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PHILIPPINES

PL - 480 TITLE I PAPER

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ANE/DP - March 1987

Acknowledgements

This paper benefitted greatly from extensive comments by David Alverson and from information provided by Catalina Jensen. I appreciate the support and information provided by the staff of the AID Mission in Manila, particularly the economics office, the program office, the agriculture office and the director's office. In Washington, Dick Fraenkel and the ANE/DP secretarial staff deserve credit and thanks for their contributions. The views expressed in this paper are those of the author.

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INTRODUCTION, SUMMARY AND CONCLUSIONS

This paper examines the PL-480 Title I program in the Philippines, from the standpoint the fit between the program and the economic/developmental situation. It is one of a set of papers on Title I programs in various countries being prepared by the ANE Bureau. The paper deals mainly with the Title I program that was initiated in 1985, and secondarily with the follow-up program in 1986.

The general outline for this set of papers is attached. The Philippines Study pays particular attention to two topics-- the choice of commodities and policy dialogue-- since these aspects of the program generated the most interesting issues and problems. Local currency programming issues are dealt with only in passing, because the 1985 program has not generated local currencies. Agricultural performance and policy issues are discussed in the context of policy dialogue, which addressed some of the key issues pertaining to markets for food and fertilizer. Performance and policy with respect to export crops are not discussed.

Basic Objectives

The basic objectives of both the 1985 and 1986 programs were to provide assistance and support to GOP (Government of

Philippines) efforts at structural adjustment, by providing financial (balance of payments and budgetary) support and by supporting policy reforms that would promote structural adjustment through increased efficiency in various agricultural markets.

Commodity Selection

The FY 85 program provided $40 million of rice to the Philippines while the FY 86 program provided $35 million of wheat. The selection of rice had several negative effects. First, the Philippines enjoyed a very good rice harvest in 1985, and did not need rice imports anywhere near the overall level ($110 million) that occurred. From the GOP standpoint, it is not clear to what extent the large imports of rice in 1985 were due to a miscalculation about rice production, versus considerations of a politically appropriate buffer stock in anticipation of possible elections. Currently, rice stocks are still very high, with growing risk of spoilage.

Second, the decision to use PL-480 funds for rice rather than wheat (which was imported from the US under CCC) significantly reduced the value of the resource transfer to the Philippines because US rice was much more expensive than rice from alternative sources. The cost to the Philippines of this decision was about $17.5 million.

Third, once the GOP (or more precisely the National Food Authority, NFA) had requested rice, pressure from US rice interests to push ahead with an all-rice program became intense. When the GOP wanted to switch to other commodities in May 1985, they were told that rice was the only possibility, despite evidence by then that a good rice harvest was in store. This also strained the policy dialogue by putting pressure on the country-team not to let disagreement on the self-help measures stand in the way of US rice exports. US wheat interests also weighed in on self-help measures pertaining to wheat imports. There is every indication that NFA readily exploited this pressure in resisting the self-help measures.

Adjustment Problems and Policies

The GOP was apparently determined to import significant quantities of rice in 1985, so that the PL 480 program did indeed provide additional foreign exchange rather than additional rice to the economy. The issues are whether the balance of payments situation and the policy response of the GOP merited BOP support, and whether policies directly affecting the productivity of foreign exchange provided for effective use of BOP assistance. The balance of payments situation and adjustment problems facing the Philippines since

1983 certainly have provided a strong justification for balance of payments and budget support from the standpoint of need. Whether broad GOP adjustment efforts merited BOP support is less clear-cut, because of lackluster performance in implementing structural reforms and exchange rate policy. However, difficult fiscal and monetary policies were implemented, which were successful in sharply reducing inflation and the current account deficit. These gains in terms of stabilization suggest that the GOP's broad adjustment efforts did indeed merit support.

On the other hand, specific policies in the market for foreign exchange-- the resource provided by PL 480-- did not provide for effective use of foreign exchange. The exchange rate remained overvalued, (indeed, the real effective exchange rate appreciated) because of excessively tight monetary policy and manipulation of the ostensibly freely floating exchange rate. Further, import restrictions and regulations were intensified, to the detriment of an efficient pattern of imports.

Policy Dialogue

The policy dialogue effort in the Philippines during 1984 and

1985 was extraordinary in several respects, and the FY 1985 Title I program assumed a pivotal role in this effort. The specific self-help measures included:

-- Lifting of controls on retail prices of milled rice.

-- Opening the importation of wheat to full participation of the private sector, in lieu of an NFA monopoly.

-- Opening domestic distribution of flour to full participation by the private sector

-- Divestiture by NFA of all of its stabilization and trading activities except those related to grain price stabilization

-- Liberalized importation and domestic distribution of fertilizer.

The main questions have to do with the rationale for each reform; the "additionality" of the reform (was it attributable to the PL 480 program or would it have been adopted in any case); the implementation of the reform; and the impact.

While additionality is inherently difficult to verify it appears unlikely that any of the reforms would have been implemented in 1985 without the stimulus of the policy dialogue surrounding PL 480. In particular, neither other donors nor the IMF were making assistance conditional on these measures.

The rationale for rice price decontrol was to improve incentives, and improve the framework for establishing incentives to producers. Implementation was satisfactory, and incentives to producers have been adequate, judging by production levels. However, an effective system for grain price stabilization needs to be established, a goal of more recent PL 480 programs. NFA's capacity to enforce support prices was weakened by abolition of the wheat import monopoly, and needs to be strengthened.

The rationales for the wheat and flour provisions were to deprive NFA of monopoly power and enhance the role of market forces, ultimately leading to cheaper and more readily available flour. Implementation of the wheat import provision was unsatisfactory under Marcos, leading to conflict and controversy not only between the US and the GOP, but within the USG, because of a clash between market development concerns and policy dialogue concerns. Implementation of both measures by the new government has been satisfactory. However, it appears that domestic flour prices significantly exceed world prices, and that the market for wheat flour is not competitive. Instead, the effect has been to transfer monopoly power from the public sector to the private sector, where it has been fully exploited. Ultimately the key to this problem is effective competition from imports of flour.

The rationale for the divestiture provisions was to diminish the role of NFA in retail and other activities, which had been at the expense of the private sector. Implementation has been slow, but has accelerated under the new government. The number of retail outlets has fallen sharply.

The rationale for the fertilizer provisions was to lower the price and improve the availability of fertilizers. The market for fertilizers has been significantly, though not completely liberalized. The effects have been impressive. Margins between domestic and world prices have been reduced and usage is up, both by substantial amounts. However, production and trade are influenced by GOP investments in both domestic and foreign production facilities, and further work needs to be done to improve the market for fertilizers. This has also been a goal of more recent Title I discussions.

Apart from examining each of the policy reforms, the study also looks at some of the more interesting aspects of the policy dialogue and the process through which it evolved. This discussion is not easily summarized, beyond what emerges in the conclusions.

Conclusions and Issues

The PL 480 program in the Philippines has been intended to provide financial support to the country and to promote policy reform.

For purposes of providing financial support, the choice of rice for the 1985 program was regrettable because the higher price of U.S. rice negated much of the concessionality of the resource transfer. While the program contributed balance of payments support, the contribution was less than would have been the case for wheat, by virtue of the relatively high price of U.S. rice compared with other sources. Further, owing to high stocks the rice has not (as of this date) been sold, so that no budgetary resources have been generated. The choice of wheat in 1986 made much more sense.

The most remarkable aspect of the PL-480 program has been the policy dialogue associated with it:

-- The policies addressed were substantive and significant, affecting some of the major determinants of incentives to farmers in the Philippines.

-- These important policy measures have not proved to be one-step actions. Despite significant progress much remains to be done in the area of price stabilization for domestically produced food grains; promoting efficiency in markets for wheat and wheat flour; lowering prices and improving availability of fertilizer; and divestiture of NFA assets. A continuing role for the Mission in these areas is desirable.

