2.2 The Indonesian experience with rice price stabilization

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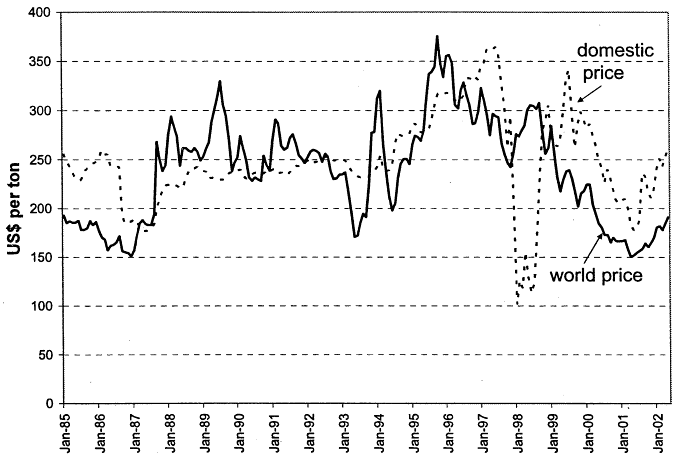
Summary

What has been done? Indonesia pursued rice price stabilization through two instruments used simultaneously: (i) intervention in marketing through public storehouses managed at a local level (ii) monopoly control over international trade. Price stabilization protects both consumers and producers by maintaining rice prices within a predetermined band and by widely disseminating floor and ceiling prices. Stable and low rice prices were a major objective of the government following the period of economic and political instability that came to an end in the mid-sixties. The rice price policy can be split into several periods, corresponding to changes in the country's context. These changes in turn have influenced the policy's implementing agency's objectives and constraints.

How has it been implemented? Rice price stabilization was implemented by a special agency created in 1968 (BULOG). BULOG managed a nationwide network of local agencies and district-level warehouses (DOLOG), which enabled it to store substantial quantities of rice. DOLOG warehouses bought rice to bring prices in rural markets up to the floor price. BULOG procured rice paddy from farmers' cooperatives as well as from private traders. Farmers were encouraged to establish village cooperatives. Major efforts were made to build capacity of BULDOG's management and staff from the beginning. Extensive analytical studies were carried out on key factors such as the size of margins between floor and ceiling prices, the size of buffer stocks, and the price of fertilizer relative to floor and world prices. A monopoly control over international trade was established, which allowed the government to import when domestic production was insufficient and to export when there was a surplus and stocks levels were already high.

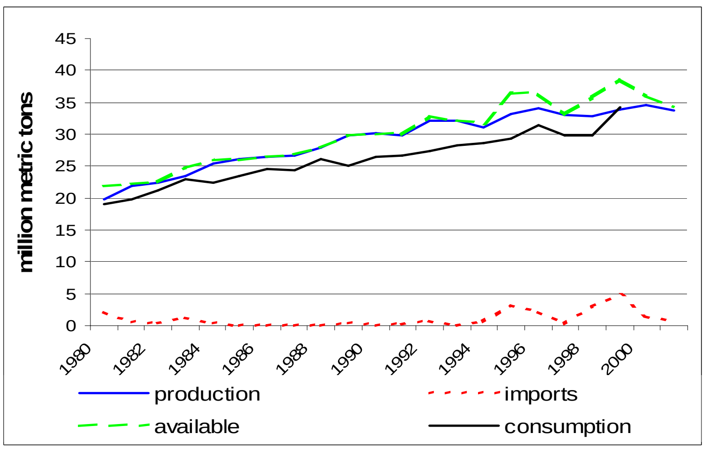
What were the effects? The supply response was dramatic: rice production increased by 10.5 millions tons over the 1978-1985 period. Fertilizer use increased by 500% between 1970 and 1985, while yields increased from 2.5 T/ha in 1965 to 4.4 T/ha in 1990. A huge improvement in food security followed.

Figure 2 : World rice prices and domestic rice prices 1985 to 2002



Source: reprint from Timmer 2004 p. 7[1]

Figure 1 : Evolution of selected indicators for rice in Indonesia (1980-2001)



Source : Central Bureau of Statistics

What recommendations could be derived? The Indonesian experience shows that government intervention can successfully adapt to a changing context and contribute to quick economic growth, but that it is difficult to implement. It is important to note that the rice price stabilization policy was only one component of the Indonesian approach to modernizing its rice economy. Public investment, not only in infrastructure such as roads and irrigation facilities, but also in human capital, through extension services and education, played an important role in the country's success. One important characteristic of government interventions is that they focused on avoiding markets failures and supporting private economic initiatives rather than substituting public initiatives for private initiatives. The whole commodity chain was not in the hands of parastatal companies.

The agricultural policy was part of a broader policy ensuring (i) macro-economic stability, (ii) making markets working more efficiently, (iii) ensuring political stability, and (iv) creating enabling environment for private investment.

Some technical lessons on price stabilization can also be drawn from the Indonesian experience:

- The target price should be aligned with international prices;
- The policy is far less costly when the country relies on imports than when it has to manage a surplus.

Key factors including the size of the margins between floor and ceiling prices, the size of buffer stocks, and the price of inputs relative to floor and world prices need to be constantly updated.