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### INDONESIA RICE POLICY IN VIEW OF TRADE LIBERALIZATION

By:

Mulyo Sidik

Bulog

Indonesia

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**INDONESIA RICE POLICY IN  
VIEW OF TRADE LIBERALIZATION**

**Mulyo Sidik<sup>1</sup>**

**Introduction**

Indonesia archipelago stretches 5,110 kilometers from west to east and 1,888 kilometer from north to south along the equator and consists more than 17,000 islands. Total population is more than 210 million people and around 60% lives in Java island which has only 7% of the total land area. Therefore in country like Indonesia, logistics function has decisive role in determining the successful achievement of national food policy, particularly in ensuring adequate food supply at affordable price. Efforts to attain food price stabilization through distribution of staple food throughout the country is of importance to the national economic development.

Rice is still considered the most important grains in Indonesia since this crop is the staple food for majority of the people. In addition millions of people engaged in rice production, rice processing and other post-harvest activities related to rice. Considering the importance of rice, Government of Indonesia has launched many programs to boost rice production in order to meet the demand, and trying not too much dependent on imported rice.

Success story of Indonesia rice production seems to become a history of government capability to formulate a comprehensive food policy with particular reference to rice, coupled with social engineering program that was able to gear-up people to boost rice production. In addition, important supporting elements ranging from provision of agricultural inputs for rice production such as increasing fertilizer supply, provision of good quality seed, credit with low interest rate etc. played a key role in providing basic support to increase productivity, improving rice quality and minimizing losses. All contributed greatly to Indonesia's self-sufficiency in rice. However, later in the development, many changes have been occurring in Indonesia food policy which directly translated into new implementation strategy. Remarkable impact on the availability of food as well as on domestic market has been noted. The demand for rice keeps moving on the upward trend, in line with increasing population and income of the people. On the other hand production seemed to move more sluggishly and is unable to keep-up with the fast increasing demand. As a result in the 1990's Indonesia has become major rice importing countries with import around 2 MMT annually. Ironically, in 1998 Indonesia had changed its status from rice self-sufficient country to become the largest importing country, after they recorded import nearly 6 MMT.

This paper briefly reviews Indonesia rice policy including the latest development in rice trade that affect the flows of rice into the country, new role and responsibility of Bulog and its impact on the food security.

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<sup>1</sup> Jl. Gatot Subroto 49, Jakarta 12950, Indonesia

## **Rice Policy in the Context of Food Security**

Rice has been considered not only as a trade commodity but also political commodity. During Soekarno era, the first president of Indonesia used rice as a vehicle to gain international support for Indonesia global political policy. As realization thousands tons of rice was shipped to other countries as a gesture of solidarity and to get positive response to strengthen Indonesia international policy.

The New Order regime led by Suharto has looked rice from different angle but still placed rice as one of the most important political instrument. Therefore in the early seventies programs to increase rice production were launched as an integral part of comprehensive food policy with ultimate objective to strengthen food security and alleviate poverty. Rice had to be made available at all time, in every place at affordable price. Rice policy at this period covered various aspect from inputs of production by providing seed, fertilizer, pesticide and financial support through special credit line set up in government banks with low interest.

Bulog used to be a para-statal organization with its main function to stabilize price of basic food commodities in line with government food policy. In executing this tasks Bulog implements buffer stock strategy, which buys rice at floor price level during harvest season to adsorb supply to prevent declining price. This farm gate price is set-up well above the production cost, aiming at ensuring farmers profit thus providing a better income for rice farmers. In the leaning months market intervention was conducted to smooth-out price fluctuation, as an effort to maintain affordability of lower-income groups to ensure their household food security.

Domestic procurement carried-out by Bulog basically to guarantee market for rice farmers to sell their product and to purchase rice for Bulog operation in supplying rice for public service obligation and for national stock reserve. Bulog was supported with special credit line set-up in Central Bank (Bank Indonesia), therefore Bulog could purchase rice without any difficulty. Farmers were very happy since they received significant subsidy through cheap fertilizer, pesticide and financial support during planting season and guaranteed market for their product.

By implementing rice policy and supported with large investment for improving irrigation and massive subsidy provided by government, rice production increased significantly at the rate of more than 4.5% in 1969-1990. These all-out efforts to boast rice production was culminated in 1984 when Indonesia was pronounced to be self-sufficient country in rice and President Suharto received an award from FAO for the country achievement. In 1984 Indonesia rice production was million metric tons (MMT), and BULOG had an ending stock more than 3.0 MMT, the largest ending stock in the history of this organization . It was the time when food security in this country including households food security was considered very strong, and the primary source of the food supply particularly rice came from domestic production. Many privileges were given to Bulog, among others monopoly right to import basic food commodities such as rice, sugar, wheat, soybean, corn etc.

