



**Strategic Road Maps for the
Development of the Agribusiness
Industry, Halal Food Industry, and
Islamic Banking and Finance in the
Bangsamoro**

Prepared for
The Bangsamoro Development Agency
by the **Foundation for Economic
Freedom**

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The preparation of the reports involved a series of consultations with officials from the National Government, Autonomous Regional Government, BDA and other official agencies, and representatives from the private sector, aid agencies, civil society, and the academe from both the island and mainland provinces of the Bangsamoro.

The reports also draw on the draft Bangsamoro Development Plan (BDP) and other selected publications and reports written in recent years on the topical themes covered in the reports, as well as on a series of workshops conducted on "Improving the Business and Investment Climate in the Bangsamoro" organized principally by the FEF and Philippine Center for Islam and Democracy (PCID), financed by the Australian Government.

The project team consisted of Thomas Allen (Team Leader), Urooj Malik (Senior Advisor), Alex Casiple (agribusiness expert), Jamil Humza Olermo (Halal industry expert), Ikram Tawasil (Islamic finance expert) and Gary Olivar (banking and finance expert). Research support was provided for the Integrated Report by Jaymee Alco-Cabangbang. Administrative support was provided by Cecilia Bermejo and Sarah Lasiak and editorial support by Ranna Pintor.

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Thomas W. Allen
Fellow and Team Leader
Foundation for Economic Freedom
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PART 1

INTEGRATED REPORT

INTEGRATED REPORT ON THE DEVELOPMENT OF THE AGRIBUSINESS INDUSTRY, HALAL FOOD INDUSTRY, AND ISLAMIC BANKING AND FINANCE IN THE BANGSAMORO¹

1. OVERVIEW

The struggle for self-determination or real autonomy is more than just political in nature – it extends to genuine fiscal and economic autonomy. While the Comprehensive Agreement on Bangsamoro appears to provide substantial revenue support to the new Bangsamoro Political Entity when it finally assumes the responsibilities of governance, getting the region out of the backwaters and on to a path of sustained and inclusive growth will be a daunting task for both planners and implementers of development programs in the new Bangsamoro.

This challenge can be met. But it will require a development strategy for the Bangsamoro that ensures environmentally sustainable and inclusive growth focused on generating employment and eliminating poverty, while recognizing the cultural and religious aspirations of the people of the region. A robust private sector will be a critical component of this strategy.

Harnessing the full potential of the *agriculture sector* will also be a critical component of this strategy. The agriculture sector now represent the economic backbone of the Bangsamoro, employing 70% of the working population and accounting for over 60% of the Regional Gross Domestic Product (RGDP). However, it is a sector of subsistence. The sector's potentials were never taken advantage of over many decades, and the years of war and the accompanying years of long neglect of agricultural productivity led to lost opportunities, chronic poverty, and consequent continued restlessness among the people of the region.

Despite its current weaknesses, the restoration of peace opens the opportunity to exploit the vast untapped and underutilized tracts of highly arable land that, if properly managed and utilized, offers the potential for sustainable and inclusive growth for many years to come.

Harnessing this potential is the principal focus of the first sector report. It looks at the critical factors that have held back the performance of the agriculture sector during the years of conflict, and proposes a road map for dealing with these factors and exploiting the opportunities over the coming years. The agriculture sector will remain the economic backbone of the Bangsamoro, but it could become a more vibrant, productive, and competitive sector,

¹ This integrated report was prepared by the Foundation for Economic Freedom (FEF) for the Bangsamoro Development Agency (BDA). The report was prepared by Urooj Malik and Thomas Allen. Research support was provided by Jaymee Alcos-Cabangbang. It is based on the sector reports on agribusiness industry (principal author Alex Casiple), Halal industry (principal author Jamil Humza) and Islamic finance and banking (principal author Ikram Tawasil).

providing quality unprocessed and processed products for local and international markets. It would be more rightly described as an ***agribusiness industry***.

The ***halal food industry*** offers a new and exciting avenue for the development of the agriculture sector in the Bangsamoro. Access to halal food and other consumer products has been the persistent clamor of Muslims in the Philippines and the rest of the world for many years. And now halal trade is on the rise and on the fast lane. Thus while offering a cultural dimension to the sector's development, the halal food industry also offers commercial opportunities for which the Bangsamoro is in a good position to exploit.

Past – but half-hearted - attempts to get the halal industry up and running have not succeeded. The successful development of the halal food industry – which is recommended to be embraced by the new Bangsamoro Authority as a *flagship economic program* – needs a concerted political push. If this is forthcoming, the success of the industry hinges on dealing with the critical factors affecting the development of the agriculture sector in general. However, there are additional issues peculiar to the halal food industry which also have to be addressed, and these are the subject of the separate sector report on this industry. Given a strong political will, there is no reason why the halal food industry cannot take a dominant position in the Bangsamoro agriculture sector within the next decade.

One of the critical factors that will have to be dealt with in the agribusiness industry is the limited *access to finance*, particularly of small scale farmers and entrepreneurs. The Bangsamoro has been consistently the least banked region in the Philippines, with over 90% of the region's municipalities not having a banking presence. Dealing with this problem opens the opportunity to Islamic financial tools, particularly microfinance, as these tools reflect both commercial and religious dimensions. And, in theory at least, Islamic financing will be an important component in meeting halal standards in food production. And, of course, the opportunities for savings to be Shari'ah compliant is also potentially important to the largely Muslim communities in the Bangsamoro.

The ***Islamic banking and finance industry***, like the halal industry, is also growing rapidly world wide, with new instruments being continually added to the tool-box, attracting Muslim and non-Muslims, governments and private sector, in their use. The opportunity is thus ripe for the Bangsamoro, and indeed the Philippines as a whole, to provide a regulatory and institutional framework to facilitate the development of the industry.

The development of Islamic banking and finance is also the subject of a separate sector report. While it covers financial instruments of relevance to the agribusiness industry in the Bangsamoro, the report recognizes that Islamic banking and finance has to be viewed within a wider context- regulatory-wise, instrument-wise, and geographical-wise. The report also reflects on the past and unsuccessful attempt to establish Islamic banking in the Philippines, and draws on the lessons learnt from this experience in plotting a road map for the industry.

Underpinning the success in developing the agribusiness industry, halal food industry, and Islamic banking and finance, will be the ability of the Bangsamoro government to create a ***business and investment climate*** conducive to the development of a robust and productive private sector, encompassing both small and large enterprises. Some of these enterprises will emerge from the current informal sector in the Bangsamoro, and other will be the result of private entities from outside the region – some foreign – realizing the opportunities offered. In this respect, making it easy to do legitimate and productive business should underpin the approach to regulatory and institutional actions. Although not initially envisaged under this project, a separate sector report on building a favorable business and investment climate in the Bangsamoro is presented.

This ***integrated report*** draws on the four sector reports highlighting:

- the prospects and challenges for developing a robust agribusiness industry, and in getting the halal food industry and Islamic banking and finance up and running; and
- the proposed strategic directions for the successful development of each of these sectors.

The reader is referred to the separate sector reports for the detailed road maps proposed for each of these sectors.

As indicated earlier, the transformation of Bangsamoro agriculture into a modern, professionally managed and market-oriented economic sector underpins the ability to achieve success in all three of these sectors. This can be achieved through targeted programs that create an environment conducive to increased production, with an emphasis on fostering investments in the infrastructure and support services required for agricultural intensification, and on the promotion of cooperation and professionalism in farming communities, agricultural technological innovations, and public – private sector partnerships in plantations and other agri-based businesses. As well as new players, the bringing of smallholder farmers out of subsistence and into the formal economy will be a critical component of the strategy.

2. BACKGROUND

2.1. The Comprehensive Agreement on the Bangsamoro - Looking Forward to a “New Deal”

The Comprehensive Agreement on the Bangsamoro (CAB) is viewed as the key for the “lasting resolution of armed conflict in Mindanao and the establishment of an autonomous Bangsamoro Government as a meaningful platform for self-governance”². The CAB, signed on 27 March 2014 between the Moro Islamic Liberation Front (MILF) and the Government of the Philippines (GPH), is the product of almost two decades of peace negotiations, and is the seminal pact to

² Draft Bangsamoro Development Plan (BDP), June 2014, p. 1

bring about the resolution to the conflict in Mindanao and the establishment of a new autonomous Bangsamoro Government.

The transition of the existing Autonomous Region in Muslim Mindanao (ARMM) into a new Bangsamoro Political Entity is underway, and a draft Bangsamoro Basic Law (BBL) has been prepared by the Bangsamoro Transition Commission (BTC). The BBL, once passed by the Philippine Congress, would then trigger the Bangsamoro Transition Authority (BTA) to assume the authority of the Bangsamoro Political Entity, and function as the interim Bangsamoro Government until elected officials assume office after the May 2016 elections³.

With the advent of the CAB, the political processes of the transition and the parallel *normalization process*⁴ to bring about “rehabilitation, reconstruction and development of the Bangsamoro”⁵, create the conditions for a “new deal” that should accelerate inclusive economic growth in the Bangsamoro Core Territories (BCT) (Figure 1). If managed well, the effects of this growth can even radiate over the long run to the island of Mindanao and even the rest of the Philippines, and beyond into neighboring Southeast Asian nations.

The BCT⁶ are located in the darkest low income corners of the Philippine economy. The decades of war and neglect negated the unleashing of the full potentials of the rich natural resources of the region, and have left more than 50% of its population living below the poverty threshold. The region is characterized by “limited livelihood opportunities, inadequate social services, weak institutions, deep political, cultural and economic inequity, and generations of systemic injustice and armed violence”⁷.

It is within this context that the Bangsamoro Development Plan (BDP) is currently being crafted. The BDP has as its principal objective the providing of a “short and medium term vision, strategy and recommendations for the recovery and development of the Bangsamoro area during the transition years and after the installation of the new Bangsamoro Government”.

³ *Ibid*, BDP Draft.P.3.

⁴ Includes both the economic programs for communities and decommissioning of MILF forces (BDP Draft).

⁵ Framework Agreement on the Bangsamoro (FAB), 15 October 2012, as quoted from the BDP Draft.

⁶ The Bangsamoro Core Territories as defined in CAB is composed of (a) the present geographical area of ARMM (b) the municipalities of Baloi, Munal, Nunungan, Pantar, Tagoloan and Tangkal in the province of Lanao del Norte and all other barangays in the municipalities of Kabacan, Carmen, Aleosan, Pigkawayan, Pikit, and Midsayap that voted for inclusion in the ARMM during the 2001 plebiscite; c) the cities of Cotabato and Isabela; and (d) other contiguous areas where there is a resolution of the local government unit or a petition of at least 10% of the qualified voters in the area asking for their inclusion at least two months prior to the conduct of the ratification of the Bangsamoro Basic Law. ARMM is composed of predominantly five Muslim provinces, namely: Basilan (except Isabela City), Lanao del Sur, Maguindanao, Sulu and Tawi-Tawi

⁷ *Ibid*, BDP Draft. P.1.

Figure 1. Bangsamoro Core Territories

A. The present geographical areas of the ARMM

- Provinces: Basilan, Sulu, Tawi-tawi, Lanao del Sur and Maguindanao
- Cities: Marawi and Lamitan

B. Areas that voted Yes to inclusion in the ARMM in the 2001 plebiscite

6 Lanao del Norte towns

- Baloi
- Munai
- Nunungan
- Pantar
- Tagoloan
- Tangkal

39 out of 208 barangays in six towns in North Cotabato

From Prof. Rudy Roob's compilation based on Plebiscite to Ratify the Amendment to RA 6734. Consolidated ARMM Plebiscite Results, 14 August 2001, Commission on Elections.

PIGAWANAN (8 of 40 barangays)	MIDSAYAP (12 of 57 barangays)	PIKOT (11 of 42 barangays)*
Lower Baguer	Damarulan	Bagwang
Babacayan	Kadigusan	Babacan
Bulcan	Kadipulan	S. Balong
Datu Bimasing	Kapinlan	S. Balong
Kadipulan	Muciangnan	Batulan
Mariac	Central Ibas	Bulok
Pitot	Malingao	Gokoran
L. Pangrikalan	Muzeng	Kabasalan
	Nabalawag	Lagunde
	Olandang	Macausil
	Sambulan	Macasdeg
	Tugal	

*PIKOT has 42 barangays as of 2012 according to the website of the National Statistical Coordination Board.

C. Cities: Cotabato and Isabela

D. All other contiguous areas where there is a resolution of the local government unit or a petition of at least 10% of the qualified voters in the area asking for their inclusion at least two months prior to the conduct of the ratification of the Bangsamoro Basic Law



MINDANEWIS GRAPHICS: KEITH BADINGCO

2.2. Moving From a History of Poverty and Social Injustice

The history of conflict and exploitation of natural resources in the Bangsamoro and Mindanao go as far back as the 16th century, beginning during the Spanish colonization and sustained throughout the American rule, the early Philippine Commonwealth, and the succeeding Philippine Republic. Escalation of the conflict between Christian Manila and the Moros began during the Marcos Administration, triggered by the infamous Jabidah massacre in 1968 which led to the eventual creation of the Moro National Liberation Front (MNLF).⁸

Subsequent Philippine administrations saw through the continued escalation of conflict in the Bangsamoro, despite a few efforts to dissipate the power struggle⁹. This prolonged conflict perpetuated the vicious cycle of insecurity, poverty, marginalization/deprivation, and underdevelopment (Figure 2).



Figure 2. The Vicious Cycle of Insecurity, Poverty and Underdevelopment.

Source: BDP Core Team (as presented in the BDP Draft 4 June 2014)

With a population of about 3.3 Million in 2010 and a projected population of 5.4 Million in 2012¹⁰, the ARMM has the highest poverty incidence of population in the country at 55.3%,

⁸ *Ibid.* P.7-8.

⁹ Which includes the 1976 Tripoli Agreement with the MNLF, creation of the Southern Philippines Zone of Peace and Development (SZOPAD) in 1996, 1996 Peace Agreement and the creation of the Autonomous Region in Muslim Mindanao (ARMM), and Memorandum of Agreement on Ancestral Domain (MOA-AD) in 2008.

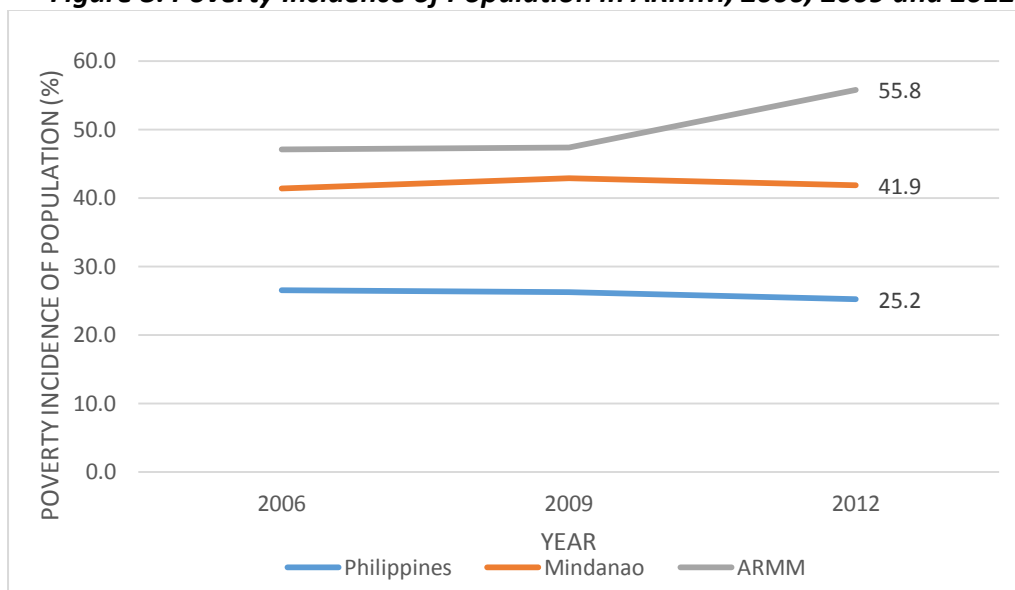
¹⁰ Given the 2.89% Annual Population Growth Rate in 2010 (Source: NSCB)

more than double the national average of 25.2% (Figure 3). Education, literacy and health access and performance indicators are among, if not the lowest, in the country.

As cited in the BDP, displacement is a defining characteristic of conflict in Mindanao, with displaced populations consistently rating lower than those who have never been displaced in terms of “food consumption, access to basic services and trust in government and other ethnic/religious groups.”¹¹

Furthermore, as articulated in the BDP, “the uncertainty caused by armed conflict and insecurity diminishes the productivity of the Bangsamoro’s resources and distorts investments and saving incentives, which results in poor economic performance.”¹²

Figure 3. Poverty Incidence of Population in ARMM, 2006, 2009 and 2012.



Source: NSCB and BDP Draft.

It is in recognition of this vicious cycle then that the BDP targets six development clusters: agriculture and livelihood; social services; infrastructure; environment and natural resources; culture and identity; and security, justice and governance, in defining the Bangsamoro’s roadmap towards “their desired quality of life, which includes the pursuit of sustainable livelihoods and political participation within a peaceful deliberative society.”¹³

¹¹ World Bank (WB) / UN - World Food Programme (WFP) Study as cited by the BDP Draft.

¹² *Ibid.* BDP Draft. P.17.

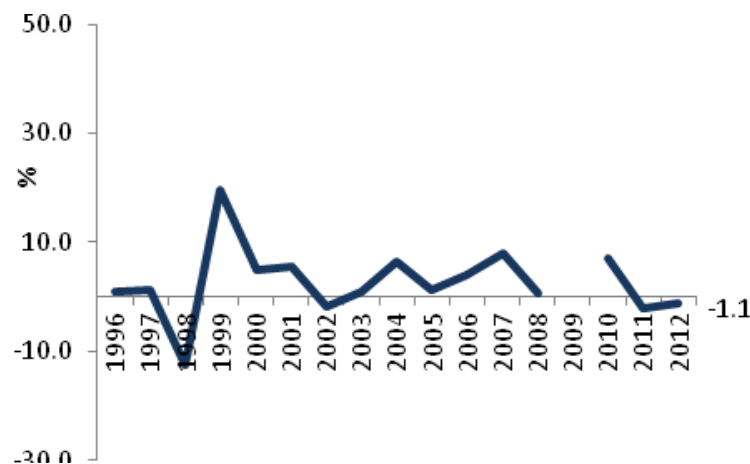
¹³ *Ibid.* FAB.

2.3. Agriculture as the Backbone of the Bangsamoro Economy

The Gross Regional Domestic Product (GRDP) of the BCT¹⁴ of about PhP 93 Billion and per capita GRDP of about PhP 17,280, is the lowest among all regions in the Philippines. This is attributed to the fact that the agriculture sector is grossly underdeveloped, despite it providing the biggest slice- 62% - of the GRDP in ARMM; the service sector accounts for 33% and the industry sector 5%.

The agricultural sector represents the economic backbone of the Bangsamoro employing about 70% of the working population. Unfortunately, the agricultural sector has a history of regular contraction, as illustrated in the figure below. The sector's poor performance is aggravated by the predominance of low-value crops such as cassava, corn, coconut and palay.¹⁵ Other principal crops include banana, rubber and coffee. Seaweeds and fisheries are also important sources of livelihood, particularly in the island communities. Except for cassava, white corn, and coffee, the average yield performance per hectare of agricultural crops falls below the national average.

Figure 4. Real Growth Rate of Gross Value Addition in the Agriculture, Forestry and Fisheries Sector in ARMM, 1996-2012.



Source: NSCB

Note: Statistical series break beginning 2009. Also, 1998-2009 series are pegged at 1985 prices while 2009-2012 series are at 2000 prices, hence cannot be completely comparable.

¹⁴ Using the projected 2012 population of 5.4 Million

¹⁵ *Ibid.* BDP Draft using data from the Department of Agriculture – Bureau of Agricultural Statistics (DA-BAS)

According to 2002 National Statistics Office (NSO) Census, there are about 248,528 farms in ARMM with a total agricultural area of 533,410 hectares employing some 799,000 people. The average farm size is 2.1 hectares, with each farm employing 3.21 workers and every hectare 1.5 workers.¹⁶

Under the current scenario of smallholder farming beset by systemic inefficiencies, lack of resources, and limited to subsistence and very few cash crops, farm productivity and thereby household income in the Bangsamoro would remain extremely low.

While smallholder Bangsamoro agriculture dominates, there are existing commercial plantations and agribusinesses within the Bangsamoro that have blazed the trail for a modern, globally competitive, high technology industry, while maintaining respect for the cultural and political characteristics of the region. Although covering only about 1% of the agricultural lands in the Bangsamoro, they are vigorously expanding, especially in the light of the promise of lasting peace and development.

At present, there are 22 medium to large scale agribusinesses in ARMM,¹⁷ including one fishery based. These are located in Lanao del Sur (Cavendish bananas, pineapples and cassava) and Maguindanao (Cavendish bananas and palm oil), catering to local and foreign markets. Although these pale in comparison to those in Regions X and XII where large corporate farms are located¹⁸, the demand for land to locate and operate large anchor plantations and outgrowerships with small to medium-sized farms is still largely unfulfilled. This does not even take into consideration the myriad network of downscale industries and suppliers of products and raw materials that can also be situated on-site and near the plantations.

However, the agriculture sector, despite its weaknesses, is not without its potentials. With the vast natural resources in the Bangsamoro and the untapped and unspoiled tracts of highly arable land, particularly in mainland Bangsamoro, agriculture can certainly prosper given the necessary infrastructure, technologies, and management.

2.4. The Failure to Get the Halal Industry and Islamic Banking and Finance Up and Running

The halal food industry has not prospered in the Bangsamoro or in the Philippines.

¹⁶ The size of the landholding per household is expected to be reduced further when, in the future, the holdings will be divided among siblings who will have their own families to feed. This is especially true if manufacturing and service sectors remain underdeveloped, and thus are unable to provide many smallholder farmers with exit opportunities from agriculture.

¹⁷ In 2008, there were only seven agribusiness establishments in ARMM that employ more than 20 employees, accounting for less than 1% of the 799,000 total agricultural workforce.

¹⁸ Dole Philippines, Del Monte Philippines, La Frutera, La Panday, Sumitomo, Busco Crystal Super Milling, and Fiesta brands

Heightened understanding of *halal food* safety awareness among Muslims and non-Muslims alike in the Bangsamoro and in the rest of the Philippines has been the product of 14 years of advocacy. The advocacy began in 2001 with the proposal of the Muslim Business Forum (MBF) for the national government to designate Mindanao as the production base for halal products. That proposal was put into a resolution - which was subsequently adopted and endorsed by the Mindanao Food Congress - to the national government in April of 2001.

Since then, guidelines for halal food standards and action plans for the development of the industry have been drawn up at the national and regional levels, but little has come of them. Halal has been a favourite subject in business conferences, campuses and roundtable discussions in many parts of the country, but very few concrete actions have been taken to capitalize on the programs, plans and standards. However, with political will and a concerted drive by a revitalized bureaucracy, there is no reason why the halal food industry cannot prosper.

Islamic banking and finance has also not prospered.

There is only one Islamic financial institution in the Philippines, the *Al-Amanah Islamic Investment Bank of the Philippines (AAIIBP)*, with nominal Islamic banking branches in Cotabato and Marawi cities and in the town of Jolo. Its remaining five branches in Mindanao and one in Makati City essentially operate a “dual-window” banking business. However, the AAIIBP has limited capital and resources, and has failed to take off as a full-fledged Islamic bank. It is now under the control of the Development Bank of the Philippines (DBP). The DBP is undertaking a rehabilitation program of AAIIBP with the aim of shifting it back to Islamic banking as soon as possible. DBP wishes to privatize AAIIBP, and believes it could effectively serve the market again by 2015.

It is not only Islamic banking and finance that has failed to take off in the Bangsamoro. The region has been consistently the least banked region in the Philippines. The number of banks operating in ARMM currently stands at 20, with each banking office servicing nearly 200,000 persons. And there are only 25 automated teller machines (ATMs) operating in the whole of the region. Moreover, 93% of the region’s municipalities do not have a banking presence, with most of the banks operating almost exclusively in the major urban centers. In like manner, the ARMM also ranks lowest among the country’s regions in terms of deposits.

Part of the reason for this is the hesitation of some Muslims to deal with conventional banks because of its *Shari’ah* non-compliant products and services. Similarly, survey business sector respondents also said that 83% of them procured start-up funding for their enterprises from their own money while 34% of them sourced it from relatives and friends.

While the conventional banking sector seems to be generally inaccessible to most inhabitants of the Bangsamoro, this gap has, to a modest measure, been filled in by non-bank financial entities, such as microfinance institutions (MFIs). It is in the microfinance area that the scope for expanded financial support to the Bangsamoro agriculture sector in particular looks encouraging.

Actions will have to be taken to spur the conventional banks to be more significant players in the region, particularly in support of the agriculture sector. And there is no reason why, given the proper regulatory and support environment, Islamic banking and finance could not prosper in both the Bangsamoro and the Philippines as a whole.

3. DEVELOPMENT PROSPECTS AND CHALLENGES

The Bangsamoro has characteristics unique within the Philippines. Notwithstanding the present weaknesses of the region, its strong agriculture potential and its socio-economic and cultural setting is deemed the fittest in terms of interfacing the country to two emerging megatrends in a globalizing world - the trillion dollar industries of Halal and Islamic banking and finance.

This position can also make Bangsamoro a prime mover for the Philippines to gain more comparative advantages in the forthcoming ASEAN Economic Integration in 2015. Some 40% or 240 Million of the ASEAN population are Muslims, with majorities in Brunei, Indonesia and Malaysia. Along with the Philippines, these countries are also part of the Brunei Darussalam-Indonesia-Malaysia-Philippines East ASEAN Growth Area (BIMP-EAGA) – a regional initiative to accelerate development of the eastern part of Southeast Asia.

Due to the decades of conflict between the Armed Forces of the Philippines (AFP) and Moro rebel groups, the regional economy suffered from longstanding underinvestment in food and nutrition security and agriculture. This reality is in spite of the fact that Bangsamoro is part of Mindanao, which is the country's premier agricultural center. Mindanao produces a diversity of agriculture and fishery products that are sold locally and internationally.

3.1. Prospects and Challenge for Agribusiness Development

The Opportunities for Agribusinesses are Considerable

The richness of the land resource throughout the Bangsamoro gives rise to wide-ranging opportunities for the expanded production of existing traditional crops – particularly through productivity enhancement – and of newer crops both at the smallholder and plantation levels for both local and export markets.¹⁹

For the local market, there is scope vegetable and native fruits²⁰, while for the national market these and products such as natural rubber, corn, palm oil, coffee, cacao and sugar are in strong

¹⁹ The focus in this report is principally on land-based activities, although many of the proposals in the report also apply to fisheries.

²⁰ Livestock – such as goats – and fish products also offer opportunities for local and national markets. Aqua-products – such as seaweeds- also offer further export potential.

demand. For the export market, coconut oil, desiccated coconut, Cavendish bananas, natural rubber, fresh pineapple, banana chips and sugar are often cited as viable opportunities.²¹

As with any other industry, the absence of a product or service is, in itself, an opportunity. In the case of the agriculture and fishery sector in ARMM - composed primarily of small scale operations and producers of raw materials - the capacity for consolidating within the value chain through integration with processors and manufacturing has been quite weak. Post-harvest and further processing activities offer considerable potential, particularly if the smallholders can effectively pool their production. This is another opportunity for small to medium-scale agribusiness investment.

A number of the agricultural products lend themselves to production on a large scale commercial plantation basis. There are various models that can be adopted for plantations, most involving out-growers through direct contract growing or through grower cooperatives. The nature of the crop and processing needs will be major determinants of the most appropriate model, although local conditions such as land tenure, cultural norms and practices, and leadership, will play a significant role. The Bangsamoro authorities will need to keep an open mind on these arrangements, and work out with the potential investors, on a case-by-case basis, the most appropriate model for the circumstances being faced.

Several non-traditional high value crops that thrive in Mindanao -such as tree fruit crops like mangosteen, marang, lanzones, rambutan, pomelo and durian - lend themselves to farming models based on sustainable smallholder systems. These should certainly be encouraged through extension services providing market, technical, and financial advice or support. Organic and Halal food production can also be expected to be an expanding part of the Bangsamoro agricultural base.

A balance between large plantation agriculture and smallholder farming will have to be sought, for reason of both social inclusiveness and environmental sustainability. However, the critical point is that it is hard to see how the Bangsamoro authorities would be able to deal with the magnitude of the employment and poverty challenges without a strong and viable commercial farming sector across a number of crops.

Elements for Success for Outside Investors

While many of the opportunities are for small scale agribusinesses, a number of which will emerge from the initiatives of emergent local entrepreneurs, many of the larger investments will come from outside the local community. Exemplary cases of outside investors in agribusiness in the Bangsamoro that have “braved” the challenging cultural and political

²¹ See, for example, Rolando Dy, *Priming the ARMM through Agribusiness Development*, 2012. Australian Aid.

environment and are considered trailblazers in the Bangsamoro economic development, manifest three key principles that are critical to their success:²²

- partner with an influential and enlightened local leader;
- invest time and effort in building trust and confidence with local counterparts, leaders and people; and
- respect and work within local cultural norms and practices, and turn them into a positive factor for the enterprise.

Other good practices highlighted in the Habito study include:

- providing appropriate incentive systems to foster higher productivity and loyalty;
- taking deliberate measures to promote workforce motivation, discipline and harmony; and
- harnessing complementary businesses for reducing costs and optimizing company resources.

The often limited infrastructure requires special attention, and Habito cites in particular the need to consider own power sources, especially via renewable energy facilities that tap local resources.

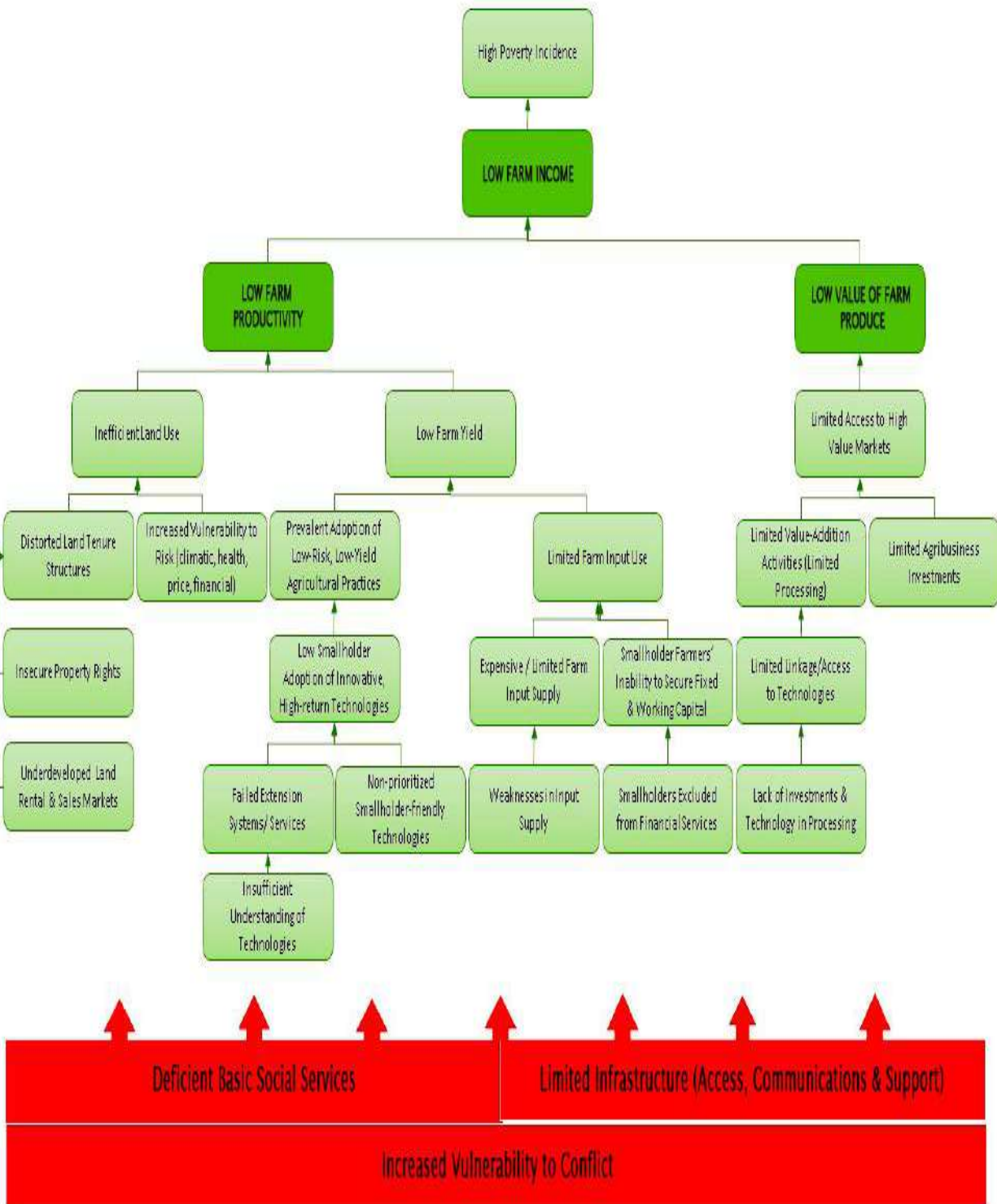
There are Numerous Barriers to Overcome in Exploiting the Opportunities for Agribusinesses

In developing the roadmap for development in the agribusiness industry, with the emphasis on identifying the entry points for the private sector, it is important to recognize the barriers affecting growth in the agriculture sector as whole, and the cause and effect relationships of these constraints.

Figure 5 below provides a graphic illustration of the problems besetting the agriculture sector in the Bangsamoro.

²² As identified for each of the six cases studied by Dr. Cielito Habito for the Australian Agency for International Development (Australian AID) in *“BRAVING IT and MAKING IT: Insights from Successful Investors in Muslim Mindanao.”* 2012.

Figure 5. Problems Analysis on the Agriculture Sector of the Bangsamoro



Continued Conflict and Violence

As mentioned in the previous sections and much recognized in any document tackling the development of the Bangsamoro, the overarching barrier to any progress in the region is the *debilitating history of conflict and violence* which then perpetuates a myriad of problems in the areas of governance, basic services, and livelihood, among others. In terms of economic losses alone, the conflict in Mindanao is estimated to cost the economy PhP20 Billion per year²³. This staggering loss reverberates into both social and economic setbacks not only for the Bangsamoro, but for the entire Philippine economy and society as well.

Although the peace agreement does mean that the major conflict between the national government and the MILF will enable some semblance of law and order to be restored,²⁴ local area conflicts continue to be of concern, mainly in the form of *rido*, or clan feuding, with land conflict being one of the most common flashpoints.

Deficient Basic Social Services and Limited Infrastructure

The delivery of *basic social services* is also compromised by the Government's ability to raise revenue which, in turn, is stalled by low economic growth. Without the safety nets for the vulnerable groups and the necessary education, health, and other social services, the well-being of the community is reduced and poverty is aggravated.

Also linked to the Government's ability to raise revenue and directly affected by the vulnerability to conflict, is the available *infrastructure* within the Bangsamoro. The BDP cites the overall security problem in the region compounded by rent-seeking activities as the main reasons for the dearth of infrastructure in the Bangsamoro.²⁵

The quality of the paved national roads is better within the Bangsamoro than Mindanao and the country as a whole. However, *farm-to-market roads*, being the most obvious and ubiquitous public infrastructure critical for sustained growth by linking the Bangsamoro and production centers to markets and the rest of Mindanao, are much less than the National and Mindanao standards. The evidence in a baseline study of the infrastructure in ARMM²⁶, shows that ARMM national roads in mainland provinces, though not fully paved, provide connectivity and accessibility within the mainland ARMM and from mainland ARMM to neighbouring regions. Similarly, municipalities within each of the island provinces are also accessed by land. However,

²³ *Ibid*, BDP Draft.

²⁴ However, breakaway groups (such as the BIFF), bandit groups (such as the Abu Sayyaf), and local warlords will still be a thorn in the side of the Bangsamoro Government and the business community.

²⁵ *Ibid*, BDP Draft. P.28.

²⁶ Tulawie, Apashra R., 2013. *Baseline Brief on the Infrastructure in ARMM*. Paper written for the Foundation for Economic Freedom (FEF).

data suggests that ARMM constituents, especially farmers, do not have easy access to basic social services and market facilities. It also suggests that connectivity between agricultural areas and markets is minimal at best.²⁷

Also in a dismal state, *irrigation* in ARMM is at lowest in terms of potential, with only 25.8% irrigated area relative to irrigable lands, way below the national and Mindanao averages.

Overall, the elements in the vicious cycle of insecurity, poverty and underdevelopment, particularly conflict, basic social services and governance (relating to infrastructure) are the fundamental barriers to growth in the agriculture sector. These affect the very basic constraints leading up to low farm income and limiting growth in the sector, as illustrated in the Problem Analysis presented in Figure 5.

Low Farm Productivity- Low Farm Yield

As indicated earlier, except for cassava, white corn, and coffee, the average yield performance per hectare of agricultural crops in the Bangsamoro falls below the national average. As shown in Figure 5, low farm productivity is caused by low farm yield and inefficient land use, recognizing that the predominantly smallholder and small-scale nature of farming in the Bansamoro also plays a role.

The prevalent *adoption of low-risk, low-yield agricultural practices as well as limited farm input use* result in low farm yield.

Smallholders' low productivity is also affected by lack of access to education, which could have helped build the skills needed to manage on-and off-farm production systems more efficiently and raise smallholder adoption of innovative and high-return technologies. This is compounded by the limited access to productivity-enhancing technologies, grounded in an environment where public and private research systems do not sufficiently prioritize smallholder-friendly technologies, and extension systems fail to help smallholders gain access to and adopt such technologies. These emerging challenges lead many smallholder farmers to pursue livelihood strategies that involve lower-risk and lower-yielding agricultural activities.

Many smallholders are excluded from productivity-enhancing financial services and are unable to secure much-needed fixed and working capital, which ranges from land and buildings to machinery, high-yielding seeds, and fertilizer. Access and costs of inputs are further aggravated by the geographic dispersion and limited access to infrastructure (including transportation networks and market facilities) in many rural areas which drive up transaction costs, lower smallholders' profit margins, and lead many smallholders to pursue more subsistence-oriented production practices.

²⁷ Airports and seaports are also very limited. For both airports and seaports, those existing are in need of improvements and rehabilitation, especially to bring them to international standards in light of the trade requirements for integration into the BIMP-EAGA sub-region and ASEAN region.

Low Farm Productivity- Inefficient Land Use

Distorted land tenure structures—including insecure property rights and underdeveloped land rental and sales markets—have been linked with less efficient land use and lower productivity enhancing investments. Added to that is the increasing vulnerability of smallholders to a spectrum of emerging climatic, health, price, and financial risks and challenges.

Delving into the deeper issues of land tenure in the Bangsamoro, the much-discussed problems at the national level on land tenure - the multiple overlapping institutions involved, the multiple inconsistent laws, the multiple land titling processes, the multiple forms of ownership, and the multiple standards for land valuation, among others²⁸ - are also the same issues plaguing the Bangsamoro. These problems are, however, magnified by the following factors:

- The long history of displacement due to conflict.
- Clash of identity and ancestral domains of the Indigenous Peoples (IPs) and the Bangsamoro - while rooted on overlapping territories, the two claims are intrinsically different in nature and character.
- Culture of the local strongman and *Datuism* - any business arrangement involving land within the bailiwick of a clan would often require the blessing of the local *Datu*. While the *Datu* acts as “gatekeeper” for gaining access to land, he also provides a service by securing boundaries and property rights within his territory.
- Informal or traditional justice systems through mediation are the most common mechanism for the resolution of competing land claims in predominantly Moro and Indigenous communities. The *Datu*, clan leaders and/or elected officials would often be the principal mediators. This is apart from the formal justice systems recognized under Philippine law for the resolution of land conflict (e.g., the *Katarungang Pambarangay* or Barangay Justice System, *Shari’ah* Justice System, and the Civil Court System).

Furthermore, in a recent report of the Joint World Bank (WB) – International Organization for Migration (IOM) Scoping Mission²⁹, it was established that “with the signing of the Framework Agreement on the Bangsamoro (FAB) displaced populations are expressing desire to return to land from which they had been forcibly displaced, sometimes decades ago. On the other hand, landowners are beginning to reclaim their lands from “squatting” displaced populations. The ensuing movement of people could bring latent claims to the fore in the absence of an effective institutional framework to deal with arising tensions.”³⁰

²⁸ *Workshop on Land and Property Rights in the Bangsamoro: Notes on Outcome and Options for Action Agenda, 4-5 June 2014.*

²⁹ World Bank and International Organization for Migration, May 2013. *Land Disputes in Conflict Affected Areas of Mindanao: Report of the Joint World Bank- Organization for Migration Scoping Mission.*

³⁰ *Ibid.* WB-IOM: Executive Summary.

Low Value of Farm Produce

Linking smallholders to commodity value chains is an important component of building smallholder resistance to shocks and improving their productivity and livelihoods. However, many smallholders in post-conflict economies are unable to participate well in value chains because they cannot meet increasingly specific and strict quality standards, high volume requirements, and logistics specifications of high value markets.

Smallholders often have limited access to markets for both inputs and outputs, and this has a significant effect on their production activities.

3.2. Prospects and Challenges for the Halal Food Industry

The halal food industry will not take root if the critical factors affecting the agriculture industry in general are not addressed. And there are, of course, additional issues peculiar to the halal food industry which need attention. Having said that, there are two parallel but related trends that define the potential for the halal food industry in the Bangsamoro:

- the globalization of the rapidly expanding halal food industry; and
- the rapidly expanding Philippine organic industry.

The Rapidly Expanding Halal Food Industry Throughout the World

Access to halal food and other consumer products has been the persistent clamour of Muslims not only in the Philippines, but all throughout the world. Halal trade is on the rise and on the fast lane. Globalization of halal made its debut when the Codex Alimentarius Commission- the food safety standard-setting arm of the World Health Organization (WHO) and the Food and Agriculture Organization (FAO) - promulgated guidelines in 1997 (CAC/GL 24) on the use of the term “Halal” in product preparation, especially that pertains to food.

This caught the attention of the Muslim world and the word spread around at such a fast pace that countries, Muslim and non-Muslim alike, took interest in developing their own halal program for their products with the barely served but huge market in mind. The Philippines was one of these countries.

In spite of these efforts, as indicated earlier, the Halal industry has not flourished in the Philippines. The successful development of the halal food industry, should this be re-embraced by the new Bangsamoro Authority as its flagship economic program, hinges on a strong policy towards the development of the vastly underdeveloped agriculture sector.

In essence, the halal industry is deemed to provide a rallying point to mobilize resources for investment, infrastructure support, capacity-building, and the introduction of better technologies for improved and efficient agricultural practices, cascading all the way down to the community level, involving micro, small, or medium scale farming *and* the processing of food crops, livestock and poultry, aquaculture/mariculture, fruits and vegetables.

Since halal food is generally agri-based, going halal should have a huge impact on the growth of rural enterprises that should benefit a majority of rural folks. Rural-based halal enterprises would actually be the backbone of the overall halal industry development with its wide ranging opportunities covering livestock and poultry, marine and fishery products, and fruits and vegetables.

The Rapidly Expanding Philippine Organic Industry

Halal food production is closely related to the organic food industry, which can be an important building block in Halal food industry development.

Organic farmers are not allowed to use synthetic pesticides or fertilizers. All kinds of agricultural products are produced organically, including grains, meat, dairy, eggs, fibres such as cotton, flowers, and processed food³¹. *Organically-grown products* – generally accepted in the food industry as clean and safe food products because of the way they are grown and processed – constitute an emerging and rapidly growing sector in agriculture, with a global niche market worth US\$40 Billion led by the expanding markets in the United States, Germany, Japan, and elsewhere.

The US is not only the largest market for organic products in the world, but is also a leading producer and exporter. As noted, global production of organic crops has not kept pace with demand, with many sectors reporting undersupply. The Asian market is reporting healthy growth because of increasing retail distribution and rising consumer awareness. Up to 90% of certified production from countries like Indonesia, Vietnam, and the Philippines is exported - largely to Europe and North America³².

No official information is readily available on the organic food market in the Philippines. However, it is estimated that it could be currently around PhP 750 million, and has in recent years been growing at a rate of 10% to 30%, depending on product type.³³

³¹ www.wwof.org

³² *The World of Organic Agriculture: Statistics and Emerging Trends*, 2007. 9th edition

³³ This estimate is based on a projection of estimates made by Stanton, Emma & Sia (Singapore) for the Embassy of Canada in the Philippines in March 2011. They estimated the market at that time to be of the order of PhP 433 million, growing at a rate of 10% to 30%, depending on product type.

According to Canono (USDA GAIN Report, 2000), the Philippines' organic market in 2000 was estimated at PhP 250 million. Of this value, domestic organic industry was about PhP 100 million while imports of organic products were estimated at PhP 150 million- the same report estimated that demand for organic products would outpace local production, while potential for increased imports, particularly for processed food products, clearly exist.

From the standpoint of Muslim consumers, organically-grown fruits and vegetables and organically-raised animals both livestock and poultry (except those that are clearly forbidden in Islam) where organic feeds and fertilizers used are free of haram substances, are closest to the institution of Halal. Patronage and consumption of organically-grown or prepared food products are on the rise on a widespread concern of consumers that the cumulative effect of chemical-based agricultural products is posing a serious threat to the health and well-being of the people.

