

Chapter 13

The Agriculture Sector and Rural Development

Jesús Antón

Over the past decades, Mexico has implemented major reforms in the agriculture sector that have resulted in economic and social gains of considerable significance. These changes, however, have also reduced the relative importance of the sector in the economy. Despite the progress, further efforts are needed to tackle numerous challenges involving sector competitiveness and rural poverty. Competitiveness and efficiency could be enhanced by shifting from a subsidies approach to one that favours targeted investments in innovation and infrastructure, improving the focus and the transparency of PROCAMPO, developing a broad risk management strategy that differentiates catastrophic from normal risks, and integrating policy-making institutions. As social policies focusing on the poor in rural areas are developed, agricultural policies and land tenure systems should be further reformed to facilitate innovation, structural adjustment, and social development. During the first weeks of his government, President Enrique Peña Nieto has signaled the priorities for this sector with a focus on increasing productivity and production to ensure food security and reduce poverty in the sector, in line with the issues discussed in this chapter.

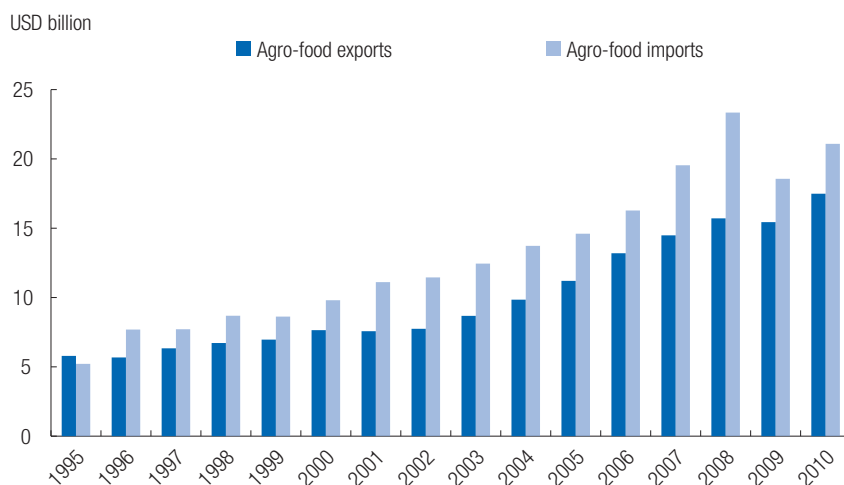
In 2010, Mexico's agriculture sector accounted for just 3.6% of GDP (Table 13.1) but still employed 12.7% of the labour force. During the past two decades, Mexico has been implementing a number of agricultural and related trade policy reforms to improve the competitiveness of the sector while reducing rural poverty. In particular, Mexico has significantly reduced border protection through WTO, NAFTA and other trade agreements. It also reduced overall producers' support while increasing direct payments to farmers, which are the least distortive form of support.

This sector remains less productive than other sectors. Furthermore, it is characterised by a marked duality between a large number of small farms (of 2 hectares or less) producing food mostly for their own consumption, and a small number of large-scale, commercial farm holdings (of more than 50 hectares) accounting for a large proportion of agricultural output. This duality requires an integrated policy approach to respond to two core objectives: further develop commercial agriculture and, at the same time, reduce rural poverty.

The sector is also characterised by a persisting agro-food trade deficit (Figure 13.1), even though Mexico is a significant and competitive exporter of several fruits and vegetables and relies on a large net trade surplus in these products.

Rural areas have vast human resources, particularly young people. In addition, their natural, cultural and physical assets could provide, in a more diversified economy, a significant contribution to national development. Improvements in the productivity and competitiveness of the agriculture sector would help promote long-term growth and reduce poverty decisively.

The Pact for Mexico signed by different political parties at the outset of the present administration establishes three objectives to transform the agricultural sector into a more productive activity. They include improvements in commercialization (commitment 64), measures to improve productivity through financing and reorientation of producer support and greater use of technology (commitment 65) as well as strengthening of environmental payment schemes (commitment 66). The objectives set by the administration are to increase production to ensure food security and reduce poverty in the sector. In the following sections options to improve the system of producer support and institutional reforms to attain these objectives in an efficient manner are presented.

Figure 13.1. **Mexico's agro-food trade, 1995-2010**

Source: International Trade by Commodity Statistics (ITCS) database.