More than three decades the price stabilization strategy was considered effective and contributing significantly to socio-economic stability which provides strong foundation for economic development. Empirical data showed that favorable conditions had stimulated remarkable increase in the contribution of agricultural sector to GDP, which grew more than 5.7% per year during 1978-1986. All sub-sector of food crops, cash crops, livestock and fisheries all enjoyed such conducive environment and progressing rapidly. Government had placed agricultural sector as

back-bone of economic development and vehicle to encounter poverty and malnutrition, particularly in rural areas. During this period Bulog had the monopoly right to import rice and other basic food commodities such as sugar, wheat, corn and soybean. Later in the development one by one these commodities was released to private importers and Bulog had no longer monopoly right for importing those commodities including rice. The argument raised by scholars primarily lingered on the accountability, transparency and efficiency of Bulog operation. They suggested that direction on Indonesia food policy should move towards more open and fair in international trade of rice and other commodities.

Economic crisis hampered Indonesia and other countries had severe impact on every facet of Indonesia economy. Industrial sector and agricultural sector were hit and many of them had closed down their plants. Further down, numbers of poor people rose significantly and there numbers of malnutrition prevalence increased rapidly. Such conditions forced government to change its strategy particularly on food policy, and it translated, among others by rationalizing the price stabilization strategy. Rather than providing general price subsidy through what so-called market operation at which government intervene the market by distributing low price of rice, a targeted subsidy program through special market intervention and later changed to rice for the poor (*Raskin*) was introduced. This program was specifically design for strengthening food security of the low-income group and the poor family. A set of criteria was used to determine target beneficiaries and the one eligible to receive this subsidized rice can get the ration 20 kg per family per month, with the price of Rp.1,000.-. The program has been launched since 1998 and annually government provides around 2.2 MMT rice distributed to the poor with total subsidy approximately Rp.4.6 trillions .

As indicated earlier basically implementation of Indonesia food policy covers the following:

1. Implementing domestic price support by guaranteeing market for rice in terms of floor price to support farmer to improve their income and to stimulate rice production. This price is reviewed adjusted annually to accommodate inflation rate which affect cost of production and also the changing of rice price in international market. On consumers side a ceiling price is set-out to maintain price stability at affordable level, particularly for the low-income groups. During leaning months rice price tend to increase due to short of supply, and to prevent excessive increase in price government through Bulog would intervene the market by releasing its stock at price level lower than the prevailing market price.
2. Control rice import. Considering free flow of rice after deregulation of rice trade, with zero percent tariff had increased downward pressure to domestic rice market, government has decided to manage rice import by imposing import tariff at around 30% (Rp.430,-/kilogram or around US\$45/ton) in 2000. The tariff should be reviewed and evaluated routinely to verify its impact on domestic rice market as well on farmers' income.
3. Provision of subsidized rice for the poor. Targeted rice subsidy through Rice for the Poor (*Raskin*) program aims at providing support to the fulfillment of minimum rice requirement for poor family. Ration of rice at the amount of 20 kg/month/family is intended to avoid malnutrition among poor family, as a part of the social safety net program which was initiated after the crisis in 1997.
4. Diversification of consumption. Recognizing dependent too much on rice as source of energy for majority of the people may have a negative impact on rice production and national food security as a whole. To meet constant increasing demand on rice due to increasing income and population growth, Indonesia has to import million tons of rice annually. Therefore diversification on consumption has to be started in a more serious manner and supported with program to increase production of other source of

carbohydrate crops.. Indonesia, in fact is rich in other sources of carbohydrate such as sago, cassava and other tuber crops. To implement this policy various programs to boost production of other food crops have been launched since 2000.

### **Rice Trade Liberalization: Whose Get the Benefit?**

As indicated earlier, the Government of Indonesia has deregulated trade of food crops, and liberalized trade of those commodities including rice. Monopoly right which used to be enjoyed by Bulog has been abolished, with expectation that such moves can reduce domestic barrier to entry and exposes domestic producers to international competition. Furthermore, government expects that the policy would promote trade, increase market access and economic efficiency and at the end improve consumers' welfare. It should be pointed-out, however, liberalizing rice trade in relatively short period of time seemed to have more negative than positive one.

