



FEED THE FUTURE

The U.S. Government's Global Hunger & Food Security Initiative



INDONESIA

RATE Country Summary

This document presents the findings of the Regional Agricultural Trade Environment (RATE) assessment conducted in the ASEAN region in 2012 by the Maximizing Agricultural Revenue through Knowledge, Enterprise Development, and Trade (MARKET) Project.



USAID
FROM THE AMERICAN PEOPLE

INDONESIA

Regional Agricultural Trade Environment (RATE) Assessment Country Summary

USAID Maximizing Agricultural Revenue through Knowledge, Enterprise
Development and Trade (MARKET) Project

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*On the cover: Co-directors of a cacao farmers group in Southeast Sulawesi
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RATE COUNTRY SUMMARY—INDONESIA

This country summary sets forth general findings from the RATE assessment that took place in Indonesia in April and August 2012. In addition to comprehensive desk research, RATE assessors conducted a series of interviews across the country's agriculture sector, including with national and local officials, port representatives, farmers and their associations, owners of agriculture enterprises, trade service-providers, market workers, business associations, nongovernment organizations (NGOs), the banking and lending community, and others. Interviews, observations, and/or follow-up discussions in October 2012 took place in and near Jakarta, Bogor, Makassar, Kendari, Bandar Lampung, and Medan. In all, the RATE team consulted more than 100 stakeholders in Indonesia.

What is RATE?

The Regional Agricultural Trade Environment (RATE) assessment is a tool designed to examine the agricultural trade enabling environments of countries in a particular region, with the objective of identifying a range of legal and institutional reforms that will help the region and individual countries become more efficient in their approach to trade.

In recent years, the international community has committed to a variety of multicountry initiatives that emphasize the collection of benchmark information. Such benchmarks allow participating countries to compare their economic and business environments to others. The accepted use of such benchmarks helps countries identify relative areas of strength and weakness and to track evolution in those rankings over time. Examples include the World Economic Forum's Global Competitiveness reports, the International Finance Corporation's Doing Business reports, and the United States Agency for International Development's (USAID) BizCLIR (Business Climate Legal and Institutional Reform) and AgCLIR (Agribusiness Climate Legal and Institutional Reform) reports.

Building on such initiatives—USAID's BizCLIR and AgCLIR, in particular—the ASEAN RATE inquiry has been conducted for Member States of the Association of Southeast Asian Nations (ASEAN) under the Maximizing Agricultural Revenue through Knowledge, Enterprise Development, and Trade (MARKET) project funded by USAID. RATE builds a knowledge base for addressing the priorities of USAID's Feed the Future initiative, which aims to increase investment in agriculture and rural development as both a lever for combating food insecurity and an engine for broader economic growth, prosperity, and stability.

RATE collects certain quantitative and qualitative information across relevant agriculture value chains in ten topical areas critical to trade in agricultural products sector, namely (1) the conditions for enterprise formality; (2) access to finance; (3) infrastructure; (4) intellectual property; (5) competition; (6) non-tariff barriers; (7) trade facilitation; (8) gender; (9) transparency and accountability; and (10) food security. Each RATE country assessment, set forth in a separate detailed, country-specific presentation and reported through a series of Country Summaries, benchmarks the national enabling environment for agribusiness and agricultural trade by identifying the private sector priorities, key market constraints, and successful national initiatives in support of agricultural trade in individual ASEAN Member States.

INTRODUCTION

Diverse, dynamic, crowded, and spread across an archipelago of some 17,500 islands spanning more than 5,000 km, Indonesia faces some of the most vexing food security challenges in the ASEAN region. The food price crisis of 2007–2008 hit Indonesia hard, with threats of rioting compelling the government to dramatically increase subsidies on rice and other staples. Since then, the country has pursued a strategy of rice “self-sufficiency,” as well as diversification of its mix of agricultural staples and high-value crops, along with protection of the domestic market from high-value crop imports.

Indonesia faces a variety of challenges with respect to continued growth and progress toward a level of economic and food security that benefits all. Farmers’ problems include access to inputs, markets, and finance. Small and medium-sized enterprises (SMEs) in rural areas are disadvantaged by significant limitations on access to finance, along with bureaucratic and expensive business licensing requirements. Larger companies and traders are especially concerned about nontariff barriers, both with respect to importing products, as well as exporting raw materials.

Although Indonesia has shown steady growth and reduced poverty gradually in recent years, improvements in the legal and institutional environment for doing agricultural business at numerous points in the country’s value chains could reduce inefficiencies in productivity, cut waste, and connect farmers with the markets they need.

Figure 1. Representative Statistics Pertaining to Agricultural Trade: Indonesia

Population (2013)	251 mn
Agriculture as % of GDP (2012)	14.4
Services as % of GDP (2012)	38.6
Industry as % of GDP (2012)	47
Percent of population engaged in agriculture (2012)	38.9
Exports (all sectors, 2012)	\$187 bn
Imports (all sectors, 2012)	\$178.5 bn
Percent of women participating in agriculture sector (2011)	35
Female/Male literacy rate (%) (2011)	90.1/95.6
Female labor participation rate (women over 15, 2011 est.)	51
Prevalence of under-nourishment (2011) (% of population)	9
Percent of children underweight (2010, % of children under 5)	18.6
% of workers informally self-employed or informal wage-earners (2011 est.)	65

SOURCES: CIA Factbook; World Bank

TOPICAL SUMMARIES

For each ASEAN Member State surveyed by RATE, assessors asked approximately 150 questions—around 15 per topic—related to the legal framework, implementing institutions, supporting institutions, and social dynamics of each of the ten topics studied by the assessment. This section summarizes the answers to these questions by setting forth the primary issues, opportunities, and challenges associated with each topic.

The Informal Economy

Throughout Southeast Asia, recent generations have witnessed a transition from economies grounded in informal activity—mostly agriculture and casual trade—to more formal and clearly defined relationships between enterprises and the regulating authority of government. Formalization begins with registration with one or more government authorities, and can result, in theory, in a number of advantages, among them limited liability, better access to finance, more opportunities to participate in higher-value pursuits, greater ability to enforce contracts, and even the benefits of a strengthened community tax base. For many

When producers, processors, and traders assume the various aspects of enterprise formality, their businesses can grow and their goods can circulate more freely, within and across borders, enhancing food security.



