



## FFTC Agricultural Policy Platform (FFTC-AP)

Available online at: <http://ap.ffc.agnet.org/index.php>

### **Recent Policy Development and Agricultural Support Estimate in Indonesia**

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#### **INTRODUCTION**

Indonesia's agricultural policy is shaped by its Food Law of 2012 and a set of core objectives. The food law sets out the principles of food sovereignty (*kedaulatan pangan*) and food self-reliance (*kemandirian pangan*) as the dominating approaches to food security. The objectives underlying agricultural policy relate to: achieving self-sufficiency in the production of selected staple-food commodities (rice, maize, soybeans, sugar and beef) to assure food security; ensuring food prices are affordable for consumers and accessible across the archipelago; diversifying production and consumption away from carbohydrates (rice and wheat) towards animal-based products, fruits and vegetables, particularly root vegetables; raising the competitiveness of agricultural production and value-added processing; and, improving the welfare of farmers through higher incomes as way to reduce the level of rural poverty.

Indonesia's policy objectives are pursued through both domestic and trade policy measures. Domestic policy measures include the use of minimum purchase prices for rice, sugar, and soybeans, substantial budgetary allocations for inputs, and payments for the provision of services to agriculture generally, in particular for irrigation, research and development and marketing and promotion. A wide range of input subsidies on fertilizers, seeds and credits are used to support agricultural producers. In turn, RASKIN, a targeted "rice for the poor" programme, is used to distribute rice at low prices to poor consumers, including rural areas. The RASKIN programme, and its required distribution system, has provided the government with the flexibility to raise the minimum prices received by farmers while trying to ameliorate some of the price impact on poor consumers. This, however, has come at the cost of increasing budgetary expenditure to finance the programme.

Trade policy measures include both tariff and non-tariff measures. The food law sets out the principles that underpin food trade. It contains provisions restricting staple food imports and exports such that “state food export can only be implemented after fulfilling National Food Reserve and staple food consumption necessity” and “food import can only be implemented if domestic food production is not sufficient or cannot be produced domestically”.

The purpose of this brief is to review the agricultural policy development during the period of 2014-2015. Based on this information a quantitative measurement of the implied support to agriculture is presented. This data and information is summarized from the report published by OECD (2015).

### **Domestic policy developments**

There have been a number of developments in Indonesia’s domestic policy settings in 2014-15. They have not only affected agriculture as there have been changes in fuel subsidies which were initially reduced in November 2014 and then removed in January (with the exception of a fixed subsidy remaining for diesel of IDR 1 000 — US\$8 cents — per litre). This move freed up significant fiscal resources, some of which will be used directly to promote agricultural production, particularly infrastructures.

Indonesia’s new administration, which took effect after elections in late 2014, has restated its commitment to achieving self-sufficiency in five key staples — rice, maize, soybeans, sugar and beef. The new administration, however, has committed to a revised timeframe for achieving self-sufficiency by the end of 2017 for rice, maize and soybeans and the end of 2019 for beef and sugar. It has launched a revised set of policy initiatives to achieve these goals which also include efforts to promote production of other strategic commodities such as chili, shallot, potato, and cocoa. For cocoa, the scheme worth IDR 101.7 billion (US\$8.6 million) is to focus on crop intensification, rehabilitation of old trees, expansion of planted area, farmer’s empowerment and quality improvement.

Indonesia has maintained its price support measures for several commodities. Producers of sugar and more recently soybeans benefit from minimum purchase prices, set for soybeans by BULOG (beginning 2013) and for sugar cane by millers and traders. For sugar, in 2013 the minimum sugar price was maintained at 2012 levels of IDR 8 100/kg (US\$775/ton), and was increased to IDR 8 500/kg in 2014 (US\$719/ton). For soybeans, while regulations were put in place in 2013 for purchases of soybeans by BULOG at IDR 7 000/kg (US\$670/ton), they have not been effective as the policy has not been financed.

