Policy Brief

partnership for economic policy pep

No. 209 February 2020

How the rural reform of the Peace Agreement will help rural Colombia recover from decades of conflict

By Dora Elena Jiménez Giraldo, Adrián Saldarriaga-Isaza, María Gaviria, and Mayra Alejandra Correa

Key messages

- **Policies in the Colombian peace agreement should help agriculture in the country recover from decades of conflict, and improve wellbeing for rural communities and the nation in general.**
- **The proposed reforms could increase agricultural production by between 15 and 28%.**
- **Increasing taxes for the financial sector to cover the cost of the changes would do the most to boost agricultural production, and close the gap between rural and urban household income.**

Helping rural Colombia recover from decades of conflict

At the end of the 20th century, Colombia was one of the most politically violent countries in the world. Decades of armed conflict in rural areas left countless people living in poverty and a vast income gap between those living on agricultural land and those in towns and cities. In fact, in 2014, rural multidimensional poverty was almost three times urban poverty. In 2016, the Colombian government reached a peace agreement with the biggest guerrilla group, Revolutionary Armed Forces of Colombia (FARC), to bring an end to the conflict.

The peace agreement includes two policy points that aim to support the recovery of the (rural) areas most affected by the conflict by 2030:

- Point 1: Comprehensive Rural Reform, which aims to help transform rural Colombia, support growth in agriculture, and ensure better health and wellbeing for people living in rural areas
- Point 4: Substitution of Illicit Crops, which aims to replace crops, such as coca, which are used to make illegal drugs, with legal alternatives.

A team of local PEP researchers evaluated the impact implementation of these policies could make to Colombia's economy, to income distribution between urban and rural areas, and to potential earnings for rural households.

Photo: UN Women/Ryan Brown

The analysis

The team built a Social Accounting Matrix (SAM) for the year 2014 using information from the National Department of Statistics (DANE) and other sources, including the most recent national agricultural census. This information was combined with data about the Incidence Index of the Armed Conflict, calculated by the National Planning Department (DNP).

The team then developed a Computable General Equilibrium (CGE) model, calibrated to the SAM, to track the effects of the proposed peace deal policy on coffee, corn, cassava, rice, and potatoes (around 55% of Colombia's crop output). The team used the model to simulate two scenarios:

- Base scenario of the Colombian economy
- Policy scenario: agricultural policy changes as per the peace deal

As implementing the policy will mean a rise in government spending, the team also compared financing options for the policy scenario:

- An increase in the direct tax rate on urban and rural households
- An increase in the direct tax rate on urban households only
- An indirect tax on commodities
- An increase in the direct tax rate on the mining sector
- An increase in the direct the tax rate on the financial sector

Key findings

The policy changes can support increased agricultural output in rural Colombia.

- Crop production would increase by an average of 24%.
  - As coffee beans are such an integral product for Colombia, it is expected that increased production would see this industry grow, with exports going up by 11%.

The general economic impact on the wider population depends on how the government finances its increased spending.

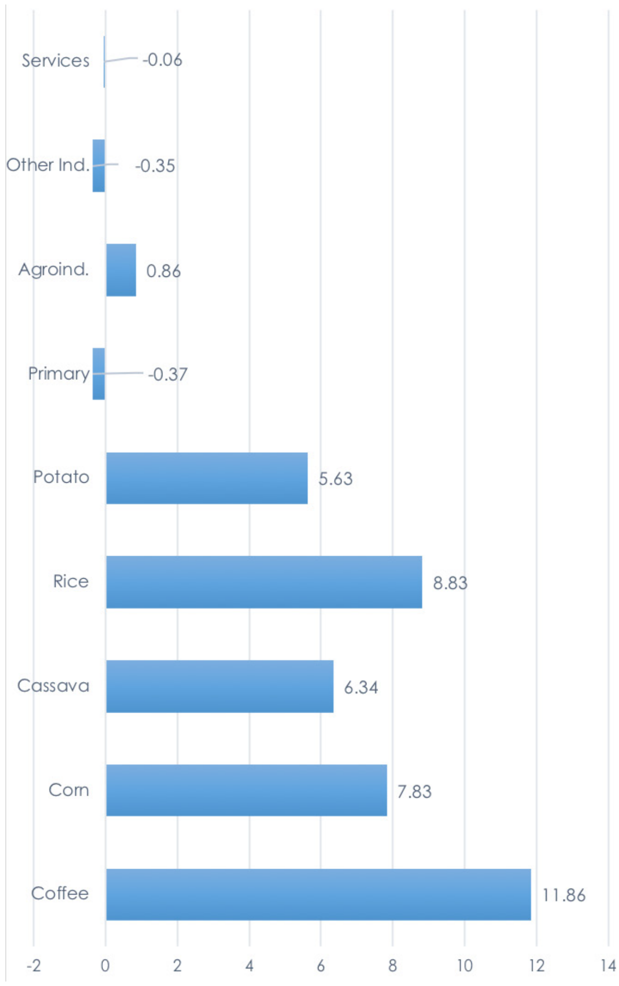
With the exception of a tax just for urban households, all the (simulated) financing options would not only increase disposable income and consumer spending for rural households, but would also reduce the income gap between urban and rural areas.

- A tax on the financial sector would do the most to improve distribution of income between rural and urban zones.
- Disposable income in rural households would increase by 2.4%
  - There would be a negligible effect on urban households.

However, other primary goods, **industries and services that are not set to benefit from the policy changes could see production fall**. In particular, agricultural output might fall by 2.3%. These changes would also have a big impact on the job market.

- Affected areas may see job opportunities increase by 18%
- Those that are not the focus of the policy might see demand fall by 3%
- Employment opportunities decrease by 0.2% overall.

Policy Scenario: change in value added (%)



Source: Author's calculations

Conclusions and **policy implications**

With the agricultural sector being a central focus, **the policies proposed in the peace agreement could have a positive impact on crops in areas that have been intensely affected by armed conflict**. Indeed, production levels are predicted to increase anywhere from 15 to 28%.

However, the benefits of these changes may come at a cost as production may fall in the sectors not set to directly benefit from the policy changes. **Depending on how the policies are funded**, and if new taxes are introduced to cover increased government spending, **rural income could fall and income in urban areas could increase, thus increasing inequality in the country**.

It's essential that the way in which the policies in the peace agreement are funded is given careful consideration. The results of this study show that **increasing the direct tax on the financial sector would reduce income inequality between rural and urban zones**.

To help mitigate the opportunity costs of these policy changes, investment should be made in public infrastructure, such as roads and irrigation systems, **in the areas most affected by the conflict, to support growth and agricultural production**. It is also vital that these areas have access to high quality technical assistance to support the implementation of new crops.

IDRC | CRDI
International Development Research Centre
Centre de recherches pour le développement international
Canada
UKaid
from the British people

This brief summarizes outcomes from MPIA-20290 supported under the PAGE II initiative (2016-2020). To find out more about the research methods and findings, read the full paper, published as part of the **PEP working paper series**.

PAGE II is a global research and capacity-building initiative for Policy Analysis on Growth and Employment in developing countries. PAGE II is supported by the Department for International Development (DfID) of the United Kingdom (or UK Aid) and the International Development Research Centre (IDRC) of Canada.