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POLICY NOTE

Policy brief: Agricultural Policies in Mexico

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Agricultural policies have experienced significant reform in Mexico during the last decade. This reform occurred in the context of a wider move towards a more open and market-oriented economy, as shown by Mexico's participation in NAFTA, WTO and OECD. Membership in each of these three international organizations has had significant institutional and economic implications for Mexico in general and for Mexican agriculture in particular. This note first describes the main thrust of the policy changes that have taken place, and summarises the resulting changes in levels and composition of support. The main economic and structural changes that have occurred in the sector are described and related to the changes in the institutional and economic frameworks. Finally, some preliminary thoughts about how the reform process can be consolidated and advanced are put forward.

Developments in domestic and trade policy

Land Reform

The reform of Article 27 of the Mexican Constitution in 1992, and the subsequent Agrarian Law, opened the possibility of defining individual property rights on land held under the *ejido* or communal property system, forms of social ownership covering an area of 102 million hectares, or about half the area of Mexico. The definition and effective protection of these rights require approval of a two-thirds majority of the *Ejido* Assembly in order to draw the map of the *ejido*, to decide on the use of the land and to register the limits and uses of the land in the National Agrarian Registry. When this process is finished, the *ejidatarios* receive a certificate with a map defining the limits of their plots, and their rights to residential and common land. The programme PROCEDE was launched in 1993 to implement these steps with all the usual guarantees. By August 2004, 69% of the *ejido* and community land had already been certified under the PROCEDE programme.

Developments in trade policy

Agreed in 1994, the NAFTA agreement established a demanding calendar of reduction in agricultural trade barriers between Mexico, the United States and Canada. Moreover, since 1995 the WTO's Uruguay Round Agreement on Agriculture (URAA) required reductions to the Most Favoured Nation (MFN) tariffs applied to Mexico's imports from other countries. However, NAFTA schedules have been more challenging because they apply to Mexico's largest trading partner — the United States — and because NAFTA requires a move to completely free trade with partner countries by 2008. In the transition period, MFN tariffs have been reduced at a much slower pace than the tariffs for NAFTA countries.

According to the provisions of the NAFTA agreement, the transition period[1] for the elimination of Mexican tariffs on most agricultural products from NAFTA countries expired at the end of 2002. The only exceptions are four important products for Mexico where complete elimination of tariffs is delayed until 2008: maize, sugar, milk powder and dry beans. Under the URAA, 2004 was the last year of the transition period for all products. For most products, bound and applied MFN tariffs are well above those within NAFTA, and some of them are well above 100% (Table 1).

1. The schedule and scope for Mexican tariff cuts under NAFTA as agreed with the United States are not the same as those agreed with Canada. The latter are, in general, less ambitious.

Table 1 Tariffs on imports of selected agricultural products

	MFN bound in 2004	Applied MFN 2004	NAFTA 2004 (from US)	NAFTA tariff zero in
Wheat	67% *	67%	0%	2003
Maize	**194% ***	**194% ****	**73% ****	**2008**
Barley	115% *	115%	0%	2003
Sorghum	45%	0%-15% ***	0%	1994
Rice	45%	20%	0%	2003
Soyabeans	45%	20%	0%	2003
Sugar	**0.36 $/kg ***	**0.36 $/kg**	**0.25 $/kg**	**2008**
Dairy products (except milk powder)	38%	20%	0%	2003
Milk powder	**125% ***	**125% ****	**47% ****	**2008**
Beef	45%	25%	0%	1994
Pigmeat	45%	20%	0%	2003
Poultrymeat	234% *	234%	0%	2003
Eggs	45%	45%	0%	2003
Dry beans	**125% ***	**125%**	**47% ****	**2008**
Tomatoes	36%	13%	0%	2003
Potatoes	245% *	245% *	0%	2003
Apples, pears and other fruits	45%	23%	0%	2003

* Intra-quote tariff is zero.
**The tariff rates depend on the dates in the year.
*** Intra-quota tariff is 50%.
Sources: Secretaria de Economia, *New import tariffs 2004*; WTO and EU Commission, *Applied tariffs database*.

Developments in domestic policy

With the reduction in tariff protection described above, domestic policies have become more relevant, and significant developments have occurred in the last decade. The agricultural program that best symbolises the reform in domestic agricultural policies in Mexico is PROCAMPO. It was launched in 1994 with the intention of supporting the income of farmers and facilitating adjustment in a defined period of reducing price support and tariff reductions under NAFTA. It consists of direct payments to eligible farmers according to the area planted in an historical base period with the level of the payment related to the expected magnitude of the decline in output prices, on condition that the land is used for agricultural or livestock production or is in an environmental program. Since 2001, there is a minimum payment per farmer equivalent to the payment entitlement for one hectare. Since 2002, PROCAMPO payments can be capitalized in a single payment up to 2008, subject to developing an investment project in agro-food, forestry or fishing. PROCAMPO is due to come to an end in 2008.