The Konawe Cocoa Farmer Group is a sophisticated operation that has financial ledgers and multiple income streams. It has received numerous grants from the government to support its activities.

producers, processors, and traders, however, registration with national or local authorities often means assuming the costs of formal tax collection and licensing interventions, without immediate or obvious tangible benefits. Enterprises typically remain informal because they perceive formalization as too costly, too complex, and not worth the effort. As long documented by the World Bank's *Doing Business* initiative, however, persistent, widespread enterprise informality undermines improvements to productivity and quality, access to markets, and economic growth.¹

Although rates of enterprise informality in Indonesia are difficult to state with certainty, most smallholder farmers operate in the informal sector, selling what they do not use for family needs to traders, to processors by contract, or directly through local markets. The national government neither pushes farmers to formalize, nor appears to withhold assistance and extension services from informal actors. National and regional governments have, however, encouraged farmers to participate in associations and sometimes required group participation in order for them to receive some extension services. A variety of government agencies provide technical assistance and association management training to participants in sectors that are deemed important to Indonesia's food security or to the

¹ See World Bank, *Doing Business in 2013* (2012), and accompanying literature at www.DoingBusiness.org.

country's objective to develop the production of high-value "cash" crops. An estimated 25 percent of Indonesian farmers belong to farmer or producer organizations, and there are about 318,000 associations of all types, including cooperatives, nationwide.²



Staples and dried fish are sold at a market near Medan on the island of Sumatra.

The process of formalizing an enterprise in Indonesia is notoriously difficult.³ Enterprise owners must obtain multiple licenses in order to do business and, since decentralization began in 1999, provincial and district governments have introduced even more permits and licenses. While these may raise revenue for government, they discourage businesses from formalizing. Some individuals consulted for the RATE assessment did have permits, health certificates, fishing licenses, and boat registrations, indicating that they are willing to formalize but only if costs and administrative burdens are minimal.

Regardless of the formality of their structure, producers in Indonesia often enter into agreements with local traders or processors, some of which rise to the level of a contract to sell a product at a certain price, in exchange for the buyer providing seed, fertilizer, spending money, or something else of value at the beginning of the growing season. These agreements are often verbal, rather than written, and often set up so that price—or even a mechanism for determining price—is absent. Then farmers, particularly those who have received cash or inputs in advance, often receive a different price at harvest than they anticipated. Certain farmers sell their product to another trader ("side-selling") in spite of the previous

² IFPRI, *Agriculture Extension and Advisory Services Worldwide—Indonesia* (2011) (citing IFPRI/FAO/IICA *Worldwide Extension Study* (2010): Survey responses by the National Center for Agricultural Development). Government officials interviewed during the RATE assessment estimated that fewer than 10 percent of farmers belong to a cooperative.

³ In *Doing Business in 2013* Indonesia ranks 166 out of 185 countries surveyed for "Starting a Business," the lowest ranking among ASEAN Member States, except for Cambodia (175) and Burma (unranked).

agreement. At the same time, traders commonly engage in behavior that limits the options available to farmers (fixing prices or creating barriers for competition among themselves), so that market choices are limited for farmers, most of whom have little access to transportation.

Extension services reach farmers, but the depth and scale of those services vary significantly by province. Most services target small or medium-scale commercial farmers or smallholder subsistence farmers. In Sumatra, for example, farmers reported receiving extension assistance to incorporate the use of organic fertilizer into production of fruits and vegetables, along with support for growing livestock. In Sulawesi, farmers received donations of cattle and equipment and fishers received fishing equipment, association development services, and business loans. The government decides which subsectors to target, and the targeted subsectors, such as fish meal products, are not necessarily the most marketable.

Access to Finance

Producers, processors, and traders seek finance for a variety of purposes: for business start-up or producer operations; to bridge the gap between production of goods and receipt of payment for them; for capital purchases, farming equipment or storage facilities; to cover swings in supply and demand conditions; or to launch a processing enterprise.⁴ In many instances, they are disappointed. The risks involved in lending are often too great for banks and other lenders to assume. These include ambiguous or highly disputed land rights, weak property registration systems, limited forms of collateral, inadequate financial infrastructure, and the particular risks faced in agriculture, such as seasonality and geographic clustering of risk.

A variety of safe and accessible opportunities to access finance helps producers, processors, and traders cope with supply and demand risks, strengthen their enterprises, and contribute to food market stability.

A range of financial services is available, at least in theory, for agricultural enterprises in Indonesia, from commercial banks to rural people's banks and cooperatives. While financial services are generally accessible throughout the country, they are less so in rural areas, and microfinance has been slow to develop. A law that would expand access to microfinance services has been under consideration for 10 years, with little movement toward enactment. Few smallholder farmers in Indonesia seek formal credit, partly because of a lack of a tradition of borrowing from formal institutions, as well as the scarcity of lending by banks. Farmers typically turn to the informal market—often traders—for loans at very high interest rates and other terms unfavorable to farmers themselves. Several farmers interviewed for RATE mentioned obtaining seeds and fertilizers from the BRI (People's Bank of Indonesia), which specializes in microfinance and financing for small enterprises. These farmers are provided with inputs, such as seed and fertilizer, and may repay in either seed or cash. Typical interest rates for micro-credit in Indonesia are about 25 percent per year, for loans covering a year or two, along with a weekly or monthly plan for repayment.

A new solidarity lending scheme intends to bring small loans to more poor farmers. Using a system of “group responsibility,” the Bank for Agriculture Promotion lends to small groups of farmers without

⁴ See USAID/Enabling Agricultural Trade, Agribusiness Commercial Legal and Institutional Reform project, *Lessons from the Field: Getting Credit* (2011).

collateral. The amounts are usually too small (up to about IDR10 Million—or about US\$1,250 per person) to be useful to farmers investing in high-cost crops, such as bananas or cocoa, and the terms often do not match the realities of agriculture (that is, the loan term may be limited to six months, while the period of investment is a minimum of eight months). Under this type of scheme, each farmer is individually responsible for the debts of the others, a model that has proven successful in other countries. Some farmer groups borrow this way, but most find the terms unpalatable and still turn to the informal system.