-- The self-help measures provided a very useful vehicle for agriculture policy dialogue. They facilitated policy discussions in connection with ESF and DA programming, where more direct linkage and conditionality were not possible.

-- For purposes both of financial assistance and policy dialogue, U.S. agricultural market-development concerns seriously hampered the effectiveness of PL-480. Once the rice lobby was mobilized, it was impossible to switch to a commodity such as wheat, which would have been of much greater value for the Philippines. Second, negotiation of the self-help measures was made more difficult by the pressures from both wheat and rice interests. To the extent that PL-480 is not really a discretionary resource, its effectiveness as a policy dialogue tool is correspondingly limited, as long as leverage is an important aspect of the policy dialogue. Finally, agricultural market-development concerns reinforced GOP efforts to sabotage implementation of the wheat import liberalization measures, and still pose a potential barrier to efforts to promote competition in the market for flour.

-- The experience in the Philippines in 1985 demonstrates both the opportunities and the limits for leverage. The fact that the U.S. placed a high priority on policy reform and was willing to withhold resources (or curtail future resource levels) was crucial in getting the reforms approved. However, the Marcos government readily took actions to sabotage some of the reforms, which it opposed in the "implementation". This called for persistent monitoring, which ultimately and inevitably proved to be a losing battle. The implication is that there is little to be gained by compelling a government to implement a reform to which is is not really committed. The contrast in implementation between the former government and the current government has been striking.

-- Even with a cooperative government, much remains to be done. There are complex, difficult issues surrounding each of the reforms. This does not mean that policy reforms need to be studied to death before any action is taken. But it does imply a need for a continued presence and interest (as opposed to a new reform agenda each year) and a significant allocation of financial and human resources.

-- The apparent outcome of the wheat/flour privatization reforms has been essentially a transfer of monopoly power from the public sector to the private sector, and even higher prices for consumers of flour, despite stable wheat prices. This is in sharp contrast to the fertilizer reforms, where competitive forces are much greater and prices have moved favorably. This suggests (or confirms) that beneficial economic effects of privatization depend crucially on whether private firms are exposed to competitive market forces.

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1. Basic Objectives.

Both the FY 1985 and FY 1986 PL-480 programs were designed to provide assistance and support to GOP efforts at structural adjustment. This goal was to be accomplished by providing balance of payments support and by supporting policy reforms that would promote adjustment through increased efficiency in various agricultural markets.

The context in which the FY 1985 program was launched was one of economic and political crisis in the Philippines, precipitated by the assassination of Benigno Aquino in August 1983. In the face of a mounting communist New Peoples Army threat, the U.S. was concerned with promoting economic and political reforms without which democratic institutions and U.S. strategic interests would be imperiled. A high-level review of U.S. policy in the Philippines led to a strategy in which the U.S. would provide extraordinary levels of assistance if and only if the GOP would undertake economic reforms on a scale commensurate with the depth of economic crisis. PL-480 was part of the resource package.

The FY 1986 program was also part of a broader U.S. effort, in this case to demonstrate support for the Aquino government and the economic and political reforms it stands for. At the signing of the agreement, Finance Minister Ongpin expressed appreciation for the timely and needed balance of payments and budget support assistance embodied in the Title I agreement and for the USG's expression of strong support for the Aquino Administration. Supporting documentation also stressed the political and balance of payments/budgetary objectives of the program, and emphasized the self-help measures contained in the agreement, which would further the agricultural reform initiatives that originated in the FY 1985 agreement.

2. Commodity Selection

The FY 85 program eventually provided approximately 138,000 metric tons of rice, worth about $40 million. There has been considerable controversy about the selection of rice. This section reviews the chronology of events that led to the selection of rice, and discusses the issues raised by these events.

The Philippines was an exporter of small quantities of rice from 1977 to 1983 although it is not clear that these exports were profitable to the National Food Authority (NFA). Because of a severe drought during 1984, the GOP imported 190,000 MT of rice, worth $42 million.

The original request for PL 480, submitted in November 1984, was for $50 million in wheat and $15 million in rice. The rice imports were justified by "the series of calamities" including typhoons, that had hit major rice growing areas, but were expected to result in a need for continued imports.

At that time, AID's FY 1985 budget contained no Title I allocation for the Philippines. In early CY 1985, the Embassy and USAID secured Washington agreement for a $40 million allocation, based on policy dialogue and balance of payments arguments. The commodity composition was left unspecified. In January 1985, the Mission paper on Agricultural Policy Reform cited "current estimates for a milled rice deficit of 400 to 600 TMT". (The eventual level of rice imports for 1985 was 538 TMT.)

In early April, the Agriculture Attache reported to the Ambassador that NFA wished to convert the earlier (November) request for PL-480 to all rice, since wheat imports could be covered under CCC. According to the communication, the PL-480 rice (estimated at the time at a value of $50 million) would cover roughly 40% of the 400 TMT (or more) import requirement, with the rest coming from Asian sources (Indonesia, Thailand, PRC). The report also mentioned that the head of NFA would make this change known through the Philippine Embassy to the U.S. rice millers, in follow-up to their visit to the Philippines that had taken place in October 1984.

The report did not consider the fact that CCC credits are non-concessional, nor did it consider whether rice could be brought in under CCC. Subsequent GOP correspondence indicated that the President himself approved an all rice program on April 18, just after approving the policy reforms to be self-help measures under the FY85 PL 480 program.

During the remainder of April and May, there was extensive back and forth concerning the self-help measures. On May 17, the Mission in a conversation with officials of the National Economic and Development Authority received confirmation that the GOP still wanted all rice. On May 24, the Agriculture Attache sent in the Bellmon determination, which documented the 400,000 MT rice import requirement, of which PL-480($40 million) would cover about 138,000 MT.

Shortly thereafter, on May 30 NEDA Director General Valdepenas sent a letter to the Mission requesting a change in the program to 50% wheat, and 50% rice, "in view of recent reports on the improved outlook of rice supply in 1985". The Mission passed this request on to Washington. The response was that the program had to be all rice or nothing, because of the domestic political pressure on the administration to promote rice exports. Accordingly, on June 8, Valdepenas rescinded the request to change the commodity composition of the program, citing Marcos' explicit April 18 decision to use PL-480 for rice.

During this period, strong conflicts emerged between the different constituencies for PL-480, and between the associated purposes for the program. According to authoritative Mission sources NFA, in its efforts to avoid the policy reforms, mounted a skillful lobbying campaign which took advantage of domestic U.S. pressures in both the rice and the wheat sectors to promote U.S. exports, in hopes that the U.S. would relent on the policy reforms in order to move commodities. On June 4, the U.S. Agriculture Attache in Bangkok reported that NFA had contacted the Thais about an additional 100 MT of Thai rice, because of doubts whether the PL-480 agreement would go through, in view of disagreements on policy reforms. This touched off sharp pressures from the U.S. rice lobby, including a June 17 cable from Congressman Breaux of Louisiana to the Ambassador urging speedy negotiation of the Title I agreement. At the same time NFA helped mobilize the U.S. wheat lobby, by indicating that cessation of the NFA monopoly on wheat imports (one of the policy reforms) might result in declines in U.S. wheat exports to the Philippines. This led to a speech by Senator Melcher on July 15, which claimed that the U.S. had sought to promote economic reforms in the Philippines at the expense of U.S. rice and wheat markets there, an argument which was later rebutted by Senator Lugar.

The GOP apparently also was subject to conflicting internal pressures, judging from the available correspondence. Apart from NFA's resistance to reforms, which were being pushed within the GOP largely by NEDA and the Prime Minister, it was clear to at least some GOP participants that U.S. rice was relatively expensive, and that from a BOP/financial standpoint PL-480 wheat would be the more valuable commodity to bring in under P.L. 480.