For rice, BULOG maintains its market operations and purchasing functions. However, due to the effects of trade barriers associated with Indonesia’s self-sufficiency policies, domestic rice prices have been consistently high compared to international prices and so official purchasing prices have not been renewed over the 2013-14 period. The market price support schemes for rice remain the most important contributor to the longer run significant increases in the level of support in Indonesia, as measured by *Producer Support Estimate (PSE)*, explaining 45% of the total PSE in this country in 2014.

To protect poor consumers, BULOG has continued to distribute rice within the RASKIN system. In 2012, this entailed large budgetary transfers to support the system of IDR 19.1 trillion (US\$2 billion), with IDR 20.3 trillion spent in 2013 (US\$1.9 billion) and IDR 18.8 trillion in 2014 (US\$1.6 billion). However, recent OECD analysis has brought into question the effectiveness of this programme in improving food security and recommended a shift towards cash transfers or food vouchers (OECD, 2015a).

Some of the savings derived from the removal of fuel subsidies have been directed towards investments in irrigation infrastructure. Much of this is targeted towards rice production. In 2015, 10 Governors of rice producing provinces have committed to increase rice production by 11.25 million tons. To support this target, the Ministry of Agriculture has committed IDR 4.2 trillion (US\$ 355 million) to rehabilitate irrigation canals covering an area of 1.5 million hectares, along with investments aimed at "optimizing" 500,000 hectares of existing land for food production. This increased investment is in addition to the current exemptions in place where farmers are not charged for the cost of delivering water from the source to the tertiary system via primary and secondary canals. In 2012, the budget for irrigation infrastructure was IDR 2.2 trillion (US\$235 million), increasing to IDR 3.8 trillion in 2013 (US\$364 million).

Increased subsidies for other inputs and fertilizers have also been announced to help spur production and meet self-sufficiency target timeframes. For example, at the end of 2014 the Ministry of Agriculture delivered direct assistance to rice farmers in 13 provinces, totalling around IDR 2 trillion (US\$169 million). Funds were used to finance 7 800 hand-tractors, 3 000 water pumps, 100 rice-transplanters, along with fertilizer and seed to encourage farmers grow rice. A further 6 100 hand-tractors, and 2 328 units of water pumps have been promised as part of the support to rice producing provinces. Overall, fertilizer subsidies remain by far the most important program through which the government provides budgetary support to agriculture. In 2013 the value of this subsidy was IDR 17.6 trillion (US\$1.7billion), accounting for 41% of total budgetary expenditures provided to support agriculture (both on-farm and agriculture as a whole as measured by the GSSE).

In September 2014 the Indonesian Parliament passed a bill that set out stricter rules on foreign ownership of agricultural plantations. While the bill did not specify an ownership cap (initially, a 30% cap was discussed), the law allows foreign ownership to be capped at the governments discretion on a case-by-case basis taking into account the type of crop, size of producing company and national and grower's interests. Earlier, in 2013 Indonesia removed its value added tax exemptions from estate crops, selected food crops, ornamental crops, and forest products sold in the domestic market.

### **Trade policy developments**

Indonesia restricts the importation of strategic commodities (those associated with self-sufficiency targets) and also imposes taxes on some of its major exports — such as for crude palm oil and cocoa. For palm oil, in the face of falling international prices Indonesia reduced its export tax from 15% in 2013 to 9%, and after moves by Malaysia (a major exporter of palm oil), it temporarily suspended the export tax from October 2014. A similar but simpler

variable export tax regime has been applied to cocoa since April 2010 with a sliding scale based on international prices of cocoa bean in New York. The tax, varying between 5-15% since introduction, has been around 10% due to lower international prices throughout 2014 and into 2015.