As noted in a 2011 article on microfinance in Indonesia, a great many lending relationships conform to Islamic banking practices:

The Indonesian central bank estimates that microfinance accounts for 70 percent of Islamic lending in Indonesia, with total outstanding loans of \$5.1 billion. Since interest can't be charged under Islamic law, the lender purchases assets for the client and sells them at a predetermined profit margin. This technicality doesn't affect the banks' profits, which enjoy a 30 percent average return per year on microloans.⁵

After the financial crisis of 1997 all banks in Indonesia were restructured and there was a national commitment to modern standards of corporate governance in the banks. This resulted in a much stronger and more transparent commercial banking system. Indonesia's larger banks have especially gained confidence from international rating authorities. Better technology makes banking practices more transparent. Formal mid-sized and larger companies, including those in food processing and trade, increasingly use formal credit, including a variety of trade finance products, to grow their companies.

Since 2006, Indonesia has run a modern system of credit information through the Bank of Indonesia. Over its short history, the bureau has improved, through such measures as strengthened data quality, better infrastructure, and wider coverage for users. There is room for more improvement, especially with respect to smaller transactions and operations of relevance to SMEs. Still, some innovative practices are in place. One cocoa processor has received IFC funding to work with banks to develop a collateral system based on traceability certification. Traceability certification provides enough information to banks on small farmers so that banks can evaluate their application for financing. The Indonesian government is also piloting a warehouse receipt system through the 2006 Law on Warehouse Receipting Systems to improve farmers' access to finance.

Indonesia's highly fragmented insurance industry suffers from a lack of transparency and weak governance. Most providers are small and many are undercapitalized. The threat of insolvency among providers means there is a lack of confidence generally in the industry. The Ministry of Agriculture is piloting crop insurance for farmers to better understand what models would work. However, a great many reforms are required, including consolidation, transparency improvements, and capacity-building among suppliers and regulators. Of course, the threat of natural disasters presents great risk to Indonesian people and their livelihoods. There is virtually no insurance against such risk in Indonesia. This lack drives up credit related costs.

⁵ *The Diplomat*, "Microfinance and Young Indonesia" (May 23, 2011).

Infrastructure

A nation's success in agricultural trade, whether domestically or in regional or international markets, is generally only as good as the ability of its producers to get their products to the next stop on the value chain—that is, to local markets, distributors, and processors, or to storage facilities, warehouses, and ports. Producers and processors also need access to inputs that are transported over long distances, including seed, feed, fertilizer, and equipment. All actors need access to market information that comes through reliable telecommunications. To support commerce that extends beyond the farm gate, governments must invest in and maintain a supporting infrastructure that incorporates transport, water, power supplies, and telecommunications.

Strong markets for agricultural products need public facilities that support production, processing, and trade, such as roads, rail, ports, wholesale markets, storage facilities, and access to communications and information.

Indonesia's domestic infrastructure—roads, airports, ports—is straining under ever-growing demand. Most is already at capacity. For example, the main airport receives double the number of passengers it was built to accommodate, and the Jakarta seaport has recently been the subject of international news stories documenting, with amazement, its ability to even function. Inadequate infrastructure is often said to be Indonesia's biggest obstacle to continued rapid economic growth. The government recently increased funding for infrastructure projects, but significantly more is needed in the world's fourth most populous country. Intra-Indonesia transport is so inefficient that the cost of shipping a container between islands is double the cost of shipping it to the United States. Poor road quality outside of Java and severe road congestion contribute to trucking costs that are the highest in ASEAN.⁶

Increasingly, it is apparent that decentralized government authority plays a role in limiting infrastructure development. In Makassar, for example, the national government is responsible for the highway leading up to the port, but the local authority is responsible for the port itself. Lack of interagency coordination resulted in a highway too small to handle the port traffic. Provinces and local authorities have limited budgets and many local infrastructure regulations are reportedly incomplete or inconsistent with one another.

DECENTRALIZATION IN INDONESIA

Law 22/1999 grants local governments significant authority over day-to-day activity in Indonesia but retains central government responsibility for fiscal and monetary matters, as well as distribution of subsidies. In practice, some districts have become both overly competitive (charging tolls, for example, on vehicles transshipping goods) and aggressive in regulating local businesses.

While most agriculture in Indonesia is rain-fed, where irrigation systems do exist, they are often weak or failing. Irrigation is now handled by provincial or municipal governments. Civil servants overseeing irrigation programs tend not to be specialists in agriculture and do not have the resources needed to oversee and implement schemes. As detailed in a 2006 analysis of irrigation systems in Indonesia:

Several large-scale forces are emerging and increasing in importance for irrigation and agriculture. These include the steady shrinking of farm sizes, especially on Java, to the point

⁶ See Indonesian Journal of Leadership, Policy, and World Affairs – Strategic Review, *Indonesia's Logistics Costs and Competitiveness* (2011).

of their becoming non-viable economically. Some sort of land consolidation, either in terms of ownership or, perhaps more likely, operational consolidation, may start becoming necessary in the future. Farming on such small fields as a quarter of a hectare or less cannot produce enough income for a farm family. In many areas of Java, farmers are only part-time and they engage in all sorts of other activities for income. This is not only because of small farm sizes but also because of low economic returns of rice and other irrigated crops. Another influence is the reality that the younger generation is losing its interest in becoming farmers and most are seeking off-farm opportunities.

