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# Mizuho Economic Outlook & Analysis

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## *Upcoming agricultural policies in the autumn of 2016*

*The key agendas are further promotion of feed rice production  
and the introduction of income insurance system*

### < Summary >

- ◆ In November 2015, the government of Japan decided “The TPP-related policies in the fields of agriculture, forestry and fisheries” and stated that it will come up with concrete measures for 12 agendas listed in the decision by the autumn of 2016.
- ◆ Among the agendas, further promotion of feed rice production and the introduction of the income insurance system are viewed as mitigation measures prepared for the abolishment of a set-aside program for rice in 2018. The abolishment might have a huge impact on the future course of Japan’s agriculture, changing the long-term trend of protecting rice growers through giving out generous subsidies.
- ◆ In order to take full advantage of the change, it is important for the government not to offer excessive financial support to farmers through the mitigation measures mentioned above. What it should do is to narrow down the range of support provided through the measures.

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## 1. Additional TPP-related measures to be decided by the autumn of 2016

In November 2015, about a month after ministers of 12 Trans-Pacific Partnership (TPP) countries announced conclusion of their negotiations, the government of Japan decided “The TPP-related policies in the fields of agriculture, forestry and fisheries<sup>1</sup>”. The decision stated that the government would work intensively toward extending measures a) to encourage competent farmers to expand their business, and b) to maintain sustainable business environment mainly for the producers of five key products (i.e., rice, wheat, beef/pork, dairy products, sweetening resources crops). Some measures listed in the decision such as increasing subsidies to farmers who want to improve profitability by procuring new machineries and facilities came into effect as early as January 2016, while other measures such as the government’s purchase of more domestic rice are planned to be carried out only after the TPP agreement actually takes effect.

However, there remains yet more measures to be decided later on. The decision stated that the government would continue to consider policies concerning 12 agendas shown in **Table 1** and would come up with concrete measures by the autumn (probably meaning November) of 2016.

**Table 1: Twelve agendas for consideration**

1.Enhancement of human resources in agriculture	7.Introduction of a “ <u>check-off system</u> ” [Note 2]
2.Revision of the pricing mechanism for production materials (such as feed, farming machines and fertilizer)	8.Introduction of the income insurance system which supplements farmers’ income for all crops and livestock
3.Establishment of processing and distribution systems to encourage transactions in favorable terms for producers	9.Further promotion of feed rice production
4.Re-examination of the <u>agricultural land improvements</u> [Note 1]	10.Steady operation of the <u>stabilization system of compound feed prices</u> [Note 3]
5.Formation of strategic export system	11.Strengthening of production infrastructure for cattle and dairy farming
6.Labeling of raw materials and country of origin on all processed foods	12.Improvement of farmers’ employment structure in rural communities

Notes: 1. The improvements are mostly funded by the government.

2. A system in which producers contribute money to fund and then utilize it to take the initiative in carrying out sales promotion activities.

3. A system for granting compensation payment to livestock farmers during times of rising compound feed prices.

Source: Made by MHRI based on the Headquarters on Creating Dynamism through Agriculture, Forestry and Fishery Industries and Local Communities

<sup>1</sup> <http://www.kantei.go.jp/jp/singi/nousui/dai17/siryou1.pdf> [in Japanese]

## **2. Two agendas with close relations to the abolishment of a set-aside program**

Among 12 agendas stated in “The TPP-related policies in the fields of agriculture, forestry and fisheries”, two agendas especially worth noting are “further promotion of feed rice production” and the “introduction of the income insurance system”. This is because these agendas are closely related to the abolishment of a set-aside program for rice in 2018, which is planned to be carried out regardless of whether the TPP takes effect or not. The major policy change for rice, the most common staple food, might have a huge impact on the future course of Japan’s agriculture.

The government plans to abolish the set-aside program by quitting to set the target ceiling for table rice production in each prefecture. Since 1970, the government has been trying to prevent oversupply and price decline of table rice by setting the target acreage or volume (currently the latter) of rice production, encouraging farmers not to grow too much table rice and offering subsidies to those who cooperate with the program. However, in November 2013, the government decided not to set the target from 2018 onwards on the ground that farmers should have more freedom in choosing what to grow.

Further promotion of feed rice production and the introduction of the income insurance system can be both viewed as mitigation measures prepared for the abolishment of a set-aside program.

With regards to the promotion of feed rice production, the government has already taken the measure of increasing subsidies to feed rice growers with high yields by up to approximately 30% since 2014<sup>2</sup>. This measure has led more farmers to grow feed rice instead of table rice on their paddies and propped up the price for table rice, contributing to farmers’ income. The feed rice acreage increased approximately from 22,000 hectares in 2013 to 80,000 hectares in 2015. However, the measure has been criticized for increasing fiscal burden and it would incur even more criticism if the ruling parties’ current plan to make the payment of the subsidies more permanent were to be realized. According to the estimate by the Ministry of Finance, the subsidies for feed rice production can increase as much as 100 billion yen if the production volume reaches the government’s goal for 2025, which totals 1.1 million tons. Besides, the measure has also been criticized for delaying the retirement of small-sized farmers and hindering farm land consolidations, which would enable cost reduction through economies of scale.