Since 2008, companies must be approved by the Ministry of Trade as registered importers to import a range of processed products manufactured from meat, cereal, sugar and cocoa. Similar restrictions were placed on animals and animal products in 2011. In line with the Ministry of Trade regulation on the Import and Export of Animals and Animal Products issued in September 2011, imports of these products can only be done by a registered importer and can only be carried out if the domestic production and supply are not sufficient to meet consumer demand at an affordable price level. In 2014, Indonesia tightened the rules for rice imports, further restricting the ability to do so, after findings of non-eligible imported rice in local markets.

As part of the government's policy on approach for soybeans (incentivizing domestic production and price stabilization for consumers), in 2013 a number of steps were made to regulate the importation of soybeans. The importation of soybeans is allowed only by BULOG, other state owned enterprises, cooperatives or private sector firms participating in the programme of fixed wholesale selling prices.

Indonesia has maintained its quota arrangements for the importation of beef as part of its self-sufficiency targets for this commodity. The quota is established annually for live cattle and, separately, for boxed beef and is based on the estimated shortfall between domestic supply and demand. In the face of high domestic prices, since 27 September 2013 BULOG has been permitted to import beef for price stabilization purposes. This policy also exempted BULOG from the requirement as registered importer. High prices resulted in some increases in both beef and live cattle, however, recent quotas for live cattle imports for the beginning quarter of 2015 show a reduction from 133,507 in quarter 1, 2014 to 100,000. The quota is further reduced to 50,000 live cattle which end up with accelerated beef price in local market from IDR 80 000 (US\$5.7/kg) to IDR 130 000 (US\$9.3/kg) in August 2015. The increase on beef price is also influenced by the policy to ban import of maize temporarily to protect domestic maize producers. In response to this problem, the government approves to import 250 000-300 000 live cattle in quarter 3 of 2015.

On 17 October 2014, the Government of Indonesia issued Law No.41/2014 (a revision of Law No.18/2009) on Livestock and Veterinary Health. The new Law provides for the importation of live animals from zones declared free from communicable diseases, such as foot and mouth disease, revising the older stricter requirement that only allowed imports if the country was declared free from disease. Based on the new Law, beef import from zone-free of Brazil and India is under consideration, with proper quarantine treatments.

### **Agricultural support estimates**

The level of support measured by PSE in Indonesia fluctuates, depending largely on the ratio of domestic prices to those on international markets. However, over the long term the level of

support (PSE) has grown from 3.9% in 1995-97 to 20.6% in 2012-14. The support is provided almost exclusively through market price support and input subsidies (mostly for fertilisers and seeds). The PSE level in 2012-2014 is slightly higher than that in China (19.2%) and much higher than OECD average (17.9%).

The total cost of support (*Total Support Estimate, TSE*) as a percent of GDP increased from 0.8% in 1995-97 to 3.6% in 2012-14. The TSE level in 2012-14, is again slightly higher than China (3.2%) and significantly higher than the OECD average (0.8%). This shows that for Indonesia, with a large agricultural sector and a relatively high level of agricultural support as measured by the PSE, the burden on the economy is relatively high and is growing.

Due to price support policy and restriction on trade of some commodities, on average, prices received by farmers were 26% higher than those observed on the world markets in 2012-14. Poultry, rice, maize and sugar show the highest price support and border protection as reflected in the *Nominal Protection Coefficients (NPCs)*. Single commodity transfers (SCT) were 73% of the PSE in 2012-14. The share of the SCT in commodity receipts is lowest for palm oil, milk and eggs and highest for sugar, poultry, rice and maize.

## CONCLUSION

Recent agricultural policy in Indonesia shows an increasing trend of support to agriculture as reflected in the percentage of PSE and TSE. The level of support is higher than some other emerging economies such as China and is significantly higher than OECD average. The support is provided almost exclusively through market price support and input subsidies. The effectiveness of this type of support in achieving food security objective is subject to question since poor consumers are adversely affected by high prices of food staples. Therefore, government support should be focused on general services support such as investments on infrastructure, research and development, training, certification, and market promotion.

## REFERENCES

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Date submitted: Sept. 4, 2015

Reviewed, edited and uploaded: Sept. 4, 2015