Irrigated land on Java is disappearing at the rate of at least 20,000 ha per year due to its conversion to urbanization. Also, when in competition with other sectors for government funds, irrigation loses out to roads, housing, municipal water supply, power, etc. Most irrigation systems have the distinctive characteristic that their maintenance can go under-financed for a few years before structures begin to fail. But when they do, expensive rehabilitation is needed.⁷

Another issue affecting Indonesia's farmers is the lack of storage facilities. Poor storage contributes to Indonesia's postharvest loss rates, which some RATE interviewees estimated as high as 15-20 percent for staples.⁸ Limited cold storage at airports further results in risks for dairy, meat, fish, fruits, and vegetables. For example, meat and pharmaceuticals must be stored at two different temperatures. Because space is insufficient, the more expensive product, pharmaceuticals, is kept at the required temperature while the meat might not be, risking spoilage. A 2004 Australian Guide for Food Exporters to Indonesia admonishes the following:

Supply chain logistics in Indonesia range from pre-modern era practices—sailing ships and cargo carried by stevedores on their shoulders—to contemporary best practice ... Java has reasonably effective distribution infrastructure and urban areas in Sumatra, Bali and Sulawesi are also developing rapidly. Infrastructure and cold storage facilities outside these centres are generally poorly developed, making the distribution of products to outlets in remote areas problematic. Imports to Indonesia generally need a shelf life of at least 6 months, and products requiring refrigerated transport and storage incur high transport costs.⁹



An Indonesian trader carries goods in a rented truck.

⁷ Douglas L. Vermillion, S.R. Lengkon and Sudar Dwi Atmanto, *Time for Innovation in Indonesia's Irrigation Sector* (Report to Asian Development Bank, 2006).

⁸ In fact, there is a dearth of information about actual rates of post-harvest loss in Indonesia.

⁹ Australian Government, Department of Agriculture, Fisheries and Forestry, *Food Exporters' Guide to Indonesia* (2004).

Although there have been many improvements in recent years, cold storage in Indonesia's remote locations is an ongoing challenge for farmers and transporters.

Finally, laws for land acquisition for infrastructure projects were insufficient until 2012, when a new Land Law was passed. Land generally is a major national issue that affects agriculture in all its forms, as recently summarized by USAID:

At least five land and natural resource property-rights issues should be addressed for the benefits of growth to be more widely shared and to increase environmental sustainability. First, ambiguities between formal and customary law are interpreted by governments, officials and citizens in ways that undermine land rights, leading to a growth in land disputes and conflicts which must be addressed. Second, a registration system that is overly complex, inefficient and ambiguous has weakened security of tenure and the development of a functioning land market. Third, land conversions driven by economic development are threatening Indonesia's vital forest resources and hold implications at the global, national and local levels, particularly related to climate change. Fourth, urban growth has not been accompanied by sufficient investments in housing and urban services despite continuing decentralization. Fifth, the problem of rural landlessness has limited the economic options, basic livelihood strategies and food security of millions of families.¹⁰

During the RATE assessment, farmers described the increasing pressure for development of agricultural land. Rural dwellers contend that they are being evicted from their prime agricultural land so that it can be sold to real estate developers or large companies.

Intellectual Property Rights

Intellectual property rights (IPR) are increasingly viewed as a key factor in development. Intellectual property is a branch of law that protects intangible property such as inventions, new plant varieties, geographical indications, and trademarks and protects against dishonest business practices. An effective IPR system makes markets more predictable and reduces investment risk. This benefits local producers and better positions a country to attract foreign investment, as international investors give substantial weight to IPR protection in their decisions on where to locate their business investments.

Investment in a vibrant food economy is enhanced by systems supporting the recognition and protection of new plant varieties, and of patents, trademarks, and copyrights used in connection with equipment, products, and services.

Indonesia is a member of nine substantive international agreements on IP but has not yet joined the agreements that facilitate the international protection of marks, industrial designs, and new plant varieties. The country recently enacted or amended laws on copyrights, patents, and trademarks. In 2000, new laws were also enacted on trade secrets, industrial designs, integrated circuits, and plant varieties.

Trademarks, in particular, are sought by Indonesian companies to protect brand names and product symbols. The process is not expensive but reportedly takes two years to complete. Once registered, a trademark remains valid for ten years but can be renewed indefinitely. Indonesia is known, however, for

¹⁰ For a detailed discussion of these and other land issues in Indonesia, see USAID Land Tenure and Property Rights Portal, Indonesia Country Report (2010).

poor enforcement of IPR, and is one of 10 countries on the 2013 Special 301 Priority Watch List of the Office of the U.S. Trade Representative (USTR). USTR is concerned that Indonesia's IPR enforcement has not been effective in curbing piracy of commercial trademarks and counterfeiting of critical agricultural products.



Many Indonesian products could be eligible for Geographic Indication protection.

From the perspective of Indonesian companies, a great deal of their products' value can be lost if laws protecting trademark and geographical indications are not enforced. Businesses complain of widespread trademark counterfeiting that includes pharmaceutical and agricultural chemical products; of inadequate protection of confidential data, where unauthorized disclosures have led to the copying of pesticide and fertilizer formulas; and of a lack of transparency in enforcement. If a trademark violation is found, for example, businesses receive little guidance on how to stop the violation or the timeline for the court to respond. If the court finds no violation, businesses rarely receive an explanation. Counterfeiting and smuggling of protected products are not adequately addressed. In particular, businesses do not have confidence that the Ministry of Agriculture's Office of Plant Variety Protection will keep their information confidential. However, business associations representing companies that manufacture crop protection products promote IP awareness and enforcement. Intellectual property is getting more attention in the educational community, and awareness of the meaning and scope of IP rights is growing.

Competition

Competition is at the heart of any successful market economy. True competition promotes economic efficiency, consumer choice and welfare, and overall economic growth and development. Competition forces companies to work as efficiently as possible and offer the most attractive array of price and quality options in response to consumer demand, rather than conspiring as cartels to fix prices or to block other companies' entry into the market.

Competition compels producers, processors, and traders to be more efficient and innovative and to offer the most attractive array of price and quality options in response to consumer demand.

Indonesia's Competition Law, enacted in 1999, was one of the first pieces of antitrust regulation in the region, and signaled a new commitment to fair competition. Today, however, a number of ambiguities and exemptions undermine enforcement. The government is heavily involved in the agriculture sector, and its control of key agricultural input and product markets significantly detracts from competition in Indonesia. For example, the government regulates the sale of rice, maintains a national floor price for rice, and also restricts rice imports. This regulation drives up rice prices for consumers, negatively impacting the poor and low-income wage earners. A government-supported fertilizer system also discourages foreign competition, while sugar imports are limited seasonally to protect Indonesian industry. In addition, the government reportedly restricts the imports of large machines that could be helpful in agricultural production, because they are perceived as undermining employment opportunities.¹¹ Seed subsidies are viewed as enriching large, politically connected companies at the expense of both improving seed quality and reaching small farmers.