The enactment of the Organic Agriculture Act of 2010 (RA 10068) gave a boost to the promotion and development of organic farming in the country, and safe food at that. The key feature of the law is for the government “to promote, propagate, and implement the practice of organic agriculture to increase farm productivity, reduce pollution and destruction of the environment, enrich fertility of the soil and prevent the depletion of natural resources”.³⁴ The law further emphasizes that the health protection of the farmers, consumers, and general public and the reduction of imported farm inputs are foremost in the minds of the framers of the law. As described, it further states that “a community-based organic farming system for the production of pure organic fertilizer and other farm inputs shall be employed as it recognizes and supports the central role of the farmers and other stakeholders at grassroots level”. The law has been backed up with a significant budget for the Department of Agriculture for the promotion of organic farming.

The new Bangsamoro Authority could mainstream this law into its own enabling law with a halal twist, say “Halal Organic Agriculture Act of 2015” and likewise provide funds in its expenditure program for the purpose.

Productivity is the key to food self-sufficiency whether it involves a thousand square meters farm lot or a much larger area. Organic farming methods are fully developed and increasingly being applied in a number of farms in the country with proven “showcases” within Mindanao to learn from³⁵.

There are pockets of organic farms in the Bangsamoro that can be expanded and replicated in other suitable areas in the region for increased production of organically-grown food products and improved productivity of farm lands and coastal waters. MILF communities, in particular, can be encouraged to engage in communal organic farming which could be transformed into estate size production bases of halal foods.

³⁴ Pollution, the destruction of the environment, and the abuse of natural resources are dealt with strongly in the teaching of Islam with an entire chapter (Al-Khalifa) dedicated to the subject. Man in particular, as God’s steward and trustee on earth, was given the task of protecting and nourishing nature and preserving natural habitats for all living things to thrive in abundance and enjoy the bounties provided to them by the grace of the Almighty.

³⁵ Kablon Farms in Tupi, South Cotabato; Tubaga Multi-Purpose Cooperative also in Tupi; Mt. Carmel Rural Life Center in Bansalan, Davao del Sur, Don Bosco Foundation for Sustainable Development in Makilala, North Cotabato; and WWOOF Philippines.

It is in the production of safe food using natural methods of farming that will serve as a novel entry point in the renewed development of the halal food industry, aimed at a niche market of health and safe conscious consumers regardless of religion or creed. Both local and export markets can be targeted.

There are Hurdles Faced in Getting the Halal Food Industry Up and Running

In a 2008 assessment paper prepared by James Lowe for the CIDA-funded Local Governance Support Program in ARMM (LGSPA) on “Halal Agriculture and Food Development”, he mentioned that the “underdeveloped agriculture and food sector from production through processing and marketing, presented a weak basis and starting point for the development of a *halal*-based industry, specifically citing the region as a net food importer while having all the potential to be self-sufficient or a net exporter of agri-products”.

Among those weaknesses mentioned are:

- poor and limited infrastructure support such as transportation, farm-to-market roads, storage, quality control measures, and other supply chain infrastructures;
- limited support and technical services to transform current farming practices to halal practices, and weak cooperatives and farmers associations to support the *halal* value-chain; and
- the financial constraints of the concerned line agencies involved in the implementation of support programs.

These are practically the same litany of woes affecting the development of agriculture in general in the Bangsamoro region.

Currently, much of the food products coming to the region are produced, processed or manufactured in other places and woefully, haram food products, both fresh and processed, circulate freely in all areas of the Bangsamoro even in areas bearing the name “Islamic”. Since the Halal industry initiatives have not really filtered down into the consciousness of the business people, growers, processors, food service providers, and agri-entrepreneurs on the ground, only a handful of halal food products are produced and distributed in the region.

As indicated earlier, the *basic requirements* for successful halal agro-based activities is the same as for all agro-based activities: peace and order, adequate infrastructures, land security, appropriate technology, extension services, access to markets and finance, etc. The requirements of Halal *add* another layer of specific needs.

As a general observation, the business sector and a large part of the population in the Bangsamoro lack awareness on the hygienic and health benefits derived from consuming Halal food products. This is changing, but a much greater effort of educating the public is required.

Need for Credible Halal Certification

What is permissible and what is not to halal consumers are best recognized in the stamp of approval by a competent certifying body on products (both food and non-food) being produced and distributed for public consumption. Halal certification is considered the cornerstone of halal industry development- it ensures that food products, in particular, are in compliance with Islamic prescription using science-based approaches to product evaluation and analysis.

The Muslim Mindanao Halal Certification Board, Inc. (MMHCBI), a non-government, not-for-profit organization was established in 2006, is one of the three halal certifying organizations accredited thus far by the National Commission on Muslim Filipinos (NCMF) - it being its mandate under Republic Act 9997. Recognized and accredited as it is, the MMHCBI needs considerably more financial assistance if it is to become a significant partner in halal industry development. This is on the assumption that the new Bangsamoro Authority would continue to extend its recognition and accreditation of the MMHCBI as the sole certifying body in the Bangsamoro.

Flawed and Un-implemented Enabling Measures

The *Halal Labelling Law of 2009* (MMA 254) is one piece of legislation critical to halal industry development because of its regulatory nature. The law is meant to regulate the use of the term “halal” in food establishments as a way to convey a message to halal consumers that the foods served are fit for them to consume. This widespread practice of unabated and spontaneous use of the term “Halal” led to confusion and deep suspicion among consumers that the food may not be halal after all.

The other component of the law is in the accreditation of organizations intending to engage in halal certification- even those accredited by the National Halal Accreditation Board (NHAB) would likewise have to secure ARMM accreditation. This needs special attention, since:

- it implies that more certifying bodies can be accredited to operate in ARMM; and
- the supposed NHAB, which was originally designed by the government agencies involved in the crafting of the Philippine national standard on food to be a private sector accrediting body, was overtaken by RA 9997 where the accreditation function and responsibility was lodged with the NCMF effectively rendering the idea of NHAB as the accreditation body as moot and academic.

This particular law in archive should be reviewed and made operational.

The *Halal Industry Development Master Plan* was supposed to be the roadmap in the development of the halal industry in ARMM. Yet after its completion in 2008, the master plan remains an un-implemented plan.

The *Halal laboratory* set up to support the certification process of the MMHCBI is non-operating. DOST-ARMM needs a properly equipped halal laboratory of its own to support the certification process of the MMHCBI.

And there are Other Pressing Concerns

Given that the promotion and development of an industry which is associated with the “way of life” of the Moro people and with those concerned with safe and clean foods, the way to nurturing the halal food industry should have the participation of stakeholders working together, and moving in tandem with a clear direction and sense of purpose. As has been observed in the past, and as raised in recent roundtable discussions and stakeholders’ forums, it takes a collective and coherent approach to make the halal industry work if it is to become the rallying point in the revitalization of the region’s agriculture.

This has not been happening. There has been minimal participation of key players – such as the private sector, academe, and hospitality sector - in policy making and planning, and no designated body to coordinate the programs of the various agencies and to prod them into action. Funding has been inadequate, and little support has been apparent at the provincial and municipal levels. There is also low awareness of halal products among the local population, and low appreciation of appropriate halal technologies.

3.3. Prospects and Challenges for Islamic Banking and Finance

Both conventional and Islamic banking and finance facilities will play a role in the Bangsamoro. It will take time for Islamic banking and finance to take root, and traditional banking and finance facilities will have to be relied on in the interim. It can be expected, however, that the conventional banking and finance system will *always* play a significant role in the Bangsamoro.

A dual banking and finance system recognizes the fact that the conventional banking and finance system underpins the economic structure of the country as a whole, while the Islamic banking and finance system can provide an alternative for the segment of the market that wishes to adhere to Islamic principles and for those, on account of financing availment criteria set by conventional finance, who remained outside of the country’s banking and finance mainstream. A well-developed Islamic banking and finance system will also attract attention from non-Muslims who recognize the unique benefits of the Islamic financial instruments.

There are Hurdles to Any Form of Banking in the Bangsamoro

Despite the statutory mandate of the ARMM to encourage banking institutions to operate in the region as embodied in the (expanded) Organic Act (RA 9054) that created it, such a mandate has largely remained unaccomplished. In this light, a number of factors could be cited, including:

- The poor state of the region's physical infrastructure makes it difficult for bank clients living in rural areas to access banking services and facilities in urban centers.
- ARMM has been identified as the poorest region of the country with the highest rate of poverty incidence and lowest rate of savings, making it unattractive to banks as a viable market.
- The unstable peace and order situation in the region has meant that the exposure of banks to operational risks is extremely high. For decades, the region has been the bedrock of Moro secessionist movements and haven of communist insurgency and notorious criminal syndicates. It has also occasionally been wracked by internecine clan wars, or *Rido*, usually among competing political families who are maintaining large private armies.
- The predominantly Muslim inhabitants of the region find it difficult to patronize *riba*-based conventional banks because of religious considerations. *Riba* (interest) in Islam is strongly prohibited and is, therefore, considered *Haram* (forbidden), which is the opposite of *Halal* (permissible).

The AAIIBP could have amply addressed this latter concern squarely had it not for its failure to take off as an authentic Islamic bank. But overall, getting the regional economy back in shape - particularly through a revitalized agriculture sector - will be fundamental to enabling a healthy banking and finance sector, both conventional and Islamic, to take root.

And There are Additional Challenges to Getting Islamic Banking and Finance Up and Running

Five principal issues will need to be addressed specifically relating to Islamic banking and finance:

- an appreciation of the nature of appropriate Islamic banking and financial institutions and instruments/products for the Bangsamoro and the country as a whole, and the steps necessary to enable them to be provided;

- making people, especially in the Bangsamoro, aware of the concepts of the Islamic banking system and its products – this includes government officials and politicians as well as the general population – and the benefits offered by these products;
- the lack of appropriate skills in the country on Islamic finance and banking;
- ensuring *Shari'ah* compliance arrangements; and
- the lack of a suitable legal infrastructure for Islamic banking and finance, of a framework for dealing with governance and accounting and auditing standards, and for ensuring a level playing field in taxation and other relevant policies for Islamic and conventional financial instruments.

The AAIIBP failed to prosper not only because of the unfavourable climate for banking in general in the Bangsamoro, but also because it was handicapped by legal support inadequacies, particularly relating to meeting reserve requirements, deposit insurance, and tax structures affecting negatively *sukuk-type* transactions. The lack of other Islamic banks with which it could deal was also a handicap.

Further, Islamic banking and finance must be looked at from the national perspective as well as from the Bangsamoro perspective because:

- of the large Muslim population outside of Bangsamoro that will also want to access Islamic financial instruments and services;
- many of the instruments and services will be provided by entities whose main place of business is Manila or even overseas; and
- of the legal mandate of the Bangko Sentral ng Pilipinas (BSP) and other national government instrumentalities.

It is thus critical for national legislation to underpin Islamic banking and finance in the Bangsamoro and the rest of the Philippines, accepting that the core of the activity will be in the Bangsamoro.

And There are Clear Benefits Offered by Islamic Banking and Finance

The Islamic banking and finance system offers benefits not found in the conventional banking and finance system. It:

- offers a wide range of products with interest-free mechanisms covered by, among others, sale and leasing contracts, and discourages leverage;

- eliminates unproductive/excessive speculation/gambling (*Maysir*) and contractual ambiguity (*Gharar*) and instead, introduces the concept of risk-sharing and partnership, with a high level of moral principles- suppliers of funds become investors rather than creditors, and share business risks with the entrepreneurs in return for share of profits; and
- has close links with the real sector of the economy- it introduces a materiality aspect that links financing directly with the underlying asset so that financing is linked to the real sector activity.

And it will not pose a “threat” to the viability of conventional banking and finance, even in the Bangsamoro. On the contrary, it should improve the overall system in both the Bangsamoro and the Philippines as well as provide the conventional banking industry with new products and services, should the regulatory environment allow Islamic banking and finance to be implemented. *Microfinance instruments* and *takaful*, in particular, will be of real value to the Bangsamoro smallholder farmers, while *sukuks* offer the potential as important financing instruments for public-private ventures in particular, and the Bangsamoro government in general.

Globally, Islamic banking and finance is a rapidly growing industry, with even London developing itself to be a major center. Major international banking institutions such as Hongkong and Shanghai Banking Corporation, Citibank, Hong Kong and Standard Chartered Bank, all have subsidiaries offering Islamic banking products and services. The global Islamic finance market (on risk-sharing, ethical, and noninterest based financing models) has over US\$1.7 Trillion in assets in 2013, and continues to grow in the 10%-15% range.

4. STRATEGIC FRAMEWORK FOR INCLUSIVE GROWTH OF THE AGRICULTURE SECTOR

It is necessary to look at the growth of the agribusiness industry within the context of the agriculture sector as a whole, as these are closely intermeshed.

4.1. The Key Actors

Inclusive growth needs to draw the interactive participation of four key actors: the smallholder farmers, the private sector, the state, and the civil society.

Figure 6. The Key Actors



Smallholder Farmers

Small family farms account for the bulk of the agriculture sector, since they make up the majority of farms in the Bangsamoro agricultural landscape. As noted earlier, the average land area in the region is 2.1 hectares numbering about 248,528 farms³⁶.

The framework of intervention for inclusive agricultural growth in Bangsamoro should be cognizant of the plurality of smallholders who represents the vast majority of agricultural producers in the region. Smallholders are classified as follows:

- *Stand alone or independent smallholders* are those who till their land on their own with no or minimal assistance from the government, non-government organizations (NGOs), or the private agribusiness sector;
- *Assisted smallholders* are represented by small farmers that usually received assistance from the government and NGOs through the provision of agri-inputs, financing and extension services; and
- *Integrated smallholders* are small farmers that are well integrated into the value chain of specific crops they propagate through joint venture arrangements with large scale agribusiness firms.

³⁶ NSO, 2002.

Private Sector

The operations of a few agribusiness firms - like La Frutera, Agumil, Matling Industrial and Commercial Corporation - inside the Bangsamoro offer insights into the important role that the private sector can play in the agricultural development of the region. It has shown that there is a rapid increase of value addition opportunities through agribusiness relative to primary production. Agro-processing enterprises like Matling Commercial Corporation are increasing demand and the effective size of the market for cassava farmers' products. Exporters (La Frutera) and agro processing enterprises (Agumil) are furnishing crucial inputs and services to the farm sector for those with no access to such inputs. This is inducing productivity and product quality improvements.

And there are the small-scale private enterprises providing various transport, support services and post-harvest facilities to farmers. As smallholders get organized, they in turn can be brought out of subsistence and into the formal sector, and operate as cooperative/private sector entities. The effective organization of smallholders is often a precondition for post-harvest facilities and processing to emerge, whether through independent private initiatives or through the smallholder organizations.

Agribusinesses also are stimulating market induced innovation through chains and networks. Domestic and export systems are becoming more mutually supportive.

Public Sector

High poverty incidence in an economy that is heavily dependent on fragmented smallholder agriculture and the slow expansion of agribusiness-led commercial ventures in Bangsamoro territories, are indications that existing regional government agricultural development programs have not sufficiently addressed the hurdles.

There is a consensus on the need for the Bangsamoro government to continue creating an enabling environment for the development of smallholder farming system, as well as for the growth of private investment through stable and well-functioning institutions, e.g. for land tenure systems and more generally for property rights, for contracts and market regulations, for incentives and support services, for business and labor regulations, and for trade.

Underpinning these will be the restoration of law and order and the rehabilitation and upgrading of essential infrastructures.

In addition, the Bangsamoro government must also continue to provide essential, high-return public goods, notably those related to public research and development (R&D) and extension services, complementing private investments in this area. Integrated policy packages that directly support smallholder market access, capacity, and efficiency will be critical, whether they be through directed government agricultural programs or the promotion of joint ventures between agribusiness firms and smallholders.

There is also a need to leverage the interest of the business sector in agriculture and related value chains. This can bring fresh capital to rural areas and contribute to increasing supply, quality, and market distribution of produce, generating positive financial, economic and social returns. It must ensure that business investments do actually create positive benefits and are in keeping with emerging principles of responsible investment in agriculture, which requires clear incentives and safeguards.

Civil Society Organizations

Civil Society Organizations (CSOs) have a wide range of roles as development actors and change agents. These include – but not limited to – the delivery of basic services, support to local development, policy influencing in support of participatory and democratic governance, and the promotion of demand-driven accountability mechanisms.

Civil society – including NGOs and foundations – can mobilize the community to meet its unique social, environmental and economic needs. It can also demonstrate innovative programs that can be scaled-up by governments and businesses, and provide risk mitigation tools that build market confidence.

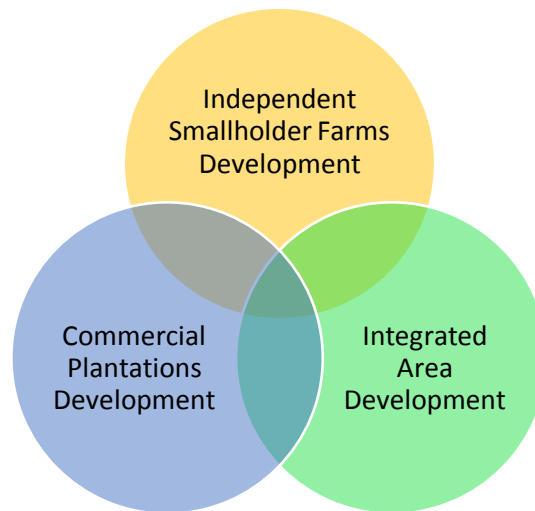
Some CSOs play a special role in serving as buffer social agents in times of state and market failures that may happen during conflict escalation or recurrence. Building resiliency to these shocks and preparing smallholders for meaningful engagement with the state or market sectors are examples of this special role.

4.2. Strategic Growth Paths

Three strategic growth paths are proposed to synergize the contributions of the above mentioned actors:

- Harness the potentials of *independent smallholder farming system* for food security and domestic and regional market demands.
- Promote *private sector led commercial crop plantation farming system* for export and high value markets.
- Develop and replicate the sustainable *integrated area development system*.

Figure 7. Strategic Growth Paths



Growth Path One. Harness the potentials of independent smallholder farming system for food security and domestic and regional demands.

The first approach would focus on the development of smallholder farms which represents the vast majority of farming units. The thrust of this approach will be to:

- increase the productivity of smallholder farms;
- facilitate the increased value of farm produce, particularly through the development of forward linkages through product enhancement and further processing facilities; and
- increase the sector's resilience to risk, including climate change.

The *increase in productivity* will come principally through:

- increased land utilization, particularly through assistance to farmers in consolidating their land use and property rights and reduced vulnerability to risk;
- increased farm yields through improved extension services to small-holders, particularly aimed at adopting sustainable agricultural practices such as soil erosion control, and facilitating access to suitable technologies, production inputs, and market information;

- improved farm-to-market roads and transport, and small-scale water harvesting and irrigation facilities; and
- improved access to rural finance.

Dealing with agri-input bottlenecks, particularly fertilizers, will be critical. Consideration should be given to providing transport subsidies for fertilizers for an interim period, being withdrawn once the appropriate infrastructures are in place and private sector providers and smallholders are sufficiently strengthened.

The facilitation of increased value of farm produce through forward linkages will involve efforts to:

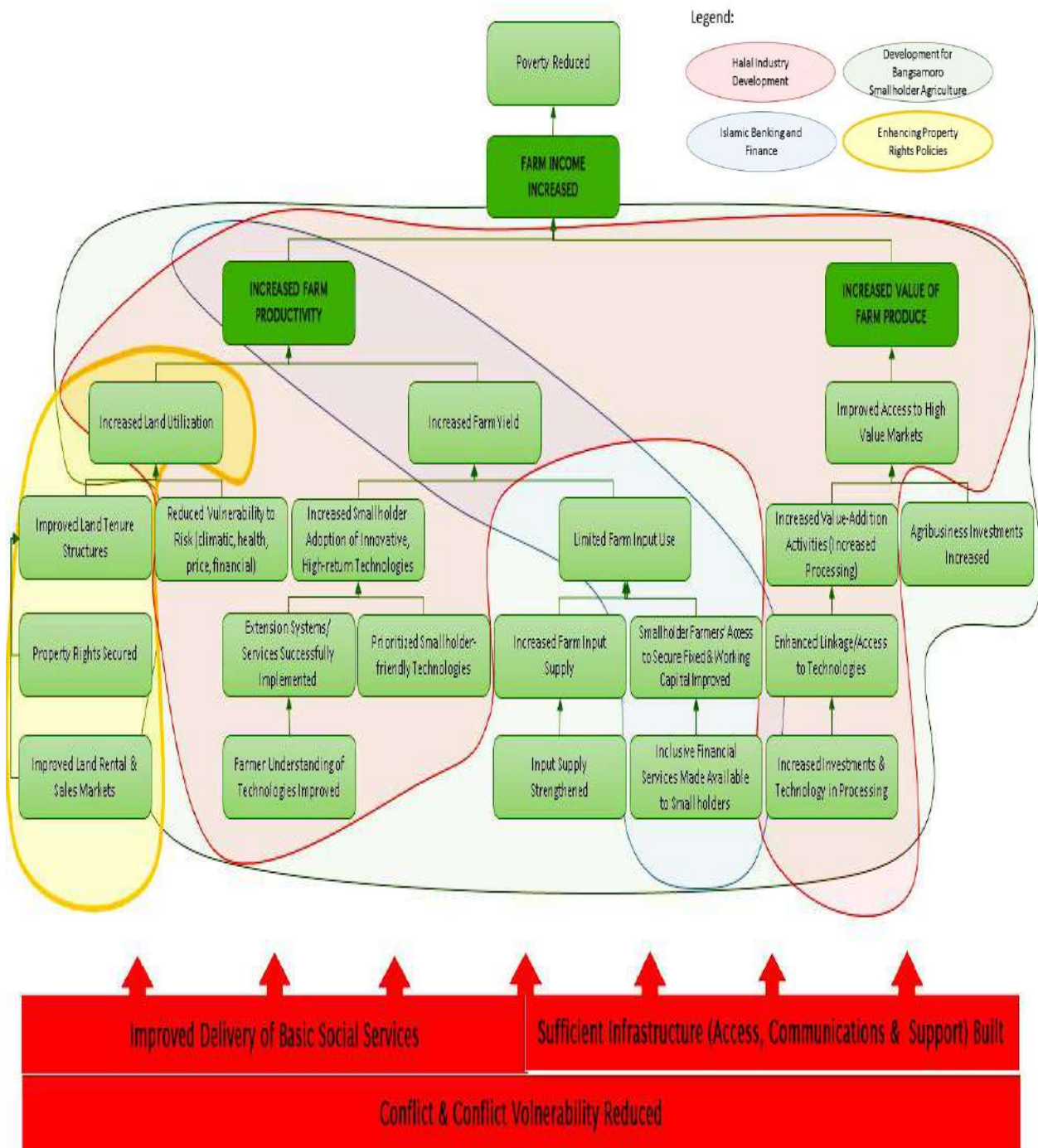
- ensure a better understanding of the value chain approach to agro-industrial development among the bureaucracy, private sector and farming community;
- enable and encourage smallholders to consolidate their production to facilitate profitable opportunities for common services (such as cold storage, drying and other post-harvest facilities) and further processing; and
- make it easier and less costly to do business, by simplifying business and labor regulations, facilitating access to finance, and providing suitable incentives.

The increase in the sector's resilience to risk will involve:

- a much better understanding of the factors impinging on farmer risks, particularly relating to the impact of climate change; and
- the design and deployment of appropriate farm finance and insurance products.

The above are summarized in the objectives analysis of agriculture development in the Bangsamoro presented in Figure 8.

Figure 8. Integrated Analytical Framework for Major Components in Developing the Agriculture Sector in the Bangsamoro



An underlying objective is to *foster knowledge driven agricultural growth through farmer cooperation*. Empowering farmers by giving them greater ability to develop solutions on their own initiative and to access the specialized forms of technical assistance that they need on particular issues is important.

Taking cues from the experiences on post conflict agricultural development interventions in African countries, this is aimed directly at making the smallholders more knowledge-intensive through professionalization and capacity-building for their organizations and through improvements in the systems for technology generation and dissemination.³⁷ Specifically, it aims to strengthen the sector's social capital base by providing farmers with organizational frameworks through which they can develop commercial linkages and function in a more entrepreneurial manner. The program includes interventions to strengthen the entities in the sector that are charged with the development of productive technologies and other forms of applied knowledge and with imparting this knowledge to farmers.³⁸

The program covers:

- Promotion of farmers' organizations and capacity-building for producers, with the aim of developing the management and entrepreneurial capacities of these organisations so that the required social capital are put in place. This will capacitate farmers' associations to become involved in higher-value activities, both at the farm level and in agro-processing activities, as well as improving their access to inputs.
- Restructuring support services, with the objective of developing an extension system that is accountable to farmers as clients and, crucially, creates the necessary incentive structures for this purpose.
- Research for transforming agriculture to better respond to farmers' priorities and needs. This will include using participatory research techniques where farmers' organizations are involved in setting research agendas, as well as strengthening the scientific and technical capacity of the formal and public research institutions.

³⁷ Track of Rwanda Post Conflict Agricultural Development Program

³⁸ Ibid

Growth Path Two: Promote private sector led commercial crop plantation farming system for export and high value markets.³⁹

The Bangsamoro authorities will have to take early special actions to help reintegrate displaced persons and ex-combatants and to “kick-start” the development process. Many of these will return to subsistence or small-scale farming and fishing, and will require immediately shelter, planting materials, tools and other basic needs. This will then have to be followed by interventions along the lines outlined in Growth Path One to improve their production. However, this uplifting of smallholder production will take time, and will not be enough by any stretch of the imagination to meet the needs and aspirations of the peoples of the Bangsamoro. Nor will the needed infrastructure programs provide sufficient sustainable job opportunities. Bolder steps will be required.

The Bangsamoro authorities – led by the ARMM Regional Board of Investments (RBOI) - will have to take special actions in the coming months to encourage the early establishment of some – perhaps two or three or four- large private sector led agro-based plantations. These could include the significant expansion of existing plantations for current or new crops. In promoting these projects, the emphasis should be “transaction-oriented”, seeking out the entrepreneurs who are most likely to deliver, and help in linking them to potential local partners. The authorities should be fairly flexible on the models for these projects, which would be driven by the nature of the crops, their location, the amount of land needed to make the operations viable, the land aspirations and cultural norms of the local population, and the way land access can be readily obtained and security assured. The models could be along the lines of La Frutera or Agumil, or some variation thereof. Aside from suitability of land and access, the ability to mobilize the required landholdings and assure security of assets and personnel will be the principal factors in determining the most appropriate locations for these projects. As well as local labor, demobilized MILF forces and returnees could be employed. Hopefully, these projects could be underway by 2016 when the new Bangsamoro Government is in place.

Restoring law and order will be a major factor in the decision of potential new investors in plantations, but they will want to be assured that:

- adequate land is available with secure tenure over the long term;
- potential local partners are available who can ensure an effective interface with the local community; and
- critical infrastructures can be in place.

³⁹ This section draws on the outputs of the *FEF/PCID Workshop on Overview of the Business and Investment Climate in the Bangsamoro* (finance by the Australian Government) held in Davao, November 2013.

The supply of progressive-minded local elected officials is critical - the *datus* should serve as “development entrepreneurs” who identify clan interests broadly in terms of development outcomes of communities within their jurisdiction.

The National Government and the Bangsamoro/ARMM Government should be ready to move on the physical and social infrastructure required to service and support these plantations, with donor support if necessary. These infrastructures could also impact other nearby areas which do not fall within the scope of the plantations, but could, with minimal further investment by the appropriate government authorities in feeder roads, link them into the infrastructure “hub”.

Consideration should be given to encouraging institutions such as the International Finance Corporation (IFC) to participate in the equity of the ventures if this is needed. A revived Southern Philippine Development Authority (SPDA) could partner the initial ventures in the Bangsamoro to reduce the risk burden of the private sector investors. The Special Development Fund could also be drawn on for these purposes. Appropriate fiscal incentives will be required, reflecting the risks, long gestation, and up-front costs associated with projects of this nature in conflict-affected areas. The National Government should also encourage organizations such as the DBP, LBP or even international organizations to consider offering some form of political risk insurance for local investors, assuming that such insurance may be available from the Multilateral Investment Guarantee Agency (MIGA) of the World Bank Group and Asian Development Bank (ADB) for foreign investors (although they have been reluctant in the past to offer insurance in conflict-affected areas).

Initial success in these efforts could trigger further investments in commercial plantations, thus becoming an integral element of the Bangsamoro development strategy over the medium to longer term. By being flexible with the “business models”, there is considerable leeway for adapting the scope and nature of the plantations to suit local conditions. As well as providing scope for more efficient and profitable small-holder production through out-grower arrangements, they would also provide job opportunities and stable income for farmers who chose to exit smallholder agriculture for greener pastures. These plantations would link the local economy to the global market by producing high value export crops.

Growth Path Three: Develop and replicate Sustainable Integrated Area Development

This approach recognizes that there are some areas that are environmentally fragile or have special characteristics that necessarily require a significant degree of government intervention, and may require transcending into cultural and social dimensions of development. These could be physical or culturally sensitive areas, including locations where security issues would preclude private sector interest - at least in the short term - because of the level of risk involved. As well as focusing on productive activities, the plans for areas under this approach would be “complete” plans incorporate physical and social infrastructures.

The nature of the integrated area development would be location specific. For example, an environmentally sensitive river basin may require an integrated planning approach with the

central focus on protecting watersheds, securing water catchments, and ensuring sustainable forest management. The presence of indigenous communities in the basin would add a further dimension. The base camps of the MILF could also be the focus of an integrated development approach, transforming them from centers of armed struggle to integrated agribusiness hubs within peaceful and productive communities.

The Bangsamoro authorities will have to make a special effort to determine locations for which an Integrated Area Development approach is justified. These should be limited, and subject to stringent selection criteria.

Some of the localities may lend themselves to commercial style plantations, but may require the government to take the lead (at least initially) - with possible private sector support - because the magnitude of post conflict fragility and risks are too big for private sector to deal with. Just as for private sector led commercial plantations, there are various “business models” which can be adopted, such as the nucleus estate model of Indonesia and the Federal Land Development Authority (FELDA) and Federal Land Consolidation and Rehabilitation Authority (FELCRA) models of Malaysia.

Essentially these involve:⁴⁰

- The government taking the lead, with the private sector playing a “back-up” role in some cases – over time, the private sector may play a greater role.
- Consolidation of fragmented small landholdings and their transformation into centrally managed, efficient, and competitive commercial plantations, with out-grower smallholder connections (some of whom may be independent of the estate).
- Agro-industrialization that will transform the produced crops into a higher value processed products – this may also include the local processing of agri-inputs, such as fertilizers.
- If applicable, generation of bio-energy that utilizes farm wastes as feedstock – this could lead to power self-sufficiency of the plantation and any surplus sold to the national/regional grid.
- Social development infrastructures, such as schools, skills development centers, mosques and religious centers, health facilities, and recreation centers.

⁴⁰ Integrated Area Development localities may be quite large (e.g. river basin development) and may thus have “sub-locations” which may have their own strategic growth paths, but still within the context of the overall integrated development. Some of these “sub-locations”, for example, may be areas where private sector led and managed commercial scale plantations would be feasible and appropriate, and other areas where “traditional” smallholders would still predominate.

- Build-operate-transfer arrangements in many cases – state and private sectors will help develop the plantation, including land-clearing for cultivation and, once developed, handed over to the smallholder for self-management.
- Integration of sustainability mechanisms both from the environmental and economic perspectives.
- Integration and access to the opportunities offered by Islamic finance and banking for investments requirements, as well as to the halal food industry industry as a market niche.

4.3. Enhanced Property Rights

Land and property rights require special and urgent attention. Small-holder farm production will continue to be the mainstay of the Bangsamoro economy for some time to come. A more certain climate for land tenure will be an important factor in enhancing the income and productivity of these small-holders, and in their ability to access finance. For investors in large commercial plantations, adequate land with secure tenure over the long term will be perhaps the most critical factor in their investment decision.

There are some *immediate actions* which are recommended to be undertaken – or at least commenced - over the lifetime of the BTA:⁴¹

- Set up a geographic information system (GIS) to capture existing and new data sets to support strategic planning by BDA - priority should be given to obtaining data on land disputes and conflict prevalence, initially focusing on mapping those areas where the prevalence of land conflicts are perceived to be the highest and/or the risks of escalation are seen to be the greatest.
- Conduct a full inventory of the laws and regulations relating to land and property rights in the Bangsamoro.
- Undertake an assessment of the capacity of the formal judicial and informal/traditional dispute mechanisms in key locations.

⁴¹ The proposed immediate and medium term actions outlined are spelt out in detail in the separate Agribusiness Industry sector report, and emerged from the FEF/PCID/UP Law Workshop on Land and Property Rights, finance by Australian Aid, held in June 2014 at the UP Law Center.

- Conduct an intentions survey among displaced persons and combatants.
- Document potential areas for commercial plantations.
- Conduct a resource potential assessment – to include forestry and minerals.

All the above actions must reflect the cultural sensitivities to the traditional forms of land ownership, especially in some Moro and Indigenous Peoples' communities where, among other things, individual titles are not necessarily desired or feasible at this time.

While it would be desirable for some of the *medium term actions* to be commenced as soon as possible, it is recognized that some will require further work to formulate an appropriate policy and/or an effective implementation program, while others will require legislative action by the Bangsamoro Government:

- Formulate a land policy for the Bangsamoro, taking cognizance of the relevant national laws and regulations, the outcomes of assessments and surveys indicated above, and the flexibility that the Bangsamoro Government will have in devising its own laws and regulations. The land policy would need to be underpinned by realistic assessment of alternative tenurial rights that would be appropriate for the Bangsamoro.
- Consider the legislative and administrative scope for establishing a single land administration agency in the Bangsamoro.
- Take steps to develop and test a streamlined process to systematically register rights in land with appropriate safeguards to ensure that the poor and less educated people have their rights protected.
- Design and implement robust community programs aimed at trust building and the reinforcement of local government through improved basic service delivery.

There is also a call for the formulation of a comprehensive and effective policy covering fishing, wealth-sharing of natural resources, coral resources and key bio-diversity sites, local marine transportation, and international shipping routes for the Bangsamoro maritime space, specifically the Bangsamoro Waters and Zones of Joint Cooperation.

Close liaison with the relevant national government agencies in all these areas will be essential.

5. STRATEGIC FRAMEWORK FOR HALAL FOOD INDUSTRY

The successful development of the halal food industry hinges on the successful implementation of a strategy along the lines proposed for the development of the agriculture sector. The strategy for the halal food industry should be seen as an integral part of that strategy.

The halal food industry should be embraced by the Bangsamoro authorities as a *flagship economic program*. In essence, the halal food industry can provide a rallying point to mobilize resources for investment, infrastructure support, capacity-building, and the introduction of better technologies for improved and efficient agricultural practices. This would cascade all the way down to the community level, whether these involve micro, small, or medium scale farming, or the processing activities associated with food crops, livestock and poultry, aquaculture/mariculture, fruits and vegetables.

Targeting both issues of low farm productivity and low value of farm produce, the development of the halal food industry aims to ride on the opportunities offered by the burgeoning global halal economy, the comparative advantage of halal agriculture and food in the country and in the ASEAN region, and the benefits of a cohesive and integrated value chain.

Since the emphasis is on improving the value-chain and linking the farmers to the halal industry, the benefits of interventions are most felt in increasing the value of farm produce. Apart from linking the farmers to the halal processors and markets, appropriate technologies and know-how would be the main intervention in increasing farm yields. Furthermore, by improving technologies and the value of the farm produce, farms (and farmers) become more resilient to price and financial risks.

At the very heart of this halal food industry is the intensive promotion and development of halal *organic farming*, or agriculture as a sustainable source of food compliant to Islamic dietary code. As outlined earlier, organic farming is recognized as a fast emerging sector in agriculture, with a niche market of its own in the country and in the nearby regional and other international markets.

Thus the strategy for the halal food industry is seen as an entry point to assist in resuscitating an ailing agriculture sector through the promotion and development of the halal food industry, with Halal organic farming at the very core of this industry-in-the-making.

Over and above the steps to be taken to revitalize the agriculture sector in general, the *thrust of the specific actions to get the halal food industry up and running* would embrace:

- enacting and strengthening policies and regulatory laws on Halal accreditation and certification, labelling, and food safety;
- designing and implementing an incentive code for halal compliant ventures, particularly for smallholders and small and medium scale enterprises;
- strengthening the institutions responsible for the promotion and development of the Halal industry, with particular emphasis on extension and support services to smallholders and small scale enterprises engaged in halal food production;

- developing and implementing a capacity building program for extension service providers, trainers, and smallholders, and encouraging state universities and colleges to engage in research and introduce new courses supportive of halal industry development; and
- developing and implementing a sustained information and communication program on Halal food.

The specific actions would be articulated within the context of a revised and enhanced Regional Halal Food Industry Development Master Plan.⁴²

While this endeavour would require substantial financial resources, the identification and validation of production zones as embodied in the halal industry development framework would serve as the catalyst for the industry build up where infrastructure support, financial resources, capacity building, and technical support, will be focused for better utilization.

It is also on the understanding that the private sector would be partners in the development of the halal industry. It is in the area of developing a home-grown halal industry to propel food production where private sector support and engagement needs to be mobilized if the industry is to move forward.

The Bangsamoro government should encourage the private sector to take the lead and be at the forefront of such an endeavour, with the former providing the enabling environment and appropriate incentives and other support programs. In some instances, public-private sector partnerships would be the most appropriate route.

6. STRATEGIC FRAMEWORK FOR ISLAMIC BANKING AND FINANCE

As indicated earlier, both conventional and Islamic banking and finance facilities will need to coexist in the Bangsamoro. An orderly development of both the conventional and Islamic systems should:

- promote healthy competition, leading to increased market discipline and improved customer service and value;
- increase the deposit base, as products like “*tabun haj*” – a savings account for the annual pilgrimage to Mecca – are introduced;
- enable Muslims and non-Muslims to choose the financial tools that are most appropriate to their needs; and

⁴² An extensive plan was drawn up in 2008, but was never implemented.

- lead to a better spread of financial risks over the economy.

All facets of the conventional banking system will have a role to play in the future Bangsamoro. With peace and order and an improved business and investment climate, it can be expected that development banks, commercial banks, and rural banks will step up to the plate and to provide financial support to, for example, business enterprises in the informal sector that wish to “move’ into the formal sector to take advantage of the new economic environment, and to new and expanding activities taking advantage of the resource base and the improved peace and order situation.

Islamic banking and finance should be looked at as a *system*, and thus it is critical that the foundations be set for the development of institutions and products across *all* these aspects of the sector, including banking, capital markets, microfinance and insurance. And it must be *viewed from the national as well as from the Bangsamoro perspective*, recognizing the legal mandate of the BSP and other national government instrumentalities, and the wider national market for Islamic financial products.⁴³

Business and economic reasons should underscore the system’s development, not merely political reasons. And the system’s development should not be rushed. The market should have the say in what is possible and what is not possible.

The legislative base should be wide and flexible enough to enable the market to do its work, recognizing the rapid evolution of Islamic financial products and their delivery mechanisms.

In recognition of this, the BSP is working with the other relevant agencies⁴⁴ to lay the groundwork for the necessary legislative and institutional agenda. The aim is to provide the appropriate regulatory framework for the licensing and supervision of Islamic banking in the Philippines, including the Bangsamoro, and for other Islamic financial instruments.⁴⁵ If these institutions provide the necessary legal framework for Islamic banking and finance at the national level, the need for legislative action by the Bangsamoro government will be minimal.

At the FEF/PCID/BSP Workshop in Banking and Finance in the Bangsamoro, Governor Amado Tetangco outlined five principles on which Islamic banking should be set up:

- the system must allow for a critical mass of market players under a competitive but well-regulated environment;

⁴³ Also, the main of business of some of the financial entities will be outside the Bangsamoro (e.g. Manila)

⁴⁴ The BSP is interacting with the Financial Services Forum - which includes the Securities Exchange Commission (SEC), Philippine Deposit Insurance Corporation (PDIC), Philippine Insurance Commission (PIC), and Department of Finance (DoF)- to secure cross-cutting and coordinated government support. The Bangsamoro Government should take a more active role in working with the BSP and Financial Services Forum on this legislative and institutional agenda.

⁴⁵ The BSP is also considering to first revise the regulatory framework for just AAIIBP operations that can then be shared and extended to other institutions.

- appropriate linkages, including interbank markets that cater to the unique characteristics of Islamic banking, must be present;
- creating a regulatory and supervisory framework that encourages a level-playing field, allowing Islamic banks to operate alongside conventional ones;
- the regulatory environment must encourage the provision of innovative products and services to address the distinctive needs of Islamic finance - Islamic financial players should be encouraged to, and not inhibited from, introducing Islamic finance products; and
- the regulatory framework must help build a broader customer and asset base by increasing investor awareness and acceptance, while ensuring consumer protection.

Ideally the legislation would be flexible enough to allow for the full range of Islamic banking arrangements,⁴⁶ recognizing that the products and instruments are continually evolving as the industry matures.

The BSP is also working with other agencies to review ways to deal with reserve requirements and liquidity management problems peculiar to Islamic banking institutions, as well as with deposit insurance, necessary tax reforms, and capital market and insurance products.

The Bangsamoro Government will have the power, subject to supervision of the BSP, to encourage the establishment of banks and financial institutions (and their branches) and off-shore banking units of foreign banks. This provides a good basis for the BSP to work closely with the Bangsamoro authorities in ensuring a local presence of financial institutions providing Islamic banking and financial products.⁴⁷

The Securities and Exchange Commission (SEC) will also have to review its regulatory base relating to capital markets to ensure an appropriate framework for Islamic capital market products, particularly *sukuks*.

It is critical for BSP and SEC to show fair treatment between conventional and Islamic institutions and products. A level playing field is important, although the embryonic nature of Islamic banking and finance in the Philippines – indeed the rest of the world even though rapidly growing – suggests some additional nurturing is required.

⁴⁶ It is still an open issue as to the range of Islamic finance products and instruments, apart from banking, that would also need to be covered in the legislation.

⁴⁷ The ongoing process of liberalizing the presence of foreign banks, from currently 10% to a maximum of 30% of commercial bank assets, would facilitate the entry as well of Islamic banks from abroad, whether as outright branches or through joint ventures with local partners.

Within this context, there are various options confronting the Bangsamoro authorities for the establishment of an **Islamic banking** presence in the region. These include the Bangsamoro Government having its own Islamic bank, which could either be a new entity or a revived AAIIBP.

If the Bangsamoro Government does wish to pursue the route of having its own fully-fledged Islamic bank, it would be wise to encourage private entities to also engage in providing Islamic banking and financial services in the region.

It could be expected that a number of the current conventional banks would want to explore the opportunities for operating Islamic windows, and some may want to consider establishing fully-fledged Islamic subsidiaries. Foreign banks may also want to enter the market, and this could be in joint ventures or technical/management agreements with local banks that do not have the necessary know-how in Islamic banking⁴⁸. There has already been some interest expressed by local and foreign commercial banks to take over AAIIBP, using it as springboard for introducing a wider range of Islamic banking and finance instruments.

Once the necessary action is taken by the national government to deal with issues relating to taxation which discriminates against Islamic financial instruments, **Islamic capital markets** perhaps offer the fastest route for introducing Islamic banking and financial products into the Bangsamoro.

The Bangsamoro government and local governments should explore meeting their “borrowing” needs through *sukuks*⁴⁹ since the drive toward financial integration with ASEAN (and indeed within greater Asia) will provide a platform for the local development of sukuks, given the growing importance of these instruments in some of these countries, particularly Indonesia, Malaysia and Brunei. Sukuks are suited to public-private partnerships (PPP), and these could form a significant component of the development thrust in the Bangsamoro, particularly to finance infrastructure in support of critical private sector projects. Major private sector projects in the region could also be encouraged to pursue sukuks in the financing of their operations. The financing can be organized on-shore or off-shore, and could be arranged without the necessity of establishing an institutional base within the Bangsamoro or even the Philippines.⁵⁰

The dominance of informal activity in the Bangsamoro and the difficulties associated with collateral over property and land, suggest that Islamic **microfinance facilities** could play a major role in expanding the economic base. However, there is a need for service providers with outreach to the rural areas where the need for support is greatest, and for suitably designed and affordable instruments tailored to the needs of the Bangsamoro market. In the Philippines,

⁴⁸ The Bangsamoro government may also want to consider a joint venture if it wishes to have its own Islamic bank.

⁴⁹ certificates of ownership in a pool of underlying assets in which the certificates are of equal value.

⁵⁰ The Philippine Stock Exchange (PSE) has taken steps towards Islamic finance. It has announced some 61 of its listed companies as *Shari'ah compliant stocks* with the ultimate goal is to develop a market index of these *Shari'ah* compliant issuers, which the PSE hopes to launch by 2015.

it is likely that cooperatives and NGOs would be the initial conduits for Islamic microfinance instruments, although rural banks may be willing to become conduits.⁵¹

The *Muhammadiyah* model of Indonesia is worth exploring for its applicability to the Bangsamoro. This model also introduces micro-*Takaful (micro insurance)* as protection to reduce risk associated with the possibility of losses. There is certainly a demand for insurance against crop failure by Muslim farmers in the Bangsamoro, but their ability to pay the necessary premiums is questionable.

Underpinning the Islamic banking and financial instruments will be ensuring that ***Shari'ah compliance arrangements*** are in place. The BSP is exploring this issue within the context of its legislative and institutional review, and the Bangsamoro government should engage with the BSP in this issue. The most suitable course of action for the Bangsamoro and the Philippines will need to be explored. This may involve adopting interim measures including tapping ASEAN expertise.