On July 1, Valdepenas, Minister of Agriculture and Food

Salvador Escudero, and NFA head Jesus Tanchanco sent a Decision Memo to President Marcos which referred to earlier memos and an apparent Marcos directive (presumably subsequent to the April 18 decision) to "get other commodities." This note addressed the fact that U.S. rice was priced much higher than rice from other sources; however, they pointed out that the concessional terms brought the cost of the U.S. rice below alternatives. Further, the memo pointed out that the U.S. had stated that only rice was available. Finally, they argued that rice would be "good PR with the U.S. government, especially now that the influential U.S. Rice Millers Association has set aside the required volume to meet the GOP request." Marcos approved the decision to stick with an all-rice PL-480 program.

As it turns out, the selection of rice had several negative effects. First, the Philippines enjoyed a very good rice harvest, and did not need rice imports anywhere near the overall level (538 TMT) that was obtained. It is not clear to what extent the large imports of rice were due to a miscalculation about rice production, versus considerations of a politically and economically appropriate buffer stock. Currently, rice stocks are still very high, with growing risk of spoilage. Further, another good harvest is expected. There is a general perception currently that Marcos "foisted" excessive rice imports onto the economy.

Second, the decision to use PL-480 funds for rice rather than wheat significantly reduced the value of the resource transfer to the Philippines, because U.S. rice was much more expensive than rice from alternative sources. For instance, U.S. rice was 75 percent more expensive than Thai rice. Only the grant element of concessional PL-480 financing made it less costly. Compared with the option of importing wheat under PL-480, and rice commercially, the decision to go with rice under PL-480 meant a sacrifice of $17.5 million by the Philippines, the amount of the overall grant element ($22.5 million in a $40.0 million program, about 55 percent) foregone by buying from a more expensive source.

Third, the decision to import rice put increased pressure on the policy dialogue, both time pressure (because rice had to move earlier than wheat) and congressional pressure. This threatened to make a supposedly discretionary resource non-discretionary, at considerable expense to its usefulness as a policy dialogue tool.

On the positive side all documentation (including GOP letters and memos) indicates that the GOP was determined to buy rice to build up stocks, so that the PL-480 provided a commodity which would have been imported anyway, and thereby provided additional foreign exchange (which was the intent of the program) rather than additional food. However, wheat would have served this same purpose more effectively.

Finally, it is clear that from the standpoint of U.S.

commercial interests, the decision to import rice under PL-480 was advantageous.

The FY 1986 agreement aimed from the beginning to provide wheat, approximately 267,000 MT with market value of $35 million. the UMR (Uniform Marketing Requirement) for wheat was reduced from 794,000 MT to 400,000 MT, facilitating the balance of payments contribution of the PL-480.

3. Adjustment/Foreign Exchange Policies

Since the FY 1985 PL-480 program was intended to help the GOP cope with its adjustment problem by providing foreign exchange in support of adjustment efforts, it is important to consider whether the overall BOP situation and adjustment efforts have merited support; and whether trade and exchange policies were conducive to the effective use of foreign exchange.

First, the balance of payments situation and adjustment problems facing the Philippines since 1983 certainly have provided a strong justification for balance of payments support from the standpoint of need. The Philippines is recognized as one of the 15 or so major debtors in the developing world. Indicators such as debt to GNP ratios suggest that the burden of debt in the Philippines exceeds that of major debtors such as Brazil, Mexico, Argentina and Peru. Second, while the Philippines dramatically reduced its current account deficit during 1984 and 1985, this improvement was achieved at a cost of a 10 percent decline in GNP over that two year period. Accordingly, considering the adjustment problem as one of achieving a sustainable BOP position while maintaining growth of income and output, the Philippines adjustment problem was (and is) clearly a severe one.

Whether broad GOP adjustment efforts merited BOP support is less clear-cut. On the positive side, the GOP finally reached agreement with the IMF on a 18-month stand-by arrangement in December 1984 after prolonged negotiations which lasted more than a year. The agreement contained not only stabilization measures but also structural policy reforms in the areas of taxes; sugar and coconuts; public financial enterprises; import liberalization; and public investment. During the course of 1985, the GOP remained on the whole in compliance with the arrangement, although several reviews and tranche releases had to be delayed. Performance on the stabilization measures was better than for the structural measures. Indeed, monetary policy was tighter than required by the program, contributing to higher real interest rates and an overvalued exchange rate. This helps account for the large (5 percent) decline in GNP during 1985. The program was successful in dramatically reducing inflation as well as the current account deficit. The program failed in maintaining income and output largely because of lackluster efforts at structural reforms, overly tight monetary policy, and manipulation of the ostensibly freely floating exchange rate. More broadly, the basic orientation of the government towards cronyism rather than market forces remained. Finally, high and mounting uncertainty about the future constrained private investment in particular. Gross domestic capital formation fell by about 50 percent from 1983 to 1985. The share in GDP fell from 27.5 to 16.6 percent. During the same period, private investment declined by about 42 percent.

Overall, the fact that the GOP remained in compliance, albeit grudgingly, with a comprehensive, very difficult IMF program suggests that adjustment efforts did indeed merit BOP support.

Specific policies in the market for foreign exchange did <u>not</u> effectively promote efficient use of the balance of payments resource that PL-480 was supposed to provide. First, the exchange rate, though ostensibly freely floating, was being manipulated and maintained at an overvalued rate during the course of 1985, by the "Binondo Central Bank" under the guidance of Roberto Ongpin, Minister of Trade and Industry. For 1985, the peso <u>appreciated</u> in real effective terms by about 10 percent compared with 1984, a move which entailed a corresponding loss of competitiveness.

Second, extensive foreign exchange and import controls were reintroduced prior to the IMF agreement. According to IBRD reports, the list of restricted goods expanded to cover about 25 percent of total imports by the end of 1985. This tended to distort the allocation of imports away from economically efficient patterns.

With respect to 1986 the Philippines' need for BOP support was as strong as in 1985. The Philippines still faces a severe adjustment problem in terms of reviving economic growth without running into balance of payments constraints. While foreign exchange reserves are currently at a comfortable level in terms of months of current imports, economic activity and import demand have been at very depressed levels. The debt burden is still very great.

With respect to adjustment efforts, the new government liberalized about 75 percent of the items that had been scheduled for liberalization in 1986 under a program formulated in 1985. Further the GOP modified Central Bank prior-approval procedures in June 1986. The exchange rate depreciated significantly (22%) in real effective terms during 1986, although it is still considered overvalued.

More broadly, the GOP reached an agreement with the IMF in October 1986 on a growth-oriented adjustment program that includes both stabilization measures (fiscal and monetary policies) and structural reforms, including most importantly exchange-rate flexibility, trade liberalization, tax reform, and reforms of public enterprises. In reaching a judgment about whether broad adjustment efforts merit support, much depends on actions to be taken over the next months. The stated approach of the new government is sound and it is so far on the right track, however, major steps are still to be taken, and there is considerable resistance to some of the needed measures.

4. Policy Dialogue

The USG policy dialogue effort in the Philippines during 1984 and 1985 was extraordinary in several respects, and the FY 1985 PL-480 Program played a pivotal role in this effort. The specific policy reforms contained in the FY 1985 agreement included:

-- Lifting of controls on retail prices of milled rice.

-- Opening the importation of wheat to full participation of the private sector

-- Opening domestic distribution of flour to full participation by the private sector.

-- Divestiture by the National Food Authority of all of its stabilization and trading activities except those related to grain price stabilization.

-- Liberalized importation and domestic distribution of fertilizer.

A. Noteworthy Aspects

Before discussing these specific policy reforms, this section presents some of the noteworthy aspects of the policy dialogue.

-- A senior-level inter-agency review of U.S. policy towards the Philippines took place during 1984. The results of this review included as one of three main goals "exposing the economy-- in particular the agricultural sector-- to the interplay of free market forces." To further this objective, economic assistance beyond the bases-related package, including DA, additional ESF and PL-480 would be explicitly conditioned on policy performance.