Statistical data showed that at zero percent import tariff (which in fact far beyond the WTO or AFTA arrangement which allow tariff up to 120% for rice until 2003) the quantity of rice import had doubled from at the average of 1.5 MMT per year in 1995 – 1997 to more than 3.0 MMT in 1998-2001. The figure of rice import remained high even until recent years averaging around 2.0 MMT. Those statistical data indicated that import dependency grew from 4.3% to 9% in 1995 – 1998, which was certainly not a good sign, recognizing too much dependent on import may jeopardize domestic rice producers. In addition, Government argues that such a situation was considered dangerous to national food security, knowing that rice in the international market is relatively limited and frequently called thin market.

On the other hand Indonesia rice production declined significantly as compared to sharp increased during 1980's. In 2002 for instance, rice output was 51.4 MMT, approximately 4.5% below the production in 1996. Rice production was low as compared to previous decade, particularly after El-Nino and La Nina phenomena hit Indonesia at the same time when economic crisis hampered this country. In addition some argued that uncontrolled rice import with relatively low tariff coupled with low price of rice in the world market had brought about domestic rice price relatively depressed. Such a low price became disincentives to rice farmers, and it might have long term effect on rice production in Indonesia which can jeopardize national food security. Liberalization was frequently accused to be responsible for low productivity and the decline in rice production. Figures on rice production and rice harvested areas as depicted in Table 1

**Table 1. Rice Harvested Area and Rice Production in 1990 – 2003**

| <b>Year</b> | <b>Harvested Area (000 ha)</b> | <b>Yield (Tons/ha)</b> | <b>Paddy Production (MMT)</b> | <b>Milled Rice (MMT)</b> | <b>Rice Import (MMT)</b> |
|-------------|--------------------------------|------------------------|-------------------------------|--------------------------|--------------------------|
| 1990        | 10,502                         | 4.30                   | 45.179                        | 29.336                   | .029                     |
| 1991        | 10,282                         | 4.35                   | 45.689                        | 29.048                   | .178                     |
| 1992        | 11,103                         | 4.34                   | 48.240                        | 31.356                   | .634                     |
| 1993        | 11.013                         | 4.38                   | 48.181                        | 31.318                   | 0                        |
| 1994        | 10.734                         | 4.35                   | 46.641                        | 30.317                   | .876                     |
| 1995        | 11.439                         | 4.35                   | 49.744                        | 32.334                   | 3.014                    |
| 1996        | 11.569                         | 4.41                   | 51.101                        | 33.215                   | 1.090                    |
| 1997        | 11.141                         | 4.43                   | 49.377                        | 32.095                   | .406                     |
| 1998        | 11.613                         | 4.17                   | 48.472                        | 30.537                   | 5.765                    |
| 1999        | 11.963                         | 4.25                   | 50.866                        | 31.118                   | 4.183                    |
| 2000        | 11.793                         | 4.40                   | 51.898                        | 32.345                   | 1.513                    |
| 2001        | 11.415                         | 4.39                   | 50.181                        | 31,283                   | 1.400                    |
| 2002        | 11.521                         | 4.47                   | 51.379                        | 32.369                   | 3.100                    |
| 2003*       | 11.453                         | 4.53                   | 51.849                        | 32.697                   | 2.000                    |
|             |                                |                        |                               |                          |                          |

Notes : a) Milling recovery rate of paddy to milled rice before 1998 was 0.65 and 0.63 after 1998.

b) MMT : million metric tons

\*) Based on third forecast of Central Statistics Agency

Source : Central Statistics Agency (2003)

Recognizing the negative impact of liberalization of rice market government was under great pressure to make a concrete step to protect domestic rice farmers from the flood of rice import. Government started imposing import tariff in 2000 at the level of approximately 30% of the world rice price. The primary objective of this tariff policy was to protect farmers from further decline in price due to deregulation of domestic rice market, and low price of rice in the world market. However, the effectiveness of import tariff was questionable since it seemed to have minimal effect on the free flow of rice into domestic market. It appears inability to enforce the implementation of tariff policy and weak coordination and in-efficient institutional arrangement had caused rice smuggling or under invoicing which had contributed to the excessive flow of imported rice to domestic market, even during the harvest season. Price disparity between international rice price and domestic retail price in Indonesia had speed-up the flow of rice into Indonesia. The direct impact was that rice price in domestic market fell below the official supported price and Bulog was accused for not being able to anticipate such conditions.