Table 13.1. **Agricultural indicators, 1995, 2010¹**

	1995	2010 ¹
Agriculture in the economy		
Agriculture in GDP (%)	5.4	3.6
Agriculture share in employment (%)	22.2	12.7
Agro-food exports (% of total exports)	7.3	5.9
Agro-food imports (% of total imports)	7.2	7.0
Characteristics of the agricultural sector		
Agro-food trade balance (USD million)	574	-3,598
Crop in total agricultural production (%)	56	51
Livestock in total agricultural production (%)	44	49
Agricultural area (AA) (thousand ha)	107 200	102 833
Share of arable land in AA (%)	23	24
Share of irrigated land in AA	6	6
Share of agriculture in water consumption (%)	85	77
Nitrogen balance, Kg/ha	24	21

Note: 1. Or latest available year.

Source: OECD Statistical databases, World Development Indicators and national data.

Improving competitiveness by reforming producers' support

Overall support has declined

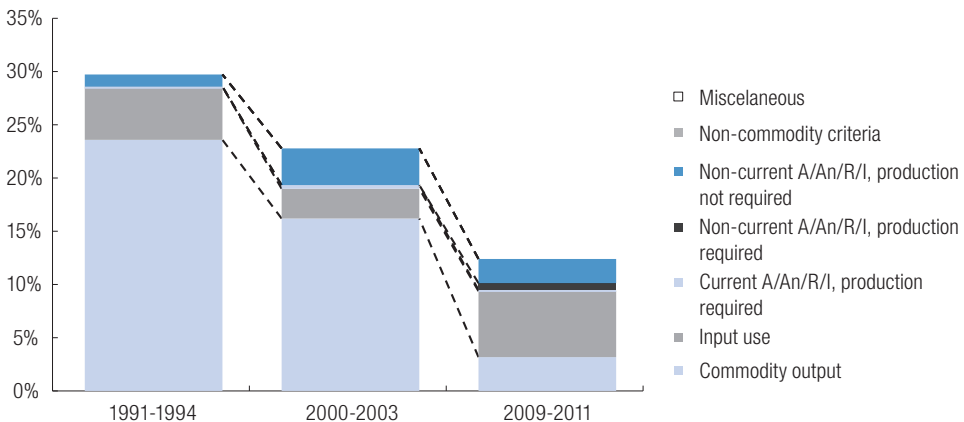
Mexico has undertaken significant agricultural policy reform in the past two decades, reducing the amount of support to producers by more than half since 1991-94, and reallocating remaining support to less distorting and more effective forms of support (Figures 13.2 and 13.3). Today, this support stands at 12% of gross farm receipts, which is below the OECD average of 20%. Mexico has notably reduced market price support (one of the most distorting forms of interventions), which now accounts for only one-quarter of producer support, in favour of direct payments based on historical parameters. In particular, Mexico has two large direct payment programmes based on historical parameters: PROCAMPO (established in 1994, see below) is based on historical planted area and PROGAN (launched in 2003) is based on historical livestock numbers and imposes environment protection conditions for production.

Increased subsidies to energy consumption and price hedging are unwelcome developments

Since 2000, Mexico has significantly increased expenditure on inputs, both fixed capital and variable (Figure 13.3). In particular, support for energy consumption (electricity and fuel) and to subsidise price-hedging contracts

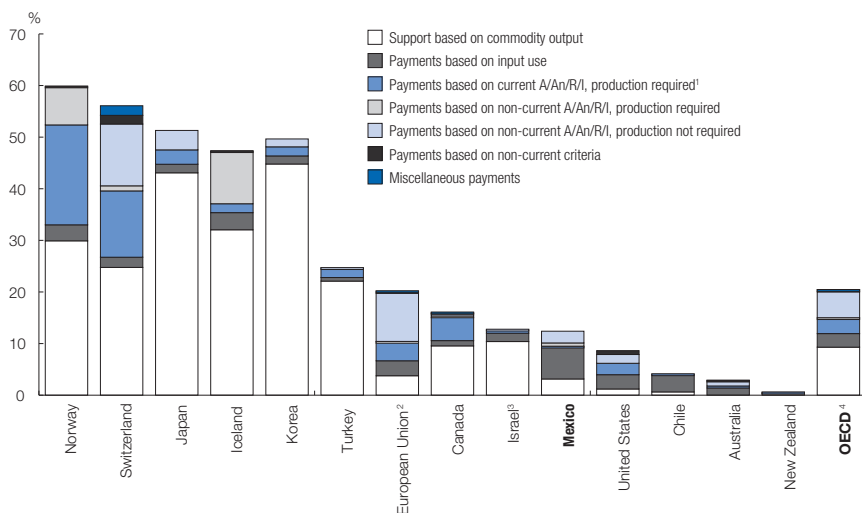
Figure 13.2. **Level and composition of producer support estimate, 1991-2011**

A = Area planted, An = Animal numbers, R = Receipts, I = Income



Source: OECD Producer and Consumer Support Estimates (PSE/CSE) database, 2012.