-- Along with the A.I.D. Mission Director, the Ambassador was directly, actively, and personally involved in policy dialogue, including discussions with the Prime Minister and the President. The Ambassador fully appreciated the economic issues surrounding the Philippines economic situation, and the need for policy reform. Policy dialogue was a central feature of U.S. diplomacy in the Philippines, and was in harmony with other major foreign policy goals.

-- Part of the analysis that laid the groundwork for the interagency review, and provided the foundation for the ensuing policy dialogue, was an A.I.D. Mission "Discussion Paper on Agricultural Policy and

Institutional Reform,' prepared in August 1984, which provided an overview of the role of agriculture in the Philippine economy; assessed major agricultural institutions and policies in terms of their impact on agricultural development; and set forth an agenda for institutional and policy reform, with emphasis on potential benefits and obstacles. This work built in part on research and analysis that had been sponsored by the Mission; on documentation associated with the August 1984 IBRD Agricultural Inputs Loan; and on studies (Fertilizer, NFA) associated with an ADB Agricultural Inputs Loan.

The Title I program was a key instrument in the policy dialogue because (unlike other fast-disbursing assistance) it could be readily associated with the agricultural sector and because the self-help provisions provided a good vehicle for policy conditionality. Further, it was a discretionary resource which could be withheld.

Communication and coordination between the field and Washington, and within Washington between various U.S. agencies, the IBRD, and the IMF was extensive. At the Ambassador's request, a senior foreign service economic officer (and former ambassador to Haiti) was appointed as special coordinator, based in Washington.

-- The policy dialogue of which PL-480 was a part extended beyond the immediate measures embodied in the self-help provisions; the U.S. was concerned with GOP compliance with the IMF agreement and with comprehensive policy discussions in the context of the full Consultative Group and the sub-group, called the "Mini-CG."

-- The PL-480 resources were obligated in early July 1985, the latest possible time, with concern expressed by the Mission that GOP compliance with the self-help measures was uncertain. At the same time, yet-to-be obligated FY 1985 assistance (DA associated with agricultural credit, and the incremental ESF for BOP support valued at $45 million) was considered to some extent contingent on satisfactory performance. <u>While direct conditionality was not feasible with respect to ESF, options about when and in what mode the ESF would be programmed were discussed with reference to policy performance</u>.

-- In the event, by December 1985 GOP compliance with some of the self-help measures, particularly regarding liberalization of wheat imports, was unsatisfactory. As a result, a cessation of PL-480 and other discretionary assistance was contemplated by the Mission during January 1986.

-- On the other hand, the government which came to power in February 1986 readily appreciated the goals and underlying logic of the self-help measures and has been positively disposed towards implementation.

B. Process

Discussion and dialogue surrounding the self-help measures followed a course which may be somewhat at variance with the usual paradigm for policy dialogue, and in any case is interesting. First, the reforms were initially identified not by in-depth, exhaustive studies of the costs and benefits of alternative policy and institutional arrangements, along with careful recommendations about alternatives, but rather review of existing sector studies (including a seminal study by Dr. Cristina David, which the Mission had funded in 1982) and identification of instances of impediments to market forces (rice, wheat, fertilizer) and public intervention (FTI, Kadiwa stores, flour distribution) that did not on their face appear warranted. Once identified, there was some fleshing out of the distortions and costs entailed by these impediments, in the aforementioned Agricultural Policy Paper, but still no in-depth study in advance by the USAID of their effects, nor of the expected effects of changes.

Second, the initial discussions with the GOP on self-help measures were hardly of a detailed, extensive nature. After considerable internal discussions, the Country Team submitted a "non-paper" to the Prime Minister and Planning Minister in early February which discussed the suggested reforms, and their rationale. This non-paper also discussed the assistance response which might be forthcoming. A considerable silence ensued. In early April, NEDA renewed its request for PL-480, in the context of changing the request to all-rice. At about the same time, Washington had cabled the field to start thinking about a minimal program for the Philippines, in view of lack of movement by the GOP on policy reforms. The Administrator and Assistant Administrator of AID visited during April 7-9. They stressed the importance of economic policy reform and mentioned the range of available U.S. resources to support the GOP in implementing such reforms.

On April 12, the Mission Director responded to NEDA's letter of early April stating that agreement on self-help measures needed to be reached soon, and mentioning the rice and wheat/flour measures in particular, but not others. By mid-April, the Mission Director and Program Officer were prepared to leave for Washington to discuss the future of the program in fairly downbeat terms. On April 17, there was general surprise at the receipt of a decision-memo from the President, approving a list of reforms recommended by the Planning Minister and Minister of Food and Agriculture, a list which was arguably more comprehensive than expected.

The key point is that up until then the policy "dialogue" had apparently been quite limited, i.e. to identification of reforms and the general rationale, and perhaps some broad "carrot and stick" communication. Even this discussion was not extensive, because the logic (if not the practice) of market economics is relatively well appreciated in the Philippines, and the suggested reforms were broadly consistent with GOP policy statements and rhetoric. In particular, the policy agenda was not challenged by Prime Minister Virata and NEDA Director-General Valdepenas so that detailed documentation was not required for the reforms to be accepted in principle. While there were some discussions with NFA and the Fertilizer and Pesticide Authority (FPA), the main organizations affected, the process had essentially been "top down." This was because decision-making in the Philippines was essentially top down and because NFA and FPA were basically hostile to the reforms.

Following the surprise April 17 decision, there remained a large amount of work to be done on "definition" and implementation, work made all the more difficult by the fact that the implementing agencies-- NFA and FPA-- had substantial vested interests in maintaining the arrangements and controls which the reforms were intended to eliminate. Further, NFA's interest in maintaining a monopoly on wheat imports coincided with U.S. agricultural interests in promoting U.S. wheat exports. Second, the task of implementation was made difficult by the complexities and changing conditions of the fertilizer sector, and by the broad scope of NFA operations which were to be privatized.

This is not an implicit criticism that more detail should have been worked out in advance. Rather, a great deal of homework inevitably had to be carried out. Since it was not carried out before, implementation has proceeded somewhat slowly and unevenly, particularly for privatization and fertilizer, and for awhile, wheat. Monitoring, negotiating, and supporting implementation have turned out to be extremely labor intensive for the Mission.

This process started with an April 26 letter from the Ambassador to the Prime Minister, clarifying the U.S. understanding of the exact nature of the reforms to be implemented. Negotiation continued (including negotiation between NEDA and NFA/FPA) on the language of the self-help measures and implementing instructions. There was considerable time pressure, because the agreement needed to be signed by early July. Congressional pressure (mentioned earlier) was also intense not to let policy reforms get in the way of wheat and rice export interests. It was also becoming clear that however much effort might be put into "rule-writing", there was no way to ensure good implementation in advance. In particular, it was clear to the Mission that NFA and FPA were not enthusiastic. Accordingly, the Mission foresaw that the tale would be told in implementation, which would need to be carefully monitored.

5. Rationale, Additionality, Implementation, and Impact of Specific Reforms

This section of the paper examines the impacts of the policy measures associated with PL-480 compared with their intended impact, and also discusses whether the measures were attributable to the PL-480 program, or whether they would have been implemented in any case.

A. Rice Price Decontrol

i. Rationale. At the time of the FY 85 PL-480 negotiations, the government maintained a ceiling on the retail price of milled rice. The Mission argued that, even though the ceiling price was poorly enforced, it had a depressing effect on incentives to millers and, ultimately farmers, because of the *risk* of enforcement, which might result in loss of license, fines, and/or seizure of stocks. The analysis also noted the expected milled rice deficit for 1985 of 400,000 to 600,000 metric tons, and emphasized the need to offer adequate incentives to farmers. At the same time the analysis acknowledged the need to prevent "extreme" fluctuations in rice prices. One option would be a "limited" buffer stock operation (limited to instances of wide fluctuations in price) with public, well-defined rules. The paper indicated that this option should be analyzed more thoroughly.