Opening domestic rice market freely also caused price fluctuation in international market directly transmitted to domestic price, which may cause price instability. When the world market reached its high level inability to shield off domestic market is certainly has negative impact on household food security of low-income family due to their low purchasing power. Empirical data showed that the world rice price was much more volatile than domestic prices over the past two decades. Such situations would pose poor- family to high degree of risk of price instability and furthermore might increase prevalence of malnutrition in this country.

Another argument on the impact of liberalization was the fact that Indonesian farmers were mostly subsistence farmers who only have very small land with average ownership less than 0.5 ha per family. Uneven competition between farmers in developed countries and Indonesian farmers and farmers in most of developing countries was even more by looking at the access to information, infra-structure, technology and human resource. Thus they are really not in the same level of playing field and certainly incomparable and farmers in developed countries even received much more subsidy from their government than their colleague in developing nations. Therefore liberalization appears to give more benefit to farmers in developed- rather than in developing countries. Free trade liberalization is often accused of bringing-about remarkable increase in food crops importation, reduced incentive and producers income and triggered urbanization of landless labors and poor farmers to the neighboring cities (Nainggolan, 2000).

Liberalization of agricultural commodities trade particularly rice has to take into consideration various important determinant factors; among others the 'status' of rice in the nation from socio-economics and political perspective. A combination of trade policy and price stabilization policy which usually translated into implementation of buffer-stock strategy, ensuring adequate supply of rice, provision of subsidized rice for the poor to ensure household food security are among the most commonly policy instruments implemented in most rice eating countries like Indonesia. It is considered too risky leaving rice price fluctuates erratically due to shortage of supply as effects of pests, or natural calamities or other reasons that cause surge in price in international market. Since it may destabilize price in domestic market and disrupt political and stability in the country due to its high degree of social cost and political consequences.

Recognizing the political and socio-economics implication of rice economy, government has to be more careful in formulating such a policy, whether it be producer- or consumers bias. From producer's side keeping the floor rice as high as possible is the most reasonable way in order to maintain farmers income and level of welfare. It would not be matter if the guaranteed price has been well above the world price, providing there is a great effort to discourage rice import and adherence to rules and procedures of import. On the other side, consumers' demands affordable price with reasonable quality of rice, and government still has to provide rice ration through targeted subsidy program or public distribution system of subsidized rice for the poor.

Indonesia still has the comparative and competitive advantage to grow rice, and rice is still the most labor-intensive agricultural activities that can be considered the best vehicle for rural development. Number of peoples engaged in rice production and post-production activities including processing, storage, transport and distribution is enormous. Adsorption of unskilled labor in rural areas and its potency to reduce urbanization are great, providing there is supporting policy that can provide environment conducive enough for maintaining rice production. Therefore it is obvious that government of Indonesia has been placing increase of rice production to keep up with the growing demand as one of the highest priority in agricultural development.

Self-sufficiency in rice and other food crops is no longer placed as national goal in agricultural development, although once in a while it is used as political jargon. It should be pointed-out, however, recognizing the great importance of rice in Indonesia economy and political stability in the country principle of self-reliance has become more frequently used as motivation to increase production. It means domestic production is still be used as a major source for meeting rice consumption for the people, which reaches more than 130 kg/capita/year. Should there be a shortfall in domestic production due to various reasons, rice import can be carried-out both by government and private importers.

### **Recent Development in Rice Policy**

As indicated in the previous section, implementation of rice policy is adjusted in line with government food policy. Institutional change has been aired since the late nineties, particularly proposal to restructure Bulog. After intensive and long winded discussion President has come to decision to agree on the proposed Bulog reorganization. As a realization since January 2003 this strong and powerful institution has officially changed its status from a para-statal agency to become State Owned Enterprise (SOE). Since then Bulog has dual functions namely to conduct public service obligations to carry-out business as commercial organization. Under its new purview Bulog still retains its public service function to distribute rice for the poor under Raskin program, and to maintain national stock reserve to encounter food shortage during natural disaster, social unrest or others. In addition Bulog is allowed to enter into trading activities of various strategic commodities as a pure profit making institution, as far as government gives the mandate to do so.

As a business entity Bulog has to compete fairly with other company either as rice importer or other food crops business activities, in order to generate income which has to be contributed to state budget. In 2003 apparently most of Bulog activities is still dominated by the implementation of public service responsibility. It should be noted, however, with the changed status, Bulog is no longer responsible for price stabilization of basic food commodities or in improving farmers' welfare. This new tasks has to be disseminated to the people, academia, observers etc. since most of them still have wrong perception on Bulogs' responsibility particularly in food price stabilization. Although it is true that ability of Bulog to maintain farm-gate price at the guaranteed buying price (used to be floor price) will contribute significantly to the farmers' income and encouraging farmers to improve rice productivity which in turn increasing rice production.