A ***communications strategy*** should be prepared to educate the public on the Islamic banking and finance principles, and the products available to them. This should be across all stakeholders, Muslim and non-Muslim, and be based on careful socio-economic research. The commercial aspects as well as the religious underpinnings should be stressed.

A program for developing the necessary ***capacity and skills*** of the public institutions – national and regional – for overseeing the development of Islamic banking and finance also has to be formulated. There is also a dearth of skills relating to Islamic financial instruments in the local banking and financial industry which has to be addressed. While some of this can be addressed through technical assistance and overseas training, local academic support is critical, and means to support financially the development of suitable courses in academic establishments will need to be explored.

Of immediate concern is the capacity of the national institutions to lay the necessary legislative and administrative groundwork for the establishment of Islamic banking and finance, and the capacity of the Bangsamoro authorities to oversee its “on-the-ground” penetration. An immediate effort should be made to get the necessary technical assistance in place.

In parallel, *a core team should immediately be set up within the Bangsamoro* to interface with the BSP and the Financial Services Forum (FSF) in laying the groundwork for the legislative and institution agenda.

⁵¹ Donors should be encouraged to expand their programs involving financial support to small farmers based on Islamic principles. These could be channelled through rural banks wishing to move away from conventional banking towards Islamic financing, cooperatives, and accredited NGOs. Associated with the financial support could be appropriate technical support, so enhancing the capacity of these organizations to sustain their programs over the longer term without the support of donors.

7. CONCLUDING REMARKS

The new Bangsamoro Government will have the opportunity to set a new inclusive growth path, provided it is willing to take full advantage of the flexibility expected to be provided by the basic law underpinning its autonomous status. While it is still uncertain as to how much flexibility it will have, it is clear that the national regulations and policies in many critical areas impinging on agriculture, industrial, and private sector development are far from appropriate for the Bangsamoro. New and innovative approaches more suitable to the unique characteristics of the region should be explored, drawing lessons learnt from local and international experiences.⁵²

Institutional capacity will be a constraint. Early action should be taken to review the skill needs and assess the capabilities currently on the ground, and where there are gaps, look for means of dealing with them. This could involve bringing in new skilled personnel, seeking donor support for enhancing capabilities of existing personnel, and/or seeking technical support from national and outside institutions, at least on a temporary basis. At the same time, a regulatory and policy framework that is both focussed and manageable should be pursued.

A major challenge will be the transition from the ARMM institutional structures and procedures to the new Bangsamoro institutional structures and procedures. While it may be tempting to dismantle all the existing apparatus and to start from scratch, this would be a big mistake. Yes, cut off the obviously diseased parts of the apparatus and those that are not relevant to the new government structure. Some functioning parts will pass muster and can remain unaltered. Modify the remainder as necessary as you move along. While this may cause some discomfort to the leaders over an extended period, it will allow a smoother transition, and avoid the pitfalls of a capacity vacuum that may never be adequately filled.⁵³

As concluded at the FEF/PCID overview workshop on the Business and Investment Climate in the Bangsamoro held in Davao, November, 2013 ... ***Perhaps the Bangsamoro can be the “beacon on a hill” with exemplary development policies for the rest of the country to emulate.***

⁵² Some of the critical regulatory and policy actions may have to be taken at the national level (e.g. Islamic banking and finance regulations). The Bangsamoro authorities will have to work closely with the relevant national government agencies in these areas, as appropriate.

⁵³ Organizations such as the current ARMM Regional Board of Investments (RBOI) will have a critical role to play, and thus should be given strong support. Although there is scope for reforming its agenda, it is one of the few organizations in ARMM that seems to be functioning effectively.

PART 2

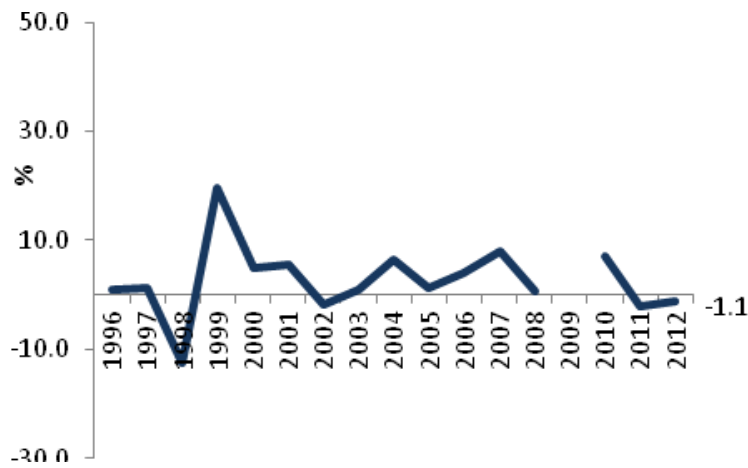
SECTOR REPORTS

ROADMAP FOR THE INCLUSIVE AND SUSTAINABLE DEVELOPMENT OF THE AGRIBUSINESS INDUSTRY IN THE BANGSAMORO⁵⁴

1. BACKGROUND

The agricultural sector represents the economic backbone of the Bangsamoro, contributing over 63% of the Regional Gross Domestic Product (RGDP) and employing about 70% of the workforce. Unfortunately, the sector has a history of regular contraction, as illustrated in the figure below.

Figure 9. Real Growth Rate of Gross Value Addition in the Agriculture, Forestry and Fisheries Sector in ARMM, 1996-2012.



Source: NSCB

Note: Statistical series break beginning 2009. Also, 1998-2009 series are pegged at 1985 prices while 2009-2012 series are at 2000 prices, hence cannot be completely comparable.

The decades of conflict has meant that the regional economy has suffered from a long standing underinvestment in food and nutrition security and agriculture in general. Primarily relying on an underdeveloped agriculture sector is a major reason why in ARMM, RGDP is the lowest, and poverty incidence is the highest, among all regions of the Philippines.

⁵⁴ This report was prepared by the Foundation for Economic Freedom (FEF) For the Bangsamoro Development Agency (BDA). The basic report was prepared by Alex Casiple, with inputs from Thomas Allen and Urooj Malik.

The aggregate Gross Value Added (GVA) of agriculture in 2012 was PhP7 Billion with crops contributing 73%, livestock (including poultry) 7%, and fisheries 20%. The primary crops are coconut, cassava, corn, rice, banana, rubber, and coffee.

1.1. Prevalence of Smallholder and Subsistence Agriculture

Agriculture in Bangsamoro has two realities:

- the agriculture of subsistence and low productivity farms – to which the majority of the farmers belong; and
- the agriculture of modern, globally competitive, and high technology plantations – which is very small, covering only about 1% of the agricultural lands in Bangsamoro.

There are about 250,000 farms in ARMM covering an area of around 533,000 hectares and employing around 800,000 workers.⁵⁵ The average farm size is 2.1 hectares, with each farm employing an average of just over 3.2 workers.

Fishing is much more important as an occupation in ARMM than elsewhere. The sub-sector employs around 130,000, which is some 17% of ARMM's labor force – the comparable figure for other regions is 2% to 5%.

1.2. Medium and Large Scale Agribusinesses in Bangsamoro

There are 22 agribusinesses (including one fishery based) listed by the ARMM-Regional Board of Investments (ARMM-RBOI). The agribusinesses are limited to:

- Lanao del Sur for Cavendish bananas, pineapples (Wao & Bumbaran), cassava (Balabagan and Malabang); and
- Maguindanao for Cavendish bananas (Paglas) and palm oil (Buluan).

These agribusinesses pale in comparison to those in Region X and XII where large corporate farms are located. Dole Philippines, Del Monte Philippines, La Frutera, La Panday, Sumitomo, Busco Crystal Super Milling, and Fiesta brands operate large anchor plantations and outgrowership with small to medium-sized farms. In Bukidnon (Region X), there are close to 400 livestock and poultry integrators. General Santos City (Region XII) is host to the tuna industry and its myriad network of downscale industries and suppliers of products and raw materials.⁵⁶

⁵⁵ The latest figures available are from the 2002 NSO census, which indicated that there were 248,528 farms covering 533,214 hectares and employing 799,000 people.

⁵⁶ Draft Transition Plan Report, PHILKOEI International, Inc.

In 2008, there were only seven agribusiness establishments in ARMM that employed more than 20 employees.⁵⁷ These establishments employed less than 1% of the 800,000 total agricultural workforce.

1.3. Primary Crops⁵⁸

Corn is the major temporary crop in the region

Among the temporary crops, corn is the major temporary crop in the region in terms of area planted. In 2002, this crop accounted for around 115,000 farms with a combined area of 272,000 hectares of land. Palay followed next with 77,000 farms covering 155,000 hectares. Tubers, roots and bulbs, ranked third with 74,000 farms and 30,000 hectares of land - unlike palay and corn, the number of farms and area devoted to tuber, roots, and bulbs production increased over the previous census period of 1991.

Coconut is the dominant permanent crop

Coconut trees were planted in more than half of the farms in the region – some 139,000 farms were planted with 21 million trees in 2002. Banana followed next with 79,000 farms planted with five million hills. Rubber ranked third with 2,000 farms planted with two million trees. In 1991, the major permanent crops in the region in terms of the number of trees/vines/hills were coconut, banana, coffee arabica, coffee robusta, and rubber.

Tending of cattle dominated the livestock raising activity

The dominant livestock raised in ARMM during 2002 was cattle. A total of 92,000 farms reported to have reared some 216,000 cattle. Cattle tended increased by around 50% over the 1991-2002.

Goat raising, which ranked one in 1991, placed second in 2002 with 200,000 heads tended, showing a 25% decrease compared to the 1991 figure. Carabao tending also fell by some 13% over this period to 128,000.

Basilan, Lanao del Sur, and Sulu had cattle as the number one livestock in terms of the headcount, while goat was the number one in Maguindanao and Tawi-tawi. Maguindanao tended more than one-third of the total cattle population in ARMM, although it tended more goats than cattle.

⁵⁷ 2008 Annual Survey of Philippine Business and Industry (ASPBI) 3 conducted by the National Statistics Office.

⁵⁸ BAS 2012. Note the latest census data available is 2002. However, the general pattern indicated by these figures is thought to be reflective of the current situation.

Chicken raising remained the primary poultry raising activity

Raising of chicken was the primary poultry raising activity in ARMM. About 160,000 farms were reported to have been raising nearly 2 1/2 million chickens in 2003, some 21% lower than the 1991 figure. Maguindanao accounted for nearly half of the chickens raised.

Raising of ducks ranked second, with 38,000 farms reporting to have been raising some 473,000 ducks in 2003. The number of ducks tended also decreased by 31% between 1991 and 2003, while the number of farms raising ducks decreased by nearly 50%. Maguindanao accounted for over four-fifths of the ducks raised.

Fisheries principally center around the island provinces of ARMM⁵⁹

The ARMM leads in the country's fisheries production. In 2012, the region recorded fisheries production of some 845,000 metric tons, which constituted some 17% of the country's fisheries production.

However, ARMM only ranks third in terms of commercial fisheries production – its 2012 production of 95,000 metric tons was under 10% of the national figure.

ARMM ranked even lower for municipal fisheries production – its 2012 production of 110,000 metric tons was around 9% of the national total, ranking it fifth in the country.

For aquaculture production, (seaweeds and other fishery species), ARMM ranks number one in the country. In 2012 it produced around 640,000 metric ton, or around one-quarter of the national production.

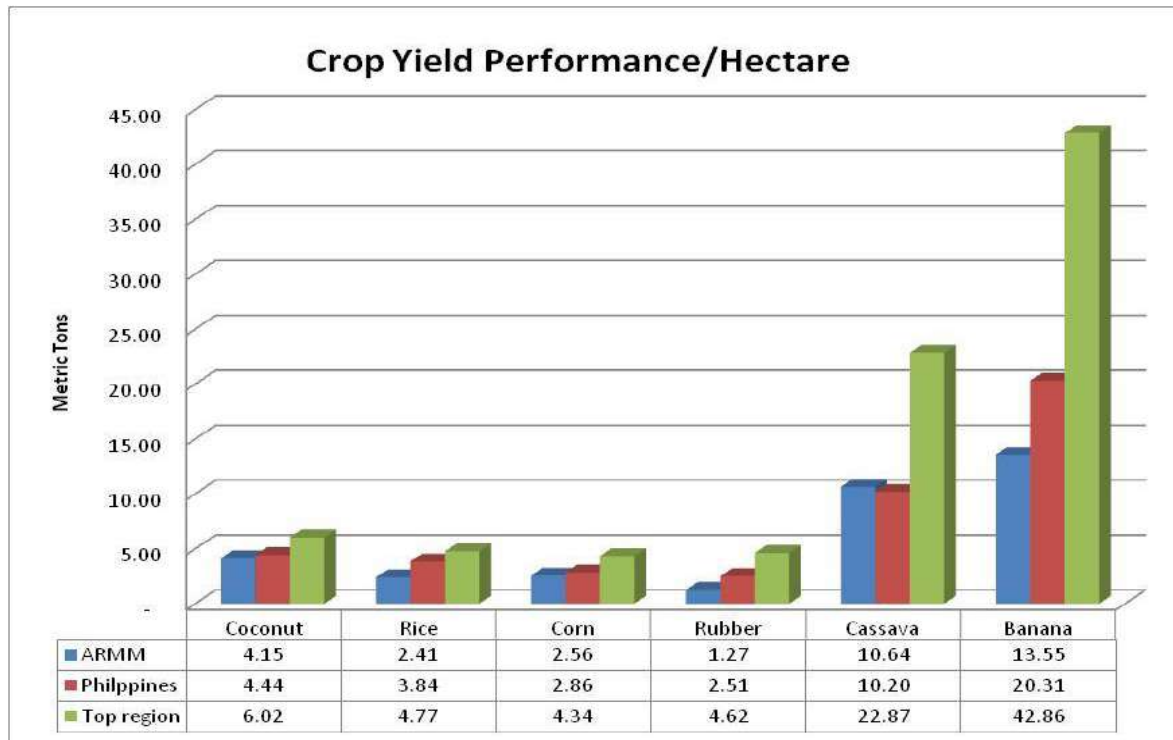
1.4. Yields and Value Added⁶⁰

The state of poor performance of agriculture as a whole is determined by aggregate productivity or yield performance of the commodities. The table below indicates that among the major crops in the region, only cassava performs an average yield per hectare that is greater than the national average.

⁵⁹ Source: Philkoe Report

⁶⁰ Extrapolated from the data available at BAS Website

Figure 10. Crop yield Performance/Hectare



Coconut is the most widely planted crop (314,000 hectares) in ARMM, but contributes the lowest in terms of GVA per hectare (Php24,000).

Cassava, on the other hand, although planted in only 95,000 hectares, contributes the biggest share in terms of GVA as a whole in ARMM and on a per hectare basis (Php133,000). This can be attributed to the presence of a cassava processing plant in Lanao del Sur that adds value of about Php10 per kilo – the plant transforms the produce of about 30,000 hectares of cassava into animal feeds, starch and other uses.

From the perspective of value chain analysis, the value performances are poor, as local benefits are mainly drawn from the production level of the value chain, which is inefficient and only marginally integrated to the other chains. This is due to weaknesses in the input supply level (finance, technology and agri-inputs) and lack of investments and technologies in the

processing level. These shortcomings mean that linkages with higher value markets are not opened up.

1.5. Challenges Facing the Smallholder Farmers

Smallholder agriculture is defined as farming over a small piece of land supporting a single family with a mixture of subsistence and cash crops.⁶¹

The 2.1 hectare average size per smallholder farm – often with insecure tenure – and poor productivity performance per unit area of most crops (lower than the national average), correlate to the high rate of poverty incidence in the Bangsamoro.

The size of the landholding per household is expected to be reduced further when in the future the holdings will be divided among siblings who will have their own families to feed. This is especially true if the manufacturing and service sectors - that could provide many smallholder farmers with exit opportunity from agriculture - remains underdeveloped.

This study suggests that the findings of many development experts on the problems faced by smallholders in less developed and developing countries hold true to the situation in Bangsamoro smallholder agriculture. Applicable insights in *From Subsistence To Profit-Transforming Smallholder Farms* (ibid) articulate well these problems:

- Distorted land tenure structures—including insecure property rights and underdeveloped land rental and sales markets—have been linked with less efficient land use and lower productivity-enhancing investments.
- Smallholders often have limited access to markets for both inputs and outputs, and this has a significant effect on their production activities.
- The geographic dispersion and limited access to infrastructure (including farm-to-market roads, transportation networks, irrigation, and market facilities) in many rural areas drive up transaction costs, lower smallholders' profit margins, and force many smallholders to pursue more subsistence-oriented production practices.
- Smallholders' limited access to productivity-enhancing technologies is grounded in an environment where public and private research systems do not sufficiently prioritize smallholder-friendly technologies, and extension systems fail to help smallholders gain access to and adopt such technologies.

⁶¹ From Subsistence To Profit-Transforming Smallholder Farms, Shenggen Fan, Joanna Brzeska, Michiel Keyzer, And Alex Halsema

- Many smallholders are excluded from productivity-enhancing financial services and are unable to secure much needed fixed and working capital, which ranges from land and buildings to machinery, high-yielding seeds, and fertilizer.
- Smallholders' low productivity is also affected by lack of access to education, which could help build the skills needed to manage on- and off-farm production systems more efficiently and raise smallholder adoption of innovative and high-return technologies.
- Smallholders have become increasingly vulnerable to a spectrum of emerging climatic, health, price, and financial risks and challenges as well.
- These emerging challenges lead many smallholder farmers to pursue livelihood strategies that involve lower-risk and lower-yielding agricultural activities.
- Such responses can help smallholders cope with adverse events, but they also cause poverty to persist, trapping smallholders in a cycle of little or no profits, with limited opportunities to undertake more productive and innovative activities.
- Moreover, subsistence oriented smallholder farming deprives farmers of the financial resources needed for education and adoption of new skills that entraps them to farming with shrinking land resources, which means providing them lesser and lesser exit opportunities.

The peace and order situation the Bangsamoro has only served to amplify these problems.

2. PRODUCTIVITY PERFORMANCE AND OPPORTUNITIES FOR PRODUCTIVITY ENHANCEMENT OF SELECTED PRIMARY CROPS IN THE REGION

2.1. Coconut

Coconut is the most widely planted and evenly distributed crops planted in five ARMM provinces and yet it contributed the least added value per hectare. In 2012 the GVA contribution per hectare is P32,740 per annum which is lower than the national average. A major reason is that the bulk of the coconut GVA is being tied up into the production of copra.

The yield performance in ARMM is lower than the national average, and the Philippine Coconut Authority (PCA) attributes this to inadequate inputa applied to trees, especially the micro nutrients fertilizers.

There are several ways to enhance the productivity of coconuts: copra route, whole nut route, and coconut sugar route.

Copra Route

Extrapolating the PCA study⁶² on the effect of micro nutrients on yield, it is estimated that if all coconut farms undergo rehabilitation through micro nutrient fertilization, the additional volume of production would increase by an average of 1200 kg per hectare per year or a total of 379,000 tons. At 2012 prices this would create an additional value of about PhP6.6 Billion per year.

Further, there is only one coconut oil mill inside ARMM, which is located in Jolo, Sulu. The plant's operation had been intermittent due to the lack of a stable source of power in the province. The province of Sulu represents only about 16% of the total coconut areas of ARMM. Hence 84% of copra produced in ARMM is processed outside the region. Processing copra into Crude Nut Oil (CNO) and into Edible Oil creates a value addition of PhP3.75 per kg and PhP4.5 per kg, respectively. Hence with an annual volume of 1.6 million tons, the untapped potential value addition is approximately PhP1.8 Billion to PhP2.05 Billion.

Whole Nut Route⁶³

The whole nut route entails the production of multiple products. This involves the diversion from copra production to the zero waste or full utilization of the components of a whole coconut, which is 35% husk, 12% shell, 33% meat and 20% water in terms of weight. Utilization of whole nut will entail the production of multiple products.

Table 1. Whole Nut

What's in a Nut?		
	Weight (kg)	Percentage
1. Husk	0.56	35%
>Coco Fiber		
>Peat		
2. Shell	0.19	12%
>Charcoal		
>Producer Gas		
3. Meat	0.53	33%
>Virgin Oil		
>Flour		
>Skimmed Milk		
4. Water	0.32	20%
Total Weight	1.6	100%

⁶² Cited by the policy paper: Priming the ARMM through Agribusiness Development by Rolando Dy

⁶³ Based on the interview with Rey Go, CEO of Regwill Industries, exporter of Coconut product derivatives

In an interview with Regwill Industries, an exporter of various coconut product derivatives, the minimum supply base of an integrated processing hub for the maximum utilization of the coconut components is 300 hectares. The projected GVA of a 300 hectares supply base along this route is shown in the following Figure 11.

Figure 11. Whole Nut Route- Volume/Revenue

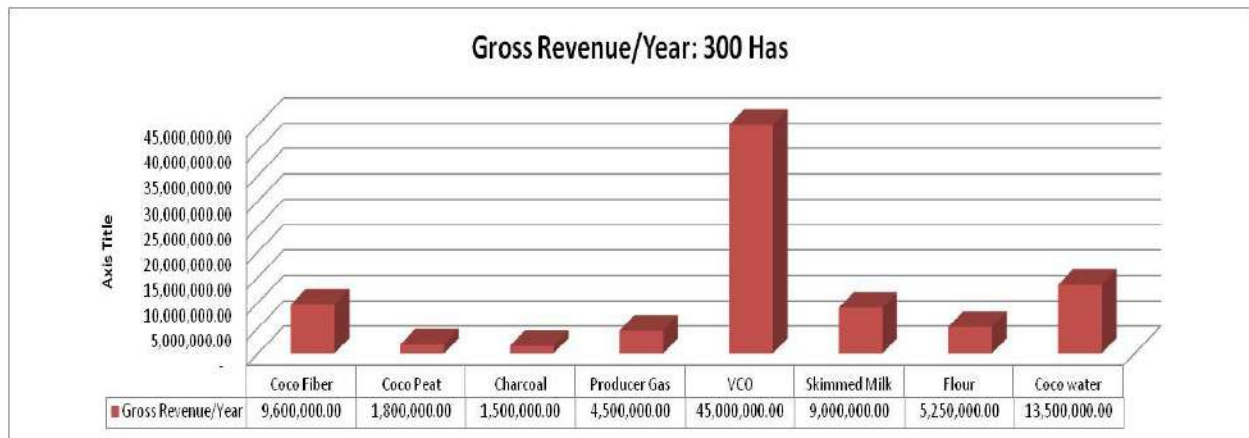
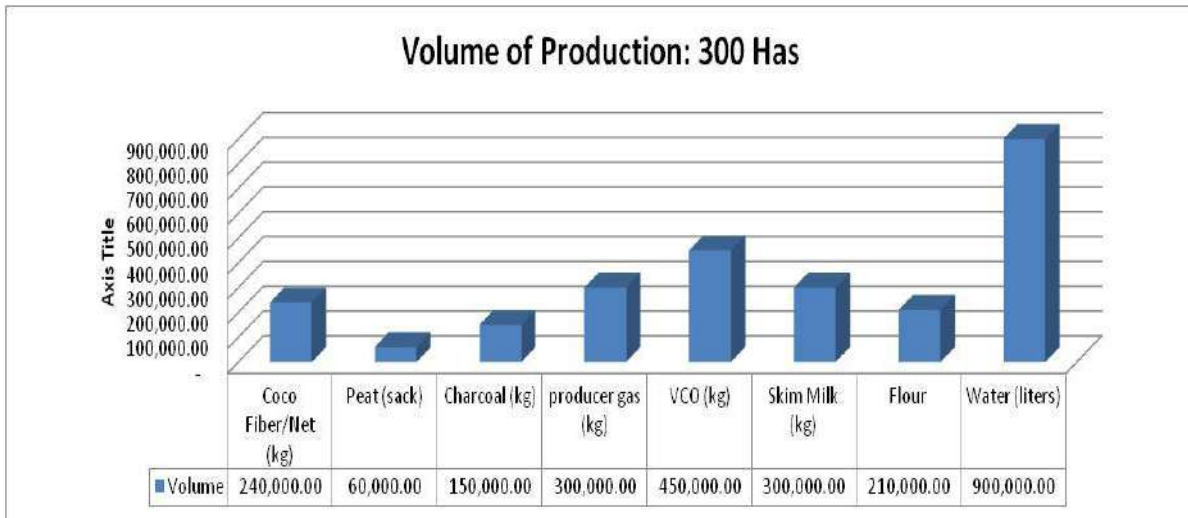


Table 2 shows that for a 300 hectare module, the difference in terms of GVA is Php80 Million or Php267,7500/hectare/year. With this scale, the total project cost of setting up a coconut integrated processing hub is about Php32 Million and the payback period is three years.

Table 2. Whole Nut Route

Whole Nut Route	
Husk	GVA
Fiber	32,000.00
Peat	6,000.00
Shell	
Charcoal	5,000.00
Producer Gas	15,000.00
Meat	
VCO	150,000.00
Skimmed Milk	30,000.00
Coco Flour	17,500.00
Coco Water	45,000.00
GVA/Ha	300,500.00
Total Hectares	300.00
Total GVA	90,150,000.00
Business as Usual (copra)	9,822,133.67
GVA Variance	80,327,866.33

Coconut Sugar Route⁶⁴

Another option for coconut light industrialization is coconut sugar processing. A coconut tree can produce 90 kgs of sugar a year. With a 100 tree population, a hectare of coconut can produce 9,000 kgs. At the current ex-plant price of Php135, the projected GVA per hectare is Php1.2 Million, the highest among other options. The GVA variance of a 300 hectare module is shown in the table below.

Table 3. Coconut Sugar Route

Coconut Sugar	
Yield Per Hectare (kg)	9,000.00
Price/kg: Explant	135
GVA per Ha	1,215,000.00
300 Hectares	364,500,000.00
Business as Usual (copra)	9,822,133.67
GVA Variance	354,677,866.33

Establishing a module will need a start up capitalization of about Php22 Million with a 30 ton capacity processing plant. On a seven year cash flow program, a total 10 processing plants can

⁶⁴ Based on the Feasibility Study Report of Strengthening for Global Competitiveness and Expanding ARB Participation in the Value Chain of the Coconut Sugar Industry in MISORET Cluster

be viably established. Coconut sugar production in the farm and plants is labor intensive with a 4:1 worker-hectare ratio.

2.2. Corn

In terms of land area, corn is the next largest crop planted in ARMM and occupies an area of nearly 300,000 hectares. Corn areas are largely concentrated in the provinces of Maguindanao and Lanao del Sur. The yield performance of corn per hectare is also lower than the national average. This is due to the rising cost of inputs, making them inaccessible to many farmers.

A recent World Bank study (Agricultural Supply Chain Analysis in Mindanao) disclosed that corn farmers in Kadilingan Bukidnon who get inputs from and sell their produce to their cooperative, earn a margin of PhP2.94 per kg. On the other hand, farmers from Wao, Lanao Sur who are charged with interest for their agri-inputs by traders who are also buyers of their produce, earn only a margin of PhP1.04 per kg. The difference is PhP1.90/kg. Under the cooperative, the cost of inputs per hectare is 25% less or PhP12,198 per hectare.

The cost of producing a kilogram of corn in Wao is PhP1.74 higher compared to Kadilingan. The factors that affect costs are the:

- higher cost of inputs due to lack of competition among agri-inputs traders;
- usurious interest rate of financing from the informal sector;
- higher cost of transport and logistics due to the non-existence or poor conditions of farm-to-market roads coupled with long distances from the markets; and
- lack of suitable drying facilities, resulting in corn losses and higher drying cost.

Based on 2012 Bureau of Agricultural Statistics (BAS) data, ARMM produces about 764.7 million kilograms of corn a year. Assuming Wao represents the whole picture of the whole region, total loss due to the above pre and post harvest inadequacies is estimated at PhP1.4 Billion a year.

The WB study also provided a comparative analysis of the cost of agri-inputs between the two cases:

Table 4. Corn: Comparative Analysis: Coop vs Trader

Comparative Analysis of Agri-Inputs Cost			
Input cost/ha	Coop led	Wao	Variance
Fertilizers	20,907.00	27,393.00	(6,486.00)
Pesticides/Herbicides	2,098.00	2,575.00	(477.00)
Seeds	13,128.00	18,363.00	(5,235.00)
Total	36,133.00	48,331.00	(12,198.00)

Extrapolation of the available data also suggests that under the cooperative-led modality, the agri-input financing requirement of the ARMM corn industry is approximately Php10.8 Billion and the total added value (aggregate savings due to innovation) is about Php3.6 Billion a year.

Barriers to Inclusive Corn Industry Growth

The World Bank study concluded that the barriers to an inclusive Corn Industry Growth are unorganized small-scale production and trade, inappropriate agriculture technology, and poor post-harvest processing.

Unorganized small-scale production and trade

A common problem identified is the lack of organization of small-scale production by farmers who are scattered in different villages. This can hinder agricultural extension workers since they cannot provide adequate technical services and training to groups of farmers. This can also hinder findings ways to multiply the impact of training and demonstration on how to improve yield and access technical agricultural information.

The lack of local organization also makes it difficult for farmers to apply for institutional credit, and make individual farmers more dependent on informal credit sources which are often usurious.

Another drawback of not having a farmers' group is lack of access to information, and ability to negotiate better prices with traders.

In order to overcome these problems, key informants from CSO suggested formation of farmers' production groups at the village or village cluster level. Farmers' production groups can then act as a node for information exchange on agricultural technology as well as market and trade information.

Organized production groups can also contribute to improving post-harvest processing and storage systems, as well as ensure quality of products in order to gain a better bargaining power against traders from outside of the village.

Development of a stronger production group can possibly regulate traders and private investors that violate contracts and agreements.

Inappropriate Agricultural production technology

Another crosscutting issue identified concerned agricultural technology that allowed sustainable use of land, and minimized future economic and environmental risks for rural households. In particular, there is a high concern on land use intensification without soil management. Already, farmers are reporting declining yields. This is largely due to intensive cropping without adequate soil management. It is therefore essential to introduce techniques to protect and improve soil fertility in areas under intensive agricultural use.

As the majority of farmers grow corn without intercropping or rotating crops, it is also important for both extension and research agencies to continue experimenting not only with different varieties, but also with different cropping techniques to sustain high yield and soil fertility.

Poor Post-harvest processing

Other important issues are the need to improve post-harvest processing, and to develop a grading system to monitor the quality of products.

Consideration has to be given as to the most effective means to support post-harvest processing facilities (especially drying facilities) and storage systems. This would include reviewing the cost-effectiveness of different options for post-harvest processing (i.e. sundried, small-scale drier, large-scale drier).

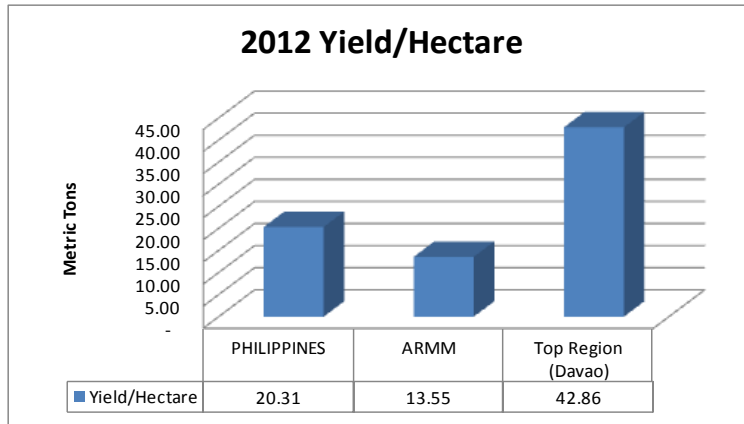
A standardized grading system should be crafted, and disseminated to curtail subjective grading that often leads to arbitrary price reductions.

2.3. Banana

In ARMM, some 32,000 hectares is planted to banana, both local (saba, lacatan) and Cavendish. The average yield per hectare is 13.55 tons per hectare, which is much lower than the national average of 20.1 tons and the top region (Davao Region) which is 42.6 tons.⁶⁵

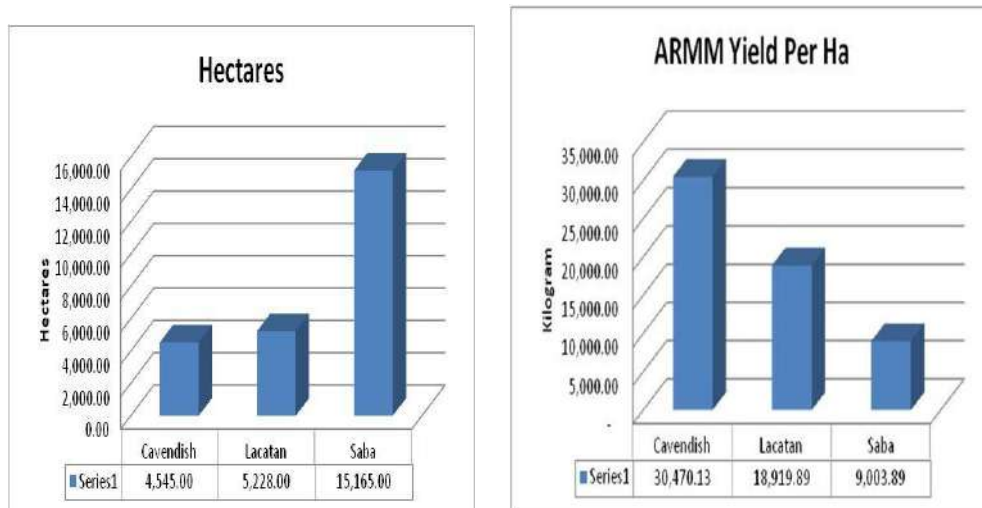
⁶⁵ BAS Data available in its website

Figure 12. Banana Yields



The *Saba* variety, which is planted in about 47% of total banana area (15,165 hectares), has the lowest yield of 9 tons per hectare, while *Cavendish* - which is planted in only 4,545 hectares or 14% of total banana hectarage, has an average yield of 30.4 tons per hectare per year.

Figure 13. Banana Yields by Variety



The local bananas are mainly planted in smallholder farms while Cavendish is planted in commercial plantations operated by big business firms. The comparably low productivity performance of local bananas is obviously due to lack of technical and agri-inputs which is a common predicament in smallholder farms.

Of the local bananas, *Lacatan* is higher in terms of yield and income per hectare because, compared to Saba, it is more integrated in the regional and national markets. Yet it still pales in comparison to Cavendish bananas which are produced primarily for exports. This was highlighted in a 2008 comparative study as shown in the table below.

Table 5. Bananas: Yield and Income

Lacatan: Cost and Return per Ha (2007, prices)		
Volume		39,605.00
Price/kg		8.60
Gross Income/ha		340,603.00
Post harvest loss		102,168.00
Materials and prodn cost		119,196.00
Labor		20,433.60
Total Cost		241,797.60
Net Income/Ha		98,805.40

Cavendish HARBCO Case (2008)		
Boxes/Ha		4,200.00
Price per Box		141.90
Revenue		595,980.00
Cost/box		81.7
Total Cost		343,140.00
Net Income/Ha		252,840.00

Source: Agrarian Reform in the Philippine Banana Chain
 Joy Hasmin De los Reyes
 Wim Peluassy

3. STRATEGIC FRAMEWORK FOR INCLUSIVE AGRICULTURAL GROWTH

It is necessary to look at the growth of the agribusiness industry within the context of the agriculture sector as whole, as these are closely intermeshed.

3.1. The Key Actors

Inclusive growth needs to draw the interactive participation of four key actors: the smallholder farmers, the private sector, the public sector, and civil society organizations.

Figure 14. Key Actors



Smallholder Farmers

The framework of intervention for inclusive agricultural growth in Bangsamoro should be cognizant of the plurality of smallholders who represent the vast majority of agricultural producers in the region. Smallholders are classified as follows:

- *Stand alone or independent smallholders* are those who till their land on their own with no or minimal assistance from the government or the private agribusiness sector.
- *Assisted smallholders* are represented by small farmers that usually received assistance from the government and non-government organizations (NGOs) through the provision of agri-inputs, financing and extension services.
- *Integrated smallholders* are small farmers that are well integrated into to the value chain of specific crops they propagate through joint venture or contracting arrangements with large scale agri-business firms.

Private Sector

The operations of the few large agribusiness firms like La Frutera, Agumil, Matling Industrial and Commercial Corporation inside the Bangsamoro offer insights into the important roles the private sector can play in agricultural development of the region. They allow for a rapid increase of value addition opportunities through agribusiness relative to primary production.

Agro-processing enterprises like *Matling Commercial Corporation* are increasing demand and the effective size of market for cassava farmers' products. Exporters (*La Frutera*) and agro-processing enterprises (*Agumil*) are furnishing crucial inputs and services to the farm sector for those with no access to such inputs. This is inducing productivity and product quality improvements.

And there are the small-scale private enterprises providing various transport, support services and post-harvest facilities to farmers. As smallholders get organized, they in turn can be brought out of subsistence and into the formal sector, and operate as cooperative/private sector entities. The effective organization of smallholders is often a precondition for post-harvest facilities and processing to emerge, whether through independent private initiatives or through the smallholder organizations.

Agri-businesses are stimulating market induced innovation through chains and networks. Domestic and export systems are becoming more mutually supportive.

Public Sector

High poverty incidence in an economy that is heavily dependent on fragmented smallholder agriculture and the slow expansion of agribusiness-led commercial ventures in ARMM, suggest that existing regional government agricultural development programs have not sufficiently addressed the hurdles.

There is a consensus on the need for the Bangsamoro government to continue creating an enabling environment for the development of smallholder farming systems and for the growth of private investment through stable and well functioning institutions, including for:

- land and property rights;
- business, labor, and market regulations;
- banking and finance;
- contract enforcement and dispute settlement;
- market regulations; and
- incentive and support services.

Underpinning these will be the restoration of law and order and the rehabilitation and upgrading of essential infrastructures.

The Bangsamoro government must continue to provide essential, high-return public goods, notably those related to public research and development and extension/support services, complementing private investments in this area. Integrated policy packages that directly support smallholder market access, capacity, and efficiency will be critical, whether they be through directed government agricultural programs or the promotion of joint ventures between agribusiness firms and smallholders.

There is a need to leverage the interest of the business sector in agriculture and related value chains. This can bring fresh capital to rural areas and contribute to increasing supply, quality, and market distribution of produce, generating positive financial, economic and social returns. It must ensure that business investments do actually create positive benefits and are in keeping with emerging principles of responsible investment in agriculture, which requires clear incentives and safeguards.

Civil Society Organizations

Civil Society Organizations (CSOs) have a wide range of roles as development actors and change agents. These include – but not limited to – the delivery of basic services, support to local development, policy influencing in support of participatory and democratic governance, and the promotion of demand-driven accountability mechanisms.

Civil society – including NGOs and foundations – can mobilize the community to meet its unique social, environmental and economic needs. It can also demonstrate innovative programs that can be scaled up by governments and businesses, and provide risk mitigation tools that build market confidence.

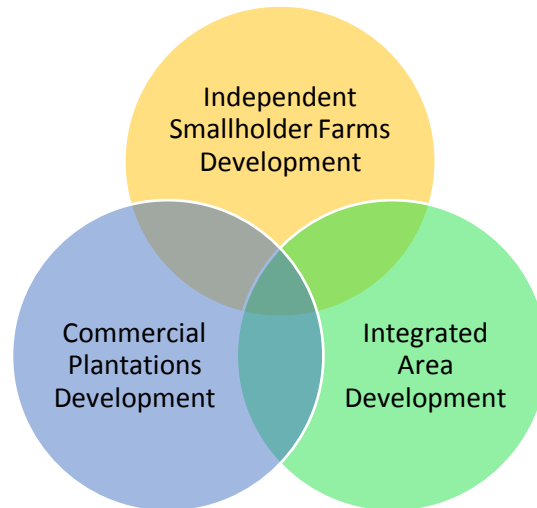
Some CSOs play a special role in serving as buffer social agents in times of state and market failures that may happen during conflict escalation or recurrence. Building resiliency to these shocks and preparing smallholders for meaningful engagement with the state or market sectors are examples of this special role.

3.2. Strategic Growth Paths

Three strategic growth paths are proposed to synergize the contributions of the above mentioned actors:

- Harness the potentials of *independent smallholder farming system* for food security and domestic and regional market demands.
- Promote *private sector led commercial crop plantation farming system* for export and high value markets.
- Develop and replicate the sustainable *integrated area development system*.

Figure 15. Strategic Growth Paths



Growth Path One. Harness the potentials of independent smallholder farming system for food security and domestic and regional demands.

The first approach would focus on the development of smallholder farms which represents the vast majority of farming units.

The thrust of this approach will be to:

- increase the productivity of smallholder farms;
- facilitate the development of forward linkages, particularly through further processing facilities; and
- increase the sector's resilience to risk, including through climate change.

The *increase in productivity* will come principally through:

- improved extension services to small-holders, particularly through assistance to farmers in consolidating their land use and property rights, adopting sustainable agricultural practices such as soil erosion control, and facilitating access to suitable technologies, production inputs, and market information;

- improved farm-to-market roads and transport, and small-scale water harvesting and irrigation facilities; and
- improved access to rural finance.

Dealing with agri-input bottlenecks, particularly fertilizers, will be critical. Consideration should be given to providing transport subsidies for fertilizers for an interim period, being withdrawn once the appropriate infrastructures are in place and private sector providers and smallholders are sufficiently strengthened.

The facilitation of forward linkages will involve efforts to:

- ensure a better understanding of the value chain approach to agro-industrial development among the bureaucracy, private sector, and farming community;
- enable and encourage smallholders to consolidate their production to facilitate profitable opportunities for common services (such as cold storage, drying, and other post-harvest facilities) and further processing; and
- make it easier and less costly to do business, by simplifying business and labor regulations, facilitating access to finance, and providing suitable incentives.

The increase in the sector's resilience to risk will involve:

- a much better understanding of the factors impinging on farmer risks, particularly relating to the impact of climate change; and
- the design and deployment of appropriate farm finance and insurance products.

An underlying objective is to *foster knowledge driven agricultural growth through farmer cooperation*. Empowering farmers by giving them greater ability to develop solutions on their own initiative and to access the specialized forms of technical assistance that they need on particular issues is important.

Taking cues from the experiences on post conflict agricultural development interventions in African countries, this is aimed directly at making the smallholders more knowledge-intensive through professionalization and capacity-building for their organizations and through improvements in the systems for technology generation and dissemination⁶⁶. Specifically, it aims to strengthen the sector's social capital base by providing farmers with organizational frameworks through which they can develop commercial linkages and function in a more entrepreneurial manner. The program includes interventions to strengthen the entities in the

⁶⁶ Track of Rwanda Post Conflict Agricultural Development Program

sector that are charged with the development of productive technologies and other forms of applied knowledge and with imparting this knowledge to farmers⁶⁷. The program covers:

- *Promotion of farmers' organizations and capacity-building for producers.* The program aims to develop the management and entrepreneurial capacities of these organisations so that the required social capital is put in place. This will capacitate farmers' associations to become involved in higher-value activities, both at the farm level and in agro-processing activities, as well as improving their access to inputs.
- *Restructuring support services.* The objective in this respect is to develop an extension system that is accountable to farmers as clients and, crucially, creates the necessary incentive structures for this purpose. The promotion of participatory learning systems will be integral to this at all levels, and the training of extension agents will emphasize this. Furthermore, a multi-tiered system will be developed that will ensure that different levels of training, necessary for specialized service provision, are available to extension agents.
- *Research for transforming agriculture.* Research needs to be better at responding to farmers' priorities and needs and doing so will require a number of activities. These will include using participatory research techniques where farmers' organizations are involved in setting research agendas, as well as strengthening the scientific and technical capacity of the formal and public research institutions.

Growth Path Two: Promote private sector led commercial crop plantation farming system for export and high value markets.⁶⁸

The Bangsamoro authorities will have to take early special actions to help reintegrate displaced persons and ex-combatants and to “kick-start” the development process. Many of these will return to subsistence or small-scale farming and fishing, and will require immediately shelter, planting materials, tools and other basic needs. This will then have to be followed by interventions along the lines outlined in Growth Path One to improve their production. However, this uplifting of smallholder production will take time, and will not be enough by any stretch of the imagination to meet the needs and aspirations of the peoples of the Bangsamoro. Nor will the needed infrastructure programs provide sufficient sustainable job opportunities. Bolder steps will be required.

The Bangsamoro authorities – led by the ARMM- Regional Board of Investments (RBOI) - will have to take special actions in the coming months to encourage the early establishment of some – perhaps two or three or four - large private sector led agro-based plantations. These

⁶⁷ Ibid

⁶⁸ This section draws on the outputs of the *FEF/PCID Workshop on Overview of the Business and Investment Climate in the Bangsamoro* (finance by Australian Aid) held in Davao, November 2013.

could include the significant expansion of existing plantations for current or new crops. In promoting these projects, the emphasis should be ‘transaction-oriented’, seeking out the entrepreneurs who are most likely to deliver, and help in linking them to potential local partners. The authorities should be fairly flexible on the models for these projects, which would be driven by the nature of the crops, their location, the amount of land needed to make the operations viable, the land aspirations and cultural norms of the local population, and the way land access can be readily obtained and security assured. The models could be along the lines of La Frutera or Agumil, or some variation thereof. Aside from suitability of land and access, the ability to mobilize the required landholdings and assure security of assets and personnel will be the principal factors in determining the most appropriate locations for these projects. As well as local labor, demobilized MILF forces and returnees could be employed. Hopefully, these projects could be underway by 2016 when the new Bangsamoro Government is in place.