Accordingly, the purpose of this reform was to improve incentives to producers. It should be noted that NFA had for some years maintained support prices for rice; however, these were not judged to have been effective in maintaining adequate incentives. Few rice farmers had ready access to NFA buying centers, and those who did faced high transactions costs.

ii. Attribution. Discussions of agricultural policy in the Philippines had for some time pointed towards the need for NFA to use some sort of buffer stock operation rather than price controls. The IBRD Agricultural Inputs Loan (August 1984) contained an action program which included a provision that NFA would "undertake to stabilize rice prices through buffer stock operations rather than mandatory price ceilings."

When the country team proposed rice decontrol as a policy condition, Washington immediately raised the attribution issue, pointing to the Agricultural Inputs Loan document as well as provisions in the IMF agreement for deregulation in agriculture. However, inquiries both in Washington and Manila indicated that rice price decontrol was not a condition for either IBRD or IMF tranche releases. Further, discussions with the GOP indicated that there was a sharp division within the government on the issue, especially in view of the expected shortfalls in rice production, and the great political sensitivity about rice prices.

Accordingly it appears that provision of U.S. resources, including PL-480, was a major factor in achieving rice price decontrol in the Philippines.

iii. Implementation. Implementation of rice price decontrol was quite satisfactory. Decontrol of milled rice prices was announced in May 1985 (at planting time) to become effective in October 1985 (harvest time). On October 1, the price was in fact deregulated.

In principle, NFA could have sabotaged the positive effects of decontrol on producer incentives by dumping large quantities of milled rice at cheap prices on the market at harvest time-- October-December. The extent to which this actually occurred is uncertain. Available data (from NFA) indicate that "injections" of milled rice during this period were quite low relative to previous years, and relative to total production. (The prices at which these injections were marketed were about the same as the previous year.) Thus, the data do not suggest that NFA took actions on the retail sale side during the latter part of 1985 which would have negated the intended effects of rice price decontrol.

During the first part of 1986, injections were similarly modest in scope according to NFA data. However, there is a general perception that large amounts of rice were dumped on the market in connection with the February elections based on the generally accepted view that NFA was used as a political tool by the KBL. The fact that NFA data do not reflect this would not be surprising.

iv. Impact. The broader impact questions are whether incentives to rice producers have been "appropriate" and whether the framework for maintaining incentives has been improved.

Currently available data suggest that incentives to farmers have been generally appropriate, at least from an efficiency standpoint. In particular, the Philippines, on the basis of good harvests in 1984/85 and 1985/86, and an expected good harvest in 86/87, has regained self-sufficiency in rice. Further significant expansion in rice production would generate a problem of surpluses, because at the current world price (around U.S. $200 per metric ton, FOB Bangkok, Thai 5 percent broken) Philippine rice would not be competitive. The average FOB cost for Philippine rice would be about $250/MT, for a much poorer quality product. Further, the IBRD projects no significant increase in the world price of rice in real terms over the next decade.

Based on these considerations--in particular, the judgement that incentives in the Philippine context should lead to self-sufficiency in rice along with maintenance of appropriate stocks, but should not lead to a large surplus that cannot profitably be exported--incentives to rice producers have been appropriate.

As far as longer run impact is concerned, the self-help condition removed an instrument for influencing consumer prices (and thereby producer prices) which was arguably inefficient and even counterproductive. There remains the problem of fully establishing new instruments--buffer stock operations--that are consistent with the "right" prices to producers and consumers, without undue administrative and budgetary costs, in an environment where international prices are expected by some observers to be unusually low for the next 3-5 years. The 1986 Title I program's self-help measures called for a suitable grain stabilization program (for both corn and rice) to be announced and established by September 30, 1986. A sound program was formulated on schedule, one which called for somewhat lower support prices for rice and corn, based on low border prices, reduced costs of fertilizer, ample production, and budgetary constraints. The program also envisioned a large spread between purchase and release prices-- to encourage private sector storage and marketing-- and more efficient marketing arrangements by NFA. However, the program has met with resistance from farmers, and recalculations of budgetary impacts showed a heavier burden on the budget. Accordingly, the program has not been implemented, and the deadline for implementation has been extended to June 30, 1987. This is one of several policy areas where a continued mission presence and involvement is clearly desirable.

B. Liberalization of Wheat Imports and Flour Distribution

i. Rationale. The National Food Authority had exercised monopoly control over wheat imports since 1974 and over flour distribution since 1983. According to Mission analysis, the results were higher marketing costs, higher prices to consumers, poorer quality flour, and less timely availability. In particular, flour prices have been and remain above world market prices. The monopoly profits generated by this arrangement were used to support overall NFA operations including rice and corn operations, and subsidies to its public enterprises, including Kadiwa operations and FTI. They were allegedly used for political purposes as well. As a rough order of magnitude, in 1983 NFA profits on grain import and distribution operations were estimated at P532 million, about $48 million at the 1983 exchange rate.* Accordingly, the intended effects of the PL-480 program in this area were to improve the availability and price of flour to consumers and to remove NFA's access to monopoly rents from the wheat/flour trade.

*See the ADB-financed report, "Organization and Systems Study for the National Food Authority", produced by PAS, January 1985. (hereafter, PAS).

ii. Attribution. Liberalization of wheat imports and domestic flour distribution would not have taken place under the Marcos government without the policy dialogue associated with PL-480. The ADB had financed a study of NFA which raised issues about its role in the wheat/flour tráde; however, there was no ADB assistance associated with policy reforms. There was no mention of wheat and flour in the Action Plan that was part of the 1984 IBRD Agricultural Sector Inputs Loan. As late as March 1985, shortly before the announcement of the reforms, the head of NFA stated that NFA could not and would not relinquish its role as exclusive importer of wheat.

iii. Implementation. Tremendous controversy surrounded the implementation of the wheat import liberalization provisions of the PL-480 agreement under Marcos. NFA continued to regulate and limit imports through licensing. (The PL-480 agreement stipulated that licensing would not be administered in such a way as to be used to restrict access to imports.) The two key groups--the millers and the bakers--were competing against one another for import permits. The bakers, who historically had close links to NFA, were organized by Eduardo Cojuanco, a powerful Marcos crony, who set up Philbake. The millers comprised a small group which included Jose Concepcion, a prominent Marcos opponent and leader of NAMFREL, an election monitoring organization. Cojuanco sought through the President to gain exclusive rights for the bakers as a group to import wheat, thus substituting a private for a public monopoly/monopsony. NFA was apparently a full participant in this attempt. Marcos initially approved this arrangement. Upon complaints by the millers, the country team objected to Prime Minister Virata, in early September. In the meantime (according to Mission sources), wheat was arriving, which Philbake sold to the millers at a high mark-up. At about the same time Cojuanco informally stated to Mission officials his intention to use the wheat import licenses to drive the millers out of business, and buy up the mills at bargain prices.

In early October, in response to the Mission's objections, the GOP announced that import licenses for wheat would be split 50-50 between the millers and the bakers. However, the definition of "wheat imports" had been broadened to include imports of wheat flour. Cojuanco proceeded to order 25,000 MT of subsidized flour from Germany, thus putting further pressure on the millers.

This activated the USDA, which under the Export Enhancement Program sought to match the terms and induce Cojuanco to purchase U.S. flour instead. This of course threatened to undermine the thrust--political and economic--of the policy reform, by reinforcing the position of a Marcos crony and would-be monopolist. This put the Ambassador, who had actively pushed for the reform, in an untenable position. In the end, the U.S. provided subsidized wheat to the millers under the EEP and subsidized flour to Philbake. However, as a result of this experience, the Mission was prepared to proceed in early 1986 to terminate the PL-480 program on the basis of non-compliance with the self-help measures.