Government in 2004 has changed the level of guaranteed price from Rp. 1,500.- /kg for paddy (un-husked rice meeting government standard quality) to Rp. 1,700,-/kg effective January 2004. With this new reference in buying price the price for milled rice has also increased to Rp. 2,750.- /kg. As a comparison the price of medium quality of Thai rice in the world market is US\$180 or equivalent to approximately Rp.1.600.-/kg and with Rp.430,-/kg import tariff the Thai rice can be sold in the retail price in Jakarta at Rp. 2,150.- or Rp2,200.-. Therefore, low price in the world market may add complication in the procurement policy implemented by Bulog. This organization is frequently accused to have preference towards imported rice for its operation in distributing rice to the poor and armed forces, as compared to domestic rice since rice import can generate a better profit. In fact rice import is only complementary to domestic procurement; meaning import is conducted whenever domestic procurement is not enough for fulfilling Bulog public service obligation. Annually Bulog procures rice from domestic production ranged between 1.75 to 2.0 MMT in milled rice term or approximately 6-7% of the total rice production

Another significant progress recently announced by the government is the control of import of rice. Recognizing the free flow of rice import to domestic market has number of negative effects, government decides that since January 2004, rice can only be imported one month before and two months after peak harvest which runs from February to May each year. The decision were made by Minister of Trade and Industry and Minister of Agriculture who specifically described the period of peak harvest of rice, in response to public demand to abolished import of rice during harvest season.

In addition there has been an intensive discussion to propose an increase in import tariff to Rp.510.-/kg (approximately US \$55/ton). The underline policy objective of this proposal is to protect domestic rice farmers from competing with cheap imported rice, which cause disincentive to farmer to increase rice production. The proposal so far has not been decided by Minister of Finance, thus the import tariff is still pegged at Rp.430.-/kg. or approximately US \$45/tons. In addition to proposal of new import tariff it is expected that a new rice policy will be announced by government in January before harvesting season, probably to replace Presidential Instruction Number 13/2003.

### **Concluding Remark**

Considering the importance of rice in Indonesia, as main staple food for majority of the people, million of peoples engaged in rice production and post-harvest activities, Government of Indonesia is considered rice policy one of the most important policies in national development. Numbers of policy instruments have been launched with primary objective to strengthen food security based on household food security. It is obvious that in order to implement such policy, strategy to increase food production especially rice is paramount to ensure availability of food.

Recognizing access to food economically can only be achieved if peoples have enough purchasing power, improvement of income especially farmers, is another step to achieve the underline objective of the food policy. Guaranteed market for rice produced by farmers using procurement price (used to be floor price) is another form of mechanism to provide a better income. On the other hand to protect consumers from uncontrollable price surge, a ceiling price is used for guideline in intervening the market conducted by Bulog. Although such policy has raised number of rational arguments in terms of its effectiveness, and cost efficiency, but it empirical data showed that more than three decades such policy has been able to provide price stability and relatively strong food security. In this regard Bulog has played a key role in maintaining price stability at both producers and consumers for more than 30 years, until recently when farm gate price fell below the guaranteed price. Bulog defendant argues that free flow of rice after market liberalization and low price of rice in the world market contribute to inability of this organization to protect procurement price. In addition buying price has been set at relatively high level even higher than prevailing import parity price. On the other hand special credit line (Central Bank Liquidity Credit = KLBI) to support Bulog procurement activity has been abolished that made this agency getting credit with commercial rate.

Reorganization of Bulog to become state owned enterprise has left question on the role of Bulog in food security analysis and food policy debate. This organization for more than three decades has played a key role in discussion to formulate food policy and food security. Over the years food policy and rice policy in particular have been changing rapidly, often these changes have been made without deep and thorough analysis or even without considering socio-economic and political implications to implement it effectively' Abrupt decision to make policy reform apparently has weakened government 's institutional capability in achieving national food policy objectives. Moreover, since the Ministry of Food and Horticulture was abolished in 1998, it

appears that there has been no single institution responsible for formulating comprehensive and coherent food policy. It is true that several ministries have been involved in food policy but each has different vision and objectives which add another complication in formulating the policy. It is not surprising to note that rice policy or agricultural trade policy changed so frequently in the past three years, which increase the degree of uncertainty exposed to farmers and food consumers. Therefore it is the time that government should realign itself and starts to assign institution for formulating comprehensive and coherent food security and food policy for the benefit of the country.

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