Forest Trends
Information Brief
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The Regulatory Imperative

Policy Lessons from the Lao Rubber Sector for Supporting Smallholder Livelihoods and Land Tenure

This Information Brief is based on one of the first research efforts on the fall in rubber prices of the last five years and its implications for the Lao rubber boom beginning in the 2000s.

Findings from this study are now being used as part of Forest Trends' ongoing research and policy dialogue on the legal and *de facto* dimensions of land tenure in the Mekong sub-region, supported by the Mekong Regional Land Governance (MRLG) Project.

Key Messages

1. Efforts to scale up smallholder rubber production in northern Laos have run into a number of problems, including unattractive terms of credit, state coercion in farmer enrollment, uneven contract design and enforcement, and most recently price volatility. While global prices are beyond the control of relevant authorities in Laos and China, falling prices since 2011 were exacerbated by these other policy and regulatory issues. Recent rises in prices have provided some relief, but do not address underlying concerns.

2. Regulatory shortcomings were not primarily due to a lack of resources. The Chinese government provided public financing in the form of subsidies to Chinese companies working with Lao farmers in order to replace opium production with rubber; these resources could have helped scale up the public financing model pioneered in Laos's Ban Hat Nyao village. Instead, subsidies seem to have been largely captured by companies rather than leveraged to help Lao farmers survive the ups and downs of the global rubber market.

3. Lack of transparency in pricing, contract terms and use of subsidies makes the northern Lao rubber sector difficult to evaluate. Available evidence suggests that Lao farmers have received low prices for their rubber not only due to depressed global demand, but also due to opportunistic behavior by the Chinese companies that hold the monopoly on importing Lao rubber into China. Heightened transparency should be a requirement for rural development cooperation projects that receive state financing in the future.

Introduction

Spurred by a booming global economy, strong Chinese demand, and successful "early mover" examples like the village of Ban Hat Nyao, authorities across northern Laos encouraged smallholder rubber planting on a large scale during the mid-2000s. Unlike southern Laos, where large-scale land concessions to Vietnamese companies formed the dominant business model, rubber in the north followed a smallholder model based on a mix of independent smallholding and contract farming between poorer Lao farmers and Chinese and local companies.

This Info Brief, based on research conducted in 2015, synthesizes lessons learned from efforts to scale up the Ban Hat Nyao model via contract farming with Laos's rural upland poor. Despite the slight rise in rubber prices since early 2016, the lessons outlined below are general, and focus on the need for more active regulation and transparency in cases where private companies work with smallholders. They are thus relevant to sectors and areas beyond rubber in northern Laos.

Research Findings

1. **Even before the fall in rubber prices during 2012-2015, the northern Lao rubber sector was in trouble due to the consolidation of plantation holdings caused by the unsuccessful effort to scale up smallholder rubber using a contract-farming model.**

   Provincial-level policy commitments to smallholder rubber were inspired by the success of Ban Hat Nyao, a Hmong village in central Luang Namtha province. But when Lao and Chinese officials introduced a contract-farming model with Chinese companies to finance the establishment of plantations and purchase the rubber produced by smallholders, these efforts ran into three sets of problems.

   Expensive credit: Unlike in Ban Hat Nyao, where villagers received a state-subsidized loan to finance their plantation establishment, contract farming with Chinese rubber companies was based on a sharecropping model, in which farmers would be paid cash for 50–70 percent of the rubber they produced, and the rest would go to pay the company back for the seedlings and other inputs. Many Lao farmers, however, were uninterested in such an offer; they thought this was too expensive. Participation rates in the initial "2+3" contract farming projects were thus very low, despite the companies receiving subsidies from the Chinese government.