Figure 13.3. **Composition of producer support estimate by country, 2009-2011 (Percentage of gross farm receipts)**



Note: 1. EU27 in 2009-2011.

2. The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.

3. The OECD total does not include the non-OECD EU member states.

Source: OECD Producer and Consumer Support Estimates (PSE/CSE) database, 2012.

has recently increased, taking the form of a number of important agricultural programmes. These measures do not contribute in a sustainable manner to the competitiveness of the sector.

Electricity subsidies are mainly used to pay for pumping water for irrigation, and are many times higher than payments recently introduced to support infrastructure for better water management. This is inconsistent with Mexico's ambitious objectives for better water management, in the context of combating climate change. Agriculture represents 77% of water consumption in Mexico (see Chapter 14 on water policy). The challenge is to develop policies that simultaneously enhance sustainability, efficient water management and agricultural production. Water should be priced to reflect its associated costs rather than to support its pumping for irrigation. Specific initiatives could be developed to strengthen the link between renewable energy and agriculture by promoting use of biomass as a feedstock to produce energy in rural communities.

The sizeable increase in subsidies to price-hedging contracts since 2005 requires a rigorous evaluation in terms of its cost-effectiveness in managing risk at the farm level. The costs of subsidising international put and call options

on contract prices are becoming very high: total expenditure in 2011 was only slightly smaller than the cost of the whole PROCAMPO programme.

Support to investment and innovation needs to be enhanced

It is very important to strengthen innovation systems to and implementation of innovations. Recent efforts to bring into a single programme investment, extension, and conservation components as in the MASAGRO programme are promising, but their effectiveness needs to be tested in the years to come, in terms of both programme implementation and the strength of the budgetary commitments in question.

Likewise, the objectives of PROCAMPO, the largest agricultural programme in budgetary terms, need to be clarified. This programme provides direct payments to farmers based on historical area. Initially, the payment was provided to landowners (including *ejido* land) who grew any of nine selected crops – most notably cereals, oilseeds and beans – during the three agricultural seasons prior to 1993. Since then, the payment has been based on the historical use of land, allowing farmers to freely decide the most competitive mix of products. By increasing farmers' production freedom, PROCAMPO has improved the market orientation and competitiveness of Mexican farms. For several years farmers could capitalise the stream of payments up to the deadline of the programme, which was foreseen for 2008 and then prolonged until 2012. This capitalised payment was aimed at financing investment opportunities that could improve productivity on the farm. But use of the payments for productive investments has become more difficult in recent years, because of the policy uncertainty over whether the programme would continue.

It is also essential to encourage activities that promote innovation in the countryside. Public spending on research and development (R&D), training and education in agriculture, and food inspection services – which would facilitate investment and innovation, and would improve overall performance of agriculture – is relatively low compared to the OECD average. General support to infrastructure and services that benefit the agricultural sector as a whole represents only 11% of total support to agriculture, well below the OECD average of 26%. Moreover, this percentage has remained constant over the past two decades relative to a growing trend in the OECD area.

Strengthening risk management policies

Recent droughts highlight the importance of managing catastrophic risks for production and the need to efficiently use scarce budgetary resources beyond the price-hedging programme. Risk management policies support farmers' management of their own risks. It is necessary to strengthen policy frameworks

through the provision of information and training to help farmers manage their risks, and through the development of market tools such as insurance. Public policies should be defined in advance and target unavoidable catastrophic risks, while enhancing incentives to develop individual risk management strategies.

Addressing institutional challenges

Reviewing the restrictions on land ownership and trading

Over half of Mexican territory operates under some type of social ownership – *ejidos* or agrarian communities – in which special management regimes govern both collective land and land plots granted to individuals. This communal land system was intended to serve certain societal needs given the absence of the broader social safety nets that exist in most OECD countries. Reforms of the community land system in 1990 had limited practical impact. Although considered socially important, some of the provisions of the community land undermine investment in the agriculture sector, as well as its efficiency and adjustment capacity. In particular, provisions that require the agreement of the *ejido* for converting land into private ownership hinder structural adjustment and investment. As social policies are developed to address these needs, Mexico could phase out current restrictions on land ownership and trading.