An important part of the reform process has been the progressive dismantling of the agencies that were in charge of managing the system of domestic supported prices. The most important was CONASUPO. This state enterprise played a major role in Mexican agricultural markets from its creation in the 1960s. Until the 1990s, CONASUPO was in charge of implementing price support schemes for barley, dry beans, maize, wheat, rice, cottonseed, sesame seed, sorghum, soybeans, safflower and sunflower seed, and was the main trader in the Mexican market.

ASERCA, already in charge of PROCAMPO, took over CONASUPO's role in trying to improve the marketing of Mexican agricultural production. Since 1995, it has provided some marketing subsidies to the first buyers of main crops in some states under the condition of buying at a minimum administered price.[2]

2. Payments for rice were always provided directly to producers as output payments.

In 2001, these subsidies were converted into per tonne direct payments to producers that in 2003 were explicitly designed to be countercyclical regarding price developments. This is a sort of deficiency payment to reach a target price (*ingreso objetivo*) in combination with PROCAMPO.

Since 1996, the set of programmes under the *Alianza Para El Campo* and *Alianza Contigo* (Alliance for Agriculture / Alliance with you), aims at enhancing investment on farms, especially in poor rural areas. It groups a variety of programs that provide subsidies to inputs (mainly investment) and on-farm services. A new program (PROGAN) of payments per head of cattle with traceability conditions was introduced in 2003.

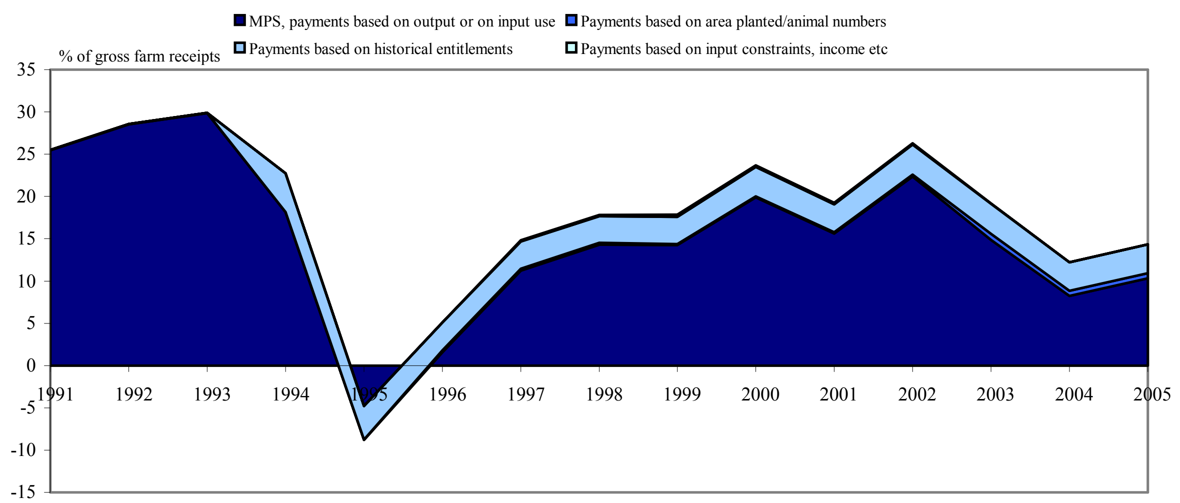
The 2003 National Agreement for Agriculture tried to respond to some unrest coinciding with the end of the NAFTA transition period for most products. The agreement foresees active action against "unfair" competition in trade, food safety and quality and establishes the already mentioned PROGAN and target price programs. It also enhances the powers of a new agency dealing with credit for agriculture, *Financiera Rural*. A new common subsidised price for electricity used for agricultural production has also been decided, and diesel used for agricultural production joined the list of subsidised inputs granted in response to the unrest in 2003.

The level and composition of support to farming in Mexico

The OECD uses the Producer Support Estimate (PSE) to gauge the level of government intervention in the sector, using a method that is applied consistently to all OECD member countries, and increasingly to large non-member countries too. The current estimate for Mexico is 14%, meaning that 14% of gross receipts in the sector come from support, either price support or government expenditure that accrues to farmers. This is much lower than the OECD average (29%), not much different from the 16% currently reported by NAFTA partner the United States, but significantly lower than Canada which currently reports 21%.

Prior to the switch to PROCAMPO, virtually all the support to Mexican agriculture came through the most distorting channels – border protection or input subsidies. Now, a quarter of all support is delivered through PROCAMPO, which is both less distorting in terms of its production impacts and more equitable in its impacts on income distribution. However, input subsidies – for irrigation, fuel and electricity – are also important in the overall pattern of support and, despite their highly distorting nature, have actually increased in relative importance in recent years. Figure 1 shows the level of PSE for the period since 1991 as well as the composition of the support.

Figure 1. Level and composition of PSE — Mexico 1991-2005



Impacts and Implications

Sorting out the influence of the changed policy and support structure as compared to other forces driving agricultural adjustment is difficult, but a number of observations can be made.