   Coercive enrollment: As a result of low farmer participation, Chinese companies and Lao officials developed a second contract-farming model, termed "1+4". Under this model, company rubber zones were created in upland villages in order to mandate participation, with a fraction of the trees being returned to villagers after planting. This model targeted poorer farmers who had been reluctant to take on the risks of "2+3", and in particular the 7-year waiting period between planting and harvest. But while it created wage labor opportunities for many such farmers, its top-down and coercive land zoning departed significantly from the community-controlled land use model that had helped Ban Hat Nyao succeed. Given these beginnings, it is hardly surprising that many of the farmers enrolled into "1+4" plantations sold them in the years that followed.

   The rise of large-holders: As poor smallholders began to sell the trees they received under the "1+4" scheme, many of the buyers were wealthier Lao elites (include public officials) and Chinese entrepreneurs based in provincial and district centers. These sales were largely informal, and their extent and locations are thus not captured in official statistics. But they are believed to be widespread; as one source in Oudomxai said, "Selling rubber plantations is normal in this province. The [sellers] are mainly poor households in villages, [while] buyers are mainly businessmen from the provincial capital as well as Chinese investors."

2. **When rubber prices fell, many large-holders simply stopped tapping, while many households continued to tap, although at very low prices. Provincial authorities' limited regulatory leverage and unwillingness to use the leverage they did have, meant that farmers suffered at the hands of both low global prices and opportunistic behavior on the part of rubber companies.**

   Farmer responses: In describing their responses to falling rubber prices, farmers distinguished between plantations tapped with household labor (i.e., true smallholders) and larger plantations tapped using hired labor. As one villager put it, "With [prices at] 4 Yuan/kg, we have to tap our rubber by ourselves. In the case of households that have large areas of rubber plantation, they tap only a little part based on their household labor forces." The extent of untapped rubber in northern Laos is unknown, but the pattern of plantation sales to wealthier buyers suggests that it is fairly high. Farmers we spoke to in 2015 told us that tapping rates across the north had fallen significantly due to low prices, and in some places were as low as 10 percent.

   Limited regulatory leverage: Most of the contracts provincial authorities had signed with the Chinese rubber companies said that prices would be based on unspecified "market" conditions, and few contracts included minimum-pricing guarantees (also see next point). In late 2012, Luang Namtha provincial authorities established a Provincial Rubber Management Committee to help smallholders to get better prices by calculating recommended prices, but these were non-binding, and Chinese companies often offered much lower. As rubber stocks piled up, the Committee negotiated a sale between Lao growers and Chinese companies, but the price increase was minimal, and came at the cost of waiving taxes that the companies would have owed to the government.

Unused regulatory leverage: In three of the districts visited, government authorities indicated that minimum prices had been written into some of the rubber company contracts, but that these were not being enforced. No hard copies of the contracts were provided to verify this, despite promises to share them. It appears that in some cases, government staff did not see the contracts as fully binding; as one explained, the company's contract had a floor price, but the company "could not afford to pay based on the contract." In another district, a government official told us that despite the existence of a contracted floor price, "rubber prices in our province and district are based on what the buyer offers."

Limited help from collective marketing: Collective marketing groups exist and were functioning well in Ban Hat Nyao and another village we visited, but effectiveness is limited:

- Limited increase in prices: Aggregation adds only about CNY 0.5 to 1 per kg to the prices farmers receive; while not insignificant, this means that collective marketing alone can only do so much; the price swings of the last few years are much larger.
- Low participation undermines collective leverage: Due to the combination of low prices and the consolidation of plantations, in some villages, not enough people were tapping to make a marketing collective worthwhile.
- Cost of overhead constrains participation: Collective market efforts typically incur overhead fees for coordination and negotiation costs. Villagers in at least one location reported not wanting to form a marketing group because they did not want to pay these fees.