Restoring law and order will be a major factor in the decision of potential new investors in plantations, but they will want to be assured that:

- adequate land is available with secure tenure over the long term;
- potential local partners are available who can ensure an effective interface with the local community; and
- critical infrastructures can be in place.

The supply of progressive-minded local elected officials is critical - the *datus* should serve as “development entrepreneurs” who identify clan interests broadly in terms of development outcomes of communities within their jurisdiction.

The National Government and the Bangsamoro/ARMM Government should be ready to move on the physical and social infrastructure required to service and support these plantations, with donor support if necessary. These infrastructures could also impact other nearby areas which do not fall within the scope of the plantations, but could, with minimal further investment by the appropriate government authorities in feeder roads, link them into the infrastructure “hub”.

Consideration should be given to encouraging institutions such as the International Finance Corporation (IFC) to participate in the equity of the ventures if this is needed. A revived Southern Philippine Development Authority (SPDA) could partner the initial ventures in the Bangsamoro to reduce the risk burden of the private sector investors. The Special Development Fund could also be drawn on for these purposes. Appropriate fiscal incentives will be required, reflecting the risks, long gestation, and up-front costs associated with projects of this nature in conflict-affected areas. The National Government should also encourage organizations such as the DBP, Land Bank of the Philippines (LBP) or even international organizations to consider offering some form of political risk insurance for local investors, assuming that such insurance may be available from the Multilateral Investment Guarantee Agency (MIGA) of the World Bank

Group and ADB for foreign investors (although they have been reluctant in the past to offer insurance in conflict-affected areas).

Initial success in these efforts could trigger further investments in commercial plantations, thus becoming an integral element of the Bangsamoro development strategy over the medium to longer term. By being flexible with the “business models”, there is considerable leeway for adapting the scope and nature of the plantations to suit local conditions. As well as providing scope for more efficient and profitable small-holder production through out-grower arrangements, they would also provide job opportunities and stable income for farmers who chose to exit smallholder agriculture for greener pastures. These plantations would link the local economy to the global market by producing high value export crops.

Growth Path Three: Develop and Replicate Sustainable Integrated Area Development

This approach recognizes that there are some areas that are environmentally fragile or have special characteristics that necessarily require a significant degree of government intervention, and may require transcending into cultural and social dimensions of development. These could be physical or culturally sensitive areas, including locations where security issues would preclude private sector interest - at least in the short term - because of the level of risk involved. As well as focusing on productive activities, the plans for areas under this approach would be “complete” plans incorporate physical and social infrastructures.

The nature of the integrated area development would be location specific. For example, an environmentally sensitive river basin may require an integrated planning approach with the central focus on protecting watersheds, securing water catchments and ensuring sustainable forest management. The presence of indigenous communities in the basin would add a further dimension. The base camps of the MILF could also be the focus of an integrated development approach, transforming them from centers of armed struggle to integrated agribusiness hubs within peaceful and productive communities.

The Bangsamoro authorities will have to make a special effort to determine locations for which an Integrated Area Development approach is justified. These should be limited, and subject to stringent selection criteria.

Some of the localities may lend themselves to commercial style plantations, but may require the government to take the lead (at least initially) – with possible private sector support - because the magnitude of post conflict fragility and risks are too big for private sector to deal with. Just as for private sector led commercial plantations, there are various “business models” which can be adopted, such as the nucleus estate model of Indonesia and the FELDA and FELCRA models of Malaysia.

Essentially these involve:⁶⁹

- The government taking the lead, with the private sector playing a “back-up” role in some cases – over time, the private sector may play a greater role.
- Consolidation of fragmented small landholdings and their transformation into centrally managed, efficient and competitive commercial plantations, with out-grower smallholder connections (some of whom may be independent of the estate).
- Agro-industrialization that will transform the produced crops into a higher value processed products – this may also include the local processing of agri-inputs, such as fertilizers.
- If applicable, generation of bio-energy that utilizes farm wastes as feedstock – this could lead to power self-sufficiency of the plantation and any surplus sold to the national/regional grid.
- Social development infrastructures, such as schools, skills development centers, mosques and religious centers, health facilities, and recreation centers.
- Build-operate-transfer arrangements in many cases – state and private sectors will help develop the plantation, including land-clearing for cultivation and, once developed, handed over to the smallholder for self-management.
- Integration of sustainability mechanisms both from the environmental and economic perspectives.
- Integration and access to the opportunities offered by Islamic finance and banking for investments requirements, as well as to Halal Industry as a market niche.

4. SEQUENCING THE ROADMAP OF INCLUSIVE AGRICULTURAL GROWTH

Since the post conflict situation will remain fragile and the thrust for inclusive agricultural growth does not develop in a linear manner, any intervention cannot be described in a “one-

⁶⁹ Integrated Area Development localities may be quite large (e.g. river basin development) and may thus have “sub-locations” which may have their own strategic growth paths, but still within the context of the overall integrated development. Some of these “sub-locations”, for example, may be areas where private sector led and managed commercial scale plantations would be feasible and appropriate, and other areas where “traditional” smallholders would still predominate.

size-fits-all” manner. The following sequencing of the critical processes towards the goal of inclusive growth can only illustrate the general pattern.

Nevertheless, the above strategic approaches will serve as guide in defining the stages and phases of agricultural transformation. These stages and phases are not strictly separated but may overlap and should be seen holistically, adjusted according to the specific circumstances of the participating communities.

4.1. Phase I: Initiation Phase

Stage 1: Smallholders Understanding the Constraints and Potentials of Inclusive Growth

The attainment of the vision of inclusive agricultural growth will require massive awareness raising among stakeholders, especially the smallholder farmers, of the agricultural conditions in Bangsamoro. This includes awareness on the strengths, weaknesses, threats and opportunities of the agricultural systems as a whole, and of the smallholder farms in particular. This will provide the basis for fostering an appreciation of the inclusive agricultural development roadmap of the Bangsamoro in the post conflict era.

Stage 2: Social Infrastructure Building

Optimizing growth requires the organization of smallholder farms into production clusters. The clusters, in turn, could be organized into barangay cooperative enterprises, and the latter may be federated into municipal enterprises. Such organizations would facilitate smallholder decisions on the strategic growth path they would like to track – whether they wish to remain independent or continue as cooperating smallholder farmers, engage in commercial ventures with the private sector, or engage with the state if in an area designated for integrated area development.

The setting up of multi-sector technical working groups – composed of representatives from the smallholder organizations, government, private sector and civil society organizations – would facilitate making the value chain of agricultural commodities more functional. Critical elements in the chain could be identified, and the role of the various stakeholders in dealing with them specified.

Stage 3: Development of the Common Vision and Plans for Inclusive Agricultural Development

The common vision and the roadmap should be internalized by all stakeholders, and translated into concrete plans at the farm, cluster, cooperative and enterprise levels, as applicable. Necessary inputs such as funding, human resources, technology logistics and infrastructure and market information have to be included in the plan. Based on the roadmap, smallholder farmers as a group would identify the strategic growth path it wishes to engage (as mentioned above).

The vision and road map could form the basis for an Agricultural Zone Development Plan that would reflect the identified strategic growth path, covering land tenure and security improvement, productivity systems development, and continuing social infrastructure building. The Zone would be defined as a contiguous estate with common or dominant farming system typologies such as:

- The irrigated rice-based farming system
- Upland cereal-based farming system
- Smallholder mixed farming system
- Industrial Crops Farming system
- Inland Fisheries system
- Marine Fisheries System
- Agro-forestry system

The *land tenure and security improvement* component of the plan will address land ownership issues, such as conflicting land claims and land dispute resolution mechanisms.

The *productivity systems development* component will address the issues such as inaccessibility (farm-to-market roads and transport) and irrigation, deficiency in the factors of production like production inputs, workforce skills, finance, and technology, and need for post-harvest facilities and processing.

The *continuing social infrastructure building* component will address the workforce health and education issues, and issues of organizational adaptability to changing conditions in the agricultural landscape, such as the need to acquire new capacities and partnerships to cope with emerging or new challenges, such as climate change.

The local Datus will no doubt play a major role in this process. They will also often be the key link with private sector interests, particularly if the commercial plantation route is the desired course. The Bangsamoro government will also need to be engaged in this process.

4.2. Phase II: Design and Implementation of Agricultural Development Programs

Stage 4: Engaging and Capacitating Stakeholders in The Agricultural Value Chain

After the appreciation of the vision and road map and the roles they should play in realizing the common vision, the stakeholders will only spring to action if the necessary technical and financial resources are at hand, as well as the enabling environment for access to such resources. Local capacity gaps should also be identified and bridged by the deployment of resources needed to fill the gaps – this applied to all stakeholders, including enablers.

In order for smallholder farmers to respond to the challenges of increasing their productivity and incomes, their first requirement is a secure and productive asset base. Property protection and land dispute mechanisms must be in place and accessible to them. They also need to be able to rely on well-functioning R&D, extension, training and information systems that could improve yield and reduce costs.

Furthermore, and critically important, they need access to a range of financial capital and services, including savings, credit, and insurance. Through organizing themselves into clusters/cooperatives, smallholder farmers can reduce input and marketing costs, and have enhanced marketing power. They are also in a better position to enhance post-harvest facilities, and encourage further processing activity.

The regional and local governments, through their service agencies must play a central role in establishing the enabling environment and mechanisms for smallholder farmers and private sector service providers to address the development constraints and respond positively to the development opportunities.

Stage 5: Institutionalization of Policy Support and Enabling Mechanisms

*Policies on Land Tenure*⁷⁰

The country's present land administration situation is plagued with many problems, including:⁷¹

- multiple agencies with duplicating and overlapping functions and complex processes;
- multiple laws leading to inconsistencies, especially on agency functions and mandate;
- multiple land titling process, with the emphasis on a judicial mode of titling (in contrast to the rest of Southeast Asia which use an administrative mode of titling);
- multiple forms of ownership; and
- multiple standards for land valuation and multiple agencies undertaking valuation.

Inefficient land record management and lengthy and expensive appeal processes in settling disputes compound these problems.

These problems at the national level are magnified in the Bangsamoro, where land-related strifes played a significant role in precipitating the Bangsamoro insurgency.

⁷⁰ This section is derived principally from the output of *the FEF/PCID/UP-LAW Workshop on Land and Property Rights in the Bangsamoro* (finance by Australian Aid) held in June 2014 in Manila.

⁷¹ Briones (2013)/Dealca (2009)

The World Bank/IOM Land Scoping Mission in the Conflict Areas of Mindanao found that there is very limited formal data on land ownership and usage.⁷² And where information on land tenure exists, the Mission found its legitimacy was frequently questioned, with better educated, more powerful individuals or groups registering land that is being claimed by others (usually the poorer and more vulnerable population who neither understand the importance of title registration, nor have access to the complicated and corruption-prone process of land titling), and allegations of irregularities within the responsible institutions further undermining trust in written records and contributing to land conflicts.

This means that it is not possible to say with certainty how much land is currently titled correctly in the Bangsamoro and how many competing land claims exist.

Based on field investigation reported in Briones (2012), the overriding consideration for customary tenure is possession, seen as legitimate occupation at the community level. Possession may not necessarily be supported by formal title.

Informal tenure is sufficiently established even to affect an orderly transfer of rights, supplanting the need for a formal sale.⁷³ However legitimacy will typically require mediation by local strongmen, i.e. clan and village chieftains, or local politicians. However, the system is not foolproof. Local strongmen may act not as a referee, but an interested party, either as a buyer of land or a seller – in such cases the outcome of a transaction may be questioned by some members of the community and even exacerbate conflict. The popularity of informal land markets implies perpetuation of the poor level of land documentation.

Informal or traditional justice systems through mediation are the most common mechanism for the resolution of competing land claims in predominantly Moro and Indigenous communities. The datu, clan leaders and/or elected officials would often be the principal mediators.

The World Bank/IOM Scoping Mission highlights some of the critical issues that would need to be addressed in formulating an action agenda to deal with land tenure in the Bangsamoro, viz:

- new dynamics are being created with the signing of the FAB - an increased number of “latent” competing land claims are becoming “actual” land disputes which, if not addressed soon, could undermine the on-going peace-making efforts;
- uncertainty about how the FAB provisions on land claims will be applied adds fuel to the new dynamics - this vacuum is encouraging some stakeholders to move and position themselves based upon their expectation of how the FAB will be implemented;

⁷² Figures compiled by Kadtuntaya Foundation in 2004 indicate that some 64% of the 527,440 total land parcels in ARMM were titled (compared to 54% for the whole of the Philippines) and 94% documented by tax declaration (compared with 89% for the whole of the Philippines).

⁷³ Gulane (2013)

- a considerable proportion of competing land claims are related to historical grievances that have never been adequately addressed;
- other competing land claims are the direct consequence of contradictory decisions on land tenure or land use taken by authorities with overlapping land management mandates and roles;
- the prevalence of unresolved land claims demonstrates that past policies were often not effectively grounded in local context;
- many conflicts are based on misunderstandings over boundaries; and
- while general patterns of competing land claims can be discerned across all of the Bangsamoro – in fact all of Mindanao - the situation and dynamics tend to differ significantly from community to community.

These issues will be magnified with returning settlers and combatants to their home areas. A significant proportion of both active and latent competing land claims have potential to trigger renewed violence and/or forced displacement.

There is no “one-size-fits-all” solution to the land problems.

Further, the lack of formal data and records on land ownership and usage, the questionable legitimacy of the data that is available, the limited capacity and conflicting mandates of the land management institutions, the significant prevalence of informal markets, and the ineffectiveness of the formal justice system, makes it difficult to deal effectively with the above issues in an expeditious and equitable fashion, and to avoid being open to elite capture and to withstand the politicization of land conflicts.

A more certain climate for land tenure will be an important factor in enhancing the income and productivity of smallholders, and in their ability to access finance. Similarly, investors in large plantations will want to be assured that adequate land is available with secure tenure over the longer term.

Thailand and Malaysia offer good models in the region. Thailand, for example, has:

- a strong and unified policy and legal framework, with systematic administrative processes for registration to formalize rights;
- a sound institutional framework, with a single land administration agency for land registration, cadastral survey and mapping, and collection of land and related fees;

- streamlined procedures and reasonable transaction costs- the registration process is through a ‘one-stop-shop’;
- a strong public confidence in the land administration system; and
- high levels of participation.

The recommended actions emerging from the FEF/PCID/UP LAW workshop on Land and Property Rights in the Bangsamoro are supported by this team and are worth repeating here.

The initial task should be setting up a GIS to capture existing and new data sets on land tenure to support strategic planning by BDA. Priority should be given to obtaining data on land disputes and conflict prevalence, initially focusing on mapping those areas where the prevalence of land conflicts are perceived to be the highest and/or the risks of escalation are seen to be the greatest. This information will help focus initial efforts to understand the nature and extent of disputes, test appropriate mechanisms to resolve them, and provide the basis for selecting initial areas to pilot efforts to systematically register land rights.

An assessment of the capacity of the formal judicial and informal/traditional dispute mechanisms in key locations should be undertaken. The sensitive nature of land tenure issues in the Bangsamoro suggest that mechanisms that would provide parties with incentives for mediation would be preferable over mechanisms focused on adjudication. However, these mechanisms should provide for sustainable settlements, framing jurisdictions acceptable to the law community and Islam.

Pending the outcome of this assessment, there is scope for capacity building for those engaged in mediation through professional training and information sharing between the different actors involved, particularly in areas with a high number of land disputes and/or high conflict potential.

Potential areas for commercial plantations should be documented. This would include assessing the availability of land and willingness of smallholders to participate in plantation ventures. A key factor would be identifying development-oriented *datus* who could assist in the mobilization of land holdings and labor, and in maintaining law and order. In parallel, alternative “models” for plantation development could be explored (see later section on inclusive plantation models) which focus on differing arrangements for land tenure and the involvement of smallholders.

Over the *medium term*, the following actions are recommended.

A land policy for the Bangsamoro should be formulated, taking cognizance of the relevant national laws and regulations, the outcomes of assessments and surveys indicated above, and

the flexibility that the Bangsamoro Government will have in devising its own laws and regulations. The land policy would provide the basis for the legislative agenda of the Bangsamoro Government on land tenure, and ensure that:

- appropriate account has been taken of other relevant laws dealing with past land and with environmental and cultural concerns at the local level;
- a broad consensus is built amongst stakeholders to ensure smooth implementation of the land use policy and avoid new tensions and conflict; and
- the actual capacity of institutions on the ground is integrated in the development of the policies from the start, to ensure that only provisions that can be implemented are adopted – temporary measures can be adopted until institutions are equipped to implement more ambitious policies.

The policy should also ensure that Indigenous People's rights are promoted and protected.

The land policy would need to be underpinned by a realistic assessment of alternative tenurial rights that would be appropriate for the Bangsamoro. This assessment would take into account the traditional value of stewardship and communal ownership, but would have to recognize the extent to which private titles are part and parcel of present day realities.

The solutions to land conflicts will involve recognition of past land injustices, and this may require strong political will coupled with financial resources for compensation of victims of these injustices.

The legislative and administrative scope for establishing a single land administration agency in the Bangsamoro should be given serious consideration. An alternative land transfer and transaction system could be adopted placing greater reliance on administrative approaches. The installation of its own professional bureaucracy for land administration with streamlined procedures, realistic compensation scale, and checks to minimize corruption and influence peddling makes a lot of sense.

Within this context, steps should be taken to develop and test a streamlined process to systematically register rights in land with appropriate safeguards to ensure that the poor and less educated people have their rights protected.

The design and implementation of robust community programs aimed at trust building and the reinforcement of local government through improved basic service delivery could have considerable value.

Small grants programs that support participatory decision-making within communities and provide incentives for local authorities to improve basic services have proved to be of

considerable value in peace building in transitional contexts in other countries. It would be worthwhile exploring their relevance to the Bangsamoro.

Policies on Context-Specific Farm-Size

Globalization or even regional economic integration - such as the forthcoming ASEAN integration - is both an opportunity and threat to Bangsamoro agriculture. Opening up borders opens up new markets, but it also opens up competition to locally-produced goods from imports. In this respect, the smallholder farmers of the Bangsamoro – with an average farm size of 2.1 hectares – are at a distinct disadvantage.

Size is a factor, and land consolidation – whether through leasing, cooperative, contract growing or other arrangements – should form part of the agricultural development policy arsenal of the Government. In this respect, the successful poverty alleviating land consolidation programs in Malaysia and Indonesia offer valuable insights.

Land consolidation should be promoted when it offers a clear and feasible alternative to increase the income of the smallholders above the poverty threshold, as well as a viable exit from low productivity subsistence farming.

Yet, a balance needs to be found between large scale private and/or government sponsored plantations of different models and independent or cooperative smallholders.

Programs for economic growth in nonfarm sectors and large-scale exit from agriculture should be implemented as well so that the opportunity to increase farm size for those who will stay in farming will be fostered.

Land policies should be drawn that enable efficient smallholders to expand their operations by acquiring or renting land from less efficient neighbours who find other employment.

Policies On Productive Social Safety Nets⁷⁴

Due to dislocation and impairment caused by the conflict, many smallholders will not be able to survive or transform themselves into profitable businesses in the agricultural sector. These farmers will need humanitarian assistance in the short run and viable exit strategies in the long run.

On the other hand, many smallholders have the potential to become profitable businesses with the support of targeted productive social-protection policies that offer opportunities for them to escape poverty, diversify their outputs, and cushion livelihood shocks.

Potentially profitable smallholders can benefit from the coupling of productivity-enhancing tools with social safety net support. This linkage could help smallholders augment their

⁷⁴ Insights drawn from *FROM SUBSISTENCE TO PROFIT: Transforming Smallholder Farms*, published by IFPRI

incomes and deal with shocks while they acquire the skills to undertake more productive activities.

To enhance productivity, social protection initiatives could promote vocational training and other education schemes tailored to the technical needs of smallholder farmers, backed by research and extension systems that promote smallholder-friendly and smallholder-accessible technologies. At the same time, such interventions could be used to help smallholders without profit potential to increase their access to nutritious foods in the short term and acquire nonfarm skills and employment in the long term.

Policies On Risk Mitigation

Bangsamoro farmers, particularly smallholders, urgently need better access to risk-management tools and strategies to increase their resilience to the myriad of shocks they face, including price, weather, and even possible resurgence of conflict. Such tools offer farmers added incentives to take productivity-enhancing risks, such as adopting new technologies and switching to high-value crops.

Insurance tools should be designed and implemented that could potentially help farmers manage risks, ranging from basic weather and agricultural insurance to the more sophisticated hedging options such as futures contracts and loan-guarantee funds.

To make insurance more affordable, “aggregators”—such as farmers’ organizations, financial service providers, and input suppliers—could provide insurance and financial products as part of input contracts and vertical coordination mechanisms to help smallholders both manage risks and meet the demands of modern supply chains.

Policies should be formulated and enforced that promote climate change mitigation and to help smallholders manage risks while improving productivity. Investments in mitigation would include helping farmers to improve their energy efficiency and to manage their land in ways that increase carbon storage.

At the same time, it is important to create policy incentives for smallholders to invest in mitigation and adaptation because many of the inputs and technologies required for low-carbon agricultural practices result in higher production costs. Brazil’s Low-Carbon Agriculture Program, for example, provides financial incentives to encourage farmers to adopt crop and soil management activities that neutralize or minimize on-farm greenhouse gas emissions, including no-till farming, planting of commercial forests, and integrated crop-livestock-forestry systems.

Policies That Promote Pro-Smallholder Value Chains

Linking smallholders to commodity value chains is an important component of building smallholder resistance to shocks and improving their productivity and livelihoods. However, many smallholders in post conflict economies are unable to participate actively in value chains

because they cannot meet increasingly specific and strict quality standards, high volume requirements, and logistics specifications.

For obvious reasons, companies tend to contract with larger farmers first and prefer farmers with certain nonland assets, such as irrigation or access to paved roads. These preferences act as barriers to significant smallholder participation in domestic and international markets. Overcoming these barriers requires institutional innovations for vertical and horizontal coordination among smallholders, including group lending, rural marketing cooperatives, and producer associations. These mechanisms will provide smallholder farmers with reduced transaction costs, improved access to market information, and increased bargaining power in the prices of inputs and outputs.

However, such coordination mechanisms require strong institutional capacity and the active promotion of smallholder participation—not just membership—within these organizations to gain the maximum benefit for smallholders.

Similarly, information and communication technologies (ICTs) can offer smallholder farmers a wealth of opportunities to acquire real-time market information—on, for example, prices, demand, quality standards, and weather. With this information, farmers can make better-informed production and marketing decisions and participate more actively in value chains.

Policies That Ensure Smallholder-Friendly Financing And Investment

Moving from subsistence to more commercially-oriented activities requires increased capital and investment flows that focus on stand alone smallholder farmers and their specific constraints and needs during times of both price stability and volatility.

Increasing capital flows toward rural areas requires innovation in the channels and instruments through which financial services are offered to smallholders.

The potential for novel approaches is wide and includes value-chain finance, rural leasing, loan-guarantee funds, and ethical and Islamic banking. When it comes to stand alone smallholders, however, more research is needed to explore the viability and benefits of these innovative services before they can be scaled up. For example, loan-guarantee funds under the Innovative Financing Program of the Alliance for a Green Revolution in Africa (AGRA) have been used to leverage much larger loans from commercial banks and have lowered interest rates for smallholders, but questions remain about whether this program has actually reached new customers who previously were unable to access such loans.

The focus of financing efforts should also be shifted toward more medium- and long-term financing mechanisms to support commercially-oriented capital investments by smallholders, such as machinery and storage facilities, which are critical for increasing productivity and modernizing smallholder agriculture.

Public and private investments in agriculture-based economies like that of Bangsamoro should focus on reducing food loss along entire supply chains, from the development of crop varieties with better post-harvest traits to better storage equipment and facilities that have low initial and recurring costs. Extension services should help smallholders build their post-harvest crop management skills and maximize the benefits of post-harvest technologies.

Areas that are worth exploring and test-piloting include the provision of long-term loans through producer organizations, development of financial leasing schemes, and the expansion of accepted collateral through the introduction of movable asset registries.

Above all, a vibrant rural financial system is needed that includes a diverse mix of financial institutions and networks that work together to support innovation and rural access among smallholders.

Public investments should be directed toward providing essential public goods that have the highest economic and social returns, including rural infrastructure (especially rural roads) and agricultural research and development. National research systems need to prioritize the development of location-specific and smallholder-friendly technological innovations across the whole agricultural value chain.

A sound legal and regulatory environment is needed to maximize the private sector's contribution to smallholder productivity and to protect the property rights of smallholders and their surrounding natural resources. In conjunction, more research is needed to define appropriate instruments and strategies for integrating public-private partnerships and foreign direct investment into local economies.

For example, regional and local governments could work with private businesses (foreign and domestic) to design and provide supportive services, including technological and organizational support, to smallholder farmers who serve as their suppliers.

Policies That Will Integrate Bangsamoro Local Agricultural Industry Into The Global Islamic Financing and Banking and Halal Industries

The opportunities for the development of Halal industries and Islamic banking and finance in the Bangsamoro are the subjects of separate reports. Suffice to say here, is that the production of Halal compliant agricultural products for both the local and overseas markets offers considerable profitable opportunities, particularly at the cooperative smallholder farmer level. Taking advantage of these opportunities will require a concerted effort by the Government to make these opportunities known to the smallholder farmers, and to ensure that the appropriate technologies and marketing support are available and accessible.

Similarly, the availability of Islamic finance – particularly microfinance – will be a boon to the smallholder farmers. Ensuring that smallholder farmers can readily access this finance will be a challenge.

Policies that Promote Inclusive Plantation Partnership Models

As indicated earlier, there are various models for plantation partnerships between local communities and the private sector and/or government. The authorities should be fairly flexible in the models for these ventures, which would be driven by the nature of the crops, their location, the amount of land needed to make the operations viable, the land aspirations and cultural norms of the local population, and the way land access can be readily obtained and security assured. Aside from suitability of land and access, the ability to mobilize the required landholdings and assure security of assets and personnel will be the principal factors in determining the most appropriate locations for these projects.

The local communities also need to be fully supportive of any venture, and must be actively engaged in determining the most suitable partnership model. Policies and guidelines should ensure *free and informed consent* by the smallholders. Smallholders should be fully aware as to the extent they could participate in decision making, the benefits that they would enjoy, and the risks that they would face along with the risk mitigation proposed. The bargaining power of smallholders for benefits would depend on the value of tangible and intangible assets they contribute to the venture – typically, the smallholders can only offer land and labor while the private sector partner would have financial, technology and market resources as bargaining chips. Often, the Government or international finance community (e.g. World Bank) can step in and provide equity, infrastructure, and other support which would serve to improve the bargaining power of the smallholders.

From the perspective of the private investor, their risks are high, and they will want to be assured that security can be maintained, land tenure can be secured, and there is an effective and trusting interface with the local community. Critical infrastructures will also need to be in place.

The Table below indicates some of the principal business models which could be considered for commercial plantation ventures which are private sector and state led.

Table 6. Types of Agri-Ventures

Type	Brief Description	Sources of Benefits for the smallholders	Main basis of decision to participate
Private Sector Led			
Leasehold	The land of the smallholders is rented to the agribusiness firms	Land Rental Fee + employment	Recommended only when small land owners need to raise capital for other projects. That's if agri-business firms are willing to pay in advance for the land rent for say, 5 years.
Farm management contract	The agri-business firm develops the farms into commercial plantations and manages the production and marketing of the outputs. Decision making power is in the agri-business firm.	Employment and profit share and based on the productivity of the specific farms.	If the smallholder has no capacities in the financing, production and marketing, and it is obvious that the alternative offers better income than managing their own farms.
Out-growership	Production is in the hands of the smallholders and market is assured thru a supply-purchase agreement between the smallholder producers and agribusiness firms.	Profit from production/self-employment	If the smallholders production capacity is at hand or will be developed by the partner agri-business firms. And prices of produce are rationalized to benefit both parties.
Joint Venture	Similar to Farm Management Contract but farmers forms a cooperative that becomes the second party of the agreement. Decision making power is shared by both parties. Business can be expanded with outgrowership with farmers who are not part of the joint venture.	Profit share and Employment.	Same as above.
Nucleus-Outgrowership	An agri-business firm builds a nucleus estate by consolidating the	Employment and Profit sharing for nucleus participants.	Same as above.

		land of smallholders either thru leasehold or joint venture agreement, as its primary production base. Then the production base is expanded thru outgrowership agreement with independent smallholders.	Technology, agri-input and market support for outgrowers.	
Build Operate Transfer		Agri-business firms develop and operate the plantation for a specified period of time then transfer the invested assets to the smallholders for self management.	Employment in the early phase and profit after transfer	Same as above
State-led				
Nucleus approach: Consolidation and Rehabilitation	Estate Land and	FELCRA MODEL: FELCRA's mandate: (1) rehabilitate and develop fragmented land holdings plus other areas; (2) develop such holdings into efficient production units; and (3) advise and assist landholders after rehabilitation to ensure efficient agriculture practices. The smallholder agrees to a long-term usufruct arrangement. FELCRA employed three profit schemes: (1) landowners have the right to revenues to their land size; (2) 80 percent of the revenues go to the participants; and 20 percent for loan repayment; and (3) all participants as shareholders are	Employment Dividend share	State takes the lead when private sector are not keen to investing in these areas and smallholders have less capacity to make their farms competitive.

	entitled to profit sharing.		
Integrated Area Development Model	The state consolidates fragmented smallholder farms or utilizes huge public land for resettlement and transforms the consolidated estate into a fully functioning community with a core agri-industrial enterprise and social infrastructures like schools, cultural, religious and recreation centers.	Employment and Income shares.	Same as above.

Policies that Promote Participation of Local Businesses in Agri-Business Ventures

The zonal road maps drawn up at the local and sub-regional levels should identify potential business opportunities for post-harvest facilities and further processing. These opportunities should be drawn to the attention of the local business community and other potential investors for their assessment.

Any potential investor will assess the viability of the project from a commercial viewpoint, factoring in the risks associated with, for example, security, the sourcing and transport of supplies of appropriate standards, and market access.

The regional and local governments should take all steps within their power to reduce the barriers to private investment not only for the large scale plantation ventures, but also for the smaller scale projects emanating from the zonal road maps. Ensuring law and order and dealing with critical infrastructure bottlenecks stand out as key factors deterring private investment, but so too are the barriers created by complex business and labor regulations, difficulties in settling disputes and accessing finance.

Although it is beyond the scope of this report to review the steps which could be taken to improve the investment climate for private investment, there are steps which can readily be taken at the regional and local level to make it much easier to do business, such as simplifying business and labor regulations and putting in place mechanisms to settle local disputes. The potential business opportunities emerging from the zonal road maps could also be listed with the RBOI thus enabling potential investors to enjoy taxation and other relevant incentives. Any

infrastructure shortcomings isolated in the zonal road maps could be drawn to the attention of local, regional and/or national authorities.

It is acknowledged that local entrepreneurs are key ingredients to sustainable business with their knowledge on local conditions, social capital and other assets that are important in building social trust in a fragile post conflict scenario. However, many are lacking the capital, technical, market and managerial expertise to effectively exploit the business opportunities. These gaps need to be bridged, principally by fostering an outsourcing environment for them to acquire the needed competencies through appropriate joint venture arrangements.

4.3. Phase III: Investment Phase

Stage 6: Project Identification and Feasibility Study Preparation

Guided by the strategic roadmap, development plans and land use zonification, projects should be identified and described by a brief concept note and project description that sets out the project in as much detail as possible, and be screened on the basis of viability, effectiveness, relevance, efficiency and sustainability.

Projects that pass the initial screening process and require *public funding* should undergo a feasibility assessment by competent professionals and service providers. The cost of the feasibility study should be incorporated into the project cost, and should be bridge funded by the government for smallholder projects and state-led integrated area development projects.

For potential *private sector projects* – large or small - the identified projects would be brought to the attention of potential private investors who would undertake their own feasibility assessment. For those listed with the RBOI, additional assessments may be required.

Care has to be taken not to be over-bureaucratic in the processes where the private sector will be the key driver in the development process.

Stage 7: Investment Commitment and Arrangement Setting

For public investments, apart from budget allocations, the following government institutions could be tapped: Land Bank of the Philippines, Philippine Crop Insurance Corporation, Guarantee Fund For Small and Medium Enterprises, Quedan and Rural Credit Guarantee Corporation, Development Bank of the Philippines, among others. International financial institutions and bilateral donors would also be potential funding sources.

The Bangsamoro government should likewise tap the resources of the the global Islamic finance and banking industry. It is hoped that a local Islamic banking and finance sector will emerge, which could play an important role in financing the agro-based industry in the Bangsamoro over the medium to longer term.

4.4. Phase IV: Project Operations Phase

Stage 8: Capacity Building for Agri-Entrepreneurship

A capacity building program for agri-entrepreneurship should be implemented by the regional and local governments, with support from the private sector and civil society organizations. Capacity building can be in the form of agro-enterprise management trainings or, when deemed necessary, deployment of embedded personnel to temporarily perform management functions through the understudy method.

The initial but critical output of capacity building interventions is the formulation of a business plan for each project, which in itself a mini roadmap and guide posts for successful project implementation. Based on the business plan, a project implementation manual should be formulated that will define the details of work processes, policies and procedures, as well as the set of rules that will govern the operations of the project.

Stage 9: Monitoring

Another important matter in project implementation is to establish the benchmark for *public project performance monitoring*. Underlying the performance monitoring is an early warning system – or the ability to detect at the earliest possible time indicators that the plans are not producing results as expected. Information technologies should be developed to enable stakeholders both from the operations to the strategic management levels of the project organization to detect non-performing or ineffective activities close to real time. This will require the development of Project Management Information System with application modules that among others:

- Establish the database of project stakeholders in the various levels of the value chain.
- Establish the database of work breakdown structure as defined in the project log-frame that forms the kernel of project performance monitoring.
- Capture, record and track the performance of project implementers: farm, enterprise and project level.
- Generate detailed and consolidated reports close to real time.
- Detect deficiencies (quantitative only) in project deliverables vis-à-vis predetermined benchmarks in a given time frame (week, month quarter, year).
- Operate using a cloud-based platform that allows data entry and report viewing anywhere there is Internet and automatically updates reports at point of data entry.

4.5. Phase V: Sustaining Phase

Stage 10: Evaluation

The strengths or shortcomings in reaching the goals and objectives of every project have to be evaluated in order to identify emergent strategies for the project to move forward.

The following points should be addressed in the evaluation process:

- Background of the project
- Objectives of the project
- Perceived advantages of agri-venture arrangement selected
- Project effectiveness in terms of attaining the objectives
- Project relevance in terms of lessening poverty
- Project impact in terms of changing the lives of people and the community
- Project efficiency and economy of scale
- Project inclusivity in terms of how the roles of stakeholders are performed in terms of participation in decision making, benefit sharing and risk taking
- Project sustainability in terms of potentials for continuity and self-reliance
- Project replicability and expansion
- Monitoring mechanisms
- Mechanisms in dealing with problems and obstacles
- General lessons

Stage 11: Replication and Expansion

Based on the lesson learned from the evaluation process, recommendations for the future design of inclusive agricultural growth model and agri-venture arrangements can be derived. To realize it, factors for success in the implementation of existing models need to be identified. Recommendations should lead to the improvement of existing practices and, from the

experience, to the development of new theories of change that could be disseminated and contributed to the global knowledge pool of the development community.

The lessons learned and the recommendations for future improvement should be shared with other communities throughout the Bangsamoro for possible replication and expansion.

5. CRITICAL SUCCESS FACTORS

The following factors indicate the success of the overall program:

- Enhancement of frontline productivity through a more diversified, financially sustainable, and market-oriented extension system, and better coordinated local institutions (extension, cooperatives, traders, research, etc.) with coherent sets of interventions.
- Improvement of industry structure to build strong public and private actors in priority value chains – the formation of joint public/private development programs should be supported through targeted incentives and appropriate regulatory frameworks. The public sector should prioritize its role as catalyst and regulator, and undertake implementation strategically, seeking to drive activities that build self-sustaining momentum and foster growth of sizeable local private sector players in key value chains.
- Adoption of a sustainable approach to preserving and expanding cultivated land by increasing yields through an integrated soil fertility management approach, and exploring land expansion systematically by developing national and regional land-use strategies that consider farming models that balance economics, sustainability, and social impact.
- Put the enabling environment in place to support the growth potential of Bangsamoro agriculture. The priority areas to address are: access to financing for actors along the entire value chain (including rural financial inclusion); the necessary infrastructure to give producers access to markets; innovative use of information and communication technology (e.g., radio broadcasts to support extension advice); and building the human capacity of the public sector.

6. MONITORING FRAMEWORK

Table 7 provides for the indicative general framework for monitoring the Bangsamoro Inclusive Agricultural Development Program. This include the critical outcomes, the corresponding key activities and the short term, medium term and long term output indicators that will serve as assessment considerations in monitoring the progress and success of the program.

Table 7. Monitoring Framework

Prime Directive				
<i>To improve the quality of life and increase the income of the Bangsamoro smallholder sectors through inclusive growth.</i>				
Key Outcomes	Key Activities	Short term Output Indicators (Transition Period)	Intermediate Output Indicators (Year 1-5)	Long terms Output Indicators (Year 6-10)
Awareness and Organization Building				
Organized farmers and their support organizations are fully aware of the Bangsamoro Agricultura Development Road Map	All farmers are organized into production clusters and clusters into community cooperative and federated in the municipal level with the vision of the roadmap as the basis of unity	The outcome has been attained in 1 pilot municipality for each of the 5 provinces	The outcome has been attained in 50% of municipalities	The outcome has been attained in 100% of municipalities.
Organized farmers are pursuing one of the three strategic approaches to agricultural growth	Presence of working models of the three strategic approaches	The outcome has been attained in 1 pilot municipality for each of the 5 provinces	The outcome has been attained in 50% of municipalities	The outcome has been attained in 100% of municipalities.
Technical working groups in various levels are operational providing strategic guidance.	Technical Working Group have crafted the inclusive agricultural development plan	The outcome has been attained in 1 pilot municipality for each of the 5 provinces	The outcome has been attained in 50% of municipalities	The outcome has been attained in 100% of municipalities.
Resource Mobilization				
Resources have been made available to fund agricultural projects	Investment plans have been drawn and committed funding had been identified	The outcome has been attained in 1 pilot municipality for each of the 5 provinces	The outcome has been attained in 50% of municipalities	The outcome has been attained in 100% of municipalities.
Islamic Banking and Finance had gain entry into Bangsamoro	An apex Islamic bank with retail financing institutions are established and networked	An Islamic Oriented Micro-finance in a pilot municipality for each province	The outcome has been attained in 50% of municipalities	The outcome has been attained in 100% of municipalities.
Technology Development and Deployment				
Extension and technical support system are present to support agricultural schemes	Convergence of line agencies and CSOs are providing support to the three models	The outcome has been attained in 1 pilot municipality for each of the 5 provinces	The outcome has been attained in 50% of municipalities	The outcome has been attained in 100% of municipalities.
Halal and other product standards have been introduced in production processes and agri-commodities gain entry into the local and global market	Presence of Halal compliance infrastructures are in place in the municipal level	The outcome has been attained in 1 pilot municipality for each of the 5 provinces	The outcome has been attained in 50% of municipalities	The outcome has been attained in 100% of municipalities.

**ANNEX 1: SAMPLE TEMPLATE OF INCLUSIVE AGRICULTURAL DEVELOPMENT PLAN FOR BANGSAMORO
SMALLHOLDER AGRICULTURE (BMSA) IN THE LOCAL LEVEL**

THE PRIME DIRECTIVE

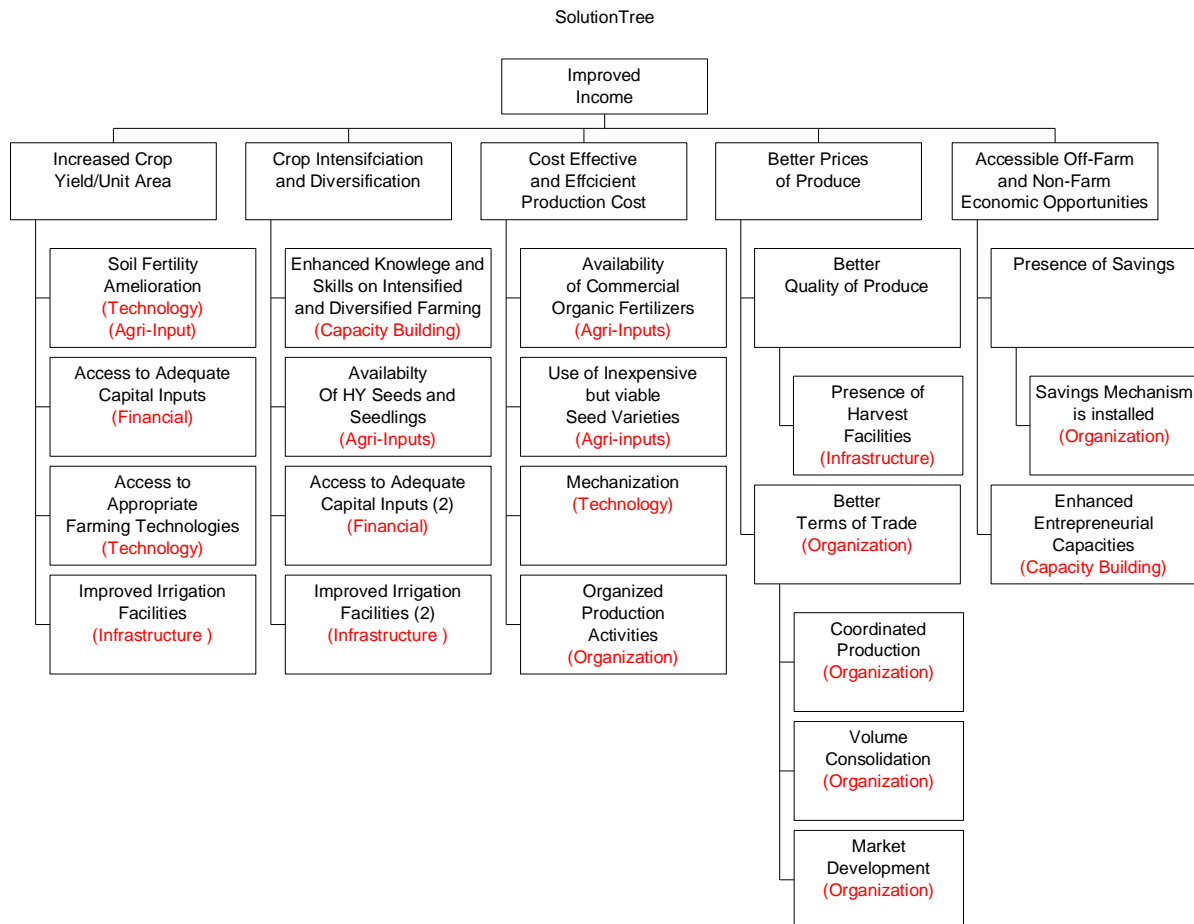
The prime directive of BMSA is **to increase the income and purchasing power of the farming households**. The main success indicator of this objective is to increase the disposable income of the farming households to a minimum average of PhP8,000 a month or PhP96,000 a year.

KEY RESULTS AREAS

The Key Results Areas that shall be attained as a measure to attain the objectives are the following:

- Increase of crop yield per unit area cultivated by the farming households.
- Crop diversification and intensification.
- Cost effective production practices and technologies.
- Favorable terms of trade rationalized prices of produce.
- Access to non-farm and off farm income opportunities.

Figure 16. Solution Tree



MAIN STRATEGIES

The attainment of the above objective and results shall be attained with the following major strategies:

Cooperation and Entrepreneurship as an Organizational Approach to Agricultural Development

This entails the grouping of 10 farmers into production clusters, the basic unit of BMSA.

The cluster shall serve as the vehicle for:

- Production credit delivery.
- Farm diversification and crop intensification.
- Farming technologies generation and promotion.
- Farm mechanization.
- Coordinated production planning and management.
- Collective risk management.
- Local savings mobilization.
- Social marketing of BMSA and the Bangsamoro Vision.

Creation of Favorable Policy Environment for Effective Governance

This deals with reengineering and mobilization of the local government bureaucracy so that all the agencies converges to directly contribute to the implementation of BMSA.

- Definition of the clear roles of various LGU agencies in the local agricultural development.
- Coordinating mechanisms between agencies.
- Division of the agricultural areas into Production Management Zones.
- Interfacing and capacitating existing structures.
- Harnessing of support to the basic productivity unit.

- The Agricultural Development Information System.
- Capacity building program for BMSA managing and implementing teams.

Creation of Favorable Financial Environment for Agricultural Development

This deals with provision and intermediation of financial support to the production clusters as well as farmers participation in the long-term capital development for BMSA leading to local self-reliance through the creation of partnerships with private, micro, and SME's investors, particularly through the Bangsamoro Agri Venture Fund (as the mechanism) to be managed by the state owned/led Bangsamoro Agricultural Development Corporation (BDC) (as the corporate vehicle).

The capital development framework espoused by BMSA will undergo several phases:

Phase 1: Creation of Disposable Income

This is entry point of all development interventions spelled by the Program. As mentioned earlier, the directive of BMSA is to increase the disposable income of farmers to at least PhP8,000 a month.

Phase 2: Savings Mobilization

Disposable income (residual income after the cost of production and meeting family needs enough to have a decent living) is a necessary condition to create savings in the personal level. To ensure this, savings will be mobilized and accumulated through conditions attached to the assistance provided to the farmers by the city and other entities.

Phase 3: Pump-priming

Accumulated Savings will be matched by funds from LGU, banks, and Private Investors to finance production expansion of the clusters or anchor enterprises and the auxiliary enterprises either in the form of loan or equity participation.