The new government (which included concepcion as Minister of Trade and Industry) removed the requirement that importers of wheat and wheat flour obtain import permits effective March 11, 1986. There remains an NFA requirement for a business license which importers of wheat and wheat flour will have to renew on an annual basis. The FY 86 PL-480 self-help conditions included a provision that the GOP will not reimpose import permit requirements for wheat and wheat flour, and that NFA will not use the business license requirement to restrict access to imports by the private sector, either by individuals or firms.

Implementation of the flour distribution provisions was less controversial. The report on implementation of the self-help conditions states that NFA stopped distributing flour in August 1985, and turned this function over to the private sector.

iv. Impact. There is anecdotal evidence that despite the continued control of wheat imports under Marcos, flour prices and availability improved. A Senate staffer reported that "conversations with small town bakers and government officials indicated that the new arrangements had resulted in price reductions to consumers in the form of larger products or lower prices for the same product."*

Beyond this sort of information, there is little firm evidence of a favorable impact of the reforms on flour prices and some indication of no impact. Mission data available in summer 1986 indicated that the average retail and wholesale prices of flour had remained steady, despite sharp falls in wheat import prices, that more than outweighed exchange rate changes. Other reports indicate that domestic prices for flour are still considerably above world prices. These price differentials would ordinarily have encouraged imports of wheat flour, which should have been permissible under the self-help provisions.

Press reports during mid-1986 contained an assertion by Felix Maramba, President of the millers' association, that Japanese trading firms were "testing the local flour market" by shipping in subsidized flour, in an initial amount of 105 MT. (sic) This flour was being marketed at about P165 per 25 kilo bag, compared with price from local flour millers at around P195 per bag. However, apart from this there apparently have been no significant imports of flour, beyond those placed under Marcos (see earlier discussion).

*Report by Frederick Z. Brown; Senate Foreign Relations Committee; September 9, 1985.

Flour milling is carried out in the Philippines by about eight firms, and there is substantial excess capacity. There is mounting evidence that this group behaves as a cartel. Between 1985 and 1986 the peso cost of imported wheat was essentially stable, while the wholesale price of wheat flour rose 8 percent. (The previous year flour prices rose by 18 percent while wheat prices in peso terms were unchanged.) Thus, privatization has not led to benefits in terms of increased efficiency and lower prices. Recent correspondence indicates that the domestic price of flour is unduly high; that the private millers are acting as a cartel; that there are no effective competitive pressures from flour imports; and that conflicts between US wheat interests and development policy interests will persist in the Philippines wheat/flour market.

C. Kadiwa Stores and Food Terminal Incorporated

i. Rationale. The problems surrounding the Kadiwa stores and FTI were documented in the ADB-financed Study of NFA cited earlier. According to this report, the Kadiwa program was initiated in 1981 to provide, through a network of government-operated retail stores, a check on spiralling costs of commodities brought about by world-wide inflation. Kadiwa stores "offer consumers a range of food and other commodities at prices which are equal to or lower than the lowest prevailing prices in the area in which the Kadiwa is located". In particular, they were outlets for commodities, subject to retail price controls. The number of outlets initially rose to over 300, but by May 1984 the number directly operated by NFA had fallen to 178 as the result of a "rationalization" program. According to the report, these stores showed a "net profit from operations" of P14.2 million during the first half of 1984, but a loss after interest expense of P458,000. Thus, the Kadiwa program operated close to a break-even point. The main rationale for divestiture is that they competed unfairly with the private sector and, with NFA becoming chiefly concerned with price stabilization through buffer stock operations rather than price controls, there was no rationale for their remaining in the public sector.

Food Terminal Inc. (FTI) began operations in 1974, and came under formal possession of NFA in September 1984. FTI comprises a Marketing operation which at the time of the study operated 25 Kadiwa stores (apart from those operated directly by NFA); a Facilities Management operation which included a slaughterhouse, a chicken processing plant, a refrigerated warehouse, and some other facilities; and a Corporate Services operation that includes all "housekeeping" functions. Total staff at the end of 1983 was 3,843. In the case of FTI, losses were a major consideration. The report found accounting information incomplete, but ventured an estimate of a P81 million loss for 1983 based on information available. Accordingly, the rationale for privatization had to do with major financial drains as well as the more general consideration of activities with little or no public justification.

ii. Attribution. The problems of the Kadiwa operations and FTI were documented in the PAS report and mentioned in Mission papers. However, curiously enough, privatization was apparently not mentioned in the non-paper to the government nor in a subsequent letter about self-help conditions for PL-480. The Mission was aware of the problem, but perceived that cutting off the income source (monopoly profits from wheat imports) would eventually exert pressure to eliminate these activities. The Presidential Decision on policy reforms (April 15) included the commitment to privatize these operations, and this was then incorporated in the PL-480 agreement.

iii. Implementation. The actual language of the self-help measure was not particularly strong. It called for NFA to bring all Kadiwa stores under FTI and then for the "transfer or divestment of the operation of Food Terminal Incorporated, including the Kadiwa operations, as a joint venture between the Government and the private sector, without prejudice to the possibility of a full transfer to the private sector immediately or ultimately". It also called for the government to contract for a definitive divestment study to be completed by January 31, 1986, after which the divestment plan would be implemented.

NFA was reluctant to comply with this condition. For instance, in an August 15, 1985 news report, Jesus Tanchanco declared that "NFA will never sell its FTI Kadiwa centers to any private group". Nevertheless, it was recognized by the Country Team that without the profits from the wheat/flour monopoly, NFA would eventually be forced to curtail these operations by budgetary stringency.

On the whole, there was no progress in this area under the Marcos government. However, the new government has reaffirmed its intention to divest itself of the Kadiwa stores and the FTI complex. An AID/PRE Bureau funded team was in the Philippines during August 1986 at the GOP's request to develop a plan for actual divestiture of these activities. The 1986 PL-480 agreement calls for a definitive divestiture plan by February 15, 1987.

In the meantime, the number of Kadiwa stores has declined steadily. In March 1987 the GOP reported to the IMF that they had closed or sold 152 out of 154 Kadiwa outlets other than those operated by FTI in Manila, and 17 out of 28 outlets operated by the Food Terminal. This report also confirmed the GOPs intention to close or sell the Food Terminal. Employment in FTI had fallen to 1,585 as of August 1986. About 2000 employees were laid off in 1985.

iv. Impact. In terms of the goals of the self-help provision, the main financial drains were associated with FTI.

It is still too early to discern much impact in terms of a smaller financial burden. The number of Kadiwa stores has been declined sharply, and press reports have emphasized the private sector thrust underlying this. Finally, it is clear that the financial pressures stemming from the wheat/flour provisions indeed generated significant pressure on NFA to get rid of these operations.

D. Fertilizer Importation and Distribution

i. Rationale. Prior to the PL-480 agreement, imports of fertilizer were limited to four companies, two of which were domestic producers. Domestic production was at a high cost, and large mark-ups on prices of imported fertilizer were allowed in order to offset these costs. During the 1980-1983 period, when international fertilizer prices dropped sharply (by 40-50 percent according to IBRD data), these declines were not passed on to domestic users. Markups ranged from 50 to 100 percent above CIF import prices. Thus, the aim of the fertilizer reforms-- freeing up imports of fertilizer and prohibiting "unreasonable" taxes, tariffs, etc., which would subsidize domestic production-- was to increase competition, allow prices to fall towards import parity levels, increase availability and usage, and thereby promote agricultural production.

ii. Attribution. While both the ADB and the IBRD had focused on fertilizer in their 1984 commodity loans, conditionality extended only to the completion of studies. Letter of instruction #1419, issued in August 1984, contained statement of intent by the government to dismantle the fertilizer cartel. However, actual deregulation began only with E.O. 1028, issued in May 1985. Accordingly, the liberalization of fertilizer trade and distribution can be legitimately attributed to the PL-480 program.

iii. Implementation. Initially, implementation of the fertilizer provisions in the FY 85 agreement received less attention than those provisions associated with NFA, in part because both the pattern of domestic production (the coming on stream of Philphos and the closing down of other firms) and international prices were changing. Also, institutional arrangements, such as joint ownership of Philphos by the GOP and the government of Nauru, GOP investments in two fertilizer plants in Malaysia and Indonesia, and agreements among Asean producers to buy and sell from one another, make the situation complex. Under the Aquino government, implementation has accelerated, although there are still issues to be resolved.

