been performed in reasonable order on the basis of conventional agreement among farmers, would be collapsed.

In addition, farmlands are owned by private individuals though, there is a social consensus that farmland is a kind of quasi-public assets which is only managed sustainably by the farmers, and, thus, supply food staffs stably.

**C. Entry of enterprises into agriculture**

In the past, JSCs were not permitted to own farmlands and, for this reason, they could not enter the land cultivation based agricultural production business. Over the past 20 years, however, the entry of enterprises into agriculture-related businesses has been increasing. These enterprises were engaged in the contract-based purchase and processing and/or distribution of agricultural products with the sales of packaged materials and technical instructions.

In recent years, they invested capital and expanded their businesses to include the direct production. The main activities of these enterprise farms are:

(a) organic products (or products produced with essentially less chemical

fertilizers and pesticides),

(b) vegetables and flowers cultivated in controlled facilities or by using hydroponics,

(c) cut & ready vegetables, tomatoes for processing, herbs, etc., and

(d) poultry, egg production and raising swine.

These types of production activities of the enterprise can be characterized as follows:

(a) Vegetable and flower productions and livestock production in controlled facilities are the major business activities of the enterprises. They do not use farmlands. Instead they produce high added-value products made in specialized facilities and the kinds of their products are therefore limited. Producing these products requires an advanced and intensive technology and large investments in facilities. These products are economical for enterprises which produce them on a large scale in factories where they can control production volume, timings of harvest, and quality using the sophisticated technology they have developed.

(b) Within these enterprises, the vertically integrated system, which was formed for conventional contract-based processing and/or distribution business, developed well-coordinated technology and tied sales networks. Their products, with standardized quality and in precisely designated amounts, are distributed directly to large-scale clients such as major super-markets, convenience stores, chain-restaurants, etc., thus significantly saving distribution costs and management risks.

(c) Although JSCs now can own farmlands, there is no evident trend for enterprises to enter the field of land cultivation based productions. JSCs seem to be engaged only in particular highly profitable areas. Thus, for the time being, CFCs and remaining traditional family farms will continue to play a major role in

- (1) the production of rice and other grains, which are basic and traditional food for the Japanese dietary but return only low profits to producers,
- (2) the productions of land cultivation based vegetables and animal feed, and
- (3) dairying and beef cattle raising sector, etc.

In other words, the food supplies of farmland cultivation based production sectors will continue to be done by the CFCs and traditional farms.

(d) In recent years, enterprises have begun to actively enter into the business of importing land cultivation based vegetables and fruits, which are produced in developing countries at their own initiative. That is, trading companies and super-

markets are transferring the techniques and varieties for producing certain products favored by the Japanese to nearby countries with low wage and commodity price levels, in order to produce them at low cost and import them into Japan. This is called "developmental importation". It is feared by domestic farmers that this business might compete with domestic agriculture and suppress its growth. However, it is widely viewed these countries as the principal sources of stable food suppliers in the future.

#### **D. Two directions of the development of CFCs**

Very recently, many traditional small size family farms, aged farms and part-time farms, are retiring and are being replaced by CFCs. In deed, a number of individuals who have well intention and management capabilities are establishing CFCs and expanding the size of business. Thus, social stratification process has begun in agricultural sector.

According to a survey conducted by the Ministry of Agriculture, Forestry & Fisheries (MAFF), the main reason for establishing CFCs was the intention to expand the size of farming business. That is, CFCs are primarily interested in obtaining high profits from "economies of scale" created by the accumulation of farmlands, capital, management capability, labor, technology and marketing networks.

The expansion of business size is occurring in two directions:

- (a) horizontal expansion (enlarging the business size in production) and
- (b) vertical expansion (creating new business sectors such as the processing, packing, and direct sales of products).

According to the MAFF survey mentioned above, employers often stated that the merits of establishing the CFCs were ease in recruiting employees from non-agricultural fields, and increased social credibility. However, disappointedly, only few employers, however, listed profitability. Moreover, there were a considerable number of responses saying that forming CFC had no advantages. In fact, another survey of the performance of CFCs revealed that a little more than 30% of all corporations surveyed were in the red. The greatest problem, which these red-ink organizations faced, was the shortage of funds. Failures in expanding marketing channels and in reducing costs were also pointed out to be associated with the losses.



Considering these survey results, an important issue for the future is how CFCs, founded by conventional farmers, can be brought into cooperation with enterprises which is intending to enter the field of farm production.

*1) Horizontal expansion of CFCs.*

Of all farmers in Japan, about 90% are weekend farmers. The average age of these farmers is rising, and they often have no successors. With retirement approaching, they cannot make further investments to renew the machines and facilities used for their farming. They manage to continue farming by entrusting near-by-younger farmers with farm works which require machines. Farmers who cannot continue farming lease their farmlands to others.