Phase 4: Divestment Phase

In the case of equity participation, LGU will divest its shares in favor of the people's organizations or cooperatives when these are already equipped to operate successfully the enterprise.

Creation of Favorable Agri-Technological Environment

This provides for a dynamic technology research and development and extension system with participation of the farmers themselves, academe, and various agencies.

Engender Favorable Terms of Trade and Cooperative Risk Management

This deals with the development of a comprehensive but doable integrated marketing plan for BMSA assisted cooperatives. A crop and price insurance system will be put in place to mitigate fluctuation of prices and natural disasters that could affect productivity.

Engender more job creation: from agriculture to industrialization (light industry)

This is about the creation of cooperative enterprises that facilitate backward and forward economic linkages anchored on agriculture to create non-farm and off-farm economic opportunities to both the rural and urban sectors.

RELATIONSHIP OF STRATEGIES TO KEY RESULTS AREAS

The table below summarizes and illustrates how the strategies relate to the desired results of BMSA:

Table 8. BSMA: Development Processes/Impact

KEY DEVELOPMENT PROCESSES	IMPACT TO				
	Yield Increase	Cost Reduction	Prodn Expansion	Better Prices	Non-Farm Income
1 Creation of Favorable Technological Environment					
a. Soil Fertility Amelioration					
b. Improved Crop and Agronomic Management					
c. Mechanization					
2 Creation of Favorable Financial Environment					
a. Farmers' access to production financing.					
b. Presence of Community Savings for Investments to agri-production					
3 Steady Supply of Required Agri-Inputs					
a. Organic Fertilizers					
b. Quality Seed/Livestock stock					
c. Chemicals and Substitutes					
4 Provision of adequate Infrastructure Support					
a. Irrigation					
b. Farm to Market Road					
c. Post harvest Facilities					
5 Capacity Building					
a. KSA on Sustainable Agriculture and Diversified Farming					
b. Enhance entrepreneurial skills					
1. Farm Planning and Budgeting					
2. Investment Decisions					
6 Organization					
a. Organized and Coordinated Production					
b. Volume Purchase of Agri-inputs					
c. Better Terms of Trade					
d. Volume consolidation of Produce					
e. Savings Mobilization					

ANNEX 2: POSSIBLE AGRI-BUSINESS ENTERPRISES WITH INCLUSIVE MODELS

BANGSAMORO SMALLHOLDER COMMERCIALISATION PROJECT (BASCO)

Project Summary

BASCO shall be a market-based extension, trading, processing program that aims to boost the incomes of at least 5,000 smallholder farmers in selected communities of the BCT while introducing sustainable farming practices. The farmers will have a substantial ownership stake in BASCO, which means they also share in the benefits of processing and marketing. The initial focus is on cereals, like rice and corn, and higher value crops such as cassava, sorghum, and soya beans.

BASCO will engage farmers who will be grouped into farmer clusters of 10 to 15 farmers, all pre-screened, and with individual land holdings of up to two hectares. BASCO will provide a 'full service package' to farmer clubs of extension advice and agricultural inputs through an Islamic micro-finance scheme. There are good opportunities to introduce mobile cash payments and micro-insurance products.

Development Benefits

By boosting yields and maintaining fixed inputs costs, the BASCO managed program offers incremental incomes of per year to the participating smallholder farmers.

BASCO will provide a guaranteed market for increased smallholder production of cereals and staples by establishing links to major buyers such as the World Food Program. The BASCO program will create 50 permanent jobs (mainly extension officers) and also generate consequent environmental benefits with the introduction of conservation farming techniques.

Financial and Investment Information

BASCO will require initial funding of around PhP 50 Million to establish further demonstration plots and build its core infrastructure. The core infrastructure will allow it to service up to 5,000 farmers with only limited additional expenditures.

BANGSAMORO RICE NUCLEUS-ESTATE MODEL (BRINE MODEL)

Project Summary

Patterned from the BAMBOI model in Ghana, Africa, BRINE is a 2,000-hectare net irrigated area farm to be developed and operated as a multi-stakeholder Public Private Partnership (PPP) for the production of high quality rice under irrigation. The farm will be shared between a nucleus commercial farm operator (1000 hectares) and up to 500 smaller sized farmers (average of two hectares each), who will all participate in irrigated mechanized rice production under a commercial double cropping regimen that is expected to yield competitive yields and profitability levels. The farm includes onsite storage and an oversize rice mill and drying plant with excess capacity for the benefit of nearby (non-scheme) farmers.

The key innovation is a PPP structure that combines a 1000-hectare nucleus farm with another 1000 smallholder out-growers. A one-time investment of public funds into infrastructure (e.g. irrigation) will attract private investment into profitable farming by lowering barriers to entry.

The land needed by nucleus farm will be pooled from farmers who will benefit from the following incentives:

A guaranteed net income equivalent to PhP60,000/ha/year, which is the average normal income.

Dividend share income from the profit of the Nucleus firm with sources coming from the following value addition:

- Increase in yield due to technology and efficient use of agri-inputs and minimization of post-harvest losses (drying plant) and improved irrigation system.
- Increase in prices of rice due to improved quality (state of the art rice mill, drying plant with parboling effect).
- Added profit due to cost minimization due to mechanization in land preparation, inbound and outbound logistics.
- Profit from the provision of logistics, inputs and market services to non-scheme out-growers.
- Bio mass power plant that also functions as fertilizer plant with the rice straw and rice hull as its feedstock. This will decrease milling cost and create new revenue stream if the excess energy is sold to the grid. An Irish biomass energy-based technology provider can be tapped for this purpose.

The nucleus farm will finance and operate most of the mechanization, processing and storage, as well as the supply chain and market linkages necessary for farmers to compete profitably, while also carrying the bulk of the cost of irrigation through the scale economies that make unit costs affordable for all farmers. The start-up capital financing for upfront infrastructure that makes the remaining project viable

for commercial investment is provided by the public sector. This allows it to set the rules of the game, i.e. private sector companies wishing to benefit from this infrastructure must agree to provide a complete portfolio of agreed goods and services to surrounding farmers at fair prices.

This PPP structure provides a private sector-led solution to a key development challenge; providing rural farmers long-term access to the holistic portfolio of goods and services, and market access, required for real income transformation in a way that is sustainable, i.e. commercially viable without requiring on-going subsidy. This is a critical test for an effective poverty reduction strategy.

At the heart of the nucleus estate is the BRINE integrated rice processing center with state of the art grain drying plant and rice mill which is estimated to cost US\$1.6 million to develop and operationalize. Brine will directly incorporate about 500 local farmers into modern irrigated production and indirectly incorporate another 500 farmers through the outgrowership program.

Development Benefits

The BRINE scheme directly benefits the 500 small and medium sized farmers who, as part of the scheme, gain affordable access to irrigation, as well as the entire suite of goods and services (improved and locally appropriate inputs, extension, mechanization, processing and storage) they need to improve yields and profitability resulting in sustainable income increases of 100-200%. Furthermore, the introduction of a scale commercial farming hub in an underdeveloped region will improve the availability of such critical goods and services for up to 5,000 local farmers within a 25 km radius improving their incomes 50% on average. Lastly, by increasing the production of a high value food import, the business improves food security, substitutes for imports and improves Bangsamoro's and Philippines' balance of trade.

Financial and Investment Information

Total cost to develop and operationalize the scheme will need to be financed publicly in project development costs for irrigation, infrastructure, and project awareness and promotion. This could catalyze an additional of PhP400 Million investment from, say, an Islamic finance institution to finance the storage, mill and farm equipment etc. At steady state, BRINE will produce 13,000 metric tons of milled rice annually.

BANGSAMORO ECO ORGANIC SUGAR NUCLEUS ESTATE (BAECON)

Project Summary

Based on the Mozambique model, the project is a commercial farm hub and out-grower project that will produce and process organic muskovado sugar for export. There will be a planned development of 2,000 hectares of organic irrigated sugar cane, projected to be out-grower production. The project will be linked to a ranch where on 400 hectares of pasture, up to 4,000 head of cattle will be raised under an intensive feedlot type program for the production of beef as well as cattle manure to be used as organic

compost in the sugar cane production process. The organic cycle is completed as sugar cane residue and molasses are to be used in the feedlot process.

Development Benefits

The number of local people employed on the farm is expected to reach 1,600 when the farm reaches its full production. Organic sugar production is very labor intensive when compared to production from non-organic plantations. The project will create between 6-8 new jobs per hectare in the core plantation and in the processing plants (muskuvado sugar processing plant, bio-energy plant cum fertilizer plant) and cattle ranch. Accordingly, up to 6,000 family members may benefit from the direct employment with the regional economic multiplier effect.

Assuming the average out-grower farm sizes is 2 hectares, then there will be 1000 out-grower farmers, with annual income of up to PhP300,000 per family if they commit to doing their own harvesting and maintenance on the sugar cane plots.

Financial And Investment Information

The estimated total projected project costs amount to PhP200 Million including PhP50 Million of development costs. An off-take agreement with organic and halal food manufacturers will be negotiated guaranteeing a minimum price and operating margins.

The projected project cash flow utilizing the floor price included in the off-take contract indicates it can support debt/lease financing based on a debt service coverage ratio of approximately PhP120 Million or 60% of project cost. The remaining balance is to be financed through equity investments. Project returns may benefit further from grant financing being applied for to support the out grower's capacity building.

BANGSAMORO HALAL AGRI-GOATS OUTGROWERSHIP INDUSTRY (BHAGO)

Project Summary

BHAGO is envisioned to be a large processor and supplier of goat products. Livestock will be improved and raised on farm as well as to be distributed to and bought from local smallholder farmers for fattening in feedlots, processed on farm and be marketed to wholesalers and butcheries and exporters.

BHAGO will build a Halal compliant abattoir onsite to shorten the supply chain and reduce shipping weight. New genetic material will be introduced to strengthen the quality of both the commercial and smallholder herds through increasing the weight/return ratio per goat.

Within five years up to 4,000 smallholder farmers are expected to benefit from this program. In addition, BHAGO will lease adequate farmland to grow the crops needed to supply the growing herd and feedlot volumes.

This business is forecasted to have good commercial returns and play a major role in creating benefits all along the goat supply chain. There is potential to scale up when market opens for halal goat meat.

Development Benefits

The smallholder producers supplying BHAGO will benefit from improved market access, and greater pricing transparency, and there is greater access for the local rural community to cheaper meat by placing refrigerated containers in strategic sales centers.

BHAGO will provide feedlots and training to more smallholder producers, and the distribution of better quality rams on a rotational scheme. Jobs will be created for the collection and herding of animals, with the potential of 100 more jobs when the abattoir is built.

Financial and Investment Information

BHAGO will need a capitalization of PHP50 Million and is forecasted to generate net earnings and reach breakeven within five years, increase income by 20% per annum within 10 years, on revenues. BHAGO will be an attractive investment opportunity for an investor wishing to support the improvement of BCT's livestock sector while generating a strong return on their investment.

BANGSAMORO HALAL CHICKENS (BHC)

Project Summary

BHC is a commercial and out-grower business producing, slaughtering, processing and marketing halal certified broiler chickens. The chickens will be marketed locally through existing and new off-take agreements to meet the growing demand for certified Halal products. Production takes place in four broiler houses and through 20 contracted out-growers, and is expected to grow rapidly.

A Halal compliant abattoir will be built, including an additional cold room and blast freezer, to reduce the existing bottleneck in production. The output will be supermarket quality chicken. A feed mill will also be built in order to process maize and cassava for chicken feed, sourced from at least 70 local smallholder farmers.

Development Benefits

The commercial farm supplies day-old chicks and concentrates to out-growers on credit, as well as training and extension services. BHC will create at least 19 new permanent employment opportunities and will engage 20 chicken out-growers and at least 70 smallholder maize producers. The venture will aim to employ at least 15 women as permanent staff members and 48% of all out-growers and smallholder farmers are women.

Incremental income to employees is expected to substantially increase and the business will play an important role in the substitution of non-halal frozen chickens.

Financial And Investment Information

BHC's estimated capitalization is approximately PhP50 Million and is forecasted to generate net and the payback period is 10 years.

BANGSAMORO BANANA NUCLEUS ESTATE (BANANUE)

Project Summary

BANANUE is a joint venture between agri-firms and smallholders. It aims to stimulate the development of the banana industry in five provinces, with Sulu, Basilan, and Tawi-tawi catering to neighboring Malaysia as transshipment partner. This will offer major benefits for large numbers of local banana growers and significant job creation. BANANUE will grow, package, and market high quality bananas for export. The nucleus farm hub will also incorporate out-grower farmers in the production of irrigated bananas, tripling yields and will substantially increase their incomes. The project is highly scalable, and the 300-hectare nucleus can be expanded to out-growers as soon as market demands are present.

Development Benefits

The intention is to establish a nucleus of 300 hectares with a large out-grower program, that could increase the size of the commercial production base to a total 1,500 hectares of assured export quality banana production in each province (subject to land suitability study). Out-growers are provided with technical support, efficient access to inputs and markets, all of which will substantially increase incomes. 450 full time direct employment opportunities will be created on the nucleus commercial farm, and in the packing facility and a critical mass of export quality banana production will stimulate much wider production of export quality bananas in the area as well as the development of associated industries.

Financial And Investment Information

The initial investment requirements are PhP300 Million (PhP 1,000,000 per hectare to reach 300 hectares) and for the banana industry to reach exportable quantities within five years, an additional PhP1.2 Billion will be required to plant an additional 1,200 hectares through an out-growership program with upgraded irrigation systems/water supply and construction of a packaging facilities.

For expansion to island provinces, BANANUE will seek investors wishing to gain exposure to a business segment with high growth potential and lower logistics cost with Malaysia or Singapore as a transshipment point to the forecasted growing halal banana market in the Middle East and Europe.

ROADMAP FOR THE PROMOTION AND DEVELOPMENT OF THE HALAL FOOD INDUSTRY IN THE BANGSAMORO⁷⁵

1. BACKGROUND

Access to halal food and other consumer products has been the persistent clamor of Muslims in the Philippines and the rest of the world for many years. And now halal trade is on the rise and on the fast lane. Globalization of halal made its debut in 1997 when the Codex Alimentarius Commission - the food safety standard-setting arm of the World Health Organization (WHO) and the Food and Agriculture Organization (FAO) - promulgated guidelines (CAC/GL 24) on the use of the term “Halal” in product preparation, especially pertaining to food.

This caught the attention of the Muslim world, and the word spread around at such a fast pace that countries, Muslim and non-Muslim alike, took interest in developing their own halal programs, with the barely served but huge potential market in mind.

1.1. Years of Advocacy

Heightened understanding of halal and food safety awareness among Muslims and non-Muslims alike in the Bangsamoro and in the rest of the Philippines has been the product of 14 years of advocacy.

The advocacy to develop the halal food industry began in 2001 with the proposal of the Muslim Business Forum (MBF), based in General Santos City, for the national government to designate Mindanao as the production base for halal products. That proposal was put into a resolution - which was subsequently adopted and endorsed by the Mindanao Food Congress - to the national government in April of 2001.

Following receipt of the resolution, President Gloria M. Arroyo tasked the Office of Muslim Affairs (now the National Commission on Muslim Filipinos), the Department of Trade and Industry, the Department of Agriculture, and the Southern Philippines Development Authority (SPDA) to submit an action plan for the proposed industry.

At the national level, the draft guidelines for the Philippine National Standard on Halal Food (PNS 2067:2008) were presented before 204 members of various Ulama organizations in six area consultations, including ARMM, for scrutiny and approval. This was followed by an oversight technical review of the draft standards by the six national agencies, led by the Department of Trade and Industry, tasked to craft the halal standards. This review was further augmented by an 18-city national campaign by the Department of Trade and Industry among

⁷⁵ This report was prepared by the Foundation for Economic Freedom (FEF) for the Bangsamoro Development Agency (BDA). The basic report was prepared by Jamil Olermo.

food and catering companies to seek their views on, and support for, the halal export program which it had drawn up. This program was supposed to take off after the promulgation of the National Standards on Halal Food by the Bureau of Products Standard (BPS) in 2008.

At the regional level, a peak was also reached in the 2006 to 2010 period when the halal certification guidelines for the Autonomous Region in Muslim Mindanao (ARMM) were presented to the stakeholders of the region, and an ARMM Master Plan drawn up for Halal Industries Promotion (2009-11). Incidentally, the certification guidelines of the ARMM-based Muslim Mindanao Halal Certification Board (MMHCBi) were used as the working paper in the crafting of the National Standard on Halal Food.

Thereafter, halal has been a favourite subject in business conferences, campuses and roundtable discussions in many parts of the country, but very few concrete actions have been taken to capitalize on the programs, plans and standards.

1.2. Halal Food Industry- A Flagship Program for the Bangsamoro

The successful development of the halal food industry - should this be *re-embraced* by the new Bangsamoro Authority as its flagship economic program - hinges on a strong policy towards the development of the vastly underdeveloped agriculture sector in the Bangsamoro, given its long recognized potential.

In essence, the halal food industry is deemed to provide a *rallying point* to mobilize resources for investment, infrastructure support, capacity-building, and the introduction of better technologies for improved and efficient agricultural practices cascading all the way down to the community level, whether these involve micro, small, or medium scale farming, or the processing activities associated with food crops, livestock and poultry, aquaculture/mariculture, fruits and vegetables.

At the very heart of this halal food industry is the intensive promotion and development of halal organic farming, or agriculture as a sustainable source of food compliant to Islamic dietary code. Organic farming is recognized a fast emerging sector in agriculture, with a niche market of its own in the country and in the nearby regional and other international markets.

While this endeavour would require substantial financial resources, the identification and validation of production zones would serve as the *catalyst* for the industry build up where infrastructure support, financial resources, capacity building, and technical support will be focused for better utilization.

It is also on the understanding that the private sector would be partners in the development of the halal food industry.

And while there have been a number of laudable initiatives in the Bangsamoro region over the last decade to propel the development of its home-grown halal food industry, the industry has not taken off. Many of enabling regulatory and insitutional measures already undertaken will thus need to be reviewed and ammended, and new regulatory and institutional measures inroduced.

Overall, it will take a strong political will by the Bangsamoro Government to push the halal food industry so that it achieves its full potential.

1.3. Situationer

In a 2008 assessment paper he prepared for the CIDA-funded Local Governance Support Program in ARMM (LGSPA) on “Halal Agriculture and Food Development”, James Lowe mentioned that the “underdeveloped agriculture and food sector from production through processing and marketing, presented a weak basis and starting point for the development of a *halal*-based industry”, specifically citing the region as a net food importer while having all the potential to be self-sufficient or a net exporter of agri-products.

Among the weaknesses mentioned by Lowe and endorsed in numerous other studies are:

- poor and limited infrastructure support such as transportation, farm-to-market roads, storage, quality control measures, and other supply chain infrastructure;
- limited support and technical services to transform current farming practices to halal practices;
- weak cooperatives and farmers associations to support the *halal* value-chain; and
- the financial constraints of the concerned line agencies involved in the implementation of support programs.

Poor and vision-less governance and the” mendicancy” nature of funding support to the autonomous region have taken its toll on the overall development of the region, especially in agriculture. Bangsamoro is very much *a food importing region* as repeatedly cited in all studies since 1996, despite the region being blessed with vast and untapped fertile lands to grow food.

Currently, much of the food products consumed in the Bangsamoro are produced, processed or manufactured outside the region and woefully, haram food products, both fresh and processed, circulate freely in all areas of the Bangsamoro, even in areas bearing the name “Islamic”.

Since the halal industry initiatives have not really filtered down into the consciousness of the business people, growers, processors, food service providers, and agri-entrepreneurs on the ground, only a handful of halal food products are produced and distributed in the region.

Since halal food is generally agri-based, going halal should have a huge impact on the growth of rural enterprises that should benefit tens and thousands of rural folks. Rural-based halal enterprises would actually be the backbone of the overall halal food industry development with its wide-ranging opportunities covering livestock and poultry, marine and fishery products, and fruits and vegetables.

1.4. Organic Farming – at the Heart of Halal Agriculture and Food Development

Organic farming refers to agricultural production systems used to produce food and fiber, relying principally on developing biological diversity in the field to disrupt the habitat for pest organisms, and on the purposeful maintenance and replenishment of soil fertility.

Organic farmers are not allowed to use synthetic pesticides or fertilizers. All kinds of agricultural products are produced organically, including grains, meat, dairy, eggs, fibers such as cotton, flowers, and processed food.⁷⁶

Organically-grown food products, known for the clean and safe way they are grown and processed, are an emerging sector in agriculture with a global niche market worth over US\$40 Billion a year, led by the rapidly growing markets in the United States, Germany, Japan, and elsewhere.

The US is not only the largest market for organic products in the world, but is also a leading producer and exporter. Global production of organic crops has not kept pace with demand, with many products reporting undersupply. The Asian market is experiencing healthy growth because of increasing retail distribution and rising consumer awareness. Up to 90% of certified organic food production from countries like Indonesia, Vietnam and the Philippines is exported - largely to Europe and North America⁷⁷.

No official information is readily available on the organic food market in the Philippines. However, it is estimated that it could be currently around PhP 750 Million, and has in recent years been growing at rate of 10% to 30%, depending on product type.⁷⁸

⁷⁶ See (www.wooof.org).

⁷⁷ The World of Organic Agriculture: Statistics and Emerging Trends 2007. 9th edition

⁷⁸ This estimate is based on a projection of estimates made by Stanton, Emma & Sia (Singapore) for the Embassy of Canada in the Philippines in March 2011. They estimated the market at that time to be of the order of PhP 433 million, growing at a rate of 10% to 30%, depending on product type. According to Canono (USDA GAIN Report, 2000), the Philippines' organic market in 2000 was estimated at PhP 250 million. Of this value, domestic organic industry was about PhP 100 million while imports of organic products were estimated at PhP150 million- the same report estimated that demand for organic products would outpace local production, while potential for increased imports particularly for processed food products clearly exist.

From the standpoint of Muslim consumers, organically-grown fruits and vegetables and organically-raised animals both livestock and poultry (except those that are clearly forbidden in Islam) where organic feeds and fertilizers used are free of haram substances, are closest to the institution of Halal. It should be noted that native chicken is widely raised in the region with no broiler chicken in the production data. This is partly due to the lingering concern among consumers for growth hormonal and antibiotic residues in broiler chickens raised in large-scale commercial poultry farms, which are the mainstay poultry supply at the groceries, fast-food shops, and restaurants.

Patronage and consumption of organically-grown or prepared food products are on the rise on a widespread concern of consumers that the cumulative effect of chemical-based agricultural products is posing a serious threat to the health and well-being of the people.

The principle of halal food (*halaalan tayyiban*) states that anything being consumed or used that is harmful to the body is non-halal. Milk, for instance, which is a recommended soft food for Muslims, could be a life-threatening product. This made headlines a few years back when a milk factory in China specializing in formulated milk for infants introduced a chemical substance known as melamine in the processing of infant milk to raise its minimum protein content as required by regulatory agency. The sale and eventual consumption of this milk led to the death of several infants and created uproar on a global scale. Melamine, as it turned out, is a chemical used in the production of plastics. And more of these industrial chemicals are used in the modern day popular food products which is best described nowadays as “deliciously dangerous food”.

The enactment of the Organic Agriculture Act of 2010 (RA 10068) gave a boost to the promotion and development of organic farming in the country, and safe food at that. The key features of the law is for the government “to promote, propagate, and implement the practice of organic agriculture to increase farm productivity, reduce pollution and destruction of the environment, enrich fertility of the soil and prevent the depletion of natural resources”.⁷⁹

The law further emphasizes that the health protection of the farmers, consumers, and general public and the reduction of imported farm inputs are foremost in the minds of the framers of the law. It further states that “a community-based organic farming system for the production of pure organic fertilizer and other farm inputs shall be employed as it recognizes and supports the central role of the farmers and other stakeholders at grassroots level”.

⁷⁹ Incidentally, the Prophet of Islam has said something to that effect; *“The world is a green and pleasant thing. Allah has left you in charge of it (mustakhlifukum fiha) and looks at how you behave – as reported by Muslim.”* Pollution, the destruction of the environment, and the abuse of natural resources are dealt with strongly in the teaching of Islam with an entire chapter (Al-Khalifa) dedicated to the subject. Man in particular, as God’s steward and trustee on earth, was given the task of protecting and nourishing nature and preserving natural habitats for all living things to thrive in abundance and enjoy the bounties provided to them by the grace of the Almighty.

The law is not just a piece of forgettable legislation. The Department of Agriculture has allocated a budget of more than PhP900 Million for the promotion of organic farming in the country, and has been active in its encouragement. It is estimated that around 14,100 hectares of land was devoted to organic farming in 2010, a significant increase over the 3,500 hectares in 2004.⁸⁰ The Philippines is now a net exporter of organic foods,⁸¹ principally bananas, mangoes, coconuts, coffee and sugar cane, largely produced through grower arrangements amongst private corporations, cooperatives, and smallhold farmers.

The new Bangsamoro Authority could mainstream the national law into its own enabling law with a halal twist, say “Halal Organic Agriculture Act of 2015” and likewise provide funds in its expenditure program for the purpose.

Productivity is the key to food self-sufficiency whether it involves a thousand square meters farm lot or a much larger area. Organic farming methods are fully developed and increasingly being applied in a number of farms in the country with proven “showcases” to learn from:

- The experiences of *Kablon Farms (KF)* in Tupi, South Cotabato for its productive farmland utilization within the vast Dole Pineapple plantation was for the record. KF brands of organic passion juices, organic processed jams, food condiments, and pure table chocolates are on sale in many popular groceries in major cities in Mindanao and beyond. The 19-hectare farm is a paradise of high value crops (passion fruits, durian, cacao, etc.) where the only space unplanted with edible plants is the road within the farm.
- The *Tubaga Multi-Purpose Cooperative* operating in the Poblacion of Tupi, South Cotabato, involving 100 hectares of various sizes from 1,200 square meters to 10 hectares, is producing internationally-certified organic bananas locally known as Bongolan to an exclusive market in Japan, harvesting its produce on a weekly basis. “Bongolan” bananas are priced almost twice as much as its close “cousin” Cavendish.
- *Mt. Carmel Rural Life Center* in Bansalan, Davao del Sur, known for its multi-cropping system or diversified mixed use of small size farmlands for increased productivity and better income, has been attracting smallholder learners from all over the country.
- *Don Bosco Foundation for Sustainable Development* based in Makilala, North Cotabato, is known for its sustainable agri-programs empowering farming families from ‘seeds to shelves’, from ‘soul to soil’, and from ‘culture to nature’ as its mission statement implies.

⁸⁰ Stanton, Emms and Sia, 2011, op cit.

⁸¹ Certification of organic exports is principally provided by European certification agencies (such as Institute for Market Ecology based in Switzerland, Naturland in Germany, and Ecocert in France).

- *WWOOF Philippines*, the country network of the Worldwide Organization of Organic Farmers, has a directory of host organic farms in the country where interested individuals can undergo hands-on experience in organic farming ranging from 15 to 45 days.

La Liga, a development policy research and advocacy non-government organization, is pushing for sustainable organic and ecological agriculture in the Philippines and the production of 'healthier' food through organic farming. It is aggressively supporting the shift from chemical-intensive farming to the more environment-friendly and low-carbon food production practices in organic or natural farming, as well as organic way of life among consumers.

La Liga and the Philippine Rural Reconstruction Movement (PRRM) led a network of citizens' groups, academic institutions, local government units (LGUs) and the private sector under the banner Go Organic Philippines in implementing the Organic FIELDS Support Program (OFSP). Institutionalization and the integration of funds for organic farming in the annual investment plan of LGUs will ensure sustainability of the program in the countryside.

Unknown to many in the Bangsamoro, organic farming (or natural farming as some people refer to) has started to take its roots in some places in the region despite little information about the national law on organic agriculture reaching the grassroots. Leadership makes it happen, as in the case of North Upi with its LGU-led program in organic rice farming. And just across the plains of Maguindanao, a cooperative in the Municipality of Mamasapano is engaged in organic rice-farming and the organic growing of tomatoes and onion bulbs, with a growership arrangement with a Cotabato City-based Mall. The Municipality of Sultan Mastura is a veritable hub of organically-grown vegetables, both in the highlands and lowlands, involving no less than five cooperatives producing safe vegetable products for markets as far as Cagayan de Oro and Davao. Similarly, a cooperative in Tugaya, Lanao del Sur, is propagating organic-growing of vegetables.

Goat raising cooperatives in Datu Odin Sinsuat, North Upi, Parang, Marawi City, and Poona Bayabao in Lanao Sur, have started to tend to their halal animals using organic methods of rearing halal animals. These municipalities could serve as the nucleus of goat-raising enterprise in the Bangsamoro mainland. The goat meat market is growing rapidly.

Abalone fishing and culture are suitable in the provinces Sulu and Tawi-Tawi, where a multi-specie hatchery produces and distributes abalone seeds. A fisher group is currently engaged in abalone pen culture at Panglima Sugala in Tawi-Tawi. Abalone is a highly sought after and highly priced commodity. The island of Sibutu in Tawi-Tawi is earning the distinction of becoming the center of grouper cage culture, with the Bureau of Fisheries and Aquatic Resources (BFAR) operating one at Simunul Island, while mud crab production (fattening) is now an agri-business venture in Basilan and Parang, Maguindanao.

According to the Iloilo-based Southeast Asia Fisheries Development Centre (SEAFDEC), science-based technologies are available to fish-farmers for quality and bountiful production of marine products.

These are pockets of organic farms that can be expanded and replicated in other suitable areas in the region for increased production of organically-grown food products and improved productivity of farm lands and coastal waters. *MILF communities*, in particular, can be encouraged to engage in communal organic farming which could be transformed into estate size production bases of halal foods.

Naturally-farmed food products fetch higher price in the market, much like any other naturally-grown or processed products anywhere in the world. Bottled water has become a pricey product to consumers owing to the public confidence of it being safe and clean – the same holds true to products produced out of organic farming. Local organic produce is sold at a price premium of between 30% and 60% over prices of non-organic equivalent products, with processed food and drinks claiming even higher premiums⁸².

It is in the production of organic foods - safe food using natural methods of farming - that can serve as a novel entry point in the renewed development of the halal food industry, aimed at a niche market of healthy and safe food conscious consumers, regardless of religion or creed. Both local and export markets can be targetted.

2. STATEMENT OF ISSUES

The *basic requirements* for successful halal agro-based activities is the same as for all agro-based activities: peace and order, adequate infrastructures, land security, appropriate technology, adequate extension services, access to markets and finance, etc.

The requirements of Halal *add* another layer of specific needs. More specifically, the growth and development of the Halal food industry is also affected by:⁸³

- lack of awareness and appreciation of the importance of halal certification;
- non-compliance to accreditation requirements for halal certification;
- mislabeling of products as halal; and
- limited halal compliant agri-fishery products.

⁸² Stanton, Emms and Sia, 2011, op cit

⁸³ See Halal Industries Promotion: ARMM Master Plan 2009-11.

As a general observation, the business sector and a large part of the population in the Bangsamoro lack awareness on the hygienic and health benefits derived from consuming Halal food products. This is changing, but a much greater effort of educating the public is required.

Further, although needed regulations, institutions, and plans have been in place, there has been limited real actions on the ground. When it comes to the crunch, the needed funding has not been there, and the political will to push the program has been sorely lacking.

2.1. Halal Certification

What is permissible and what is not to halal consumers is best recognized in the stamp of approval by a competent certifying body on products, both food and non-food, being produced and distributed for public consumption. Halal certification is considered the cornerstone of halal industry development as it ensures that food products, in particular, are indeed in compliance with Islamic prescription using science-based approaches in product evaluation and analysis.

The Muslim Mindanao Halal Certification Board, Inc. (MMHCBi), a non-government, not-for-profit organization, was established in 2006 in a tripartite agreement involving DTI-ARMM, ARMM Business Council, and the Darul Ifta (House of Opinion). It was deemed as the first step in support of the halal industry development. This was on the consensus that moulding a halal certifying body requires time for capacity-building to reach desired levels of competence, recognizing the sensitivity in the halal certification process and to gain public confidence.

Having a single accredited certifying body is desirable for the ARMM. There are some 52 certifying organizations and individuals in the country, although only three have been accredited thus far by the National Commission on Muslim Filipinos (NCMF) - it being its mandate under Republic Act 9997.

Muftis of the ARMM, together with Shari'ah specialists and Muslim technical people trained in the fields of medicine, food technology, bio-chemistry, veterinary medicine, nutrition, and pharmacology (all of whom provide professional voluntary services), participated in a series of workshops to craft halal certification guidelines, which were then presented to the constituents of the ARMM for appreciation. The same guidelines were actually used as a working paper in the crafting of the Philippine National Standard on Halal Food.

Members of the MMHCBi likewise made country visits to Thailand and Malaysia as part of their learning program, and for benchmarking best practices in halal certification, education, food processing, institutional development, and halal industry development initiatives. They have also attended seminars on food safety systems (GMP, SSOP, HACCP) in the Philippines, and on halal auditing and conformance structure workshops in Malaysia. They had simulation training in the evaluation of food and non-food processing practices in more than 18 companies in the Philippines and abroad.

Recognized and accredited as it is, the MMHCBI is getting less government attention to its crucial role in the industry. As has been a normal practice for accredited organizations, the government normally extends financial assistance to projects of the accredited organization in support of the greater program of the government, especially if it's not within its area of expertise or outside of its mandate. Some local governments go to the extent of providing decent office space for the accredited organization, complete with administrative provisions, to make it effective in its role as a certifying body.

The MMHCBI needs considerably more financial assistance if it is to become an effective partner in halal industry development. This is on the assumption that the new Bangsamoro Authority would continue to extend its recognition and accreditation of the MMHCBI as the sole certifying body in the Bangsamoro.

2.2. Flawed and Un-implemented Enabling Measures

The ***Halal Labelling Law of 2009*** (MMA 254) is one piece of legislation critical to halal industry development because of its regulatory nature. The law is meant to regulate the use of the term “halal” in food establishments as a way to convey a message to halal consumers that the foods served are fit for them to consume. This widespread practice of unabated and spontaneous use of the term “Halal” for the purpose as mentioned resulted to confusion and deep suspicion among consumers that the food may not be halal after all.

As it is now globally practiced, halal food products to be considered as halal-compliant would require third party attestation, and that “self-claimed” halal products is a form of misrepresentation and false advertisement.

While a regulatory law is indeed desirable, this particular law in archive may have to be immediately reviewed.

The ***Halal Industry Development Master Plan***, as described by the Assistant Director of the Regional Planning and Development Office (RPDO), was supposed to be the roadmap in the development of the halal industry in ARMM. Yet after its completion in 2008, the master plan remains an un-implemented plan.

The master plan should have been a source of pride for the Moros, as this was prepared by the ARMM planners themselves. Planning officers of the DTI-ARMM, DAF-ARMM, RBOI-ARMM, DOST-ARMM, DOH-ARMM, and similar representation from the provincial level and representative of the chambers, crafted the plan over an eight month period. The expected immediate oversight review of the master plan did not take place, and thus – like many such plans – shelved.

The **Halal laboratory** set up to support the certification process of the MMHCBI is non-operating. DOST-ARMM should have a halal laboratory of its own to support the certification process of the MMHCBI. The Japan International Cooperation Agency (JICA) initially constructed a laboratory building in 2008 besides the DOST-ARMM main building on a lot provided by the regional government with provisions of initial laboratory equipment for basic testing. In 2013, another set of laboratory equipment worth PhP9.8 Million was installed through a special funding support from DTI-ARMM.

However, DOST-ARMM contends that even with the additional equipment, its halal testing capacity is still very much wanting, even by basic halal laboratory standard. It thus requested funding support for the acquisition of new equipment worth PhP20Million. This was turned down by the Department of Budget and Management (DBM) and instead, it approved a budget for the purchase of furnitures. It was a big let-down to the premier science and technology agency of the ARMM hoping to at least approximate, even by small measure, the state-of-the-art halal laboratory of the Halal Research Centre at Chulalongkorn University of Thailand worth 100Million Thai Baht (PhP130 Million), and the 10 Million Ringgit (PhP140 Million) laboratory facilities of the Halal Food Products Institute at the University Putra Malaysia (UPM).

Having a decent halal laboratory facility at DOST-ARMM provides a much needed science-based and evidence-based support to the halal certification mandate of the MMHCBI and, in the process, provides assurance of halal compliance of food products being marketed in the region.

2.3. Other Pressing Concerns

Given that the promotion and development of an industry which is associated with the “way of life” of the Moro people and of those concerned with safe and clean foods, the way to nurturing the industry should have the participation of stakeholders working together and moving in tandem with clear direction and sense of purpose.

As has been observed in the past, and as raised in recent roundtable discussions and stakeholders’ forum, it takes a collective and coherent approach to make the halal industry work if it is to become a rallying point in the revitalization of the region’s agriculture.

Whether by perception or by experience, cited below are some of the observations and issues raised that should merit serious consideration:

- Minimal participation of the private sector in policy making and planning.
- No coordinating body/office with access and answerable to the regional head has been formed or designated to coordinate the various programs being undertaken by the departments involved.

- Non-involvement of the hospitality sector (hotels and restaurants, fast-food and street-food) to create demand-supply chain for halal products.
- Non-involvement of the academe in the industry development.
- Rich in policies and pronouncements, very little on the ground to see.
- Unclear or incoherent Halal development program.
- Agriculture and fishery programs have not effectively migrated to the halal development program.
- Minimal or unclear mandate funding, as learned from the main department players of ARMM (DAF-ARMM, DTI-ARMM, DOST-ARMM, DOT, DOH,), of agencies ostensibly responsible for implementing the policy to develop the halal food industry.
- Policy has not been adopted at the LGU level (Provincial, Municipal).
- Few or negligible halal initiatives at the provincial and municipal level.
- State Universities and Colleges (SUCs) based in the ARMM have no offered courses supportive of the halal food industry and in the promotion of Islamic finance as a back-to-back component of the industry.
- Low awareness of halal products among the local population.
- Low appreciation of appropriate halal technologies.

3. STRATEGIC APPROACHES

3.1. Regulatory and Institutional Measures

Regulatory and institutional measures are important pillars for the development of the halal food industry on the heel of a fledgling agriculture.

In the *short term*, some of the pressing enabling measures the Bangsamoro government should take are as follows:

- Immediate review and updating of the Regional Halal Food Industry Development Master Plan.

- Immediate review of the Halal Labelling Law (MMA 254).
- Create a law on the promotion and development of Organic Farming patterned after Republic Act 10068, otherwise known as the Organic Agriculture Act of 2010, but with emphasis on halal organic agriculture, and include the same in the expenditure program of the region.
- Create a law on food safety (a component of halal assurance system) to be initiated by DOST-ARMM in collaboration with DOH-ARMM and MMHCBI.
- Establish or designate an office within the Office of the Chief Minister with the rank of Minister to act as the coordinating secretariat with access to, and reporting directly to, the Chief Minister.
- Designate halal action officers to replace focal persons representing the agencies to the Halal Industry Development-Technical Working Group (HID-TWG).
- Draw up a capacity development program for halal extension service providers in regional and local government, and for both the trainers and smallholders engaged in agriculture productivity program involving halal products.

And in the **medium term**, the government sustains the early actions taken with the following interventions:

- Establish an Incentive Code or Magna Carta for Micro, Small, and Medium Enterprises (MSMEs) providing a Stimulus Fund specifically for halal-compliant agri-ventures. This could include a program for matching grants.
- Encourage SUCs to introduce new courses supportive of the halal industry development (food technology, food sciences, agribusiness, nutrition and dietetics, pharmacology, halal management, Islamic finance and economics, interim short courses on food safety and Islamic microfinance).
- Designate and strengthen ARMMIARC (ARMM Integrated Agricultural Research Centre) as the lead R&D agency in halal food production with complementary effort from the academe.
- R&D on processed and manufactured food products to include non-food could be undertaken by participating SUCs complementing DOST in the process.

3.2. Private Sector Engagement

Private sector engagement in the halal effort has been minimal. Apart from the unstable business environment in the Bangsamoro and the basic factors affecting private investment in the region in general, the lack of investor interest in halal production can be attributed principally to the low level of awareness of the halal marketing niche, the unharmonized halal assurance system, and unfamiliarity with the technologies involved in halal production.

Some of the steps which can readily be taken by the Bangsamoro authorities to engage more effectively the private sector in halal production include:

- Institutionalize the Muslim Mindanao Halal Certification Board Inc. (MMHCBI- a non-government, not-for-profit organization) - through appropriate recognition by the Bangsamoro Authority as the sole certifying body in the region with funding provisions for its programs.
- Participation of the members of the hospitality sector (hotels and restaurants, catering services, and even street foods) in halal compliance program to be initiated by the Department of Tourism in collaboration with MMHCBI, DOST-ARMM and DOH-ARMM.
- Allowing the private sector to operate facilities of non-operating or least attended DAF facilities (Poultry slaughtering facility at Datu Odin Sinsuat, 23-hectare breeding station at Nuling and the five slaughterhouses put up by National Meat Inspection Service in the five provinces of ARMM) and turn them into a viable enterprise (these could be entrusted to the cooperatives).
- Increasing awareness of business support organizations of halal business opportunities, and engaging them in halal-related advocacy, which would include halal trade and data base development.
- Encouraging business support organizations, Muslim Religious Leaders, and accredited halal business organizations to take the lead in undertaking halal capacity building programs for micro and small enterprises, with financial support from the government.
- Designating halal production in selected activities in the Investment Priorities Plan of the RBOI, and provide appropriate incentives to encourage private investor interest, local and foreign.
- Exploring the possibility of providing matching grants to small and medium scale enterprises switching to halal production.

3.3. Production Measures

These measures focus on programs and actions to directly stimulate halal production:

- Build on existing pockets of smallholder organic and other producers in every province, and expand them into clusters of halal production zones, providing them with material, technical, equipment and Shari’ah-compliant micro-financing support (e.g. North Upi, Mamasapano, Sultan Mastura for organic rice and vegetable production; DOS, North Upi, Parang for organically-raised goat production).
- Expand the “Organic Gulayan sa Barangay” Program of DAF.
- Support the organic rice farming programs (Palayang Organiko) of the LGUs.
- Promote the development of organically-raised halal animals and poultry (Kahayupang Organiko).
- Increase population of small and large ruminants production through the Artificial Insemination (AI) program of DAF, which is a Darul Ifta approved method to increase livestock population.
- Introduce improved breeding program for the livestock sector.
- Discard the animal dispersal program as this has been known as a failed program, and instead package the livestock program cum training and convert into an organized cooperative endeavour.
- Adopt viable and proven models or showcases from the experiences of Mt. Carmel Rural Life Center, Kablon Farms, Tubaga Multi-Purpose Cooperative, and the Don Bosco Sustainable Agriculture Program, to increase productivity of small and medium-size farms.
- Promote investment in integrated halal poultry and livestock production through partnerships of smallholders with successful and well immersed local companies, such as Matling, Philtrade, Alnor’s, and Lam San.
- As identified in the 2011 JICA local industry promotion study, Sulu, which is the center of commercial fishing in the Island provinces with 43 commercial fishing ports, could be the site for private sector investment in fish processing, while mariculture of exportable abalone and grouper - which are premium marine products in the market - could be raised in all island provinces.

- Aquaculture, milkfish and mudcrab production can be expanded in the provinces of Lanao, Maguindano and Basilan, while tilapia raising would be most suitable to propagate in Lanao and Maguindanao.
- Native chicken, increasingly in demand by the consumers at large, could be expanded in all provinces of the region using new organic methods of raising them and better farm management.

In the immediate and medium term, the focus would be to satisfy persistent domestic demand or access to halal-compliant fresh and processed food products. At the core of this effort is the promotion of halal organic farming.

3.4. Practical steps

Not all enabling measures to re-ignite the halal industry development necessarily have to go through lengthy, bureaucratic, and circuitous process. To show the government's resolve to push through with the halal program, and without having to spend a centavo, here are some of the steps that can be taken by a mere stroke of a pen:

- A directive from the Office of the Chief Minister to all departments, attached bureaus, and specialized agencies in the region that catering services to all government-hosted functions (training, seminars, conventions and conferences, Kanduli (thanksgiving), banquet hosting of specials guests) should be first halal certified by the MMHCBI– the certification fee to be shall be borne by the host department or agency.
- Similarly, a communication from the Office of the Chief Minister to all aid agencies operating in the Bangsamoro requesting that catering services to its capacity-building activities, trainings, seminars, and conferences being held within the Bangsamoro region to be halal certified by the MMHCBI, with the certification fee being shouldered by the host aid agency (no fee would be paid for duly certified restaurants providing catering services to functions).
- Through the Department of Interior and Local Government (DILG), a directive to the provincial and municipal governments that catering services to similar functions as above-mentioned be certified first by the Provincial Committee of the MMHCBI.
- A communication, through the Department of Tourism, encouraging owners and operators of hotel and restaurants, fast-food chain, eateries, and even street food carts to observe compliance in clean, sanitary, and hygienic handling and preparation of food following the Codex Guidelines on street foods, the certification guidelines of the

MMHCBI, and the food safety guidelines to be formulated by the DOST-ARMM and DOH-ARMM.

- A separate communication from the Office of the Chief Minister to the fastfood chain franchise holders operating in the ARMM and adjacent cities pleading to make available menu-based halal certified food to Muslim patrons as a show of goodwill and cultural sensitivity.
- A letter of invitation to big food companies (San Miguel Purefoods, Swift Foods, Bounty Agro Ventures, Century Canning, Universal Canning, RD Exports, 10-Point, others) to invest in Halal integrated livestock, poultry, and feeds production in partnership with local companies the likes of Matling, Lam San, Philtrade, and Alnors in the mainland, with similar partnership in the island provinces for fishery and marine products processing.
- A directive from the Office of the Chief Minister to the Department of Agriculture and the Bureau of Fisheries and Aquatic Resources that all food production programs of DAF and BFAR covering livestock, poultry, aquaculture/mariculture, fruits and vegetables to adopt Halal compliance based on the Darul Ifta-DAF and MMHCBI guidelines and within the halal assurance framework as contained in the PNS 2067:2008 which promotes “Farm to Plate” halal coverage.