The 1986 PL-480 agreement noted the increased number of firms in the market, but called for further study to develop further recommendations for the fertilizer sector, with the goal of establishing the "lowest practicable prices" for farmers. A fertilizer sector study sponsored by the Mission is supposed to get underway in CY 1987.

iv. Impact. While there are remaining issues to be resolved, the impact of the reforms so far has been positive and significant. Forty-four firms were registered as importers in mid-1986, and twenty-five of these were still active by end-year. A number of inexperienced new firms quickly collapsed but without adverse impact on the overall market.

Both international and domestic prices of fertilizer have declined, and consumption is up sharply. The key question is the extent to which international price declines have been fully passed on.

Figures cited in a June 30 1986 FPA monthly report, and repeated in the press, indicate that on the whole domestic price declines have exceeded international price declines. According to FPA, import prices on a weighted average basis declined by 19.3 percent during January-May 1986, compared with January-May 1985, while retail prices declined by an average of 27 percent. (Since the exchange rate depreciated by roughly 10 percent between these two periods, this difference is even more impressive. The removal of the 10 peso per bag levy would have explained perhaps 4 percentage points of the average decline in retail prices.) For urea, which accounts for roughly half of total fertilizer consumption, the figures were 31.4 percent and 35.18 percent. For several grades, CIF costs rose, but retail prices declined. The same report indicated that in response to the 27 percent decline in retail fertilizer prices, usage had increased by 65 percent.

More recent (January 1987) reports show major declines for gross markups-- the ration between the retail price and the import price in pesos-- for most types of fertilizer, implying that declines in domestic retail prices have been for greater in percentage terms than declines for import prices. (See Table) Since distribution and handling costs peresumably depend mainly on unit weight and volume rather (which have not changed) than on import prices, this decline in markups in the face of declining import prices is even more remarkable.

Overall demand was up by 37 percent in 1986 compared with 1985 (from 675 TMT to 925 TMT). Of this increase, less than 20 percent was for increased inventories, implying a significant rise in usage of fertilizer.

Currently, there is an issue of how to deal with Philphos, the large, new public sector fertilizer producer which came onstream under Marcos. Philphos produces both for the domestic market and for export, but is considered to be a high cost producer. Locally produced phosphatic grades of fertilizer are not allowed to be imported, but Philphos is obliged to sell its output at prices that entail parity with import prices.

Recent reports indicate that while margins between domestic and import prices have been reduced, they may still be unduly high. Similarly, while usage has increased, it is still sub-optimal. Issues raised by public sector interventions in both domestic and international markets-- GOP equity in both domestic and foreign firms, associated trading arrangements; GOP obligations with respect to Planters Products; and FPA's role in regulating imports and trade-- need to be resolved. A complicating factor is that international markets are not perfectly competitive, and prices have been volatile. A fertilizer sector study to be sponsored by the mission in CY 1987 is expected to address these issues.

Conclusions and Issues

The PL-480 program in the Philippines has been intended to provide financial support to the country and to promote policy reform.

For purposes of providing financial support, the choice of rice for the 1985 program was regrettable because the higher price of U.S. rice negated much of the concessionality of the resource transfer. While the program contributed balance of payments support, the contribution was less than would have been the case for wheat, by virtue of the relatively high price of U.S. rice compared with other sources. Further, owing to high stocks the rice has not (as of this date) been sold, so that no budgetary resources have been generated. The choice of wheat in 1986 made much more sense.

The most remarkable aspect of the PL-480 program has been the policy dialogue associated with it:

-- The policies addressed were substantive and significant, affecting some of the major determinants of incentives to farmers in the Philippines.

-- These important policy measures have not proved to be one-step actions. Despite significant progress much remains to be done in the area of price stabilization for domestically produced food grains; promoting efficiency in markets for wheat and wheat flour; lowering prices and improving availability of fertilizer; and divestiture of NFA assets, implying a continuing role for the Mission.

-- The self-help measures provided a very useful vehicle for agriculture policy dialogue. They facilitated policy discussions in connection with ESF and DA programming, where more direct linkage and conditionality were not possible.

-- For purposes both of financial assistance and policy dialogue, U.S. agricultural market-development concerns seriously hampered the developmental effectiveness of PL-480. Once the rice lobby was mobilized, it was impossible to switch to a commodity such as wheat, which would have been of much greater value fo the Philippines. Second, negotiation of the self-help measures was made more difficult by the pressures from both wheat and rice interests. To the extent that PL-480 is not really a discretionary resource, its effectiveness as a policy dialogue tool is correspondingly limited, as long as leverage is an important aspect of the policy dialogue. Finally, agricultural market development concerns reinforced GOP efforts to sabotage implementation of the wheat import liberalization measures.

-- The experience in the Philippines in 1985 demonstrates both the opportunities and the limits for leverage. The fact that the U.S. placed a high priority on policy reform and was willing to withhold resources (or curtail future resource levels) was crucial in getting the reforms approved. The Marcos government readily took actions to sabotage some of the reforms, which it opposed in the "implementation". This called for persistent monitoring, which ultimately and inevitably proved to be a losing battle. The implication is that there is little to be gained by compelling a government to implement a reform to which is is not really committed. The contrast in implementation between the former government and the current government has been striking.

-- Even with a cooperative government, much remains to be done. There are complex, difficult issues surrounding each of the reforms. This does not mean that policy reforms need to be studied to death before any action is taken. But it does imply a need for a continued presence and interest (as opposed to a new reform agenda each year) and a significant allocation of financial and human resources.

The apparent outcome of the wheat/flour privatization reforms has been essentially a transfer of monopoly power from the public sector to the private sector, and even higher prices for consumers of flour, despite stable wheat prices. This is in sharp contrast to the fertilizer reforms, where competitive forces are much greater and prices have moved favorably. This suggests (or confirms) that beneficial economic effects of privatization depend crucially on whether private firms are exposed to competitive market forces.

Table 1

Value Added - Domestic Economy and Agriculture
(Billion Pesos, 1972 Prices and percent)

	1978	1979	1980	1981	1982	1983	1984	1985	19
GDP	82.8	88.0	92.6	96.2	99.0	99.9	94.2	90.4	
(growth rate)	5.5	6.3	5.2	3.9	2.9	0.9	-5.7	-4.0	0.
Industry	29.6	32.0	33.5	35.0	35.7	35.9	32.2	28.9	
(growth rate)	6.1	8.1	4.7	4.5	2.0	0.6	-10.3	-10.2	
Services	31.5	33.4	35.4	36.6	37.9	39.1	36.6	35.5	
(growth rate)	5.7	6.0	6.0	3.4	3.6	3.2	-6.4	-3.0	
Agriculture*	21.6	22.6	23.7	24.6	25.4	24.9	25.4	26.0	
(growth rate)	3.8	4.6	4.9	3.8	3.3	-2.0	2.0	2.4	3.
Crops	13.2	14.1	15.2	15.3	15.7	15.0	15.6	16.2	
Paddy	3.7	4.0	4.1	4.3	4.5	3.9	4.2	4.7	
Corn	1.4	1.4	1.4	1.5	1.5	1.4	1.5	1.7	
Coco	1.3	1.2	1.3	1.4	1.4	1.3	1.0	1.3	
Sugarcane	1.2	1.3	1.3	1.3	1.4	1.2	1.4	0.8	
Banana	2.0	2.1	2.4	2.3	2.3	2.4	2.4	2.4	
Other	3.4	4.0	4.7	4.5	4.7	4.8	5.0	5.4	
Livestock/ Poultry	3.2	3.3	3.5	3.8	4.2	4.7	4.8	4.7	
Fishery	3.7	3.8	3.9	4.1	4.3	4.4	4.3	4.4	
Forestry	1.5	1.4	1.1	1.2	0.9	0.8	0.8	0.7	