With regards to the income insurance system, the government has been considering it

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<sup>2</sup> The government promotes feed rice production for the purpose of preventing farmers from producing too much table rice on their paddies. The government also encourages high-yield production of feed rice so that the price would be more competitive with other feed ingredients (ex. maize).

for some years and plans its introduction in 2018 at the earliest. For core farmers who grow rice, wheat, soybeans, and some other crops, the government currently offers a measure (commonly called *narashi* meaning “to even out”) to compensate for reduced income when farmers’ annual income fall below the standard level<sup>3</sup>. The government envisions to abolish and consolidate the *narashi* with the income insurance system which supplements farmers’ reduced income for all crops and livestock in times of natural disasters, major price declines, etc. Basically, farmers eligible for subscription of the insurance are likely to be limited to those who file “blue form tax return” which entails more detailed financial information compared with the other form (i.e., white form of tax return) to the government<sup>4</sup>. While the new system is expected to offer stronger safety net for farmers, some agricultural experts fear that the system a) overlaps with existing mutual aid insurance called *NOSAI* which compensates farmers’ income for some crops and livestock in times of natural disasters, and b) may invite moral hazard among farmers (Chart 1).

**Chart 1: Mitigation measures prepared for the abolishment of a set-aside program**

[ Mitigation measures ]

<u>Further promotion of feed rice production</u>	<u>Introduction of the income insurance system</u>
<ul style="list-style-type: none"> <li>– The government has increased the subsidies to feed rice growers with high yields since 2014</li> <li>– There is a possibility for the payment of the above subsidies to be made more permanent</li> <li>– Criticisms for increasing fiscal burden and hindering farm land consolidations exist</li> </ul>	<ul style="list-style-type: none"> <li>– The government plans to introduce the system in 2018 at the earliest</li> <li>– Farmers who file "blue form tax return" to the government are eligible for subscription of the insurance</li> <li>– Overlap with <i>NOSAI</i> and the risk of inviting moral hazard are major concerns</li> </ul>

Source: Made by MHRI

### 3. Importance of avoiding overprotection

Amidst the criticism against the promotion of feed rice production and the concerns for the introduction of the income insurance system, it is important for the government not to offer excessive financial support to farmers. What it should do is to narrow down

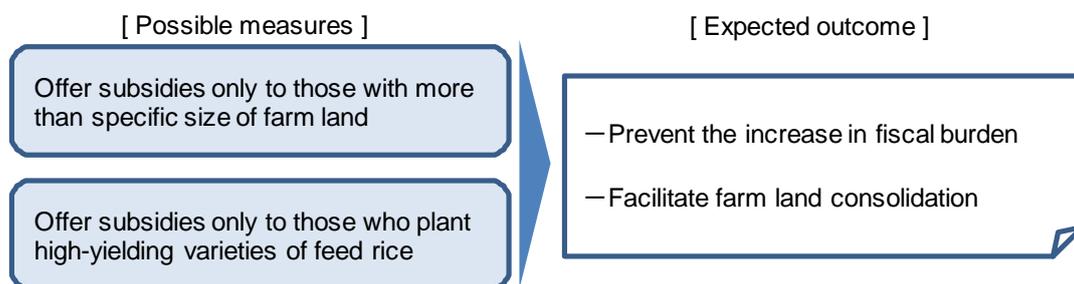
<sup>3</sup> Under the measure, 90% of the balance (the standard level of income minus the income for the reference year) is compensated. The government and core farmers contribute to the compensation fund by the ratio of 3 to 1. The standard level is calculated through averaging three out of five recent years of annual income in each prefecture, excluding two years which showed the maximum and the minimum figures.

<sup>4</sup> It has been reported that approximately 42,000 farmers filed blue form tax return in 2015 whereas the population of farmers reach 1.9 million. Note that the farmers herein include part-time farmers.

the range of support so that the abolishment of a set-aside program would exert positive effects on promoting “aggressive development of agriculture”<sup>5</sup> without spoiling farmers’ self-reliant efforts.

In order to narrow down the range of support for feed rice production, for example, such measures as offering subsidies only to those with more than specific size of farm land or to those who plant high-yielding varieties can be suggested (**Chart 2**). With regards to size of farm land, requirements for the *narashi* until March 2015 seem fit to be applied. The requirements had limited the payment of subsidies to a) farmers who manage (either by owning or borrowing) more than 20 hectares of land in Hokkaido, b) farmers who manage more than four hectares of land in places other than Hokkaido, and c) community-based farm cooperatives which manage more than 20 hectares of land. The suggested measures are expected to contribute to preventing the increase in fiscal burden as well as facilitating farm land consolidations, thereby making it easier for motivated farmers to expand their business operations and improve profitability through cost reduction.

**Chart 2: Examples of narrowing down the support for feed rice production**



Source: Made by MHRI

The abolishment of a set-aside program in 2018 may be a catalyst for changing the long-term trend of protecting rice growers through giving out generous subsidies related to the program. In order to take full advantage of the change, the government should prevent itself from allowing mitigation measures (i.e., further promotion of feed rice production and the introduction of the income insurance system) to be overprotective. In doing so, the government can truly claim that it has paved the way for “the new era of agricultural policies”<sup>6</sup>.

<sup>5</sup> Quote from "Basic Policy on Economic and Fiscal Management and Reform 2016" by Cabinet Office of Japan.

<sup>6</sup> The government’s recent slogan which appeared in “The TPP-related policies in the fields of agriculture, forestry and fisheries” in November 2015 as well as in the policy speech by Prime Minister Shinzo Abe at the opening of the 192th session of the Diet in September 2016.