The above start-up and practical steps could trigger the demand-supply chain process for halal sources, such that it could encourage farm producers and investors to get interested in the agribusiness potential of going halal and organic with a clear market to serve. And in the near future, investments in integrated farming would begin to take shape.

3.5. General Recommendations

While it is true that the development and transformation of the Bangsamoro region cannot simply be left to the government alone, a weak and unenthusiastic private sector is also not in a position to take the lead.

In relation to the development of the halal agriculture and food development, policy directions are indicators where future economic initiatives are heading, where both the government and the private sector share the burden and the rewards of an economic program the stakeholders have been trying to develop for years.

As it is, a partnership of sort would be the better approach in getting this industry moving again, with the government providing the enabling environment and incentives for opportunities to flourish.

Below are some of the recommendations to the policy-makers of the new Bangsamoro Authority:

- In the case of the Bangsamoro region and for all its distinction from the rest of the country, promoting and developing the halal industry should NOT be relegated to the fringes of agriculture - rather, it should be at the core of agricultural development.
- Desired policy should be directed towards *a balanced approach* between encouraging large-scale plantation-based ventures and the strengthening of the smallholder enterprises as a just approach to agriculture development in general, and halal food industry development in particular.
- While keeping the export market in mind for halal products, the initial focus should be on meeting the domestic demand (the common sense thinking is that food surplus is the one that should go to the export market) - the exception would be for some privately-led ventures that by the nature of its products are profitably meant for foreign market (oil palm, Cavendish bananas, cacao, etc.).
- Ensure balanced investment strategies and diversified production of agri-commodities based on the region's strengths and weaknesses (in resources), as both provide ample opportunities for investment.
- Government's limited resources for halal should focus on smallholders and agri-diversification, and allocate sufficient resources for technical, financial, and capacity building support (the BIG players can stand on its own).

How ever plans are laboriously and brilliantly crafted, good governance and strong leadership remain the key to any successful implementation of the agriculture development plan in general, and halal industry development in particular.

Table 9. Specific Recommended Steps cum Indicative Initial Investments
(Transition period, 2014 – mid 2016)

Activity	Date of Implementation	Participants/implementers	Indicative investment (Shared responsibility)
1. Review of the Halal Food Industry Development Master Plan	2015 (1 st Quarter)	Regional and provincial planners (DOST, DTI, DOH, RBOI, DAF, DOT, DILG, Chambers, coops, academe, BDA)	P 500,000.00
2. Review and revision of the Halal Labelling Act of 2009	2015 (1 st Quarter)	DTI, DOST, DOH, chambers, coops, academe, RLA representatives, RLA Research Staff, BDA)	P 50,000.00
3. Identification and assessment of halal production zones for development	2015 (1 st Quarter-2 nd quarter)	HID-TWG; BDA	P 500,000.00
4. IEC on organic farming and halal at the provincial and municipal level	2015 (2 nd Quarter)	BDA, DAF, DILG, Bureau of Information; Provincial and Municipal Agriculturists; coops, MILF community leaders; religious leaders	P 800,000.00
5. Orientation-seminar on organic farming and farm management	2015 (2 nd quarter)	BDA, existing/new coops engaged in organic farming; Provincial/Municipal agriculturists and technicians; academe extensions services; MILF communities	P 1,000,000.00
6. Learning visits to organic farms and mariculture centers	2015 (3 rd quarter)	BDA, existing/new coops engaged in organic farming; Municipal agriculturists and technicians; academe extension services; MILF communities	P 800,000.00
7. Coops training on basic organizational management, basic accounting, record-keeping, project planning and implementation	2015 (3 rd quarter)	Existing/new coops engaged in organic farming	P 1,000,000.00
8. Orientation-seminar on	2015 (3 rd quarter)	DOT, MMHCBi, owners of	P 800,000.00

halal conformance specifically for the hospitality sector (hotel and restaurants, fastfood chains, eateries, and street- food operators)		hotels and restaurants, fastfood chains, eateries, and street-food carts	
9. Orientation-seminar on Good Governance	2015 (3 rd Quarter)	BMLI, Heads of implementing agencies; chamber and coop presidents	P 800,000.00
10. Organic farm internship for farmers/fish-farmers with 10 years of education	2015 (4 th quarter)	Existing/new coops engaged in organic farming	P 1,000,000.00 (a donor agency may be tapped to shoulder the cost)
11. Continuation of activity 3, 4,5,6, & 7	2016 (1 st - 3 rd quarter)	Other coops unable to avail of the 2015 training	P4,000,000.00
12. Capacity-building for Business Chambers on database development and management; project planning and implementation; investment promotion	2016 (2 nd quarter)	Executive Directors and incoming officers for the year	P 500,000.00 (a donor agency may be tapped to shoulder the cost)
13. Initiate the process to create a law on Halal Organic Agriculture and Food Development	2016 (3 rd quarter)	C/o Executive department, DAF, RLA. HID-TWG	P 100,000.00
14. (continuation...)IEC on organic farming and halal at the provincial and municipal level	2016 (3 rd quarter)	BDA, DAF, DILG, Bureau of Information; Provincial and Municipal Agriculturists; coops, MILF community leaders; religious leaders	P 800,000.00
15. Initiate the process to create a law of food safety	2016 (3 rd quarter)	Executive department, DOH, DOST, appropriate RLA chairs, RLA research department	P 100,000.00
16. Upgrading of DOST Halal laboratory	2016 (3 rd quarter)	DOST; HID-TWG	P 20-million (a donor agency may be tapped to provide the equipment and training component)
17. Initiate the process to create a law on Incentive Code or Magna Carta for micro and small enterprises engaged in the production	2016 (3 rd quarter)	Executive department, DAF, DTI, appropriate RLA chairs, RLA research department	P 100,000.00

and processing of halal and organically-grown products to include the establishment of P 1-billion stimulus fund spread over 5-year period (infrastructure support to production zones, technical training , and Shari'ah-compliant credit facilities)			
18. Organic farm internship for farmers/fish-farmers with 10 years of education	2016 (3 rd quarter)	New coops engaged in organic farming	P 800,000.00
19. Setting up of a Scholarship Fund for young Moros enrolling in agri-related courses	2017 (1 st quarter)	DAF-TWG	P 5,000,000.00
20. Select farmers/fish-farmers with 10 years of education to attend new technology training at the Agriculture Training Institute/Regional Fishery Centers/ or SEAFDEC	2017 (2 nd Quarter)	Participants from identified production zones	P 2,000,000.00
21. Continuation of activity 9	2017 (3 rd quarter)	At the provincial and municipal level	P 1,000,000.00

ROAD MAP FOR THE DEVELOPMENT OF ISLAMIC BANKING AND FINANCE IN THE BANGSAMORO⁸⁴

1. BACKGROUND

1.1. Banking in the Bangsamoro

The Autonomous Region in Muslim Mindanao (ARMM) has been consistently the least banked region in the Philippines. The number of banks operating in ARMM currently stands at 20, with each banking office servicing nearly 200,000 persons. And there are only 25 automated teller machines (ATMs) operating in the whole of the region.

Table 10. Municipal Banking Presence in the Philippines

Region	2011		2012
	Banks per 10,000 adults	ATMs per 10,000 adults	No. of persons served by each banking office
NCR	3.5	5.1	4,066
CAR	1.3	1.1	11,840
I Ilocos	1.1	0.8	13,170
II Cagayan Valley	1.2	0.6	12,339
III Central Luzon	1.3	1.1	10,985
IV-A CALABARZON	1.6	1.6	8,979
IV-B MIMAROPA	1.0	0.4	16,212
V Bicol	0.7	0.5	20,198
VI Western Visayas	1.0	0.8	14,718
VII Central Visayas	1.2	1.4	12,231
VII Eastern Visayas	0.6	0.5	26,324
IX Zamboanga Peninsula	0.8	0.7	19,102
X Northern Mindanao	1.1	0.8	13,401
XI Davao Region	1.1	1.0	12,971
XII SOCCSKSARGEN	0.7	0.7	21,835
XIII Caraga	1.2	0.5	13,381
ARMM	0.1	0.1	195,174

Source: BSP

⁸⁴ This report was prepared by the Foundation for Economic Freedom (FEF) for the Bangsamoro Development Agency (BDA). The basic report was prepared by Ikram Tawasil, with inputs from Gary Olivar and Thomas Allen. It draws heavily on the outputs of the FEF/PDIC/BSP Workshop on Banking and Finance (financed by Australian Aid) held at the BSP in March, 2014.

Moreover, 93% of the region’s municipalities do not have a banking presence. Most of the banks operate almost exclusively in urban centers such as Marawi, Isabela and Cotabato cities (although officially, the latter two are not part of the ARMM), and the towns of Jolo in Sulu and Bongao in Tawi-Tawi. Household incomes and level of clientele reach are higher, and the rate of poverty incidence lower, in these localities compared with the rest of the region (although ARMM as a whole lands at the bottom in these measures against other regions). Also, peace and order condition in these localities is comparatively stable and thus more conducive to banking business, particularly in high-risk undertakings such as cash assistance transactions and deposits transport activities.

Table 11. Distribution of Banks in ARMM

Isabela City	Basilan
1 Allied Bank	1 UCPB Savings Bank
2 Development Bank of the Philippines	
3 Landbank	Lanao del Sur
4 Metrobank	1 Landbank - Wao
5 Philippine National Bank	2 Landbank - Marawi City
	3 Philippine National Bank - Marawi City
Cotabato City	4 Bagong Bangko Rural ng Malabang, Inc.
1 Allied Bank - Cotabato City	5 Al Amanah Islamic Bank of the Philippines-Marawi City
2 Allied Bank - S.K. Pendatun	
3 Banco De Oro - Cotabato City	Maguindanao
4 Bank of the Philippine Islands - Cotabato Main	1 Landbank - Buluan
5 Bank of the Philippine Islands - SouthSeas Mall	2 Landbank - Parang
6 Chinabank - Cotabato City	3 Rural Bank of Datu Paglas, Inc.
7 Development Bank of the Philippines - Cotabato City	
8 EastWest Bank - Cotabato City	Sulu
9 Landbank - Cotabato	1 Allied Bank - Jolo
10 Landbank - Rosary Heights	2 Development Bank of the Philippines - Jolo
11 Landbank - Cotabato City Hall EO	3 Landbank - Jolo
12 Metrobank - Cotabato (Main)	4 Metrobank - Sulu
13 Metrobank - Cotabato (Quezon Avenue)	5 Philippine National Bank - Jolo
14 Philippine National Bank - Cotabato City	6 Al Amanah Islamic Bank of the Philippines
15 Rizal Commercial Banking Corporation (RCBC) - Cotabato City	
16 Rural Bank of Cotabato, Inc.	Tawi-tawi
17 UCPB - Cotabato	1 Allied Bank - Tawi-Tawi
18 Al Amanah Islamic Bank of the Philippines-Cotabato City	2 Landbank - Bongao
	3 Philippine National Bank - Bongao

Sources: BSP; BPAP; various bank websites

In like manner, the ARMM also ranks lowest among the country’s regions in terms of deposits which totalled a negligible Php3.9 Billion and loan availment of only Php435 Million resulting in a dismal loan-deposit ratio of only 11%, a far cry from the National Capital Region (NCR) ratio of 81%.

This means that there is a substantial non-utilization of deposits generated by banks in the region for the requirements of its inhabitants. This may logically result in its availment instead by other regions of the country.

Further, the 2011 Japanese International Cooperation Agency (JICA) survey reveals that only 32% of those surveyed maintained deposit accounts with banks while the rest kept their cash at home and elsewhere.

Part of the reason for this is the hesitation of some Muslims to deal with conventional banks because of their Shari'ah non-compliant products and services. Similarly, business sector respondents surveyed also said that 83% of them procured start-up funding for their enterprises from their own money, while 34% of them sourced it from relatives and friends.

While the *Development Bank of the Philippines (DBP)* and *Land Bank of the Philippines (LBP)*, both have a presence in ARMM, their operations are limited - DBP has three offices in the region while LBP has eight offices. A problem for these – indeed the commercial banks as well – has been the inability to ensure clear land titles for the collateralization of loans. DBP once withdrew from participating in financing the Agumil palm oil project in Maguindanao because it required the participating grower cooperative members to collateralize their loans using their land titles.

There is only one Islamic financial institution in the region, the *Al-Amanah Islamic Investment Bank of the Philippines (AAIIBP)*, with nominal Islamic banking branches in Cotabato and Marawi cities and in the town of Jolo. Its remaining five branches in Mindanao and one in Makati City essentially operate a “dual-window” banking business. However, AAIIBP has limited capital and resources, and has failed to take off as a full-fledged Islamic bank. It is now under the control of DBP. AAIIBP is discussed more fully in the following section.

While the formal banking sector seems to be generally inaccessible to most inhabitants of the Bangsamoro, as demonstrated by their absence in 93% of the region's constituent municipalities, this gap has, to a modest measure, been filled in by non-bank financial entities such as *microfinance institutions (MFIs)*.⁸⁵ It is in the microfinance area that the scope for expanded financial support to the Bangsamoro agriculture sector in particular looks encouraging.

According to the Institute for Development and Econometric Analysis, Inc., the Asian Development Bank (ADB) and Japan in tandem with the DBP and Al-Amanah Islamic Bank have “put in place a program of support for agribusiness” aimed at providing Islamic credit facilities to 2,000 households. The ADB, through its Rural Microenterprise Finance Project, has been funding microfinance institutions focusing on the 20 poorest provinces in the Philippines, including those in the Bangsamoro. However, the project failed to include Sulu, Basilan and

⁸⁵ The Economist Intelligence Unit ranked the Philippines first worldwide from 2009 to 2012 in microfinance policy and regulatory framework.

Tawi-Tawi because there are no eligible MFIs in these island provinces. Also, the Growth with Equity in Mindanao Program (GEM) of United States Agency for International Development (USAID) has been assisting proponents in procuring bank loans and joint venture funds.

The 2011 JICA study showed that there are 13 MFIs and two rural banks providing conventional microcredit facilities to the marginalized and women sectors in the ARMM, sectors that have long been disenfranchised from the country’s banking and financial mainstream. Their aggregate financing exposure has assisted approximately 22,000 beneficiaries - 4% of total ARMM population - in the region’s 34 municipalities, representing 29% coverage. The USAID-funded Microenterprise Access to Banking Services (MABS) program, through the Rural Bankers Association of the Philippines, has provided technical assistance in “setting up and implementing profitable microfinance operations” to three resident rural banks: the Rural Bank of Datu Paglas in Datu Paglas, Maguindanao, the Bagong Banko Rural ng Malabang in Malabang, Lanao del Sur, and the Rural Bank of Cotabato.

Table 12. Institutions Engaged in Microfinance Lending in ARMM

Institutions Extending Microfinance Facilities in the ARMM	Address
1. CARD Bank	Cotabato City
2. Rural Bank of Cotabato	Cotabato City
3. Rural Bank of Datu Paglas	Datu Paglas, Maguindanao
4. Rural Bank of Malabang	Malabang, Lanao del Sur
5. Extension Farmers MPC	Wao, Lanao Del Sur
6. Nagdiab Foundation	Isabela City, Basilan
7. KCCDFI	Lamitan and Isabela City, Basilan
8. CARD	Sulu
9. MSU-Sulu	Sulu
10. KCCDFI	Tawi-Tawi
11. CARD	Bongao, Tawi-Tawi
12. MSU-Tawi-Tawi	Tawi-Tawi

Source: JICA, 2011 Development Study on Local Industry Promotion in the ARMM

The brighter prospects that MFIs bring notwithstanding, the foregoing backdrop nonetheless clearly illustrates the fact that despite the statutory mandate of the ARMM to encourage banking institutions to operate in the region as embodied in the (expanded) Organic Act (RA 9054) that created it, such a mandate has largely remained unaccomplished.

In this light, a number of factors could be cited, including:

- The poor state of the region’s physical infrastructure makes it difficult for bank clients living in rural areas to access banking services and facilities in urban centers.

- ARMM has been identified as the poorest region of the country with the highest rate of poverty incidence and lowest rate of savings, making it unattractive to banks as a viable market.
- The unstable peace and order situation in the region has meant that the exposure of banks to operational risks is extremely high. For decades, the region has been the bedrock of Moro secessionist movements and haven of communist insurgency and notorious criminal syndicates. It has also occasionally been wracked by internecine clan wars, or *Rido*, usually among competing political families who are maintaining large private armies.
- The predominantly Muslim inhabitants of the region find it difficult to patronize *riba*-based conventional banks because of religious considerations. *Riba* (interest) in Islam is strongly prohibited and is, therefore, considered *Haram* (forbidden), which is the opposite of *Halal* (permissible).

The AAIIBP could have amply addressed this latter concern squarely had it not for its failure to take off as an authentic Islamic bank.

1.2. Islamic Banking in the Philippines

The first serious attempt at institutionalizing the Islamic banking and finance system in the country dates back to 1974 when the *Philippine Amanah Bank*, created a year before through Presidential Decree (PD) 264, was directed under amending PD 542 to conduct its operations following the “no-interest and partnership” principle of Islamic banking.

Owing to the inadequate depth of the amendment and the general unfamiliarity of government regulators with this entirely foreign banking concept, the decree’s objective never materialized. However, in 1990 RA 6848 - authored by then Maguindanao representative Michael Mastura and his Senate counterparts, Senators Santanina Rasul and Mamintal Tamano - was signed into law creating the *Al-Amanah Islamic Investment Bank of the Philippines (AAIIBP)*, or better known as the Al-Amanah Islamic Bank and repealing PD 264 (as amended) which created the Philippine Amanah Bank.

Under existing legal realities, the AAIIBP is the only Islamic financial institution that is allowed to conduct Islamic banking business in the country. However, it could not proceed completely with that mandate because of certain legal support inadequacies. This prompted the bank to adopt a “dual-window” banking operations, offering simultaneously Islamic and conventional services and facilities. For instance, the challenge posed by compliance with liquidity reserve requirement through purchase of government securities - such as treasury bills - adversely affects its Islamic reputation. Treasury bills, as they are interest-based, are not

eligible for Islamic banking purposes. Also, as there are no other Islamic banks with which it can appropriately deal, its unavoidable engagements in Shari'ah non-compliant interbank call loan transactions further erode its credibility as an Islamic bank. There is the issue of insurance, more particularly deposit insurance as pursued by the Philippine Deposit Insurance Corporation (PDIC). Moreover, the prevailing tax structure, particularly that which relates to capital gains tax and documentary stamp tax, tend to be unfriendly as they may render Islamic banking facilities - such as asset-acquisition *Al-Bai Bithaman Ajil* and *Bai Muajjal* financing - unattractive to the banking public because of potential double taxation that may be levied on these facilities.

In 2008, the ARMM sought to take over the ownership and management of the AAIIBP simultaneously with the DBP, which reportedly wanted to do what the Development Bank of Singapore (DBS) did a year before when it established its subsidiary Islamic bank, the Islamic Bank of Asia (IBA). For its part, the ARMM, on the other hand, planned to designate the bank as its official depository and financial arm to link its economy with that of the Muslim world's. Despite failing in its bid to acquire the bank, the ARMM continued to pursue its aspiration, this time with the aim of creating an ARMM-owned Islamic bank (Zambotimes, February 19, 2009) which was overtaken by the Maguindanao Massacre and thus never materialized.

There have been two failed attempts by the DBP to sell the majority share of AAIIBP to foreign Islamic banks. The DBP is undertaking a rehabilitation program of AAIIBP with the aim of shifting it back to Islamic banking as soon as possible. Personnel have been sent to Malaysia for training with the Islamic Financial Services Board (IFSB).

The Board of DBP has already decided to divest and privatize AAIIBP, but the process was suspended pending the completion of Bangsamoro autonomy.

2. STRATEGIC APPROACHES

2.1. A Dual System of Conventional and Islamic Banking and Finance

Both conventional and Islamic banking and finance facilities will play a role in the Bangsamoro. It will take time for Islamic banking and finance to take root, and traditional banking and finance facilities will have to be relied on in the interim. It can be expected, however, that the conventional banking and finance system will always play a significant role in the Bangsamoro.

A dual banking and finance system recognizes the fact that the conventional banking and finance system underpins the economic structure of the country as a whole, while the Islamic banking and finance system can provide an alternative for the segment of the market that wishes to adhere to Islamic principles and for those, on account of financing availment criteria set by conventional finance, who remained outside of the country's banking and finance mainstream.

A well-developed Islamic banking and finance system will also attract attention from non-Muslims who recognize the unique benefits of the Islamic financial instruments.

Islamic banking and finance must be looked at from the national perspective as well as from the Bangsamoro perspective because:

- of the large Muslim population outside of Bangsamoro that will also want to access Islamic financial instruments and services;
- many of the instruments and services will be provided by entities whose main place of business is Manila or even overseas; and
- of the legal mandate of the Bangko Sentral ng Pilipinas (BSP) and other national government instrumentalities.

It is thus critical for national legislation to underpin Islamic banking and finance in the Bangsamoro and the rest of the Philippines, accepting that the core of the activity will be in the Bangsamoro. This is now being explored by the BSP (see later section on ***Legal Infrastructure and Standards***).

The Islamic banking and finance system offers benefits not found in the conventional banking and finance system. It:

- offers products with interest-free mechanisms covered by, among others, sale and leasing contracts and discourages leverage;
- eliminates unproductive/excessive speculation/gambling (*Maysir*) and contractual ambiguity (*Gharar*) and instead, introduces the concept of risk-sharing and partnership, with a high level of moral principles - suppliers of funds become investors rather than creditors, and share business risks with the entrepreneurs in return for share of profits; and
- has close links with the real sector of the economy - it introduces a materiality aspect that links financing directly with the underlying asset so that financing is linked to the real sector activity.

And it will not pose a “threat” to the viability of conventional banking and finance, even in the Bangsamoro. On the contrary, it should improve the overall system in both the Bangsamoro and the Philippines as well provide the conventional banking industry with new products and services, should the regulatory environment allow Islamic banking and finance to be implemented. Globally, Islamic banking and finance is a growing industry, with London developing itself to be a major center. Major international banking institutions such as Hongkong and Shanghai Banking Corporation(HSBC), Citibank, Hong Kong and Standard Chartered Bank, all have subsidiaries offering Islamic banking products and services.

An orderly development of both the conventional and Islamic systems should:

- promote healthy competition, leading to increased market discipline and improved customer service and value;
- increase the deposit base, as products like “*tabun haj*” – a savings account for the annual pilgrimage to Mecca – are introduced; and
- lead to a better spread of financial risks over the economy.

2.2. Conventional Banking and Finance in the Bangsamoro

All facets of the conventional banking system will have a role to play in the future Bangsamoro. With peace and order and an improved business and investment climate, it can be expected that development banks, commercial banks, and rural banks will step up to the plate and provide financial support to, for example, business enterprises in the informal sector that wish to “move” into the formal sector to take advantage of the new economic environment, and new and expanding activities taking advantage of the resource base and the improved peace and order situation. However, this will require dealing with:

- the risks posed by unclear property rights, especially with regard to lands titles; and
- accessibility problems for many savers and investors, given the limited branch network of most of the development and savings banks.

Proposal for dealing with the property rights issues are outlined in the report on agro-based industries. Accessibility issues should diminish as peace and order is restored and transport links are established.

Local institutions providing non-collateralized loans, especially rural banks, appear to have the greatest potential in the short term for enhancing the flow of funds in the Bangsamoro. Microfinance programs run by cooperatives and NGOs will continue to be active, but they also have been handicapped by problems of security. Donors continue to be active in putting in place financial support for MSMEs, and some of these involve support for agri-businesses based on Islamic financing modes. These programs should be further encouraged.

The Land Bank of the Philippines (LBP) has been the most active bank in the region, and it is expected that it will be in a position to significantly expand its lending program once peace and order has been restored. It could be a more effective conduit of funds to the more localized rural banks and microfinance institutions. The Development Bank of the Philippines (DBP) has

been less active. It should be encouraged by the National Government to have a more active presence.⁸⁶

2.3. Principal Issues and Policy Options Relating to Islamic Banking and Finance

The real challenge is getting Islamic banking and finance up and running. Five principal issues will need to be addressed:

- an appreciation of the nature of appropriate Islamic banking and financial institutions and instruments/products for the Bangsamoro and the country as a whole, and the steps necessary to enable them to be provided;
- making people, especially in the Bangsamoro, aware of the concepts of the Islamic banking system and its products – this includes government officials and politicians as well as the general population – and the benefits offered by these products;
- the lack of appropriate skills in the country on Islamic finance and banking;
- ensuring *Shari'ah* compliance arrangements; and
- the lack of a suitable legal infrastructure for Islamic banking and finance, of a framework for dealing with governance and accounting and auditing standards, and for ensuring a level playing field in taxation and other relevant policies for Islamic and conventional financial instruments.

It must be recognized that the current market for Islamic banking and financial products in the Bangsamoro – and indeed in the Philippines as a whole - is small, and this will limit the pace and nature of their introduction. A demand survey is perhaps called for.

Underpinning the efforts to develop Islamic banking in the Bangsamoro – and indeed conventional banking - will be the restoration of law and order and the development of a business climate conducive to a vibrant private sector - both will be essential to dealing with the extensive poverty and low consumer savings in the region.

Institutions and Instruments of Islamic Banking and Finance

All aspects of Islamic banking and finance potentially have some role to play in the Bangsamoro - and the Philippines as a whole, viz: banking, capital markets (including sukuk, stock market and mutual funds), and non-banking financial institutions, including takaful and microfinance. Islamic banking and finance should be looked at as a “system”, and thus it is critical that the foundations be set for the development of institutions and products across *all* these aspects.

⁸⁶ The merging of DBP and LBP is actively being considered by the national government.

Business and economic reasons should underscore the system's development, not merely political reasons. And the system's development should not be rushed. The market should have the say in what is possible and what is not possible.

The legislative base should be wide and flexible enough to enable the market to do its work, recognizing the rapid evolution of Islamic financial products and their delivery mechanisms.

Islamic Banking

There are two general categories of Islamic Banking:

- fully-fledged Islamic banks; and
- conventional banks operating Islamic banking windows.

Some of the fully-fledged Islamic banks could be set up as a subsidiary of conventional banks, where the operations and management are clearly separated.

While fully-fledged Islamic banks ensure compliance in line with *Shari'ah*, avoid co-mingling of funds, and avoid conflicts in management objectives, the arguments for allowing Islamic banking windows – especially in a “green field” environment - are strong:

- gradual implementation is more easily absorbed, noting that it will take time to build up a customer base, educate the public, develop human resource capabilities and mould the regulatory environment;
- cost efficiency is more readily achieved, since existing infrastructure can be leveraged and duplication of resources minimized;
- the technological know-how of the conventional banks can often be readily transferred; and
- it is easier to attract the non-Muslim market to Islamic instruments.

There are number of options which could be pursued.

A *first option* could be for the Bangsamoro Government to set up its own fully-fledged Islamic bank, which could also serve as a depository for regional and local government funds. Experienced partners could be brought in under a management or technical assistance contract. This could, of course, be a revived AAIIBP. However, complementary regulatory actions would be required to enable AAIIBP or a new fully-fledged Islamic bank to effectively operate.⁸⁷

⁸⁷ Annex 1 sets out a scenario for the Bangsamoro Government having its own fully fledged Islamic bank either through the take over of AAIIBP or the establishment of a new fully-fledged Islamic bank.

A *second option* would be to allow only fully-fledged Islamic banks to be set up, as this avoid the moral hazard associated with the possible contamination associated with conventional banks operating Islamic windows. Under this option, a start could be made by reviving AAIIBP, perhaps by bringing in experienced partners from Malaysia or the Middle East. The downside of this option is that the contamination and image of Al-Amanah may be such that potential buyers may not have trust in the institution. However, the fact that AAIIBP is the only Islamic bank in the country, with a powerful charter, may be the major attraction for buyers.

A *third option* would be to provide for both Islamic banking windows and fully-fledged Islamic banks,⁸⁸ allowing the “market” – appropriately guided and monitored by the BSP – to determine the most suitable form of delivery mechanism for Islamic banking products. The challenge is to appropriately “ring fence” the windows to ensure they are not contaminated by the conventional banking operations.

Islamic banks, to be viable, need other like banks with which to appropriately relate and transact. This requirement becomes more crucially indispensable in the area of interbank transactions which, at present, are not Shari’ah-compliant. Malaysia and Indonesia have successfully developed their Islamic banking system by allowing existing conventional banks to offer both conventional and Islamic banking products and services, and/or set up subsidiary Islamic banks (as pursued by multinational banking institutions such as CitiBank, HSBC and Deutsche Bank).

Thus if the Bangsamoro Government does wish to pursue the route of having its own fully-fledged Islamic bank, it would be wise to encourage private entities to also engage in providing Islamic banking and financial services in the region.

It could be expected that a number of the current conventional banks would want to explore the opportunities for operating Islamic windows, and some may want to consider establishing fully-fledged Islamic subsidiaries. Foreign banks may also want to enter the market, and this could be in joint ventures or technical/management agreements with local banks that do not have the necessary know-how in Islamic banking. There has already been some interest expressed by local and foreign commercial banks to take over AAIIBP, using it as springboard for introducing a wider range of Islamic banking and finance instruments.⁸⁹

As a starting point and while the legislative base is being formulated, the possibilities of exploiting the AAIIBP charter to set up subsidiaries and introduce alternative Islamic financial instruments could be explored.

⁸⁸ The fully-fledged Islamic Banks could include a Bangsamoro Government owned Islamic bank.

⁸⁹ The government may wish to consider encouraging Land Bank to open an Islamic banking window, since it has the most extensive network of branches of all banks in the Bangsamoro.

The legislative base should allow for all these possibilities. Islamic banking is still evolving, and it will be important to provide flexibility in the way banking services are provided.

Islamic Capital Markets

Islamic capital markets perhaps offer the fastest route for introducing Islamic banking and financial products into the Bangsamoro.

Sukuks – certificates of ownership in a pool of underlying assets in which the certificates are of equal value – offer a means for mobilizing funds for expanding and new projects, and supporting ongoing business ventures. A return is obtained through a sharing or leasing of assets, and reflects the profitability of a project or business venture. Assets are not there as security, but are used for creating *Shari'ah* compliant returns associated with the ownership or leasing of assets. These are flexible instruments and can be customized to needs. They attract both Islamic and conventional lenders, the latter purely from their economic opportunity.

The drive toward financial integration with ASEAN (and indeed within greater Asia) will provide a platform for the local development of *sukuks*, given the growing importance of these instruments in some of these countries, particularly Indonesia, Malaysia and Brunei. *Sukuks* are suited to public-private partnerships (PPP), and these could form a significant component of the development thrust in the Bangsamoro, particularly to finance infrastructure in support of critical private sector projects. Major private sector projects in the region could also be encouraged to pursue *sukuks* in the financing of their operations. The financing can be organized on-shore or off-shore, and could be arranged without the necessity of establishing an institutional base within the Bangsamoro or even the Philippines.

The Bangsamoro government and local governments should also explore meeting their “borrowing” needs through *sukuks*.

However, under present Philippine taxation regulations, they would be prohibitively expensive instruments, since the transfer taxes, value-added tax and capital gains tax associated with the asset transfers put them at a considerable disadvantage to conventional bonds. The regulations would need to be amended to ensure a level playing field - this issue is being addressed by the BSP/SEC and Financial Services Forum.

The Philippine Stock Exchange (PSE) has taken steps towards Islamic finance. It has announced some 61 of its listed companies as *Shari'ah compliant stocks* - 24 of these companies are in the industrial sector, 12 in the service sector, and 11 in mining and oil. The screening was based on the globally accepted Accounting and Auditing of Islamic Financial Institutions (AAOIFI) standards. *Shari'ah* compliance is monitored by Ideal Ratings from Egypt.⁹⁰ The ultimate goal is to develop a market index of these *Shari'ah* compliant issuers, which the PSE hopes to launch by 2015.

⁹⁰ Ideal Ratings was initially cleared by the NCMF to carry out this task.

Once the Shari'ah index is launched, the PSE then proposes to go the next step with the creation of exchange traded fund investments (ETFs) in this index to serve as actual investment vehicles. Beyond that, a Shari'ah index futures market is envisaged, which the PSE plans to reverse-engineer from the design of the general market index futures market in Singapore.⁹¹

This has now provided Muslim Filipinos from the Bangsamoro and elsewhere with a local alternative for *Shari'ah* compliant investments, when otherwise they would have had to look to suitable overseas investments. Market education is a major challenge locally - the PSE expects that the initial investor interest will come from outside the Philippines, particularly from the Islamic counties within ASEAN and in the Middle East.

To further enhance product integrity and competitiveness, the setting up of a Shari'ah board in the SEC as in Malaysia's Securities Commission or as an in-house Shari'ah compliance tool in the PSE may be explored.

Microfinance

Products of a "grass-roots" nature, such as microfinance, offer considerable potential, since they are seen to target combating of poverty directly, particularly in rural areas.

In many respects, a "bottom-up" approach to introducing Islamic financial products makes a lot of sense. This would be in keeping with the undeveloped nature of Bangsamoro economy and the lack of awareness of the more sophisticated Islamic banking and financial instruments.

The dominance of informal activity in the Bangsamoro and the difficulties associated with collateral over property and land, suggest that Islamic microfinance facilities could play a major role in expanding the economic base. However, there is a need for service providers with outreach to the rural areas where the need for support is greatest, and for suitably designed and affordable instruments tailored to the needs of the Bangsamoro market.

Village and rural banks provide around three-quarters of *Shari'ah* compliant microfinance products in Muslim countries, with the remainder being split among NGOs, Cooperatives, commercial banks, and other non-bank financial institutions. In the Philippines, it is likely that cooperatives and NGOs would be the initial conduits for Islamic microfinance instruments, although rural banks may be willing to become conduits.⁹²

The *Muhammadiyah* model of Indonesia is worth exploring for its applicability to the Bangsamoro. This model also introduces micro-*Takaful* (*micro insurance*) as protection to

⁹¹ The shariah compliance of these investment vehicles and the Shariah index futures market will need to be assured.

⁹² Donors should be encouraged to expand their programs involving financial support to small farmers based on Islamic principles. These could be channeled through rural banks wishing to move away from conventional banking towards Islamic financing, cooperatives and accredited NGOs. Associated with the financial support could be appropriate technical support, so enhancing the capacity of these organizations to sustain their programs over the longer term without the support of donors.

reduce risk associated with the possibility of losses. There is certainly a demand for insurance against crop failure by Muslim farmers in the Bangsamoro, but their ability to pay the necessary premiums is questionable.

Means of providing affordable takaful needs to be explored further. It is understood that the Insurance Commission of the Philippines is already working on drafting regulations with the intention of introducing takaful products into the country.

Trade finance will provide a ready avenue for the adoption of Islamic finance principles, especially with the onset of the ASEAN free-trade regime starting next year. This would be built on the traditional trade flows between Muslim Mindanao and its Indonesian and Malaysian neighbors. Trade finance could be along the lines of Murabahah. The CIMB model offers an example.⁹³

Educating the Public

Raising the public awareness for Islamic banking and finance operations is critical. Most Muslims in the Bangsamoro and the rest of the Philippines have been exposed to conventional banking and finance over many years, and are unaware of Islamic products and their benefits. Based on feedback during the recent Bangsamoro Stakeholders' Forum in Cotabato City, even seasoned Muslim business owners are unfamiliar with this financial paradigm. For Islamic banking and finance to succeed, this has to change.

A communications strategy should be prepared to educate the public on the Islamic banking and finance principles, and the products available to them. This should be across all stakeholders, Muslim and non-Muslim, and be based on careful socio-economic research. The commercial aspects as well as the religious underpinnings should be stressed.

The Bangsamoro government should be at the forefront of this undertaking utilizing both the mainstream media and informal communication channels, including social media. Muslim academics, professionals and local leaders who have respect of their local communities should be active partners the campaign in the Bangsamoro. Chamber of Commerce and other business associations could also be avenues of dissemination. Even schools could be an avenue for basic understanding of *Shari'ah* principles underlying Islamic financing.⁹⁴ While the mosques offer a convenient avenue for dissemination of this information, care should be taken that the messages are not "hi-jacked" and misused.

⁹³ CIMB is a listed universal bank based in Kuala Lumpur. It operates throughout Asia and the Pacific, and has as a part of its group a separate Islamic bank, one of the largest in the world. It offers a wide range of Islamic financial products, including *Shari'ah* compliant trade finance.

⁹⁴ The Bangsamoro government may also require or encourage local educational institutions to incorporate in their curricula a subject on basic principles of Islamic banking and finance as, at the least, an elective or special academic requirement.

The campaign should emphasize Bangsamoro links to regional and global Islamic banking, and the potential for the Bangsamoro to be a business and cultural hub not only to BIMP-EAGA, but also as a gateway to the rest of ASEAN.

Development of Skills

There is a dearth of skills in Islamic banking and finance in the Philippines, let alone the Bangsamoro. No less than the AAIIBP admitted that it still suffers from this inadequacy. A program for developing the necessary skills will have to be formulated, and the BSP and the Bangsamoro government should squarely address this basic need.

Academic support is critical, and means to support financially the development of suitable courses in academic establishments will need to be explored. This would include formal courses in universities, and short term-programs through institutions such as the Bangsamoro Leadership and Management Institute, Technical Education and Skills Development Authority (TESDA) and Development Academy of the Philippines. Partnerships and twinning arrangements with, and/or technical support from, Malaysian and Indonesian (or other Muslim countries) universities and training institutions should be considered.

As an alternative option, the BSP in partnership with the appropriate Bangsamoro entity, could explore the feasibility of setting up a local Islamic Finance Training Center utilizing both domestic and foreign expertise. For this purpose, a Training and Manpower Development Program Concept Paper for an Islamic Bank is attached (Annex 2). This can be undertaken either in-Bank or externally, locally or abroad.

Shari'ah Compliance Arrangements

The approach to *Shari'ah* compliance will be a major challenge. The dearth of knowledgeable scholars in both Islam and finance will be a limiting factor over the near term.

In most mature Islamic banking and finance systems, there are *Shari'ah* advisory boards in both the banking and finance regulatory agencies - principally the central bank, in the case of banking (financial product with *Shari'ah* laws, and their decision is accepted as final).

In Malaysia, Islamic banks – including private commercial banks that wish to open Islamic windows - have their own *Shari'ah* advisory boards, which determine whether financial products are *Shari'ah* compliant. The CIMB banks, for example, have in-house regulators. However, the success of this type of self-regulation depends on the acknowledgment that all banks adhere to principles of *Shari'ah* and are equally compliant - no bank is more compliant than the rest.

The Indonesian system does not rely on the issuance by muftis of rulings or opinions on *Shari'ah* (or determination whether a non-banking financial product is compliant or contravenes *Shari'ah* principles). There is no recognized hierarchy of muftis. Instead, the system relies on the collective opinion of religious scholars (ustadj, imams who are chosen to

represent their organization/party) who constitute the advisory board. They determine whether a financial product is *Shari'ah* compliant (decisions are reached by majority vote), and issue fatwas (opinion). All fatwas are compiled and provided to the central regulatory agency, which formulates the corresponding regulation based on the fatwas.

In the Philippines, there is an issue of credibility over fatwas, particularly where the mufti's deliberation may be influenced by factors other than interpretation of *Shari'ah* law. In conflict areas, "transactional considerations" may be given more weight than actual application of *Shari'ah* law.⁹⁵ The *Darul Ifta* or "House of Opinions", an association comprised of respected and formally-educated Islamic scholars and jurists may be the safest way in this regard or better still, a *Shari'ah* board selected from the best in this organization can be resorted to.

The most suitable course of action for the Bangsamoro and the Philippines will need to be explored. This may involve adopting interim measures including tapping ASEAN expertise.

Legal Infrastructure and Standards

The legal infrastructure is critical, and a number of institutions will have a role to play, including Bangko Sentral ng Pilipinas (BSP), Securities Exchange Commission (SEC), Philippine Stock Exchange (PSE), and Department of Finance (DoF). If these institutions provide the necessary legal framework for Islamic banking and finance at the national level, the need for legislative action by the Bangsamoro government will be minimal.

In recognition of this, the BSP is working with the other relevant agencies to lay the groundwork for the necessary legislative and institutional agenda. The aim is to provide the appropriate regulatory framework for the licensing and supervision of Islamic banking in the Philippines, including the Bangsamoro, and for other Islamic financial instruments.⁹⁶

At the FEF/PCID/BSP Workshop in Banking and Finance in the Bangsamoro, Governor Amado Tetangco outlined five principles on which Islamic banking should be set up:

- the system must allow for a critical mass of market players under a competitive but well-regulated environment;
- appropriate linkages, including interbank markets that cater to the unique characteristics of Islamic banking must be present;
- creating a regulatory and supervisory framework that encourages a level-playing field allowing Islamic banks to operate alongside conventional ones;

⁹⁵ In the early years of AAIIBP, operational manuals were formulated based on *shari'ah* concepts and principles. It was suggested these could be updated and used as a reference point for *shari'ah* compliance, at least in the interim.

⁹⁶ The BSP is also considering to first revise the regulatory framework for just AAIIBP operations that can then be shared and extended to other institutions.

- the regulatory environment must encourage the provision of innovative products and services to address the distinctive needs of Islamic finance - Islamic financial players should be encouraged to, and not inhibited from, introducing Islamic finance products; and
- the regulatory framework must help build a broader customer and asset base by increasing investor awareness and acceptance, while ensuring consumer protection.

Ideally the legislation would be flexible enough to allow for the full range of Islamic banking arrangements,⁹⁷ recognizing that the products and instruments are continually evolving as the industry matures, viz:

- establishment of new fully-fledged Islamic banks or conversion of conventional banks into Islamic banks, whether domestic- or foreign-owned, commercial or rural;
- establishment of Islamic banking windows or subsidiaries within conventional banks;
- opening of branches that operate as Islamic banking branches or converting conventional branches to Islamic banking branches; and
- establishment of sub-branches or Islamic banking services within conventional branches, and converting and upgrading the status of conventional sub-branches to that of Islamic banking branches.

The BSP is also looking at means to deal with reserve requirements and liquidity management problems peculiar to Islamic banking institutions. It will also have to work closely with other government agencies for allied activities such as:

- deposit insurance;
- supporting non-banking institutions providing Islamic capital market and insurance products; and
- necessary reforms to the tax system to reflect the special nature of Islamic financial instruments, and in particular to nullify the inherent advantage the current system offers conventional bonds over sukuks.

⁹⁷ It is still an open issue as to the range of Islamic finance products and instruments, apart from banking, that would also need to be covered in the legislation.

The intention is to use the Financial Services Forum (comprising BSP, SEC, PIC, and PDIC) in order to secure cross-cutting and coordinated government support. In Annex 1, the approaches taken by selected other countries in dealing with these issues are outlined.

The extent of legislative action required in these areas needs to be looked at carefully. There may be enough scope under existing laws – through changes in regulations and operating procedures – to effect many of the necessary policy actions without the need for legislative changes.⁹⁸

It is encouraging to note that the BSP is an associate member of the governance and operational standard-setting Islamic Financial Services Board (IFSB) headquartered in Kuala Lumpur Malaysia from which it can substantially procure support in this regard.⁹⁹ Another similar international body, the Middle East-based Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) can likewise be tapped towards this end.¹⁰⁰ Also, the BSP, aside from organizing an Islamic Banking Supervision Department in its midst, may also explore the possibility of constituting an in-house Shari'ah Advisory Board much like the one at Malaysia's Bank Negara.

Note that the Organic Act underpinning ARMM provided for the BSP to set up a regional office, but this did not happen. If the Basic Law currently being prepared has the same provision, the BSP should be encouraged to move ahead and establish the office, and use this to spearhead for supporting Islamic banking in the Bangsamoro.

The Bangsamoro Government will have the power, subject to supervision of the BSP, to encourage the establishment of banks and financial institutions (and their branches) and off-shore banking units of foreign banks. This provides a good basis for the BSP to work closely with the Bangsamoro authorities in ensuring a local presence of financial institutions providing Islamic banking and financial products.¹⁰¹

The Securities and Exchange Commission (SEC) will also have to review its regulatory base relating to capital markets to ensure an appropriate framework for Islamic capital market products, particularly sukuk. The SEC is already building up its own capacity on Shari'ah compliant securities, and recently had briefings by the Securities Commission in Malaysia under Australian technical assistance.

⁹⁸ There were encouraging views propounded on this matter by representatives from the Insurance Commission, the Securities and Exchange Commission, and from legal corporate experts during the FEF/PCID/BSP Banking and Finance Workshop.

⁹⁹ The BSP is actively engaged in capacity building. It has sent personnel for training in Malaysia (a BDA staff member was included in this training program), and recently had an in-house workshop using World Bank resource persons. A follow-on technical assistance program is being worked on.

¹⁰⁰ The Philippine Association of Islamic Accountants could also play a role in setting accounting and auditing standards for Islamic banks, following the principles set out by the AAOIFI.

¹⁰¹ The ongoing process of liberalizing the presence of foreign banks, from currently 10% to a maximum of 30% of commercial bank assets, would facilitate the entry as well of Islamic banks from abroad, whether as outright branches or through joint ventures with local partners.