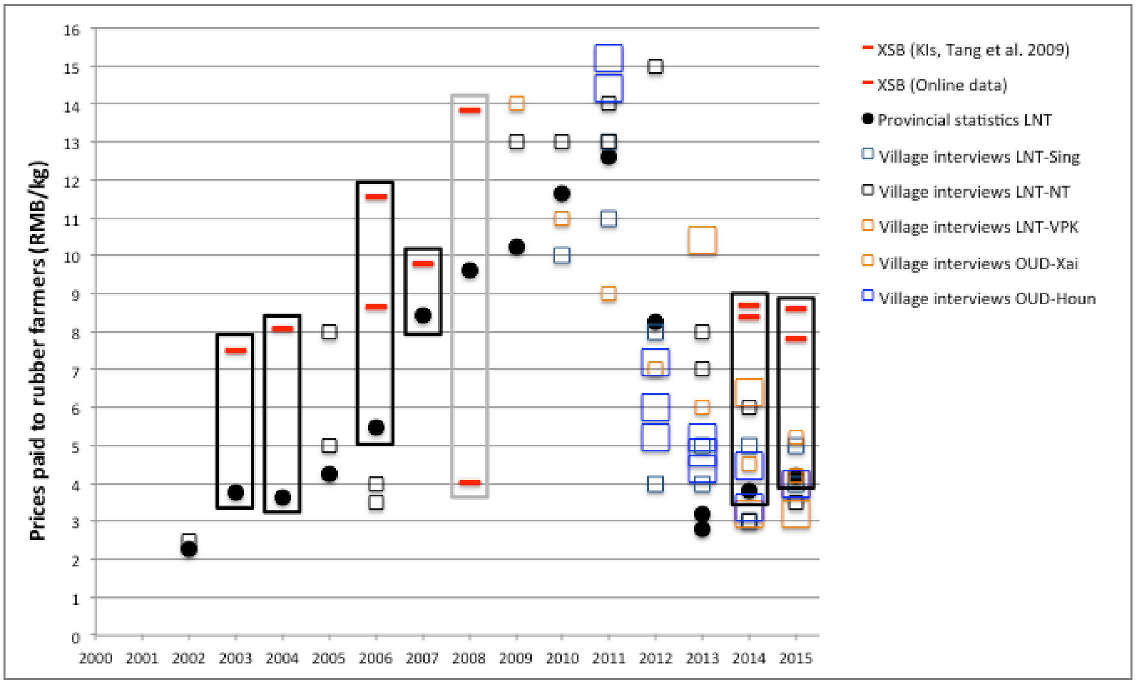
3. **Key details about the rubber sector in northern Laos remain opaque. Available evidence nonetheless suggests low prices are caused not only by weak global demand, but also by opportunistic behavior by Chinese companies that were insufficiently regulated, despite receiving public subsidies.**

Shortage of price data: While purchase prices are posted daily at Chinese processing facilities in northern Laos, and provincial authorities maintain annual (average) statistics, higher-frequency (weekly or monthly) data on rubber purchase prices is not readily available for either Laos or China. This basic form of transparency would help farmers and government authorities monitor changes in price and would facilitate more strategic decision-making at the household as well as provincial government levels.

Opportunistic behavior and market power: Due to the lack of widely available data, it was possible to compare purchase prices for rubber in Laos and China for only six years between 2003 and 2015 (Figure 1, black boxes). The data for these years suggest significant differences between purchase prices for Lao and Chinese rubber producers, with Lao producers getting roughly half the prices of their Chinese counterparts. While some of this difference is probably due to transportation costs and differences in quality, the discrepancy between the Provincial Rubber Management Committee's recommended prices and actual prices offered, as well as numerous complaints about the monopoly power of Chinese rubber traders, suggests that market power is also a factor.

Insufficient regulatory oversight: A small number of Chinese companies control the import quotas for Lao rubber into China. Although these companies received substantial subsidies from the Chinese government beginning in 2004, the history of the "2+3" and "1+4" contract farming schemes suggests that these subsidies were not administered in ways that required them to be used for their intended purpose of helping Lao farmers convert to crops other than opium. One reason for this may have been that the subsidies were administered at the provincial level, where Chinese business interests may have been more powerful than if subsidies had been administered centrally.