* Includes Forestry, Fishery

Table 2

Agricultural Crop Production

Volume (000 MT)

Year	Rice	Corn	Sugar	Copra	Bananas
1976	4,052	2,717	2,880	2,742	2,271
1977	4,280	2,775	2,685	2,440	2,447
1978	4,607	2,796	2,335	2,517	3,156
1979	4,847	3,090	2,289	1,912	3,582
1980	5,093	3,123	2,267	2,076	3,977
1981	5,020	3,110	2,315	2,316	4,073
1982	5,279	3,290	2,447	2,192	4,077
1983	5,040	3,126	2,465	2,264	3,668
1984	5,097	3,346	2,335	1,435	3,819
1985	5,330	3,439	1,719	1,806	3,698

Table 3

Agriculture/Food Trade Balance
($ Million)

	1980	1981	1982	1983	1984	1985
Exports	1,925	1,758	1,433	1,350	1,413	1,069
Food Imports	493	563	650	528	425	426
Fertilizer/Urea	139	105	108	91	88	106
Balance	1,293	1,090	675	731	900	537

Table 4

Balance of Payments - Current Account

	1980	1981	1982	1983	1984	1985	198
Exports	5,788	5,722	5,021	5,005	5,391	4,629	4,7
Imports	7,727	7,946	7,667	7,487	6,070	5,111	4,9
Trade Balance	-1,939	-2,224	-2,646	-2,482	-679	-482	-1
Service Earnings	2,222	2,896	2,983	3,127	2,626	3,288	3,8
Service Payments	2,621	3,205	4,023	3,867	3,449	3,262	3,1
Service Balance	-399	-309	-1,040	-740	-823	26	6
Transfer Receipts	451	485	498	483	387	388	[illegible]
Transfer Payments	17	13	12	11	1	9	[illegible]
Transfer Balance	434	472	486	472	386	379	4
Current Account Balance	-1,904	-2,061	-3,200	-2,750	-1,116	-77	9

Table 5

Total Food Imports

	1980	1981	1982	1983	1984	1985
	Value ($ Million)					
Wheat	149	151	158	135	131	106
Rice	0	0	0	0	42	110
Corn	35	42	43	71	29	33
Dairy Products	113	135	167	128	66	72
Fish/Fish Preparations	26	30	38	7	1	1
Others	170	205	244	187	156	104
Total	493	563	650	528	425	426
	Volume ('000 MT)					
Wheat	786	796	924	797	766	663
Rice	0	0	0	0	190	538
Corn	250	253	341	528	182	281
Dairy Products	109	93	118	106	67	82
Fish/Fish Preparations	29	30	42	9	1	5
Others	NA	NA	NA	NA	NA	NA

Table 6

Selected Agricultural/Food Exports
($ Million)

	1980	1981	1982	1983	1984	1985
Cocunut Products	811	750	590	680	727	459
Copra	47	34	49	4	0	0
Cocunut Oil	567	533	401	516	580	347
Dessicated Coconut	116	102	68	88	106	76
Copra Meal/Cake	81	81	72	72	41	36
Sugar	657	604	441	316	279	185
Refined	624	566	416	299	246	169
Molasses	33	38	25	17	33	16
Fruits&Vegetables*	118	127	136	116	140	143
Bananas	114	124	146	105	122	113
Raw Coffee	45	39	49	47	76	70
Fish/Fish Prod	107	90	71	77	69	99
Rice	73	24	0	9	0	0
Total	1,925	1,758	1,433	1,350	1,413	1,069

Volume (TMT)

	1980	1981	1982	1983	1984	1985
Coconut Products						
Copra	121	108	178	16	0	0
Coconut Oil	918	1040	921	998	588	651
Dessicated Coco.	87	86	90	89	77	65
Copra Meal/Cake	545	620	589	551	364	444
Sugar/Products						
Refined	735	1,222	1248	963	877	572
Molasses	443	376	463	500	516	422
Fruits & Vegetables						
Bananas	923	869	927	643	800	789
Raw coffee	16	20	25	22	33	31
Fish	58	45	26	29	28	32
Rice	256	75	0	40	0	0

*Mainly pineapple & pineapple products. Includes mangoes

Table

Average Prices Wheat and Wheat Flour

	Wheat Imports ($/MT; CIF)	Exchange Rate	Wheat Imports (Pesos/MT)	Wheat Flour Wholesale (Pesos/MT)
1983	186.6	11.1	2,071	4,110
1984	191.9	16.7	3,205	6,670
1985	172.9	18.6	3,216	7,860
1986	160.1	20.4	3,266	8,520

Table 8 - Fertilizer Prices and Margins
(Prices in Pesos/MT)

	1982	1983	1984	1985	1986
Urea (45-0-0)					
Import Price, CIF	1,666	1,630	3,199	3,103	2,268
(% Change)	--	-2	96	-3	-27
Retail price	2,565	3,434	5,546	5,627	3,143
(% Change)	--	34	62	-5	-40
Markup (%)	54	111	73	70	39
Ammosul (21-0-0)					
Import Price, CIF	852	986	1,799	1,805	1,338
(% Change)	--	24	29	0	-26
Retail Price	1,938	2,424	3,124	3,095	2,283
(% Change)	--	24	29	0	-26
Markup (%)	127	146	74	72	71
NPK (14-14-14)					
Import Price, CIF	1,532	1,880	3,002	3,186	3,473
(% Change)	--	23	60	6	9
Retail Price	2,506	3,377	5,204	5,083	4,250
(% Change)	--	35	54	-2	-16
Markup (%)	64	80	73	60	22
Potash (0-0-60)					
Import Price, CIF	986	1,113	1,958	1,741	1,719
(% Change)	--	13	76	-11	-1
Retail Price	2,259	3,185	4,010	4,013	3,320
(% Change)	--	41	26	0	-17
Markup (%)	129	186	105	130	93

Table 9 Fertilizer Supply and Demand
(Thousand Metric Tons)

	1982	1983	1984	1985	198[illegible]
Urea					
Production	--	--	--	--	--
Imports	365	320	283	370	55[illegible]
Exports	--	--	--	--	--
Supply	365	320	283	370	55[illegible]
Demand	342	371	256	301	49[illegible]
Ammosul, etc.					
Production	1	7	15	150	1[illegible]
Imports	152	118	113	13	19[illegible]
Exports	--	--	--	--	--
Supply	153	125	128	163	20[illegible]
Demand	140	138	119	120	15[illegible]
NP and P					
Production	24	36	34	311	58[illegible]
Imports	95	73	89	91	2[illegible]
Exports	--	--	--	181	55[illegible]
Supply	119	109	123	221	5[illegible]
Demand	143	145	122	104	11[illegible]
NPK					
Production	100	120	55	39	11[illegible]
Imports	44	27	87	125	3[illegible]
Exports	--	--	--	--	5[illegible]
Supply	144	147	142	164	9[illegible]
Demand	162	150	134	125	12[illegible]
Potash					
Production	--	--	--	--	-[illegible]
Imports	111	75	53	0	5[illegible]
Exports	--	--	--	--	-[illegible]
Supply	111	75	53	0	5[illegible]
Demand	57	73	34	24	4[illegible]
Total					
Production	126	163	103	500	71[illegible]
Imports	756	613	626	600	86[illegible]
Exports	--	--	--	181	61[illegible]
Supply	891	776	729	919	96[illegible]
Demand	846	878	665	675	92[illegible]