It is critical for BSP and SEC to show fair treatment between conventional and Islamic institutions and products. A level playing field is important, although the embryonic nature of Islamic banking and finance in the Philippines – indeed the rest of the world even though rapidly growing – suggests some additional nurturing is required.

Capacity Constraints and Technical Assistance

In an earlier section, the need for skill development to support the evolution of the Islamic banking and finance system was highlighted. A more immediate concern is the capacity of the national institutions to lay the necessary legislative and administrative groundwork for the establishment of Islamic banking and finance, and the capacity of the Bangsamoro authorities to oversee its “on-the-ground” penetration.

The BSP itself recognizes its own capacity constraints, and has been taking steps to deal with this through special in-house workshops (with World Bank resource persons) and sending personnel for training in Malaysian institutions. It is also working on possible technical assistance for continued training, and would welcome technical assistance to conduct a demand study on Islamic banking and finance (which would make the concept of Islamic windows more marketable to local banks), and assist the BSP in securing inter-agency support and coordination in formulating the legislative and institutional agenda- a starting point would be for the Department of Justice to provide a ruling on how liberally existing rules and regulations administered by BSP, SEC, BIR, PDIC, etc. can be construed to accommodate Islamic banking and finance.

The capacity in other agencies to deal with Islamic banking and finance is also limited- in some cases, non-existent. All the agencies interviewed for this report expressed a need for technical assistance to deal with the issues relevant to their portfolios. The National Tax Research Center (NTRC) management, for example, candidly admits that the organization – and indeed the Department of Finance (DoF) as a whole - does not have the necessary expertise in this area, but understands the fiscal benefits of setting up a parallel Islamic banking and finance system in the country. The NTRC and DoF would thus welcome technical support to help think through the outstanding taxation and related issues.

Thus an immediate effort should be made to get this technical assistance in place.

In parallel, *a core team should immediately be set up within the Bangsamoro* to interface with the BSP and the Financial Services Forum (FSF) in laying the groundwork for the legislative and institution agenda. Within this context, this team would also:

- explore the necessity, desirability, and scope for legislative and regulatory actions at the regional level to supplement the national legislative and regulatory actions;
- assess the desirability and feasibility of the Bangsamoro Government having its own fully-fledged Islamic Bank, and if so, (i) whether this would be best achieved by setting

up a new entity or by taking over the operations of AAIBP, (ii) the most appropriate ownership structure and capitalization, and (iii) management and operational parameters;

- work with the BSP to determine suitable Shari'ah compliance arrangements;
- determine with BSP and other agencies suitable programs for skills development, with particular relevance to the Bangsamoro;
- prepare and embark on a program for educating the Bangsamoro public, both as "savers" and "borrowers", on Islamic banking and finance; and
- determine the most appropriate means to get Islamic microfinance up and running as quickly as possible, particularly to support the smallholder farmers under the agribusiness development program.

The challenge for this team - of around four to five personnel - will be to undertake this work while at the same time, develop its own capacity. The team will need technical support, and will require a capacity building program.

ANNEX 1. SCENARIO FOR THE BANGSAMORO GOVERNMENT HAVING ITS OWN FULLY FLEDGED ISLAMIC BANK

OPTIONS FOR FULLY FLEDGED ISLAMIC BANK

This could be achieved through either:

- taking over the Al-Amanah Islamic Investment Bank of the Philippines (AAIIBP); or
- setting up a new fully-fledged Islamic bank.

Both would require supportive actions on enabling regulatory and institutional infrastructures.

This scenario will have for its key objectives the following:

- Establish a financial arm that could effectively enable the economy of the Bangsamoro in particular and the country in general to access the Muslim world's US\$1.8 Trillion Islamic finance services industry and US\$2.3 Trillion global *Halal* market (includes non-food halal products).
- Provide the Bangsamoro a natural institutional differentiation advantage that offers opportunities which it can exclusively or primarily exploit to sufficiently address its huge development requirements.
- Create an institutional avenue through which Filipino Muslims can be properly assimilated into the country's banking and financial mainstream and become productive members of the national economic society.
- Utilize the Islamic bank as the focal and pivotal point from which to finance private sector initiatives in the development primarily of the agribusiness, halal and Islamic microfinance institutions serving micro, small and medium enterprises (MSMEs) in the region.

Take Over of the Al-Amanah Islamic Investment Bank of the Philippines (AAIIBP)

As a short-term option, this may be doable within the transition period and obviously easier to do, given the immense goodwill that has presumably been generated between the National Government and the MILF by the peace process. This can be done simply by buying into the shareholdings of the bank either wholly or by way of majority ownership of its authorized capital of PhP1 Billion. In this light, the BSP has formulated a two-point eligibility criteria for such acquisition which it needs to approve: Business Plan and a Management Team.

However, it must be stressed that this policy option carries with it the assumption that the bank has passed a due diligence and audit review, a usual and necessary acquisition or privatization undertaking process.

The AAIBP's capital structure as embodied in its charter, RA 6848, is as follows:

- Series "A" shares shall comprise five million one hundred thousand shares equivalent to Five Hundred Ten million pesos (PhP510,000,000) to be made available for subscription by the present stockholders of the Philippine Amanah Bank namely, the National Government, and such other financial entities as it may designate.
- Series "B" shares shall comprise nine hundred thousand shares equivalent to Ninety million pesos (PhP90,000,000) to be made available for subscription by Filipino individuals and institutions.
- Series "C" shares shall comprise four million shares equivalent to Four Hundred million pesos (PhP400,000,000) to be made available for subscription by Filipino and foreign individuals and/or institutions or entities.

In a recent interview, Idiosa Ursolino, Al-Amanah Islamic Bank's Senior Vice-President for Operations argued that the bank's foremost chief challenges are *low level of deposits, insufficient capitalization, and lack of working knowledge on Islamic banking.*

Low Level of Government Deposits

AAIBP's total deposit portfolio stands only at PhP241 Million (no deposit from the ARMM) broken down as follows: PhP78 Million -Private; PhP163 Million-Government. The bank's low government deposit level may be attributed in part to its non-inclusion as an accredited government servicing bank under the Modified Disbursement System (MDS) as embodied in Memorandum Order No. 192, despite its charter's provision to the contrary.

As a Bangsamoro government-owned bank, its problem on low level of government deposit will be squarely addressed as the autonomous government budget and those of its constituent political units and its local funds will be placed in the bank as its official depository. In addition, this will also include, as far as possible, funds of foreign donor organizations and multi-lateral institutions which are implementing projects in the Bangsamoro

Meantime, its non-inclusion in the MDS could be resolved by a Bangsamoro government request for an amendment of the aforesaid memorandum order. Further, the hesitance of Muslims in patronizing Shari'ah non-compliant products and services of conventional banks would no longer apply in the case of a full-fledged Islamic bank which is assumed to have secured the support of the Muslim religious sector.

Insufficient Capitalization

Insufficient capitalization can be adequately addressed through available Islamic financial instruments (e.g. *Sukuk*) in partnership with foreign Islamic financial institutions, and with the support from the

National Government. According to Standard & Poor, in a report released on February 5, 2014, Sukuk issuances worldwide will top US\$100 Billion in 2014. Likewise, Thomson Reuters report projects that it will reach US\$421 Billion by 2016.

Some of the more successful Sukuk issuances involving western corporations and governments were those of the German state of Saxony-Anhalt in 2004 (US\$124 Million) backed by Ministry of Finance buildings, General Electric Capital Corporation of the US in 2009 (US\$500 Million), Tesco PLC of the United Kingdom in 2007 (US\$180 Million), and a Toyota Motors Corporation unit of Japan in 2008 (US\$312 Million).

The Wall Street Journal (November 5, 2013) notes that given its extraordinary growth in the last two to three years, “sukuk are much closer to being a mainstream asset class.” In fact, in 2012, sukuk already outpaced conventional bonds to “represent more than half of new issuances,” according to Michael Grifferty, president of the Gulf Bond and Sukuk Association based in Dubai.

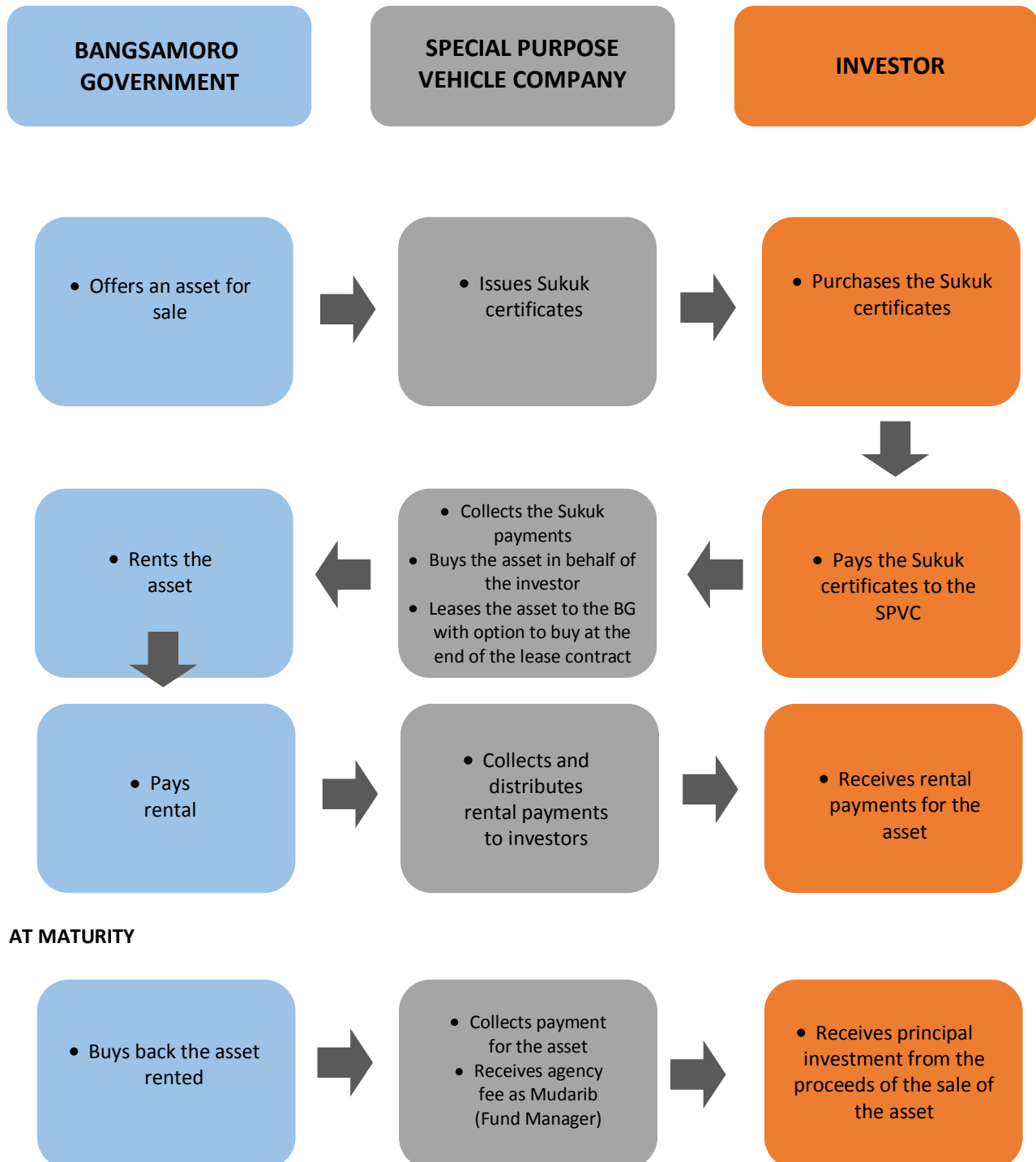
This obviously means that the global demand for sukuk is so huge (estimated between US\$800 Billion to US\$1 Trillion, according to Azhar Nazim, partner and head of the Global Islamic Banking Center at Management Consultancy EY in Bahrain) that current supply (US\$250 Billion) cannot sufficiently meet. He adds that this offers “a great opportunity for governments as well as corporations to mobilize capital in this investor pool.” For example, the US\$500 Million sukuk issued by Al-Hilal Bank of Abu Dhabi was oversubscribed by 12-fold.

In the case of the Bangsamoro owned or controlled (majority ownership with foreign partner) Islamic bank, sukuk issuance could be done in the most popular way, *Ijarah sukuk*.

Example of Ijara Sukuk

Assumptions

- Issuance of US\$15 Million Sukuk Ijarah to capitalize or expand capitalization of Islamic Bank
- Lead arranger – Islamic Bank and its foreign Islamic bank partner or reputable international bank
- Market – Preferably, Bursa Malaysia
- Term - 7 years



The Special Purpose Vehicle or Acquisition Company (SPVC) in the above *Ijara Sukuk* example should be classified as Shari'ah-compliant based on the following criteria (Malaysian model):

- the proposed business activity should be Shari'ah compliant;
- the proceeds raised from the issuance should be placed in an Islamic account; and
- in the event that the proceeds are invested, the investment should be Shari'ah compliant.

On the other hand, if the bank's capital base is found to be insufficient, it could be resolved by a simple amendment to its charter aimed at expanding its authorized capital to a viable level. Meantime, operational, management, organizational capacity building can be procured through a serious and comprehensive manpower training program locally or abroad, particularly in Malaysia either independently by the Islamic bank or as a joint undertaking with a foreign partner, assuming that the 40% of the bank's authorized capital has been subscribed and paid in by such partner.

Setting Up a New Fully-Fledged Islamic Bank

Because this may require a legislative enactment and hence, a longer period to undertake, the same may not be possible to accomplish within the transition period.

However, the Islamic bank that will be created through this option is comparatively easier to operate as its books will start clean with no requirement on the drafting of an Islamic conversion program necessary for a conventional bank intending to adopt full Islamic banking operations. The law that will create it may already include the resolution of the issues and constraints identified herein. Also, it will have the advantage of freely organizing, training and capacitating an effective and efficient manpower force, and designing a more appropriate and updated operational system to carry out its Islamic banking mandate. Moreover, the funds that would be used to capitalize it may come from permissible (*Halal*) sources which will help enhance its Islamic integrity even more.

ENABLING REGULATORY AND INSTITUTIONAL INFRASTRUCTURES

The more fundamental and demanding challenges in this scenario are those that pertain to the enabling regulatory and institutional support infrastructures. These are being addressed by the BSP and the Financial Services Forum composed of relevant Government agencies, and hopefully solutions will be found and embodied in appropriate regulations before the end of the Aquino administration.

As a pertinent perspective, the following strategies initiated by other countries in addressing these challenges are relevant.

Statutory Reserve Requirements

In the case of the Kuala Lumpur-based Bank Islam Malaysia Berhad (BIMB), the concern relating to compliance with the liquidity reserve requirement, which is presently done by Philippine banks through the purchase of non-Shari'ah compliant government securities such as treasury bills, was initially addressed by allowing the BIMB to instead purchase *Qard Hasan* (benevolent loan)-based non-tradable certificates known as Government Investment Issues (GIIs) issued in 1983. This was ultimately perfected in 2001 when the Malaysian government replaced them with *Bai al-Dayn* (debt trading)-based GIIs, thus making the certificates as tradable instruments.

In Sudan, this concern was addressed by the issuance of the Government Investment Certificates covered by *Bai Salam*, *Ijara* and *Murabaha* contracts and the profit-sharing Government Musharaka Certificates. In like manner, Bahrain, in 2001, replaced the conventional treasury bills with *al-Salam* sukuku so that "Islamic banks would face a level playing field vis-a-vis traditional banks in terms of investment opportunities" and "the authorities could engage Islamic banks in the conduct of monetary policy" (IMF Working Paper, 2007).

As the foregoing were achieved by legislation - which in the local setting may take a longer time to undertake - two alternative ways may be considered in the meantime. These are:

- the BSP purchasing Sukuku in the global capital market and selling them to the Islamic bank as a compliance to the existing liquidity reserve requirement regulation; and
- the BSP allowing the Islamic bank to purchase Shari'ah-compliant stocks at the Philippine Stock Exchange or stocks of public utilities companies.

Inter-bank Call Loans/Overnight Lending Transactions

In 1994, Malaysia created the Malaysian Interbank Money Market allowing Islamic banks to engage in interbank transactions compliant with the requirements of Shari'ah. In the same vein, the Bahrain Monetary Authority established the Liquidity Management Center (LMC) in 2002 for the same reason.

For the purpose of the local Islamic bank, the first alternative above may be resorted to exclusively between it and the BSP.

Islamic Insurance (*Takaful*) particularly *Takaful* Deposit Insurance

As to insurance and taxation concerns which are comparatively less intrinsic issues, government regulators have expressed an open mind on the subject, as noted during the FEF/PCID/BSP Banking and Finance Workshop.

Government regulators and policymakers may want to draw the experiences of other countries in this instance. Insurance as it is understood and operated conventionally is not permitted in Islam (IMF Working Paper, 2007). Therefore, an effort must be exerted to allow the establishment of *Takaful*

(Islamic insurance) companies, particularly deposit Takaful (DT) entities, to build and maintain public confidence in deposit-taking Islamic financial institutions such as Islamic banks.

The International Association of Deposit Insurers (IADI) identified certain basic issues that need to be considered in launching a DT, to wit:

- The scheme's coverage - should the DT cover all Islamic deposits, or only those that are demand deposits? (e.g. *Al-Wadiah* current and savings deposits)
- Its funding and investing policies - how should the DT be funded? Where should it invest its assets?
- The resolution process for dealing with failed banks.

Turkey has pioneered in this field when, in July 2003, it allowed Islamic banks to create an Islamic Deposit Takaful (IADI, 2006). In 2005, Malaysia followed suit by establishing the *Perdaban Insurans* Deposit Malaysia (PIDM) to "administer the Deposit Insurance System (DIS) and the Takaful and Insurance Benefits System Protection (TIBS) to protect depositors and owners of takaful certificates and insurance policies in the event of a member institution's failure." The deposit insurance coverage for varied types of deposits may reach up to RM250,000 each.

Meantime, as could be gleaned from the statements of insurance regulators made during the FEF/PCID/BSP Banking and Finance workshop, Takaful companies may be allowed in the country by instituting certain adjustments to existing insurance regulations. In fact, a 2-day Takaful Workshop sponsored by MAA General Assurance Philippines, in partnership with its Malaysian partner, has just been concluded. According to Allan Unson, Vice President for Business Development of MAA General Assurance Philippines, a Takaful launch is being eyed within the year in cooperation with the Insurance Commission.

Taxation

Islamic financial transactions, as they are carried out on the basis of actual economic activity backed by tangible assets and usually covered by sale and leasing contracts such as *Ijara*, *Murabaha* and *Bai Bithaman Ajil*, will naturally engender tax issues when ownership over these assets change hands. For instance, in the case of *Bai Bithaman Ajil* fixed asset acquisition financing, the Islamic bank will provide the asset by first purchasing the same, and then selling it to the customer to be paid on a deferred term. Upon full payment, the customer acquires ownership of the asset. When it originally buys the asset for this financing, the Islamic bank may be made to pay the concomitant tax on it by the seller. Similarly, when it consequently sells the same asset to its customer, it is required to pay the relevant taxes pursuant to applicable Philippine tax law, in which it may factor such cost in the pricing of the transacted asset, and thereby making the financing of such asset comparatively more expensive than its conventional counterpart.

In addressing these tax issues, several countries have introduced relevant tax reforms to institute equal tax treatment on both conventional and Islamic financial transactions.

In the UK, through the Finance Act of 2005, “transaction taxes” for acquisition of real estate involving “alternative finance arrangements” are levied a stamp duty land tax (SDLT) only once during the first transactional phase (Islamic Banker, 2014). Likewise, the same reform was also promulgated by Luxembourg which issued Tax Circular L.G.A. No. 55 affording tax neutrality on *Murabaha*, *Musharaka*, *Mudaraba*, *Ijara*, *Istisna*, and *Sukuk* transactions (Chevalier & Sciales, February 24, 2010). In Malaysia, the application of Income Tax Act of 1967 was liberalized to ensure equal tax treatment on all Islamic financing facilities.

COLLATERAL OPTIONS

It should be stressed that the succeeding additional policy options are contingent upon the acquisition or creation of an Islamic bank owned and controlled by the Bangsamoro government. Hence, the period within which they are undertaken will depend on which of the above-mentioned options – take over of AAILBP or establishing a new fully-fledged Islamic bank - the Bangsamoro government prefers.

Collateral Option One: Extension of start-up financing assistance to preferably non-bank Islamic microfinance institutions (IMFIs) through applicable Islamic banking financing facilities by the Islamic bank

Why non-bank IMFIs? Because formal existing MFIs operating under BSP regulatory supervision, such as rural banks, may be prohibited from engaging in Islamic banking business as there is not yet a law under which they can secure a license allowing them to do so. In contrast, non-bank (meaning, no deposit-taking operations) MFIs, either conventional or Islamic, such as those registered with the Securities and Exchange Commission (SEC) and the Cooperatives Development Authority (CDA), have a free hand in crafting their financing modalities to include Islamic financing products and services.

For this, the Indonesian and Malaysian experience can be a source of valuable reference and great encouragement.

Dominated by Bank Rakyat Indonesia (BRI), rural banks (Bank Perkreditan Rakyat Syariah, BPRS) and the *Ulama*-supported Islamic financial cooperatives such as the *Baitul Mal wat Tamwil* (BMT) and the *Baitul Tamwil Muhammadiyah* (BTM)¹⁰², the Islamic microfinance sector has remarkably helped reduced Indonesia’s rate of poverty incidence from a high of 60% in the 1970s to 11.5% in 1996. Even after the debilitating effects of the regional currency crisis in 1997/98, that rate has since settled below 20%.¹⁰³ In 2011, Indonesia’s poverty rate settled at 12.4%.

In Malaysia, the three main Islamic financial institutions at the forefront of the Islamic microfinance sector are Amanah Ikhtiar Malaysia (AIM), Yayasan Usaha Maju (YUM), and the Economic Fund for National Entrepreneurs Group (TEKUN). Other minor players include government development institutions such as Bank Rakyat, Bank Simpanan Nasional and Agrobank. Except for AIM which is a non-government organization but whose activities are nevertheless funded through interest-free loans from

¹⁰² These two microfinance cooperatives alone have a combined membership of some 65 million.

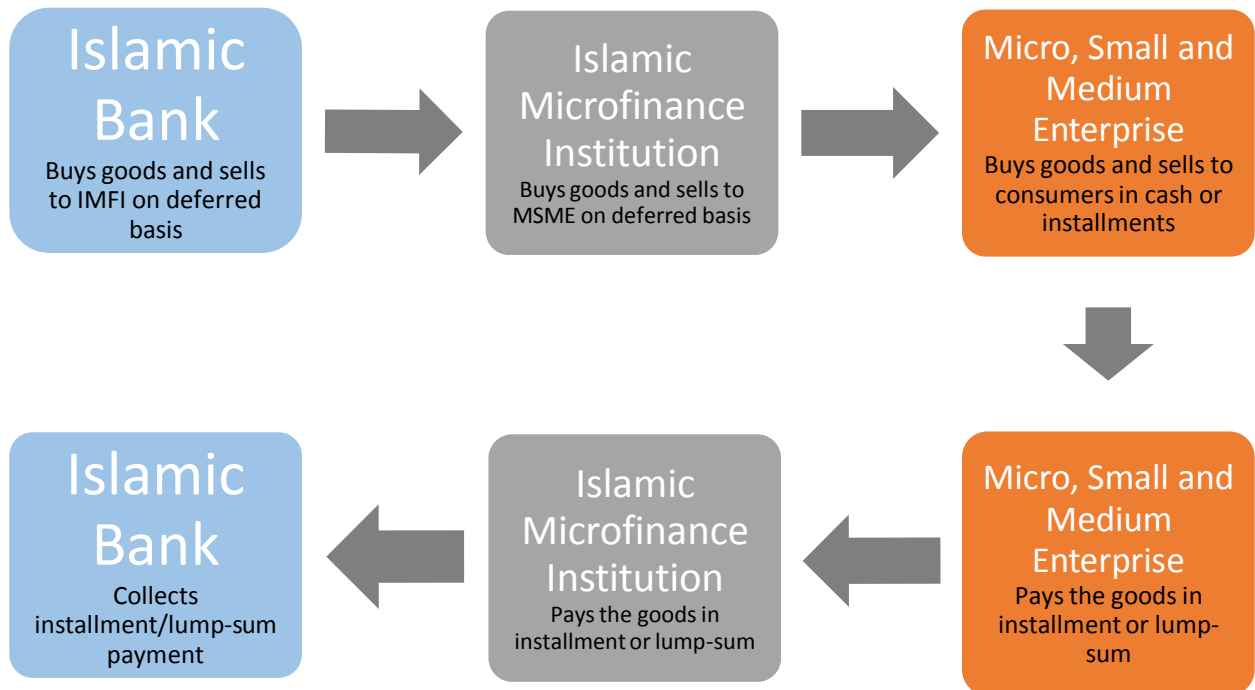
¹⁰³ Hans Dieter Seibel, Islamic Microfinance in Indonesia.

the Malaysian government, the rest are under the Ministry of Agriculture and Agro-based Malaysia. One notable poverty-alleviation strategy used by AIM was its Qard hasan (interest-free/benevolent loan) facility extended to a group of five persons living below the poverty threshold to finance their micro enterprise activities. In addition, private financial institutions led by CIMB Bank and Maybank are also involved in microfinance program. The microcredit facilities used are mostly *Al-Rahnu* pawnbroking financing, *Qard Hasan* loan and *Bai ul-Inah* credit. The micro enterprises in Malaysia constitute more than 80% of all businesses in the country and employ over 1.2 million people. As of end of 2010, total microfinancing outstanding reached US\$255 Million with the number of clients totalling over 570,000.

As far as feasible - which shall be determined by a later study - a minimum of five IMFIs could be organized in every city and province in the Bangsamoro region and extended a start-up capital assistance of not less than PhP500 Thousand each, or a total of PhP15 Million for 30 IMFIs in one city and five provinces in the region. The modalities by which this credit assistance is provided by the Islamic bank must be variably Shari'ah-compliant ranging from the Islamic partnership financing of *Al-Musharaka* and *Al-Mudaraba*, *Al-Ijara* leasing to cost-plus *Murabaha* and *Qard Hasan* benevolent loans depending on the evaluation conducted by the Islamic bank and the nature of funds used for the purpose which, in the case of Malaysia, were similarly Shari'ah-compliant.

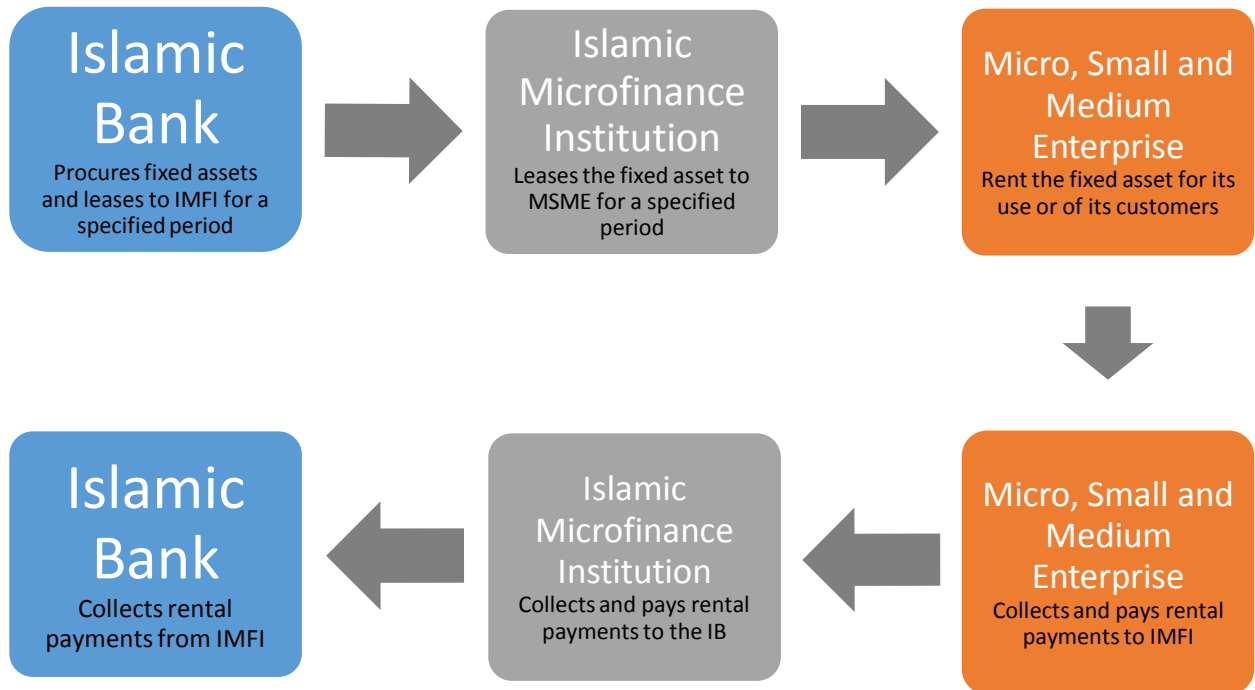
EXAMPLES OF ISLAMIC FINANCING MODES FOR ISLAMIC MICROFINANCE INSTITUTIONS (IMFIs)

Al-Murabaha Working Capital/Credit Line



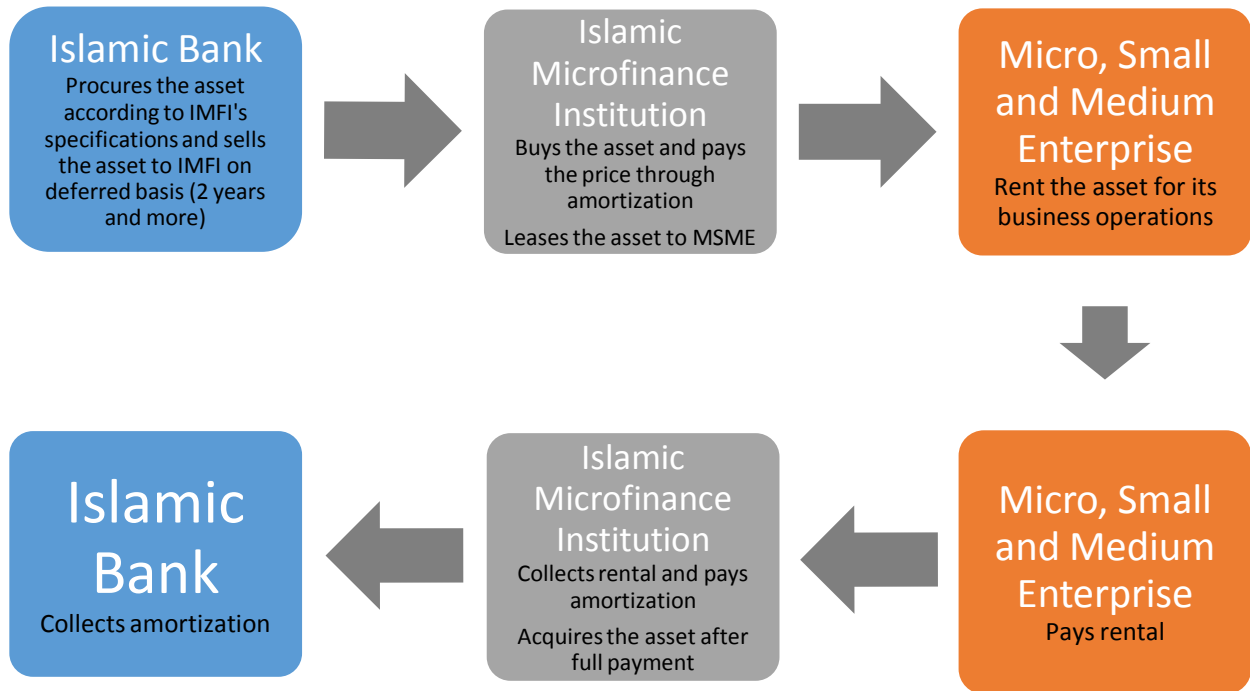
The availment of this financing mode, as it is normally unsecured, should be accompanied by a risk-mitigating measure such as accreditation of financing applicants. Proposed accreditation criteria involving the submission of eligibility documents are enumerated in Annex C. Otherwise, some form of a collateral securing the extension of this financing facility should be required.

Al-Ijara Financing

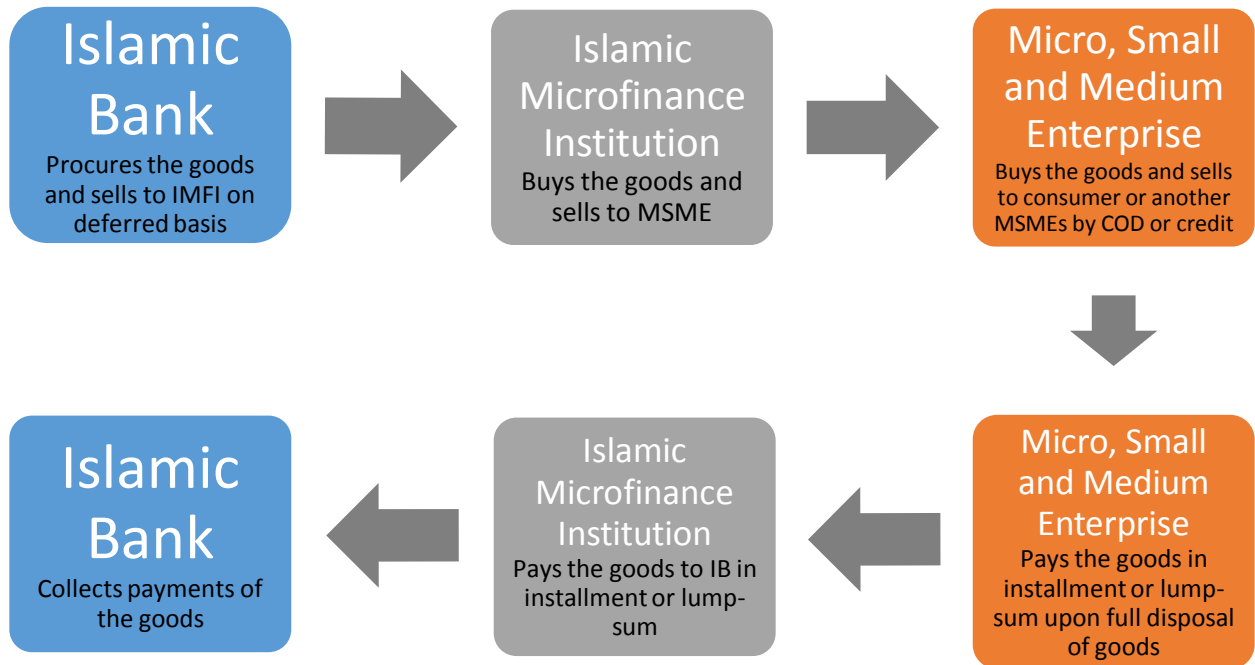


Note: In case the Ijara contract provides an option for the IMFI to purchase the assets subject of leasing, (Al-bai ul-Takjiri) at the termination of the contract, the rental payments made shall form part of the purchase price of the subject asset.

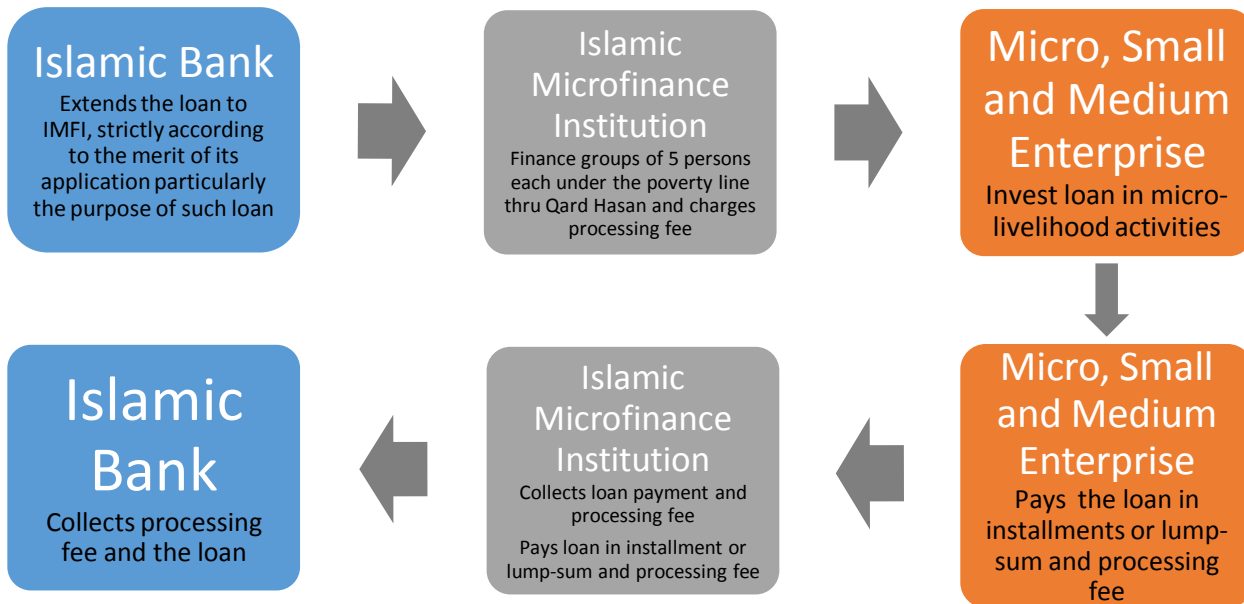
Al-Bai Bithaman Ajil Financing (e.g. warehouse)



Al-Murabaha Trade Financing



Qard Hasan Loan*



*Funds for this financing should come from Zakat or non-deposit sources or non-profit participating deposits.

Collateral Option Two: Extension of Islamic financing facilities to halal-compliant agri-based enterprises to include micro and small halal organic farming ventures in the countryside

As halal and Islamic financial services industries are inseparable twins to help effect the needed change in the socio-economic landscape of the new Bangsamoro region, this collateral option clearly looks tenable. The amount and manner (Islamic banking financing facilities) by which the assistance is to be provided will be on a case-to-case basis giving particular attention to each beneficiary's needs and peculiar conditions. This may require therefore the issuance by the Bangsamoro authority or its Islamic bank of a comprehensive implementing guidelines for this purpose.

The Islamic financing examples for Islamic microfinance institutions as illustrated above can, among others, be utilized to serve the financing requirements of halal-compliant and agri-based enterprises.

A PhP100 Million initial start-up funding for this sector is suggested.

Collateral Option Three: Extension of Islamic Financing Facilities to Other Agribusiness Enterprises

Owing to the agricultural sector's continuing role as the "economic backbone" of the Bangsamoro region in which about 70% of the region's workforce are employed, and contributing the biggest share (63%) to its Regional Gross Domestic Product (RGDP), this collateral option may well be the most significant as it has the biggest potential in reshaping the socio-economic landscape of the Bangsamoro.

Research for this report (Alex Casiple, 2014) indicates that there are still about 150,000 hectares in the region which have remained idle. Developing them into viable agribusiness ventures would translate into at least 150,000 new jobs (1 job per hectare) thereby reducing drastically the region's unemployment rate and poverty incidence. But job creation and poverty alleviation will not be the exclusive objective of Islamic financing – just as importantly, raising the bar of economic empowerment of agricultural smallholders will also result.

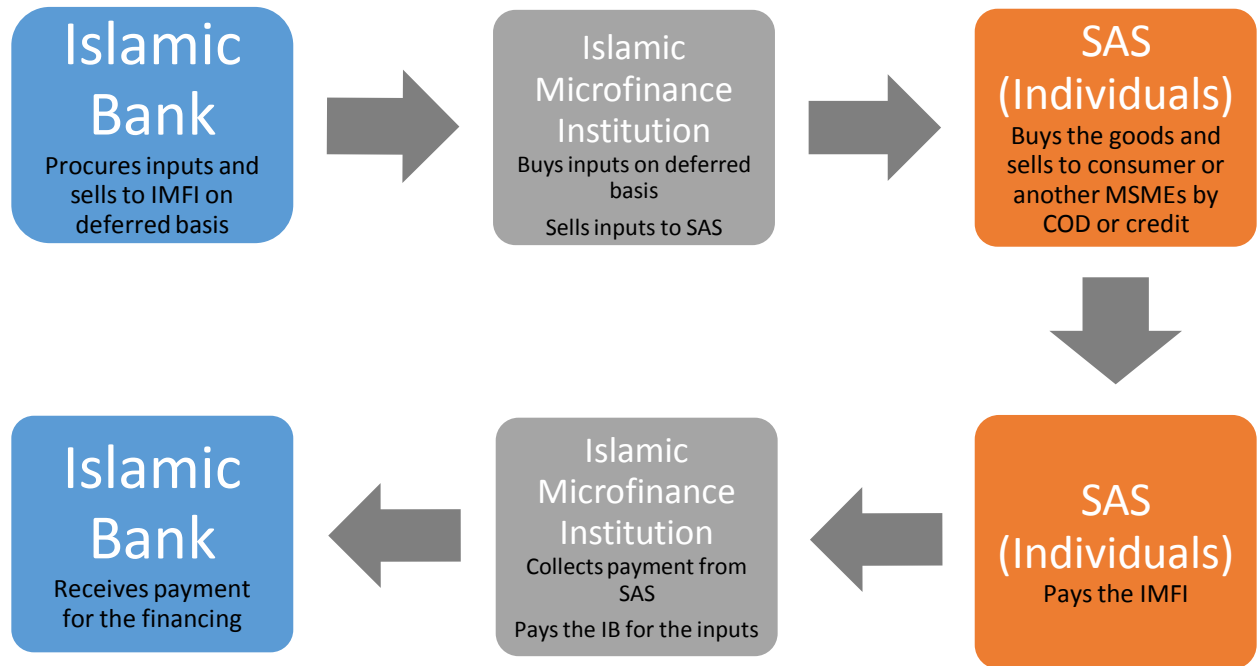
As a pilot, 10,000 hectares could be developed into agribusiness enterprises using, among others, Islamic modes of financing illustrated in the following charts. PhP10,000 could be earmarked for every hectare, for a total of PhP100 Million.

EXAMPLES OF ISLAMIC FINANCING MODES FOR AGRIBUSINESS

Stand Alone Smallholder, SAS (Individuals)

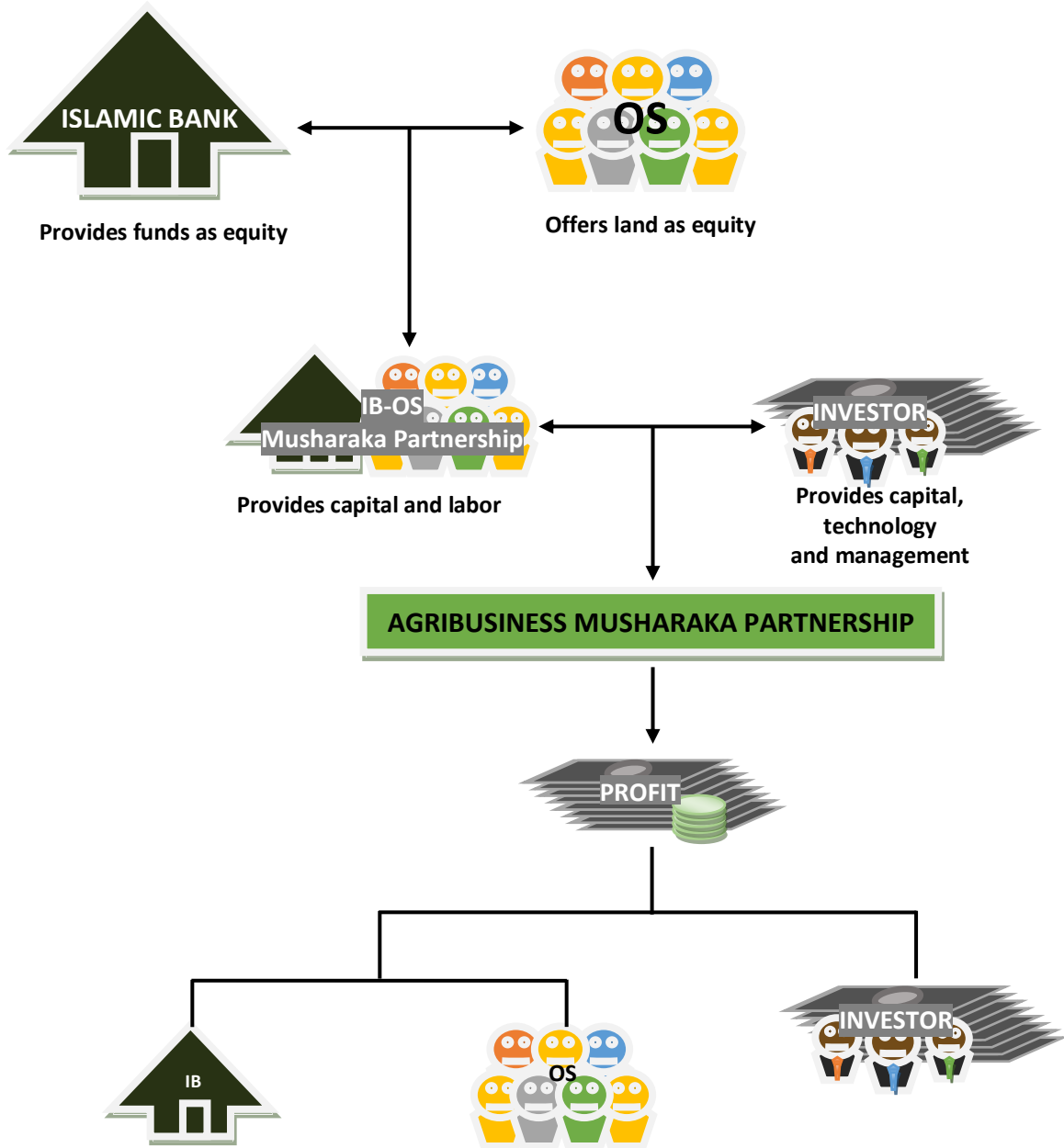
Al-Murabaha Working Capital Financing

(For provision of farm inputs)



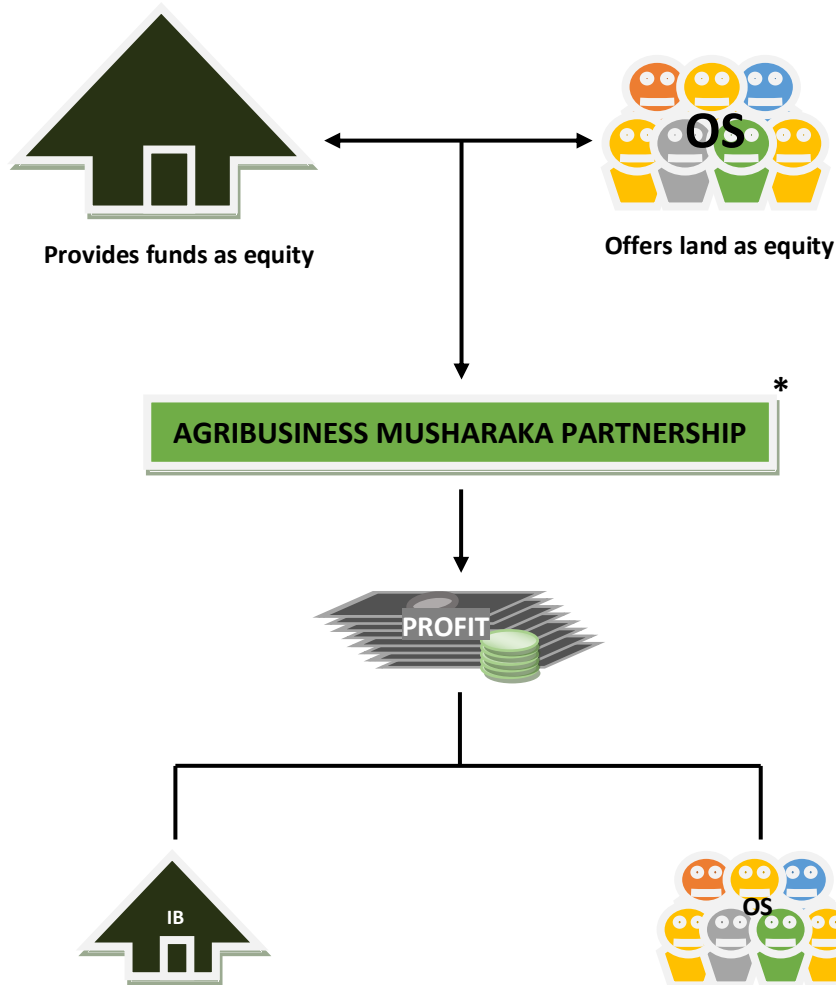
Organized Smallholders (OS)

Al-Musharaka Financing (Diminishing)*



* OS may periodically buy out equity contribution of the IB and end up as the only remaining partner of the investor (Diminishing Musharaka).