However, farmland is divided into small, scattered, and disconnected lots, which are common features in Asia. This feature is unfavorable for land leasing, because it impedes efficient farm works on an expanded size. For this reason, there is no effective farmland lease market, and farmlands that cannot be cultivated by their owners tend to be left unused. This would unfavorably affect the regional economy and reduces the domestic food self-sufficiency and the land-preserving function of farmlands, leading to national welfare loss.

To facilitate collective accumulation of farmlands into farm complexes, which can be cultivated more efficiently than scattered small lots, an independent agency coordinating sale and lease farmlands and allot the custom works has been established in each village. This is called the Farmlands Utilization Coordinating Committee of Village. Under this system, CFCs and farmers can expand the size of business by renting nearby farmland lots collectively. Existing cooperative system in the village gives a good motivation for establishing CFC for willing farmers that allow a larger scale of farm business.

*2) Vertical expansion of CFCs.*

Another direction of development of CFCs is vertical expansion, which involves processing and distribution of their own products (including purchased products from nearby farms on a contract basis). The kinds of products that can be handled by the processing business is limited by the necessity of high production skills, large investment into facilities, and restrictions imposed by the Food Sanitation Act and other statutes related to environmental preservations. Despite these limitations,

the food product processing business is expanding.

The produced and/or further processed products are retailed to consumers or wholesaled directly through the channels of the producer's stores, the food processing companies, super-markets, chain restaurants, and even through the internet e-commerce sale. This development follows the intention of obtaining added value by incorporating processing and sales activities into the producers' own business. A condition, however, for success in the direct sales business is that the products handled must be differentiated such as organic products or non-GMO products produced and marketed through the identified supply channels.

The vertical expansion of CFC makes it possible for its manager to become independent of the agricultural cooperative. Now, it is doubted that the agricultural cooperatives, which played a principal role in marketing agricultural products in the past, are actually needed or not.

#### **E. Conclusions: Future strategy and appearing issues**

*1) Retirement of elderly part-time farmers and establishment of CFCs by young and willing farmers for their survival.*

As low-price imported food products expand their market share in Japan, it is becoming increasingly more difficult for part-time family farms to continue. Not many but young full-time farmers are now expected to play an important role to manage entire farmlands in the village. It is a social interest that these willing farms realize high productivity and continual stable farm business with improved technology and management ability by expanding their business size to an appropriate scale either in horizontal or vertical directions. CFC and/or JSCs meet to these purposes. We expect drastic changes in the type of business form will occur and reconstruct the organization of Japanese agriculture.

*2) Entry of JSCs into agriculture vs. establishment of CFCs by farmers.*

Enterprises are now legally permitted to own farmlands, although at present their commitment is confined to non-farmland cultivation productions. Instead, agricultural products whose productions require farmlands have increasingly been imported from foreign countries, and this business (developmental importation) is now the greatest threat to domestic agriculture. The production of basic foodstuffs (rice, etc.) and animal feedstuffs, which would not expect tremendous productivity

improvements within some future period, owes much to CFCs and traditional farms.

### *3) Issues for the future.*

(a) From now on, agriculture in Japan will be increasingly exposed to the influence of the global economy under the WTO legislation, as well as to social demands for producing food products using less chemicals, adopting an environmentally friend production technology. New business chances may be obtained by responding appropriately to such social demands. However, it needs higher management abilities. It is now needed to appeal to JSCs and CFCs, so that managers with adequate capabilities can be invited, and that these managers can exert their capabilities sufficiently.

(b) It is not correct to regard JSCs entering agricultural industry as being in opposition to CFCs founded by farmers. There are many aspects in which these two forms can be complemented each other. It is desirable that these two organization forms specify their fields of activity and establish an agricultural industrial system under which they can complement each other, and cooperate when necessary to advance business activity. One suggestion is to make arrangements so that enterprises can join CFCs. Both sides can surely obtain benefits.

(c) The presence of JSCs and CFCs will inevitably cause themselves to be independent of the traditional agricultural cooperatives. Reconsideration concerning to the roles of agricultural cooperatives is required.

(d) The CFCs are economic organizations dedicated to earn private profits though, profits might not be high enough because of its nature, namely land cultivation based production. However, staple food supply and, therefore, the food security of the nation is entrusted much to CFCs (and to traditional family farms). Recognition that we are sharing social benefits of CFCs will help to get national consensus for government supports that encourage qualified farm managers or groups of managers to establish organized farms. Expected social roles of them are as follows:

- (1) supply of the staple foods needed in this country and prevention from further deterioration of the productivity,
- (2) prevention of farmland abandonment, thus contributing to preserving the environments, protecting natural landscape, etc., and
- (3) maintain job opportunities for people living in rural districts, and stabilization of the local economy.

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