As might have been expected from a reduction of protection and a switch to decoupled payments crop production has fallen somewhat relative to trend, has become more land intensive and less labour intensive, and seemingly less purchased input intensive. These developments are summarised in Table 2. Imports of some major crops have grown noticeably, but given that domestic production of most of these crops has also increased, the import growth appears to reflect primarily an expansion of domestic demand. At the same time, domestic livestock production has increased much more rapidly than imports, and exports of some labour-intensive agricultural products have grown.

Table 2. Production and imports of main agricultural products in Mexico 2001-2004 and 1990-1993

	Average production 90-93	Average production 01-04	Change in production	Average net imports 90-93	Average net imports 01-04	Change in imports relative to 90-93 production
	(thousand tonnes)		(per cent)	(thousand tonnes)		(per cent)
Wheat	3799	2919	-23	917	2460	41
Maize	15985	20638	29	1691	5112	21
Barley	541	893	65	171	139	-6
Sorghum	4555	6441	41	3547	4167	14
Rice	356	252	-29	332	622	81
Soyabeans	598	115	-81	1747	3829	348
Total crops above	25833	31258	21	8406	16329	31
Sugar	3577	4937	38	393	-204	-17
Beef	1202	1483	23	-21	42	5
Pigmeat	803	1058	32	47	208	20
Poultrymeat	908	2095	131	70	234	18
Total meats above	2912	4636	59	95	485	13
Milk	6807	9646	42	1957	1502	-7
Eggs	1137	1891	66	9	13	0
Dry beans	1168	1332	14	83	85	0
Tomatoes	1713	2211	29	-381	-827	-26

Mexico's state of development is such that considerable shedding of labour from the agriculture sector could be expected to continue – it has already fallen from 27% in 1990 to 16% in 2004. Although the policy changes described here probably contributed to that reduction, other factors are likely to have been much more important. Moreover, it is unclear how much of the adjustment in labour use in Mexican agriculture came about via changes in the amount of time farm households devote to on-farm versus off-farm activities, and how much may have come about via people leaving the sector.

Although much work remains to be done to understand fully their distributional consequences, some aspects of the reforms probably brought about improved outcomes. Eligibility for PROCAMPO payments is based on whether a farmer *produced* an eligible crop in some base year. Importantly, eligibility does not depend on whether the farmer sold the crop. Many PROCAMPO recipients, most likely the poorest, produce only for home consumption. So, for that part of the population, the combination of reducing market intervention and introducing income payments yielded an unambiguous net income gain. A recent change in the rules making the one-hectare payment a minimum even for farmers with eligible plots of less than one hectare further augments this progressive re-distributive effect.

Defining land rights inside the *ejidos* has been a significant step, even if so far it has had a limited impact on the agricultural land market in Mexico with some expansion of land renting. The land in the *ejidos* had always been rented informally. Now this can be done in the certified plots with more guarantees, but the amount of agricultural land that has been sold from the *ejidos* seems to be marginal. However, allocation of individual property rights to land may already have improved incentives for investment in the land and, in the long run, with easier transfer of land among individuals, this process could be significantly strengthened.

The Way Forward

Overall, Mexico's agricultural policy reforms over the past two decades must be judged in a positive light. Despite recent moves back to price based interventions, links between the domestic and world markets for most of Mexico's agricultural commodities and farm inputs are today much closer than when the process of agricultural policy reform began. This improvement in market orientation is all the more remarkable because it occurred in a country at a relatively early stage in the economic development process, undergoing an economy-wide transformation. The way the reforms were implemented, gradually individualising property rights to land and replacing coupled price supports with less coupled historical entitlement payments, sets an example that could serve well for implementing reform in other, more advanced, OECD countries that still adhere to outdated policies.

Mexico now has a unique opportunity to consolidate and further deepen the reforms already undertaken. The removal of remaining high tariffs under NAFTA is already scheduled. Legislative authority for a key programme – PROCAMPO – is also due to expire.

Mexican agriculture is already quite open to market signals and will be more so once tariff elimination under NAFTA is completed. Some key policy measures have been decoupled to a significant degree and are being implemented in ways that ensure that they are more oriented towards the poorest and most needy households than the measures they replace. These policy trends could be reinforced through improved targeting that would further enhance their social and distributional role.

Mexico continues to deliver some support through price-linked output payments. Consideration should be given as to whether scarce public funds are best used in this way, given Mexico's urgent needs in terms of developmental investment in infrastructure, education, sanitary or other services that would help the sector become more efficient and competitive. The same questions could be asked about the growing emphasis on variable input subsidies, particularly those to energy. These are potentially highly distorting, in addition to which they may well be adding to the pressure on natural resources, especially water. This is an area in which particular attention is required. On land reform, remaining obstacles to land consolidation and the development of a more efficient land market should be removed to allow improved resource allocation.

As the economy evolves, broad rural development measures will need to be reinforced if households whose only resource is a small plot of land are to be given the opportunity to increase their income and diversify their income sources without migrating to the largest urban centres.