The above Diminishing Musharaka financing may have another variation as follows:



This Musharaka variation will require the engagement of the services of a Management Team which would manage the partnership by providing the necessary expertise to ensure the success of the agribusiness venture either under the principle of *Al-Wakalah*, by which the Management Team will be paid with a management fee, or *Al-Mudaraba* Trust partnership, in which the Management Team will share in the profits generated by the agribusiness venture.

Similarly, this variation will also have the same feature as the above-illustrated Diminishing Musharaka by which the Islamic bank equity in the partnership will be gradually bought out by the OS who will eventually acquire full ownership of the agribusiness venture.

INDICATIVE FUNDING REQUIREMENTS

Islamic bank's capitalization	PhP 1,000,000,000
Financing for IMFIs	150,000,000
Financing for halal-compliant agri-based enterprises	100,000,000
Financing for agri-business enterprises	100,000,000
TOTAL	<u>PhP 1,350,000,000</u>

ANNEX 2. TRAINING AND MANPOWER DEVELOPMENT PROGRAM: CONCEPT PAPER

RATIONALE

The advent of Islamic banking in the country's financial milieu has created major challenges for corporate policy-makers and strategists of the Islamic bank and government regulatory authorities.

Among these major challenges is the development of an effective manpower force capable of meeting all the requirements necessary in the full operationalization of the Islamic Bank. In the larger context, this concern shall and must be, in fact, the focal point that will demonstrably spell the difference between the success and failure of Islamic banking in the Philippines.

Against this backdrop, it is thus apparent that the formulation of a manpower and training program becomes not only a compelling necessity but an indispensable requisite as well.

NATURE AND SCOPE

The Program is designed exclusively for an in-bank training exercise which will be carried out primarily to address the peculiar manpower needs of the Islamic Bank. Such needs are specifically identified and classified into various phases and levels from specialized trainings to management courses.

This, therefore, does not include training concerns which are not internally available due to inadequacy in necessary facilities and technical knowhow. For instance, trainings on Islamic capital market operations, *Takaful* (Islamic Insurance), *Sukuk* structuring and issuance, International Finance, Corporate Investments, Corporate Planning and similar areas may be made available by reputable government and private training centers.

OBJECTIVES

The objectives of the Program are to:

- afford Bank employees the opportunity to acquire vital skills and knowledge of their respective assignments and responsibilities;
- imbue Bank employees with positive work attitude to insure corporate cohesiveness and organizational solidarity;
- develop and strengthen the ability of bank employees for optimum productivity;
- evolve a unique corporate culture for the Islamic Bank consistent with its operational principles, character and philosophy;
- serve as a primary determinant of personnel job competence and technical ability; and

- serve as a principal tool by which the entire personnel complement of the Islamic Bank be continuously equipped with all the basic technical manpower requisites necessary in Islamic banking operations.

TRAINING CONCERNS

The training areas identified in this Program are limited to those which could be internally carried out by the Islamic Bank.

In each of these areas of concern, a corresponding Training Manual will be devised. The Manual will contain as far as necessary all key elements such as training systems, procedures, methodologies, reading materials and schedules as well as relevant handouts and illustrations as additional supplements. More importantly, the Manual shall be modulized in specific cases.

The Program shall cover the following training areas:

1. Bookkeeping
2. Cashiering
3. Tellering
4. Project Evaluation and Monitoring Development
5. Treasury Operations and Fund Management
6. Accounting System and Procedures
7. Investments and Accounts Management
8. Bank Management
 - 8.1 Basic Bank Management Course
 - 8.2 Junior Executive Training Course
 - 8.3 Senior Executive Training Course

A training and manpower development program has been prepared by the author of this report and will be made available separately.

ANNEX 3. REQUIREMENTS FOR ACCREDITATION OF ISLAMIC MICROFINANCE INSTITUTIONS (IMFIs)

1. Securities and Exchange Commission (SEC)/Cooperatives Development Authority (CDA) Registration
2. Articles of Incorporation
3. General Information Sheet duly notarized
4. Certification from SEC and CDA that the said IMFI has not been dissolved/Certificate of Good Standing
5. Board Resolution of the IMFI indicating latest election of its officers
6. Audited Financial Statements (last 3 years, with initial of an independent auditor on every page)
7. Statement of Management Responsibility on the correctness of the financial statement of the IMFI duly signed by its president and treasurer
8. Business Permits
9. Certificate of Registration from the Bureau of Internal Revenue (BIR)
10. BIR Tax Clearance
11. Proof of deposit with the Islamic bank

ANNEX 4. GLOSSARY OF ISLAMIC BANKING AND FINANCE

Al-Bai Bithaman Ajil – an Islamic financing principle where an asset is procured by the Islamic bank and subsequently sells it to its customer at a price comprising the principal investment of the bank and a margin of profit, payable on installments or lump sum. It is usually used in financing fixed assets or projects of customers.

Al-Ijara – an Islamic financing principle where an asset is procured by the Islamic bank and subsequently offers it for lease by its customers. If the customer desires at the expiration of the lease contract to exercise the right to purchase the asset subject of lease with all the rentals paid forming part of the purchase price of the asset, an *Al-Bai ul-Takjiri* leasing principle is utilized.

Al-Rahnu – an Islamic financing principle used in pawnbroking where the Islamic bank extends a *Qard Hasan* loan to a customer secured by a collateral usually in the form of jewelry or qualified consumer goods under the principle of *Al-Wadiah* (safe custody) for which the Islamic bank charges the loan client a safekeeping fee during the term of the *Qard Hasan* facility. This is over and above the principal amount of the loan to be paid by the borrower upon the maturity of the loan.

Al-Wadiah – literally means safekeeping, refers to the deposited property, the acceptance of sums of money for safe-keeping in Shari'ah-compliant framework under which it will be repaid.

Al-Wakalah – means agency or the delegating of a duty to another party for specific purposes and under specific conditions in exchange for a pre-determined fee. This Islamic financial principle is widely used by Islamic mutual funds and finance companies.

Bai Al-Dayn – a sale and purchase of Islamic securities and quality debt certificates (e.g. the default risk of the debtor is low and the debt must be created from a business transaction that conforms with Shari'ah). This financing scheme, although accepted in Malaysia, is not widely practiced in the Middle East due to some fundamental differences in opinion as to its Shari'ah application and interpretation.

Bai Muajjal – an Islamic financing principle where the bank sells goods, purchased as per order and specification of the client, to the client at an agreed price payable at any fixed future date in lump sum or within a fixed period by fixed installments. This financing facility is popular among Islamic microfinance institutions in Bangladesh.

Bai Salam – a sale whereby the seller undertakes to supply some specific goods to the buyer at a future date in exchange of an advanced price fully-paid at spot. A *Salam* contract cannot be cancelled once signed.

Bai ul-Inah – an Islamic financing principle where an Islamic bank extends a financing by purchasing an asset offered by a customer with the condition that the customer buys back the same asset

from the Islamic bank after an agreed period comprising the purchase price paid by the Islamic bank plus a profit margin.

Halal – act or product that is permissible under Shari’ah.

Haram – an act or product that is prohibited under Shari’ah.

Istisna – a sale where a commodity is transacted before it comes into existence. It is usually used in a sale transaction whereby an order is issued to a manufacturer to manufacture a specific commodity for the purchases.

Other Islamic banks use *Istisna* in a sale contract between the bank and the buyer of buildings and residential units described in the sale contract and transacted before it comes into existence, payable in installments or lump sum within or after the manufacturing/construction period. The price of the subject asset is fixed before construction/manufacturing begins.

Murabaha – an Islamic financing mode whereby the Islamic bank procures goods and sells them to its customer on a deferred term normally ranging from 30 to 120 days payable in installments or lump sum. This facility is used usually for working capital, manufacturing and trade financing although some Islamic banks in the Middle East use it to finance fixed assets requirements of their customers.

Qard Hasan – an Islamic loan facility which does not carry any interest payment obligation. The borrower’s liability extends only up to the principal sum borrowed although Shari’ah encourages him to share any profit generated out of the utilization of the loan but such is a matter of absolute discretion on the part of the borrower. The Islamic bank usually charges a processing fee to defray administrative overhead for this financing.

Riba – any predetermined fixed return for the use of money.

Rido – a bloody fratricidal clan war between Muslim families.

Salam – an Islamic financing concept whereby goods are bought and paid at spot to be delivered at a specific future date.

Sukuk – a financial certificate which has similar characteristics of a conventional bond with the key difference being that they are asset-backed. It represents proportionate beneficial ownership in the underlying tangible asset(s) of a particular project or economic activity for which the certificate is issued.

Takaful – literally means “guaranteeing each other” or joint guarantee through mutual support and shared responsibility whereby a group of persons agree to jointly guarantee among themselves against a defined loss, popularly based on the Qur’anic principle of mutual assistance (*ta’awani*).

ROAD MAP FOR BUILDING A FAVORABLE BUSINESS AND INVESTMENT CLIMATE IN THE BANGSAMORO¹⁰⁴

1. BACKGROUND

From the viewpoint of the Bangsamoro leadership, political autonomy cannot be achieved without fiscal autonomy. In this respect, a robust private sector is seen as critical. Equally important is the need to ensure employment creation and income generating opportunities for the millions of poor in the Bangsamoro who long for a decent livelihood and a peaceful existence. Again, it is seen that this cannot be achieved without a robust private sector. And the longer-term sustainability of the Bangsamoro regions' natural resources and respect for the natural environment is fundamental in the thinking of the Bangsamoro leadership. Any form of investment, private or public, must take cognizance of this.

In looking at the barriers to investment, industry road maps offer an appropriate planning mechanism. The road maps identify the constraints that have to be addressed, the horizontal (e.g. business environment) and vertical (e.g. common industrial infrastructures) measures to deal with them, and the coordinating mechanisms for the design and implementation of the measures. The road maps for the agribusiness and halal food industries follow this approach.

However, there are common elements of the business and investment climate across all sectors that have to be addressed.

2. BARRIERS TO PRIVATE BUSINESS EXPANSION AND INVESTMENT

The extent of the development challenge in the Bangsamoro is daunting. As indicated earlier, all the economic and social indicators suggest that the Bangsamoro is at the bottom of the heap. This reflects the years of carnage and neglect or mismanagement of the physical and social infrastructures, and the inability to attract the private investment essential for sustainable, inclusive, and equitable growth. Add to this the need to find employment for a growing and under-employed workforce, the MILF troops to be re-deployed, and the potential workers to be resettled; the challenge becomes even more daunting. Some of the workforce will be absorbed into subsistence farming and fishing and informal activities and others employed in public work

¹⁰⁴ This report was prepared by the Foundation for Economic Freedom (FEF) for the Bangsamoro Development Agency (BDA). The report was prepared by Thomas Allen, and draws extensively on the outcome of the *FEF/PCID Workshop on an "Overview of the Business and Investment Climate in the Bangsamoro"* (supported by Australian Aid) held in Davao, November, 2013.

programs. Some will start their own businesses. But most potential workers – largely unskilled and mostly illiterate - will be looking for jobs in private sector enterprises. The success of the transition to an autonomous Bangsamoro will depend to a considerable extent on the ability of the authorities to attract the private sector investment in new or expanded enterprises necessary to absorb the bulk of these workers, and thus help lift families out of extreme poverty.

Geography poses further challenges. As well as posing administrative complications, the dispersed nature of the Bangsamoro region poses transport and other infrastructure challenges that will affect the logistics and cost of doing business. Further, the differing characteristics of the ‘mainland’ provinces and the ‘island’ provinces of the Sulu Archipelago suggest differing strategic directions for their development. Initiatives for trade and investment should essentially build on the individual strengths and characteristics of each area.

Just as there are challenges, there are considerable business opportunities. As indicated in the agribusiness industry report, the agriculture sector offers the bulk of these opportunities, but there are opportunities in other sectors as well, such as mining, forestry, and manufacturing. The exploitation of these opportunities will hinge on creating a favorable business and investment climate, and this will require the Bangsamoro government to immediately focus on dealing with the critical barriers to private business expansion and investment.

2.1. Peace and Order

Securing lasting peace and restoring law and order tops the agenda. Private investment in business activities on the scale needed will not be forthcoming if the security of assets and personnel cannot be assured, and the ability to obtain needed supplies and to move goods to markets is impeded. It is recognized that this will take time, but the Bangsamoro authorities will have to provide a clear signal that it will be able to bring things under control, and illustrate its intent through instituting policies and initiating actions to deal with issues such as disarming and reintegrating combatants, outlawing private armies, resettling displaced persons, and ridding the justice system of discriminatory practices.

The peace agreement with the MILF provides the foundations for this, but only the foundations. The pockets of resistance and banditry still have to be dealt with, and the dealers in drugs, guns, and other illegal trades confronted. The courts – Shari’ah and civil – need to be functioning and seen to be dispensing justice. The police, rather than the army, should be seen patrolling the streets. This will take time.

The approach to securing law and order is beyond the scope of our agenda, and is being focused on at the highest levels. However, it needs to be emphasized that a vibrant private sector will be important in supporting this law and order. This would suggest that, as an interim measure, security zones be set up around key private sector agribusiness ventures and their transport corridors and in selected localities. The Polloc Freeport could be promoted as a security zone for other manufacturing activities. These zones would provide a “safe haven” for business activities. Hopefully, this would only be an interim measure, with the security zones being expanded as banditry and rebellious remnants are reduced to smaller and smaller pockets and ultimately brought under control.

2.2. Physical and Social Infrastructure

Dealing with the critical *physical infrastructure* bottlenecks will also be high on the agenda. Water, land, and air transport facilities need substantial improvement, with a more conscious effort to integrate them into a more seamless logistical network linking production to supplies and markets. This requires a multi-modal approach to transport systems. Power, telecommunications, and water supply are also inadequate, but whose provisions extend beyond geography.

The high cost of inter-island shipping is a major constraint to the competitiveness of producers in all of Mindanao, a result of inefficiencies and poor freight handling facilities in most of the ports, and the lack of competitiveness in inter-island shipping operations. The repeal of the cabotage law and enhanced logistics for RO-RO – where feasible- would be major boosts to competitiveness.

The road network urgently needs to be upgraded. The construction of farm-to-market roads in previously neglected areas has been highlighted in the agribusiness industry report, but other transport modes also need to be rehabilitated and expanded. National roads are less of a problem, as the paved ratio in the ARMM is better than other regions in the Philippines. In contrast, the secondary and tertiary (farm-to-market) roads, the responsibility of local governments, are deficient.

Power outages are common because of the bulk power supply shortage in the entire Mindanao grid. At the retail level, system losses by rural cooperative distributors are excessively high, due largely to poor management. Many communities do not have access to electricity. A similar structural problem can be found in the provision of water supply to urban centers and communities. Water districts are poorly managed and exhibit low collection and high leakages.

Water and environmental management, erosion, drainage and flood control infrastructures are lacking in vulnerable watershed and river basin areas. As indicated in the agro-industries report, irrigation systems are in dire need of repair. The list goes on. The prospects for attracting new private investment and the expansion and efficiency of existing agriculture and other

businesses will be very much dependent on these vital infrastructures being in place. Since the problems cannot be remedied overnight, priorities must be carefully chosen, particularly between infrastructures for social reasons (e.g. access to schools and health services) and for economic imperatives (e.g. access to markets).

The Bangsamoro Development Plan puts considerable emphasis on the rehabilitation and expansion of vital infrastructure. Addressing them effectively will involve looking at the needs in an integrated fashion, and recognizing that in many cases a Mindanao-wide approach to dealing with them will be required.¹⁰⁵ In power generation, for example, scale economies dictate that the Bangsamoro should continue to link to the Mindanao transmission grid, accepting that there is scope for small-scale hydro and other renewable energy sources that can be tapped, particularly in the islands of the Sulu Archipelago. And, of course, there are actions that need to be taken locally to reduce the system losses and improve the efficiency of power distribution through electric cooperatives. Perhaps some of the larger commercial plantation and mining enterprises may want to put in their own facilities (even if only for back-up purposes) and could be encouraged to add extra capacities to provide also for the needs of other sectors in their locality. Addressing the challenges in access to electricity will be critical in spurring the diversification of the Bangsamoro economy, notably in the further processing of agricultural produce and other manufacturing. In addition, good governance of electricity cooperatives will be key.

Similarly, planning for the core transport network will require a Mindanao and even wider regional approach. Decisions on ports and primary roads that link the Bangsamoro to the rest of Mindanao, the country as a whole, and even to other countries, cannot be taken in isolation without severely compromising efficiency. The decisions on local ports (particularly Polloc port which is vastly underutilized) and secondary and tertiary roads and bridges will, of course, be primarily dependent on local conditions and requirements, but will still be influenced by decisions on the primary network.

The watershed and river basin areas require special attention, and lend themselves to the Integrated Development Area approach as outlined in the agribusiness industry report. The Pulangi watershed and river basin ecosystem is the life-blood of the Bangsamoro mainland. What happens in the upper Pulangi river basin – which comprises nearly half the province of Bukidnon – has a substantial influence on what happens in the vast Pulangi agricultural basin and downstream provinces of the Bangsamoro. The river basin also hosts a major dam - the Pulangi Dam - that produces hydroelectric power and supplies water for irrigation. The Liguasan Marsh – the largest wetlands in Mindanao and home to over one million Maguindanaon Muslims – is also an integral part of the Pulangi River Basin. The development (or deliberate conservation) of the Liguasan Marsh exemplifies the complex variables that will have to be

¹⁰⁵ The Bangsamoro authorities should also interact with NEDA, MinDA and other relevant regional and national agencies in planning for those areas where interconnections of Bangsamoro with the rest of Mindanao are vital, such as power, transport networks, and river basin developments.

considered and from which the infrastructure provisions will follow. Obviously, the planning of infrastructure for the downstream provinces of Pulangi in the Bangsamoro cannot be done in isolation of upper Pulangi. The floodings in Maguindanao, reinforced by the run-off of water after extensive rainfalls in upper Pulangi - brought about by the denudation of the forests – and the subsequent erosion and thus siltation of the Pulangi Dam and river systems, underscores this need.

It makes sense to look at the Pulangi watershed and river basin as the focus of integrated ecosystems development, covering land use, water and environmental management, erosion, drainage and flood control infrastructures, irrigation systems, and transport networks. Designated areas for plantation and smallholder agriculture and reforestation would be included in the planning, as would sustainable aquaculture in the rivers and Liguasan Marsh.

The above are the big-ticket physical infrastructure items that will feature in the development plans for the Bangsamoro.¹⁰⁶ However, other support infrastructure should not be neglected, and there are small projects that need not wait for the “master planning” exercise. For example, as indicated in the agribusiness industry report, cold storage and other post-harvest facilities for key high value commodities are generally inadequate, and these may, initially at least, require some Government investment.

Much work has been done on the value chain analyses for a number of local products – see for example the JICA Industry Promotion Study for ARMM and the USAID-Growth with Equity for Mindanao (GEM) Program - and these can be used as a guide to appropriate support infrastructure from upstream (e.g. power, water supply, irrigation) to downstream (e.g. transport, communications, storage) to serve the entire value chain. This analysis could be extended to selected agri-processing and other manufacturing activities (and cover not only support infrastructures but also support services and inputs, including labor). Indeed, it would make sense to work through the value chain with potential larger-scale investors, whose decision to invest may in the end depend on a critical support infrastructure. And it may make sense to phase infrastructure developments around some of the large-scale investments, since they could be the key strategic drivers of development in localities that would otherwise remain depressed.

Possibilities for public-private partnerships in infrastructure projects also need to be explored. Innovative approaches will be required in some sectors, particularly where it involves Islamic financing and/or interacts with critical private sector projects, such as those in large commercial plantations and mining. Some may be quasi-private, in that they are projects that in normal circumstances would be purely private sector, but require a transitional period with government involvement until the security situation stabilizes and throughput enables them to

¹⁰⁶ The infrastructure needs, both physical and social, for the Bangsamoro are addressed in the preparation of the development plan that is now nearing completion. JICA has finished an extensive review of the region’s physical infrastructure, and the MinDA has been engaged in formulating programs addressing Mindanao-wide infrastructure needs, especially for the various development corridors and river basins.

be self-standing. An example could be cold storage and other post-harvest facilities for certain crops. Some may also cross regional boundaries, and thus involve both the Bangsamoro and National governments. We would propose a small team be set up to work with the Bangsamoro and national (including MinDA) authorities to explore these possibilities.

Attention to the ***social infrastructures*** will also be crucial. The Bangsamoro fares poorly on all social indicators, including education achievements. ARMM, for example, has the lowest elementary and high school participation and completion rates in the Philippines. And more than one-third of the workforce is illiterate. The lack of requisite skills and educational attainment of workers will be a handicap in attracting desirable private sector investments.

The importance of developing relevant and good quality *education and training programs* accessible to the masses at elementary, secondary and post-secondary levels cannot be over-emphasized. As well as technical and cognitive learning, character traits formation (discipline, trustworthiness, curiosity, etc.) and universal values in the context of Islamic culture and a society committed to pluralism, should figure in these programs.

As well as focusing on how to keep children and youth in school, the out-of-school youth should be given special attention since they are the ones most likely to be attracted to bandit and rebel groups. Apart from intensive return-to-school campaigns, financially supported vocational or apprenticeship training schemes may be a viable option. The region also desperately needs appropriate skills and expertise in areas of leadership development, business management and entrepreneurship. The mismatch of skill requirements of enterprises and the curriculum of the education institutions needs to be addressed. But the most urgent is dealing with the extremely high illiteracy levels among the adult workforce. TESDA-like programs, as well as utilization of facilities and trainers in private entities operating in the local areas, can create beachheads. Basic literacy and numeracy are prerequisites to enrolment in such vocational programs - the applicability and value of livelihood and skills training are largely diminished where potential trainees have not mastered basic reading and writing skills.¹⁰⁷

Education and capacity building for women will be a key foundation for inclusive and sustainable economic growth in the Bangsamoro. In particular, women's education has proved to be linked higher productivity, higher returns to investment, higher agricultural yields, and a more favorable demographic structure.

And one should not forget the vital importance of a *healthy workforce*. In this respect, the provision of Level 1 water supply to many remote villages can be, and should be, high priority as they impinge on health and sanitation.

¹⁰⁷ The Australian Aid BEAM project in ARMM provides a good framework for approaching basic education needs, noting its recent study on work-force skill requirements of enterprises will help shape the skill-curriculum balance.

2.3. Financial System

Developing a robust financial system is critical. This is the subject of the report on Islamic banking and finance (which also covers conventional banking and finance), so will not be covered here. Suffice to say that without this in place, the ability to get the agribusiness – and indeed other businesses - up and running on a sound footing and sustainable basis would be near impossible to achieve.

2.4. Land and Property Rights

Land and property rights are another core constraint. Approaches to dealing with this are outlined in the agribusiness industry report. Migration and settlement of vast tracts of Mindanao exacerbated land conflicts between settlers, Muslims and indigenous peoples. The liberation movements have been rooted in issues over land and sovereignty. The various laws introduced over the years at the national level relating to the ownership of land have “muddied the waters”, often conflicting with traditional land rights based on customary law. Competing claims over land have been a principal cause of the continuing conflict. Uncertainties surrounding land ownership and access can undermine the ability of the Bangsamoro authorities to promote large-scale investments in many localities, particularly in agri-plantations and mining. Although La Frutera’s banana plantation found ways to deal with the land ownership issue by setting up a corporate venture through the lease of land from smallholders but with due consideration of their culture and traditional leadership, there is no certainty that its approach is readily replicable in other locations, and that it will hold sway over the longer-term. Agumil initially adopted a similar approach for its palm oil plantation, but problems arose when agreements with a Datu were not honored by his successor upon his death - the enterprises’ current model clusters individual growers into cooperatives. As mentioned earlier, the Bangsamoro authorities will initially have to be flexible in the approach used for a specific plantation, modeling it on the nature of the activity and on the population and characteristics of the location(s) where it will be operating.

Of course the protection of property rights extend beyond land and resources. It also encompasses contractual arrangements underpinning business relationships, as well as the dispute settlement mechanisms and rule of law relating to them. Both the formal and informal justice systems operate in the Bangsamoro, and within the formal system, the Barangay Justice System, the Shari’ah Justice System, and the Civil Courts System operate. It is critical that the avenue for settling disputes of various types be clearly articulated and disseminated, and that the appropriate capacity in all these systems is in place.

2.5. Cultural and Environmental Dimensions

Cultural and environmental dimensions of doing business in the Bangsamoro will be challenging for a number of enterprises. Dealing with land and property rights is, of course, one of these challenges. The resolution of disputes, for example, could be through civil courts, Shari'ah courts, or alternative customary modes. Financing could be through commercial banking or Islamic financing channels, if available. Integrating business activities with a community's cultural system and environmental concerns will be a challenge for some enterprises, especially in mining, forestry, and other extractive industries. The recognition of cross-cultural sensitivities and the promotion of trust within an organization will be crucial to the success of many enterprises.

Further, leveraging the cultural and historical ties of the Bangsamoro with Muslim South East Asia, the region can be the "front door" of the Philippines to Brunei, Indonesia and Malaysia, instead of the "back door".

2.6. Business and Labor Regulations

A dual track to approaching business and labor regulations is proposed.

- The first track will focus on the broad options (within the legislative leeway for the Bangsamoro) for the basic business and labor regulations – their nature, application and administration – which will underpin the development effort over the medium to longer-term, and will thus require time and extensive deliberation to formulate.
- The second track will focus on the options for utilizing and modifying the existing regulations and institutions to move quickly on encouraging investment and expanded business activity so as to "kick-start" the development process.

Within the context of the latter, the importance of giving confidence to the existing and new investors that the "rules of the game" will not be changed to their detriment needs to be recognized.

Business regulations and investment promotion¹⁰⁸ merit thorough deliberation. There is a plethora of laws and regulations pertaining to the establishment and operations of business enterprises in the Philippines. They are complex, and among the costliest in the East Asia region. They also afford considerable scope for corruption. There is a nationwide imperative to streamline the processes and minimize the transaction costs involved in setting up a business and the overall costs of doing business. The imperative is even more applicable to the Bangsamoro, where the nature and forms of business activities differ significantly from the

¹⁰⁸ Business and labor regulations will be the subject of an upcoming FEF/PCID Workshop planned for September 2014.

national norm, and where the bulk of business activities are concentrated in the informal sector.

The Bangsamoro Government should fully exploit any flexibility it has in simplifying business regulations, and dispensing with unnecessary or inappropriate ones. It would make a lot of sense for the Bangsamoro authorities and the local private sector to immediately take up the offer of the National Competitiveness Council to set up a Regional Competitiveness Committee for the Bangsamoro.¹⁰⁹ This committee would be tasked with reviewing the business regulations, and designing and implementing competitiveness and productivity programs, particularly through cutting red tape by simplifying procedures underpinning business licensing and operations at the regional and local government levels.

Further, the Bangsamoro Government should also fully exploit any flexibility it has in devising its own regulations and procedures pertaining to investment promotion through incentives and guarantees, and explore the options suitable for the type of business activities that it would regard as priorities. Again, the emphasis should be on simplification and relevance of the incentive offered. Consideration should be given for the adoption of an “across-the-board” approach where the basic incentive provisions are automatically made available for both local market and export enterprises which meet specified, but limited, basic conditions over the entire Bangsamoro territory.

Failing the adoption of an across-the-board approach, the appropriateness of special economic zones¹¹⁰ should be reviewed. If the zonal approach is adopted - and even the current legal framework suggests that the regional government has the leeway to do this - then the appropriate criteria for designating the location of the special economic zones and the appropriate incentives and regulations will need to be specified.¹¹¹

In any event, it would make sense to designate industrial estates or zones in key locations where security can be assured and basic infrastructure can be readily put in place. These zones could be expanded as security is improved. However, many of the agri-based enterprises are likely to be “off the beaten track”, and these should not be discriminated against for the availment of incentives and simplified regulations.

¹⁰⁹ ARMM is the only region in the Philippines without a Regional Competitiveness Committee. Note the International Finance Corporation (World Bank) also can be tapped to support any review of business regulations, drawing on their experience both in the Philippines and overseas.

¹¹⁰ There are various models for these zones, including free trade zones, export processing zones, enterprise zones, single factory zones and specialized zone, such as technology parks.

¹¹¹ The simplified labor regulations and wage setting mechanisms as proposed by Sicat (outlined later in this document) should form part of this package.

As an interim measure, consideration should be given to designating the entire Bangsamoro territory as a special economic zone under the PEZA.¹¹² If this is not possible because the basic criteria for designating a zone cannot be met (for example, concerns about controlling smuggling or infrastructure deficiency), then at least a number of locations throughout the region should be designated,¹¹³ and considerable flexibility given in designating agri-industrial economic zones as potential ventures emerge. In addition, the Regional BOI should designate fairly broad categories of enterprises (e.g. agri-based processing, halal food industry) with limited eligibility criteria for incentive availment.

The importance of *extension services and R&D support for agricultural and marine pursuits and of support programs for micro and small and medium enterprises* must also be emphasized. These activities have been, and will continue to be, important in the economy of the Bangsamoro.

The provision of extension services to the countryside has been hampered by the continued conflict and difficulties in accessing many communities. With the peace and order situation stabilizing, and priority being given to improving access to rural communities, the ability to extend the required R&D, technical, and market support to these communities opens up. However, this assumes that the institutional capacity is in place to provide these services effectively, a capacity that does seem to be prevalent in many parts of the Philippines, let alone the Bangsamoro.

In this respect, it is essential to initially focus the services on key priority areas and activities in the agribusiness sector, particularly halal food production, and gradually build up the capacity within the required institutions. The donor and NGO community – and in some cases the private sector - can be called on to assist in this, and to help build up the appropriate capacity of the service providers.

The Philippine **labor regulations** are, like the business regulations, complex. Many firms find them difficult to comply with. As a result, as pointed out in the recent World Bank Philippine Development Report, “there is high rate of non-compliance on various labor standards, high *de facto* cost of keeping workers, and low formal sector employment generation ...the excessive regulation has also exacerbated the dualism between the formal and informal sectors”, the latter falling outside the Labor Code. Minimum wage rates in the Philippines are also high by a number of standards, “thus contributing to its lack of competitiveness in labor-intensive manufacturing”.

¹¹² The Special Economic Zone Act (R.A. 7916) provides for the establishment of Ecozones under the Philippine Economic Zone Authority (PEZA). The criteria for establishing the zones are fairly strict, and the simplified regulations and fiscal incentives are aimed to facilitate foreign investment in export oriented activities.

¹¹³ The ARMM Government has already designated Polloc port as a special economic zone. It would be difficult to find localities in the Bangsamoro which meet all the criteria for SEC status under R.A. 7196, so some flexibility in interpretation of these criteria will be required

These, and any proposed regulations of the National Government relating to labor, should be assessed for their relevance to the Bangsamoro. Within the scope of the powers of the Bangsamoro Government, various options for labor protection and wage setting appropriate to the conditions in the Bangsamoro should be explored.

In this respect, the Bangsamoro Government should aim to move towards simplified labor regulations and more flexible wage setting. In this context, the relevance of proposals for labor employment zones - which aim to exempt enterprises from the application of minimum wage and other selected regulations – should also be reviewed. Gerardo Sicat, for example, has proposed that special labor employment zones for industrial and agricultural employment be set up in various parts of Philippines. In these zones “requirements of minimum wage, employment regularization, restriction on fixed term contracts, and other forms of labor protection are suspended.... Let us have government put in place humane employment practices that allows workmen’s compensation insurance, social security, and other desirable labor protection clauses¹¹⁴ to be in place as they have been under the labor laws. Let the private sector undertake the construction of the industrial employment zone and allow many of the provisions of the PEZA laws regarding customs and other regulatory requirements for the import of raw materials and other types of access to other labor, including the import of foreign technical labor, so that these areas can attain the highest level of labor supply suited to the labor using industrial operations.”¹¹⁵

While the Sicat proposals refer to labor employment zones throughout the country, it is proposed here that the entire Bangsamoro territory have similar simplified labor regulations, dispensing also with minimum wage setting. If the zonal approach is decided on, even if only for the short term, then the simplified labor and wage-setting regulations should overlay the special economic zone incentives.¹¹⁶

2.7. Business and Institutional Capacity

Building *business capacity* has not been given the attention it deserves, not only in the Bangsamoro, but also in the rest of the Philippines. Even if we get prices and institutions “right” and strip away the bureaucratic red tape, we would still need entities capable of responding to the new profitable opportunities. While foreign and other Philippine entities will be a key part of the mix, for reasons of both equity and political economy it will be important that local Bangsamoro enterprises - particularly the small-scale – participate strongly in the supply response to a reformed business environment.

¹¹⁴ Such as worker safety.

¹¹⁵ To Raise Labor Income and Employment Faster. Gerardo P Sicat, June 2012

¹¹⁶ It does not make sense to have separate labor zones and economic zones- these should be integrated.

Attracting catalytic established domestic and foreign investors through joint ventures and other forms of business arrangements with local entities will be an important means of building local business capacity. Restrictions on the recruitment of experienced expatriate personnel, strict conditions governing the terms under which foreign firms can invest, and obstacles to technology transfer, are all factors which inhibit building of local business capacity, and thus all efforts should be made to minimize these restrictions.

However, relying on these investors for building local business capacity will be nowhere near sufficient. Special programs will need to be put in place by the Bangsamoro Government to foster enterprise learning across the whole spectrum of business activities, although these should initially be focused in the agro-based industry.

As indicated earlier, basic education, apprenticeship, and vocational programs will go a long way to improving the skill base of the workforce. However, enterprise learning is more than just basic education and technical skills, as it extends into understanding how businesses operate and are managed, and what it means to be an “entrepreneur”. It will be a tough job for the Bangsamoro government to build up basic education and vocation programs, and to expect it to have the capacity to also oversee enterprise-learning programs in-house is expecting too much. Other approaches have to be explored.

Some of the approaches that have shown promise in other parts of the world start from the premise that entrepreneurs learn best from the experience of other firms. The matching grants programs adopted successfully in various countries throughout the world are examples of public money being used to catalyze private-to-private learning, not to deliver training programs directly. In these programs, costs are shared - on, say, a 50-50 basis - between the government and the recipient firms, with a focus on inducing firms to learn from other firms. Such schemes are very flexible, and can be used to support a variety of learning mechanisms. In addition to fostering learning at the level of individual firms, they can be used to foster collective learning, such as enabling business associations and other groupings to strengthen the provision of technical and other productivity-enhancing services to their members. Matching grant schemes can also be used to promote R&D, technical transfer, market development, and new products (such as halal food products) at the enterprise level. And they can support in-house training of workers. Matching grants hold the promise of fostering a more inclusive, small-scale enterprise-oriented pattern of participation.

The programs of bilateral and international organizations such as USAID, JICA, ADB, and the World Bank in support of business capacity development and small scale enterprise development – some of which include matching grant programs - generally should also be explored to see how they be effectively integrated into the Bangsamoro industrial development framework. IFC, the private sector arm of the World Bank, has done extensive work on the value chain in the agri-based industries in various parts of the Philippines (including Mindanao), and has helped develop industries from scratch through providing necessary financing and demonstration effects (e.g. the horticulture industry in Uganda). It is suggested that the BDA

bring these donors together at a forum to put on the table the best practices and lessons learned from their business capacity building and support programs, and see how best these practices and lessons can be incorporated into the Bangsamoro development program.

It is not only business capacity that has to be built up, but also the ***capacity of the public institutions*** in the Bangsamoro to plan and deliver on these programs.

Government institutions influence private performance via their impact on risk, transaction costs, and the cost of doing business. Where public institutions are weak – and the risk of arbitrary political actions are commensurably high – the private sector will be hesitant to embark on long gestation projects. Well functioning public institutions can help reduce risks facing enterprises by:

- imparting confidence that the policy regime will remain stable over time by maintaining both predictable policies and social legitimacy;
- defining the rules of the game for public-private interactions in ways that restrain arbitrary action by public officials; and
- providing a judicial framework for monitoring and enforcing private-to-private contracts, often as a complement to private mechanisms for conflict resolution.

As mentioned earlier, where public institutions enmesh with much red tape, the transaction costs of doing business will be high, including through enhanced scope for corruption. Bureaucratic overload fuels corruption as firms pay their way through the inevitable red tape. Arbitrariness fuels corruption as firms bribe officials and politicians in an effort to tilt discretionary decision-making in their favor. Indeed, the challenges of strengthening the institutional underpinnings of private sector development and of fighting corruption are one and the same: to refocus public institutions away from heavy-handed (and often corrupt) controls and towards an approach that aids and supports private sector development.

Within this context, it is important to give confidence to the existing and new early investors that the “rules of the game” will not be changed to their detriment, and this may require some form of “grandfathering” arrangements. However, signaling and convincing investors that the Bangsamoro government is moving in a direction which recognizes the critical role of the private sector in the development effort and aims to make life easier for business enterprises will be the most important factor in this regard.

The steps outlined earlier towards, for example, simplifying business and labor regulations, will go a long way towards relieving the pressures on public institutions. However, they will not be enough. The pressure points within the bureaucratic structure will need to be recognized, and appropriate action taken to deal with them. These pressure points will be closely aligned to the

development agenda, and this is where the initial capacity building efforts and technical support should be focused.

A major challenge will be the transition from the ARMM institutional structures and procedures to the new Bangsamoro institutional structures and procedures. While it may be tempting to dismantle all the existing apparatus and to start from scratch, this would be a big mistake. Yes, cut off the obviously diseased parts of the apparatus and those that are not relevant to the new government structure. Some functioning parts will pass muster and can remain unaltered. Modify the remainder as necessary as you move along. While this may cause some discomfort to the leaders over an extended period, it will allow a smoother transition, and avoid the pitfalls of a capacity vacuum that may never be adequately filled.

Organizations such as the Regional Board of Investments (RBOI) will have a critical role to play, and thus should be given strong support. Although there is scope for reforming its agenda, it is one of the few organizations in ARMM that seems to be functioning effectively.

There will be capacity gaps in the transition and after. These need to be recognized early in the transition so that action can be taken to deal with them. As mentioned earlier, simplifying regulations and procedures will go along way towards dealing with the capacity issue, but there will still be a need for specialist skills for dealing with, and supporting, business enterprises. Often in the transition not enough thought is given to these needs. It is strongly recommended that the Bangsamoro authorities review in the very near future the skill needs and assess the capabilities currently on the ground, and where there are gaps, look for means of dealing with them. This could involve bringing in new skilled personnel, seeking donor support for enhancing capabilities of existing personnel, and/or seeking technical support from outside institutions, at least on a temporary basis.

2.8. Government-Private Sector Interaction

Government-private sector interaction will be critical in business-related policy making. It is suggested that a Bangsamoro Business Advisory Council - composed of prominent businessmen from the national, regional and local levels - be established to advise and interact on a regular basis with the Bangsamoro Government on business and investment policy matters on a regular basis. This Council would not be a substitute, but a supplement, to the Bangsamoro government's interaction with local business organizations such as the ARMM Business Council, the Muslim Business Forum, and the various industry associations. These organizations would have valuable local perspectives on many issues. Some of these bodies could be represented on the Business Advisory Council. The National Competitiveness Council, which has affiliated regional bodies throughout the country, has indicated its desire to have an affiliated body in the Bangsamoro, a role that the ARMM/Bangsamoro Business Council could possibly play.

It may make sense to eventually expand the scope of the Business Advisory Council to include other relevant labor and civil society organizations to enable a more inclusive dialogue on the business development agenda.

3. CONCLUDING REMARKS

The new Bangsamoro Government has the opportunity to set a new inclusive growth path, provided it is willing to take full advantage of the flexibility provided by the basic law underpinning its autonomous status. While it is still uncertain as to how much flexibility it will have, it is clear that the national regulations and policies in many critical areas impinging on agriculture, industrial, and private sector development are far from appropriate for the Bangsamoro. New and innovative approaches more suitable to the unique characteristics of the region should be explored, drawing lessons learnt from local and international experiences.

List of Abbreviations

AAIBP	Al-Amanah Islamic Investment Bank of the Philippines
ADB	Asian Development Bank
AFP	Armed Forces of the Philippines
ARMM	Autonomous Region of Muslim Mindanao
ASEAN	Association of Southeast Asian Nations
BAS	Bureau of Agricultural Statistics
BBL	Bangsamoro Basic Law
BCT	Bangsamoro Core Territories
BDA	Bangsamoro Development Agency
BDP	Bangsamoro Development Plan
BIMP-EAGA	Brunei Darussalam-Indonesia-Malaysia-Philippines East ASEAN Growth Area
BPS	Bureau of Products Standard
BSP	Bangko Sentral ng Pilipinas
BTA	Bangsamoro Transition Authority
BTC	Bangsamoro Transition Commission
CAB	Comprehensive Agreement on the Bangsamoro
CSOs	Civil society organizations
DAF-ARMM	Department of Agriculture and Fisheries ARMM
DBP	Development Bank of the Philippines
DOST	Department of Science and Technology
FAB	Framework Agreement on the Bangsamoro
FAO	Food and Agriculture Organization
FEF	Foundation for Economic Freedom, Inc.
FELCRA	Federal Land Consolidation and Rehabilitation Authority
FELDA	Federal Land Development Authority
FSF	Financial Services Forum
GIS	Geographic information system
GPH	Government of the Philippines
GVA	Gross value added
HID-TWG	Halal Industry Development Technical Working Group
IFC	International Finance Corporation
IMFIs	Islamic microfinance Institutions
IOM	International Organization for Migration
IP	Indigenous People
JICA	Japan International Cooperation Agency
LGUs	Local government units
MBF	Muslim Business Forum
MFIs	Microfinance institutions
MILF	Moro Islamic Liberation Front
MMA	Muslim Mindanao Act
MMHCBi	Muslim Mindanao Halal Certification Board, Inc.

MNLF	Moro National Liberation Front
MSMEs	Micro, small and medium enterprises
NCMF	National Commission on Muslim Filipinos
NGOs	Non-government organizations
NHAB	National Halal Accreditation Board
NSO	National Statistics Office
PCA	Philippine Coconut Authority
PCID	Philippine Center for Islam and Democracy
PNS 2067:2008	Philippine National Standard on Halal Food
PPP	Public-private partnership
PSE	Philippine Stock Exchange
RA	Republic Act
RBOI	Regional Board of Investments
R&D	Research and Development
RGDP	Regional Gross Domestic Product
SEC	Securities and Exchange Commission
SPDA	Southern Philippine Development Authority
SUCs	States Universities and Colleges
WB	World Bank