Farmers complain that unscrupulous traders band together to fix prices and territory.

¹¹ Ministry of Finance Decree No. 19/2009, adopted on 13 February 2009, raised import tariffs on some products that are perceived as competing with locally manufactured products. This includes products such as milk, animal or vegetable oils, fruit juices, coffee and tea, chemicals, silver, steel, electronic products (machines, TVs etc.), as well as manufactured products: packaged juices (10 to 15%), instant coffee (5 to 10 %), iron wire (7.5 to 10%), wire nails (0 to 7.5%) and electrical and non-electrical milling machines (0 to 7.5%). At the same time certain tariffs were reduced, mainly on input products needed for local manufacturing (e.g. dairy products and base chemicals).

Indonesia's competition authority (the KPPU) is respected for the quality of its staff, the independence and transparency of its processes, and its leadership in the region. Despite considerable resistance from the government and traditionally privileged commercial actors in the economy, the KPPU has stood by its mandate to oppose anticompetitive actions through its enforcement powers and to engage in competition outreach and advocacy. The KPPU issues 10 to 20 recommendations each year, chiefly on laws and regulations pertaining to finance, transportation, and telecommunications. Of the seven policy recommendations pertaining to agriculture it issued between 1999 and 2011, four resulted in policy change. With respect to trade policy, four out of ten policy recommendations resulted in change.¹²

Indeed, although advocacy by the competition authority does not invariably result in competition-directed change (its overall rate of achieving change is 43 percent), an absence of advocacy would clearly result in less competitive agricultural markets and trade policy. As Indonesia continues to enact laws and regulations that undermine the competitiveness of its agricultural markets, the KPPU remains vigilant in pursuing its mandate to speak out in favor of genuine competition, despite the “deaf ears” of other agencies of government.¹³

A lack of competition—that is, a range of potential buyers and conditions for sale—is evident along many agricultural value chains, particularly in rural areas. A small farmer typically sells to a local trader or local collection center, which then sells to a middleman, who typically takes the product to a larger collection center in a larger city. These trading relationships are based on family ties or other relationships between community members.

There is little competition and few farmers try to break out of the system, partly because doing so would disrupt the social structure. Rent-seeking takes place at many points, including among transporters. Access to market information does farmers little good, because they are unable to obtain the prices stated

Figure 2. Sample Commodity Price Comparisons, January 2012 (US\$ per kg)

Country	Price of Rice	Price of Wheat
Bangladesh	\$0.30 -6.7%	\$0.25 -4.0%
China	\$0.59 +1.7 %	\$0.65 +1.6%
India	\$0.43 +4.9%	\$0.41 +5.1%
Indonesia	\$1.15 +3.6%	\$0.81 0%
Pakistan	\$0.66 +3.1%	\$0.32 0%

SOURCE: IFPRI Food Security Portal. Percent change is based on the previous month.

Figure 3. Sample Rice Prices (US\$ per kg)

Country	2011		2012	
	February	August	February	August
Brazil	1.10	1.16	1.10	1.04
Cambodia	0.34	0.37	0.34	0.37
India	0.43	0.48	0.44	0.50
Indonesia	1.03	1.11	1.17	1.10

SOURCE: FAO/USAID Food Security Portal. Cambodia and Indonesia are the only ASEAN countries for which 2011 and 2012 price data was available.

¹² A. Junaidi, Bureau of Policy, KPPU, “Exchange of Experience in Setting Up Strategy in Competition Advocacy” (2011).

¹³ See *Kompetesia, Newsletter on Indonesian Competition Law and Policy* (2011) (“There are not a few government policies which do not support fair competition.”)

from the few traders in their area. Farmers who decide to sell directly to larger traders in regional towns reportedly find that the payoff is equal to or less than selling directly to the trader in their village—poor infrastructure and a lack of transporters drives up transport costs. As a positive contrast, in one case observed by RATE, a large corporate processor reached out to rural cacao farmers directly in Southeast Sulawesi by building a network of rural collection centers. Local farmers appreciate that these centers provide clarity on market prices.

From the 1970s to the 1990s Javan families were offered land in remote areas of Indonesia, such as Sulawesi and Northern Sumatra. Farmers who participated in these transmigration programs benefited from ample government assistance. Upon relocating, they received food subsidies and cash wages for the first few years, and later land, training, and supplies for farming. These farmers have continued to receive significant extension services (fertilizer, training, livestock, small equipment) even years after relocating.

Nontariff Barriers

Although the formal definition of what constitutes a “nontariff barrier” (NTB) varies according to the source, NTBs are generally viewed as government-imposed or government-sponsored measures—other than tariffs—that are used to protect a domestic industry from international competition. A great many measures can be interpreted as an NTB, ranging from restrictions on food imports due to food safety considerations, to business licensing requirements that are especially difficult for outsiders to fulfill, to outright quotas. For the purposes of agricultural trade, NTBs may include import restrictions on inputs, sanitary and phytosanitary (SPS) regulations, animal and plant health standards, food safety standards, business licensing procedures, labeling and packaging requirements, and constraints on trade in services. Some of these are sanctioned by the world trade community through agreements, while others can be challenged by trade partners as restrictive of trade.

Markets function more efficiently when trade is managed through transparent tariffs and legitimate health and safety measures, rather than via more opaque quotas, licenses, and other barriers.

In Indonesia, the prevailing attitude of regulatory agencies and domestic sector associations, particularly in sectors vulnerable to international competition, is protectionist. In 2011, Indonesia announced the fourth-highest number of restrictive import and export measures tracked by international authorities—59 in all.¹⁴ The government also unveiled new import-licensing procedures, restricted the number of entry and exit points, and applied higher import and export duties. It introduced further restrictions on exported raw materials, such as cocoa beans, in addition to the existing export tax of 25 percent on raw exports.