Figure 1: Farm-gate Rubber Prices in Northern Laos versus Xishuangbanna, Yunnan



Source: Interviews (Laos data) and secondary and online sources (China data); see main report for details

Recommendations

1. **Invest in regulation and active policy smallholder support for commodities that are deemed strategic.** Countries that have made rubber a successful smallholder crop have invested heavily in not only technical support, but also periodic price supports when global demand falls. Moreover, when companies are involved in helping bring smallholder commodities to market, these should be regulated in order to facilitate fair dealing and smallholder benefit so that companies do not behave opportunistically. Especially since many companies in Laos receive monopoly concessions over particular areas, more active (and state-funded) regulation is often needed.

2. **Explore possibilities for transnational regulatory cooperation.** Laos and China share an interest in having Chinese rubber companies work well with Lao smallholders, given the social goals of China's poppy-replacement program. In light of Beijing's recent efforts to develop guidelines for Chinese companies investing abroad (including in the rubber sector), openings for regulatory cooperation are likely to exist.

3. **Support community efforts to regulate land use by increasing community land tenure.** Community control over land management was a key feature of Ban Hat Nyao's success, but it was not only a function of strong internal rules and customary leadership: it also depended on outside recognition and support. Today, as individual land deals grow increasingly prevalent – such as in the banana sector – the importance of communities' ability to regulate land transactions within their own borders cannot be overstated. The type of locally organized, outwardly recognized land-use planning that helped Ban Hat Nyao succeed highlights the benefits of community land tenure and should be encouraged on a wider scale.

4. **Institutionalize knowledge and data management.** During the course of our research, we identified at least three areas where information should have been available, but was not. These examples – contracts not being on file, missing price data, and out-of-date statistics on different types of rubber planting schemes – highlight the need for information management and, in some cases, additional data collection, by relevant government institutions. In cases where this information is on file with companies, these shortcomings highlight the need for greater disclosure.

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ບໍລິການ-ສົ່ງເສີມກະສິກຳຮອບດ້ານ LURAS Lao Upland Rural Advisory Service ບສກຮ

5. **Support further research that builds on the above-mentioned findings.** Our work identified a number of specific topics that demanded additional investigation. These include:

   - ***Encouraging better conditions for smallholders in contracts and enforcement of contract law:*** How can existing laws, regulations and contracts be better enforced to help smallholders? Can existing contracts that are inadequately detailed be renegotiated in order to help farmers? How can contracts be better written in the future?
   - ***Household impacts of low prices:*** As falling prices have made rubber production rely only on household labor, what have been the impacts of this at the household level and below (e.g., on the distribution of labor among family members)?
   - ***Indebtedness***: Has indebtedness caused by the rubber price crash been a factor in the boom in land transactions (e.g., land rentals for bananas) that has occurred over the last few years?
   - ***Differing interests within the Chinese agribusiness sector***: What are the interests of various Chinese companies operating in the rubber and other agribusiness sectors? Which companies are committed to long-term development of a particular sector (e.g., the rubber sector), versus looking for shorter-term business opportunities? What types of opportunities exist for Lao and Chinese authorities to better encourage or regulate Chinese investors to support shared interests in the development of a sustained smallholder economy in northern Laos?

For More Information

- **Read the paper:** http://mrlg.org/resources/after-the-boom-responding-to-falling-rubber-prices-in-northern-laos/
- **Read about the larger project**: http://publications.mrlg.org/wp-content/uploads/2016/03/Multi-Scalar-Evidenced-Based-Dialogue-A-Regional-Approach-to-Improving-Small-Holder-Land-Tenure-final.pdf

Contact the Authors:

- Michael Dwyer, PhD, Associated Senior Research Scientist, Centre for Development and Environment, University of Bern: dwyerdwyer@gmail.com
- Naomi Basik Treanor, Manager, Forest Policy, Trade & Finance, Forest Trends: nbasik@forest-trends.org