Developing an integrated approach

Lack of clarity regarding institutional roles among the many government agencies involved in agriculture, fisheries and rural development led to duplication of activities. It also sometimes gave rise to inconsistent approaches across the full range of government programmes that have diminished the impact of Mexico's significant public expenditures in the sector.

The idea of an integrated approach to agricultural and rural policies was developed in the 2001 Law on Sustainable Development. The commission in charge (CIDRS, Inter-Ministerial Commission on Sustainable Rural Development) has developed a combined budget from several ministries and government bodies, the Special Concurrent Programme (PEC). This programme has not worked within an integrated policy programming process. It operates more as an inventory of programmes rather than a tool to exploit synergies among programmes impacting on rural areas, and includes programmes and institutions not necessarily oriented to rural development. This produces a less-than-accurate picture of the federal rural policy strategy, and data on rural spending that do not fully correspond to the reality on the ground. In order to take full advantage of the PEC, efforts should be devoted to developing a fully integrated framework based on a joint national strategy with common goals and priorities on rural

development. First steps in this direction would include improving transparency regarding the criteria for programme inclusion into the PEC and engaging in a dialogue that could result in the merging, transferring and elimination of certain programmes.

Addressing poverty issues

More than 60% of the Mexican poor are rural. Agriculture policies are not the most appropriate policies to alleviate poverty (see Chapter 2 on poverty issues), although they can have an impact on income and investment opportunities for the poor. Agricultural policies have traditionally had a regressive impact on rural income. Even though the situation has improved following the introduction of PROCAMPO in 1994, large producers continue to benefit disproportionately from agriculture support. These direct payments are also provided to farmers who do not sell their crops but merely consume them, that is to say subsistence farmers who could not benefit from supported prices. Despite recent efforts to set special payment rates for producers with less than five hectares, larger farmers continue to benefit more from PROCAMPO than small (and poor) ones because the payment is proportional to the land surface.

Promoting a multi-sectoral rural policy, which assesses and capitalises on local comparative advantages, is a way to integrate agricultural policy with an improvement of the effectiveness of poverty reduction interventions. Mexico has put in place such a multi-sectoral policy to support rural development over the past decade. The new approach integrates the actions of the different sectoral ministries (for instance SAGARPA and SEDESOL) and the different tiers of government (federal, state and municipal) in rural areas. The aim is to promote non-farm rural activities (NFRA) that can have a positive impact on the income of rural dwellers. Regardless of the agricultural policy in question, it is very important that government interventions in rural areas take into account the assets of the regions, to maximize their usefulness.

OECD Key Recommendations

- Agricultural support should shift towards targeted investments in innovation and infrastructure, moving away from distorting subsidies on variable inputs and price-related measures, in order to improve sector performance and competitiveness.
- Reorient policies towards the provision of general services facilitating the diffusion of innovation in the agri-food sector. These include agricultural information systems; public R&D focused on specific local demands; agricultural education and training; technical and economic advice to help farmers improve productivity; sustainability and competitiveness

measures; and infrastructure investment, notably for transport, irrigation, and marketing. While the provision of income or investment support is likely to positively affect farmers' capacity to invest and innovate, policies should be targeted to remedy specific market failures.

- Agricultural policies should be made more consistent with environmental sustainability, in particular by reducing or eliminating electricity subsidies for water pumping and fuel subsidies. Specific support could be provided to the production of renewable energy through agricultural residues.
- Carry out a rigorous evaluation of the large increase in subsidies to price-hedging contracts.
- Promote broader risk management by providing information and training to farmers and helping farmers cope with unavoidable catastrophic risks.
- As social policies are developed to address these needs, Mexico could phase out current restrictions on land ownership and trading.
- Increase the clarity of the objectives of PROCAMPO with a view to targeting the available funds toward explicit goals and intended beneficiaries.
- Strengthen the Special Concurrent Programme (*Programa Especial Concurrente*, PEC) by developing a coherent, horizontal strategy covering infrastructure, health, education, social and environment policy areas, to foster development in rural zones.
- Adopt a multi-sectoral approach for rural development and focus on promoting innovative ways to deliver key services to rural dwellers and non-farm businesses.

Further reading

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