For most food products, most importers consider Indonesia’s importation process burdensome, slow, and inefficient. All imported packaged food products—that is, every shipment—must be registered with the National Agency for Food and Drug Control (BPOM). Registration is generally through a local agent or importer, but the time it takes is usually much longer than the mandated 45 days, extending to as long as 9 months. In addition, mandatory inspections at the border are lengthy and require that goods be submitted with detailed information that may cause the prospective importer to divulge proprietary information.

¹⁴ European Commission, Directorate General for Trade, 9th Report on Potentially Trade Restrictive Measures (2012).

Indonesia's strict labeling requirements are more cumbersome than those required in other ASEAN Member States.

In 2012, Indonesia introduced legislation to restrict the quantities of fresh and processed fruits and vegetables admitted into the country, as well as the ports through which horticulture imports may flow. This legislation would have redirected 90 percent of Indonesia horticulture imports, and received a great deal of criticism from trade partners including the U.S. However, in May 2013, the Agriculture Ministry announced it was replacing the horticulture import regulation with a new regulation that lifts import bans and instead applies quotas to each product on a seasonal basis. The new regulation still limits imports of certain products when similar ones are in the harvesting season in Indonesia, in order to avoid over-supply and deflated prices.¹⁵

In November 2012, the Indonesian House of Representatives passed Law 18/2012—the new Food Law—which replaced the previous overarching food law, enacted in 1996. The new law regulates all food and food products, including processed and unprocessed food and beverages for human consumption, to include food additives, raw materials and other materials used in the preparation, processing, or production of food and/or beverages. The new law integrates the priorities of the government of Indonesia, which, as summarized by the U.S. Department of Agriculture, require “protections for producers, as well as consumer of food” and “the concepts of Food Resilience, Self-Sufficiency and Food Security.”¹⁶ Against this backdrop, the USDA notes that traders of food products in Indonesia continue to face uncertainty:

Many of Indonesia's regulations related to the marketing of food and food products are unclear and confusing, not enforced, or are enforced on a cursory basis in a haphazard manner. While a review of relevant regulations is important, the reality of what actually occurs in practice may be quite different. Therefore, it is essential that exporters confer with local importers/agents to determine prevailing requirements on imports.¹⁷

Although definitions of NTBs tend to center on goods, related types of barriers also apply to and restrain trade in services. Indonesian law and institutions have become increasingly unfriendly to trade in services. For example, in 2012, a decree was issued that prohibits wholly Indonesian-owned companies from hiring foreign staff for senior positions. Indonesia has experienced a dramatic drop in trade in services as a percent of GDP in recent years—from approximately 12 percent in 2004 to around 6 percent in 2011.¹⁸

¹⁵ Jakarta Post, “Government to loosen horticulture import rule” (May 6, 2013).

¹⁶ USDA Foreign Agricultural Service, Global Agricultural Information Network, *Indonesia: Food and Agricultural Import Regulations and Standards – Narrative* (February 5, 2013).

¹⁷ Id.

¹⁸ See WTO Trade in Services database.

Trade Facilitation

Prudent and effective international trade facilitation requires high-quality, transparent government services at the border, including predictable and consistent procedures by customs agencies, health and agriculture inspectors, immigration agencies, and others. Governments throughout the world increasingly recognize that capable and responsible trade-related operations are a prerequisite for development.

Because of their greater perishability, foods in particular require efficient trade regimes and border crossings. Food security is enhanced when cross-border flows of products are “facilitated” to minimize time spent by food-related cargo in trade, thus reducing both physical losses and costs.

The volume and efficiency of markets improve when procedures and controls governing the movement of goods across borders are transparent, accessible, and consistently administered by customs agencies and other key border agencies, including port authorities, health agencies, quarantine services, and immigration.

In 2006, after consulting with private sector and international experts, Indonesia amended its Customs Law to bring principal border functions up to international standards. Along with other policy and regulatory initiatives, including a national logistics strategy, Indonesian law increasingly supports efficient and competitive trade in agricultural products.

Nevertheless, customs processes in Indonesia are not as efficient as they could be. With significant international assistance, Indonesia has been working to strengthen its risk-management procedures for several years. The ongoing implementation of the National Single Window (NSW), which has entailed improvements in automation, has bolstered the country’s efforts to manage risk. The use of online processes has significantly reduced face-to-face interactions between traders and customs officials, diminishing opportunities to solicit unofficial fees. Nonetheless, exporters and importers complain that printouts from e-customs systems do not always reflect what was entered through the web-based interface and this forces the refiling of paperwork and cargo delays. Businesses feel that a one-stop shop for permits, paperwork, and licenses would simplify exporting and importing.

Indonesia’s main ports in Jakarta and Surabaya are perceived as inadequate due to low port productivity and only partial implementation of the NSW. There is demand for a new deep-water port. The World Bank has recommended expanding port capacity, considering a 24/7 work regime, streamlining document-processing, and strengthening the NSW. It also recommends a new gate system and better information technology systems.¹⁹

Indonesia identifies four of its ports as “international.” All goods exiting and entering the country must pass through them. Some companies have been able to get an exemption from this rule, although not for the import of rice. One company was able to obtain the exemption in 2012, while competitors received it in 2011. Companies find that this regulation raises costs for transportation and imposes costs as they seek exemptions.

Private sector associations play an important role in representing their trade-related needs to the government. Sector-specific groups represent the interest of producers and exports of coffee, cocoa, palm

¹⁹ See World Bank, *Trade Logistics Index and Report* (2012).

oil, rubber, fish, meat, and flowers. Despite this, government officials often implement regulations that hinder the free flow of commerce. For example, the government changed the process for airports to inspect cargo, resulting in significantly higher fees for shippers. Transporter associations were not consulted beforehand and are working to have the ruling overturned.



Yellowfin Tuna are sorted, tagged, and prepared for export processing.

Gender

As underscored by USAID’s 2012 Gender Equality Policy, gender equality and female empowerment are “fundamental to the realization of human rights and key to effective and sustainable development outcomes.

Although many gender gaps have narrowed over the past two decades, substantial inequalities remain across every development priority worldwide—from political participation to economic inclusion—and remain a significant challenge across all sectors in which USAID works, particularly in low-income and conflict-affected countries and among disadvantaged groups.” Women engaged in agriculture are particularly vulnerable in many developing country environments:

Strengthening educational and economic opportunities for women can lead to more robust and equitable economic growth.

Women and men tend to work in very different parts of the economy with little change over time ... In almost all countries, women are more likely than men to engage in low productivity and labor-intensive activities. They are also more likely to be in unpaid family employment or work in the informal wage sector. In agriculture, especially in Africa, women operate smaller plots of land and farm less remunerative crops. Across all regions, as entrepreneurs, women tend to own and manage smaller firms (measured by sales, employment, and assets) and to concentrate in less profitable sectors. As a result of these differences, gender gaps in earnings and productivity persist across sectors and forms of economic activity, including wage employment and entrepreneurship.²⁰

Indonesia's Constitution prohibits discrimination generally, but, unlike most countries, does not outlaw discrimination on the basis of sex specifically. In 1984, Indonesia enacted the Convention on the Elimination of all forms of Discrimination Against Women (CEDAW); however, the country's Marriage Law continues to designate men as "heads of families" and women as responsible for maintenance of households. The legal age of marriage is 16 years for women and 19 years for men.²¹

Land inheritance rights are governed by the 1847 Civil Code in the case of non-Muslims, and by Islamic law in the case of Muslims. Under the Civil Code, women and men have equal rights to inheritance. But the vast majority of women do not necessarily have that privilege, and, under customary practice (*adat*) and Islamic law, sons and daughters are treated differently with respect to inheritance. In many communities, each son receives a share that is twice as large as each daughter's share. In others, women are provided with certain land rights, but these often go undocumented, which diminishes their worth.

Men and women working in Indonesia's agriculture sector generally assume different types of work. Government extension typically focuses on the production side of agriculture—that is, in Indonesia, the male side, while the female-dominated processing side (at the cottage industry level) is reportedly neglected. Moreover, rural



Women are predominantly market retailers, but typically not midlevel traders or moneylenders.

²⁰ USAID, Gender Equality and Women's Empowerment Policy (2012), at 8.

²¹ See OECD, Social Institutions and Gender Index – Indonesia (2012).

women interviewed during the RATE assessment stated that they feel that training programs provided, such as in entrepreneurship, management, and finance, are targeted at men.

Although women may be very influential in their own households, most are heavily discouraged from participating in any activity, trade, or leadership role that would interfere with domestic obligations or take them away from their families. Conditions for urban women, women with higher education, and women who work at the professional level are far better and more accommodating than for those with less education and who work on the farm or in lower-level trades. In all, the rate of women's participation in Indonesia's workforce is far less than that of men – 51 percent versus 84 percent.

Rather than seek jobs with businesses, women are more likely to enter the Indonesian Civil Service, where they feel they have a better chance of obtaining fair employment and where working conditions are more likely to be supportive of women's obligations to family and home. In 2012 women held five of 37 Cabinet posts and 18 percent of parliamentary seats. Many women-focused organizations do exist, such as the Indonesia Women's Business Association, which has more than 16,000 members.

Transparency and Accountability

When discussed in terms of governance, the term “transparency” pertains to the free and full availability of critical information to the public. “Accountability” refers to the authority which citizens confer to those they elect to govern on their behalf, such that it is always limited, provisional, temporary, and subject to recall through regular elections or other arrangements. In the absence of transparency and accountability, corruption ensues. In the popular definition long espoused by Transparency International (TI), corruption is “the abuse of entrusted power for private gain.” As TI has long maintained, corruption hurts everyone who depends on the integrity of people in a position of authority. It also raises the cost of doing business. Thus, issues of transparency, accountability, and corruption are relevant in all sectors of an economy, including within public and private institutions involved in the agriculture sector.

Transparency and accountability in all aspects of agricultural trade—including production, processing and trade—facilitate increases in regional and international cooperation and trade.

In the late 1990s, Indonesia began a process of decentralization, devolving more government responsibilities to the provincial, regent, and municipal levels. This created challenges for ensuring transparency in government processes. At the national level, Parliament publishes most draft laws for comment, but at the local level little information on budgets, revenue, and management of public finances is released. Decentralization, while at first streamlining some processes, now seems to be adding layers of bureaucracy. Less attention is paid to corruption by officials at the provincial and local levels. For example, additional permits and licenses are required by local and national authorities. Provinces compete with one another: one provincial government has imposed fees for fish imports from an adjoining province whose prices are significantly cheaper and perceived as flooding the local market.

Indonesia's Criminal Code has anticorruption provisions, including prohibitions against bribery. The Law on the Eradication of the Criminal Act of Corruption expanded on the Criminal Code and significantly increased penalties. The law is very clear that bribery of public officials, whether through a gift, promise, or other valuable item, is illegal.

Indonesia has made progress against corruption. Its Transparency International “Corruption Perceptions Index” ranking went from 130 out of 163 countries surveyed in 2006 to 118 out of 176 countries surveyed in 2012. Still, perceptions remain across the communities visited during the RATE assessment that few individuals suffer consequences for offering or accepting informal fees. The Indonesian Corruption Eradication Commission has pursued corruption cases against police officials and judiciary.



Transport of goods between districts can entail burdensome taxes and fees.

Interviewees frequently mentioned that “voluntary” fees are required to facilitate container processing, the issuance of permits, or inspections by government officials. In addition, there is little confidence in official statistics on agricultural production, because over-reporting of yields is incentivized through additional input subsidies to provinces. Moreover, the annual importing process for essential commodities such as rice and beef is nontransparent. Importers do not know how the government determines what quantities are allowed each year, making it difficult to make business decisions.

With respect to the private sector generally, the Forum for Corporate Governance of Indonesia set out in 2000 to establish a strong example of private sector initiative and leadership in the country’s efforts to banish corruption. The influence of the organization and its members, including major business associations, ebbs and flows. In 2006, after extensive public consultation, the National Committee on

Governance issued Indonesia’s new Code of Good Corporate Governance. This nonbinding code sets guidelines that companies are strongly encouraged to follow, and aims to “shame” noncompliant companies.

Food Security

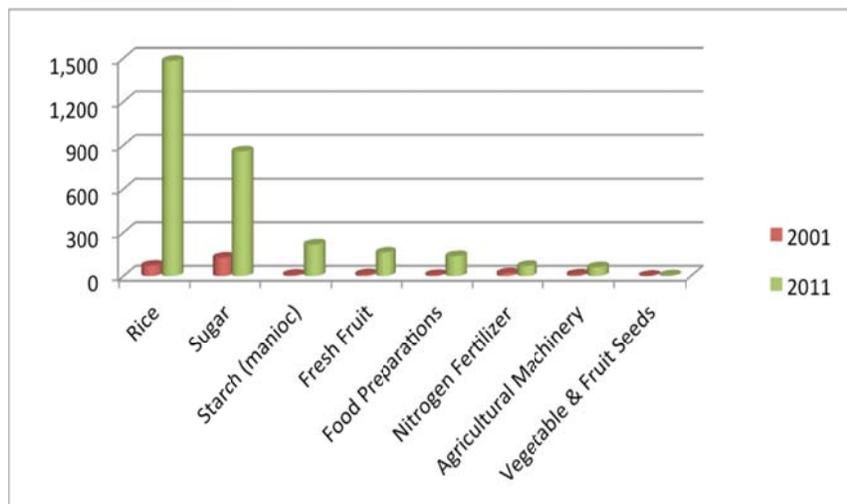
As the world’s fourth most populous nation, food security is of grave concern in Indonesia. Many of the food security problems it faces relate not to supply but to distribution and market efficiency.

According to the World Bank, 9 percent of Indonesia’s population was under-nourished as of 2011 and 19 percent of Indonesia’s children were underweight as of 2010.²² (These figures also suggest problems with access to health care and other critical services.)

Food security exists when all people, at all times, have physical and economic access to sufficient, safe, and nutritious food to meet food preferences and dietary needs for active and healthy lives.

Over the past generation, Indonesia has emphasized self-sufficiency as a primary goal for food security, especially with respect to the five commodities: rice, soybeans, beef, corn, and sugar. The government controls the supply of various staple crops and intends to expand the number and type of controlled commodities in its remit. The new food law passed in October 2012 highlights food sovereignty, self-sufficiency, and security as its three principle objectives. It also states that food commodities can only be imported if the domestic supply is not sufficient.²³

Figure 4. Indonesia's Major Agricultural Imports from ASEAN Member States, plus Imports of Key Inputs, 2001-2011 (US\$ millions)



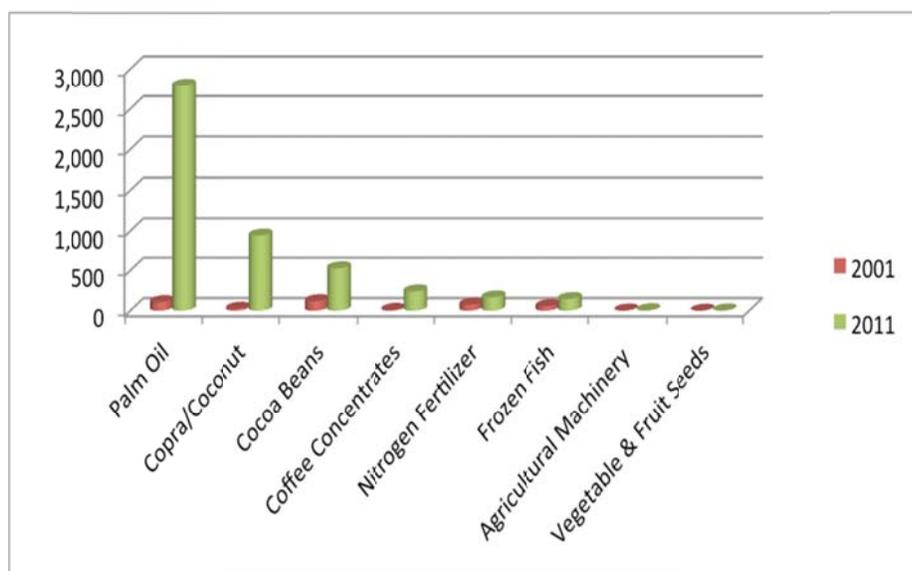
²² See World Bank data (available at <http://data.worldbank.org/indicator/SN.ITK.DEFC.ZS>).

²³ Law Concerning Food, Bill of the Republic of Indonesia (2012), available at http://usdaindonesia.org/wp-content/uploads/2012/11/FOOD-LAW-NO-18-2012_ENG_PRESIDENT-SIGNED.pdf.

Against this backdrop, advocates of free trade in the government are not particularly influential. Still, domestic protests in 2012 about rising soybean prices—a commodity for which Indonesia imports more than 60 percent of its total consumption requirement from the United States—led the government to suspend its 5 percent tax on soybean imports.

Government policies favor increasing productivity through subsidized fertilizer and seed and improved irrigation systems. Policymakers are less encouraging about the use of international trade to ensure food security (e.g., making cheaper imported staples available to the poorest). Private companies play a large role in public dialogue on agriculture, but SMEs, farmers, and traders feel that they are not significantly included in the debate.

Figure 5. Indonesia's Major Agricultural Exports to ASEAN Member States, plus Exports of Key Inputs, 2001-2011 (US\$ millions)



CONCLUSION

Indonesia's emphasis on food self-sufficiency has many domestic champions, but the country's tactics to discourage imports vex its ASEAN neighbors, who consider themselves generally receptive to Indonesian products. Indonesia's protectionist trade measures directly conflict with the country's commitment to free trade as established through its membership in the WTO and ASEAN. While the policy of high protection against imports does minimize food price instability in domestic markets, such stability comes at cost to consumers. Rather than isolating its consumers from the benefits of free trade and competition, Indonesia could instead improve support for Indonesian producers, processors, and traders alike, thus improving efficiencies along the food value chain and translating efficiencies into lower prices for consumers. Such improvements could include strengthening national infrastructure at all junctures of the value chains, strengthening access to finance, bolstering women's opportunities to participate in the economy, reducing petty corruption, and continuing improvements to trade facilitation.