

THINKING OF ADDRESSING AGRIBUSINESS INEQUITY IN INDONESIA ECONOMIC RECOVERY

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Development Inequality

- ❑ Between regions

- ❑ Between economic sectors

Consequences:

- The economy is vulnerable to shocks

- Economic competitiveness is difficult to improve

- Difficulty of reducing the poverty level

- ❑ Gini Ratio: 0.381 (March 2020) to 0.381 (March 2021)

Economy concentrated in Java Island

Java island: 7 % of land area and 56% of population of Indonesia

Role of Java on Indonesia GDP

| AREA | SHARE OF GDP (%) |
|---------------------|------------------|
| Java Island | 59.1 |
| Jakarta + West Java | 30.8 |
| Jakarta | 17.67 |

The agricultural sector is the center of the agribusiness system in Indonesia

- 58.74% agricultural sector products were employed in the manufacturing/processing sector
- 2.28% products of manufacturing/processing sector were used in agriculture sector

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- 6.51% agricultural sector products were used in accommodation and food and beverage service activities
 - 0.06% accommodation and food and beverage service activities were used in agriculture sector

Problems in the agricultural sector could be transmitted to the agribusiness system as a whole.

Main characteristics of “modern agribusiness” (Edwards and Shultz, 2005)

From farm centric to more customer- and market-centered activities

- Larger
- Diversified
- Complex
- Strategic
- Political
- Multinational

Driver of modern agribusiness → consumers' desires and needs

Strategy → effectively manage **value chain**

The concept of “value chain” at the firm level was introduced by Porter (1985) which explains all activities from the initial entry of raw materials, through several stages of production, distribution to consumers, and final disposal after use.

The use of value chains and value chain analysis has been extended to various applications beyond the study of individual firms (entire industries and industry clusters, and activities that are increasingly spread over several countries or the so-called “global value chain”).

GVC defines economic upgrading:

“The process by which economic actors – nations, firms and workers – move from low-value to relatively high-value activities in global production network” (Gareffi, 2005).

Economic upgrading → lead to social upgrading?

Share of Agriculture and Agribusiness in GDP (2019)

| SEKTOR | SHARE OF GDP (%) |
|--------------|------------------|
| Agriculture | 12.72 |
| Agribusiness | 19.36* |

*Estimated

Domestic orientation of agricultural sector

| Sector | Total import/GDP sectoral (%) | Total export/GDP sectoral (%) |
|--|-------------------------------|-------------------------------|
| Agriculture, forestry, fishery | 3.81 | 2.58 |
| Processing industry | 17.45 | 15.65 |
| Accommodation & Food and beverage service activities | 9.12 | 8.27 |

Output & Employment Imbalances in Agriculture Sector

Share of Agriculture on GDP and Employment

| Year | Share on GDP | Share on Employment |
|------|--------------|---------------------|
| 1978 | 33.1 | 60.9 |
| 2008 | 14.48 | 39.7 |
| 2019 | 12.4 | 27.3 |

Causes of the declining share of agriculture in national output

Income elasticity of food demand is lower than that of non-food demand (Engel effect).

Increased income is also accompanied by a smaller component of agricultural products in household food consumption.

The higher the degree of commercialization of farming, the greater the input component that comes from the non-agricultural sector.

Rate of growth selected sectors

| Sector/subsector | 2016 | 2017 | 2018 | 2019 |
|--|------|------|------|------|
| Agriculture, livestock, forestry, fishery | 3.37 | 3.92 | 3.89 | 3.64 |
| Food and beverage industry subsector | 8.33 | 9.23 | 7.91 | 7.78 |
| Wholesale and retail | 4.04 | 4.39 | 4.99 | 4.81 |
| Food and beverage service activities subsector | 5.03 | 5.48 | 6.03 | 6.92 |
| Transportation and communication | 7.45 | 8.49 | 7.06 | 6.40 |
| GDP | 5.03 | 5.07 | 5.17 | 5.02 |

Structure of the agricultural sector has changed

- ❑ Plantation, animal husbandry and fisheries are increasingly important.
- ❑ Agricultural sector is becoming more commercialize and market-oriented.
- ❑ Changes in the structure of agriculture need to be followed by changes in the structure of agribusiness as a whole.

Structural Change in Agricultural Sector

Share of Subsector on Agriculture Sector GDP

| SUBSECTOR | 1980 | 2019 |
|----------------------------------|-------------|-------------|
| Food & horticulture crops | 59.55 | 32.93 |
| Plantation | 19.32 | 29.90 |
| Livestock | 5.94 | 12.38 |
| Forestry | 9.87 | 4.66 |
| Fishery | 5.32 | 18.63 |
| Agriculture services and hunting | - | 1.50 |

Agribusiness system needs to be:

- More efficient and competitive
- Fairer sharing of benefits and burdens between participants

Inequity in distribution of created income in the agribusiness system

Case of Rubber Industry in Jambi Province

| Beneficiaries | Proportion of income received (%) |
|--|-----------------------------------|
| Farm workers | 2.31 |
| Farm households and village collectors | 10.21 |
| Subdistrict collectors | 22.51 |
| District and provincial collectors | 18.56 |
| Corporation | 30.16 |
| Government | 16.24 |

Source: Machmud et al, 2019

Imbalances in price spread from producer level to retail market (2019/2020)

| Price Spread | % of producer price level |
|---------------------------------|---------------------------|
| SHALLOT | |
| Producer → wholesaler | 18.15 |
| Producer → modern market | 120.00 |
| Producer → traditional market | 48.85 |
| Wholesaler → modern market | 88.52 |
| Wholesaler → traditional market | 30.69 |
| RED CHILI | |
| Producer → wholesaler | 27.15 |
| Producer → modern market | 162.43 |
| Producer → traditional market | 69.90 |
| Wholesaler → modern market | 135.27 |
| Wholesaler → traditional market | 42.74 |

Rice marketing margin (April 2020)

| Description | Value |
|--|-------|
| Price of unhusked rice at farm level (IDR/kg) | 4600 |
| Rice equivalent price at farm level (IDR/kg)* | 8679 |
| Price of premium rice at rice milling unit (IDR/kg) | 10081 |
| Price of premium rice at wholesale level (IDR/kg) | 12382 |
| Price spread farm level → rice milling unit (%) | 16.15 |
| Price spread rice milling unit → wholesale level (%) | 22.82 |
| Price spread farm level → wholesale level (%) | 42.67 |

*Conversion factor: 0.53

Burden of economic crisis falls unequally

Relative per capita wages and salaries by household group (agricultural labor household as *numeraire*)

| Household group | 2000 | 2008 |
|--|------|------|
| Agricultural labor household | 1.00 | 1.00 |
| Agricultural entrepreneur household | 2.13 | 2.26 |
| Non agricultural low income level rural household | 2.32 | 2.53 |
| Non agricultural high income level rural household | 4.79 | 5.46 |
| Non agricultural low income level urban household | 4.10 | 3.83 |
| Non agricultural high income level urban household | 7.50 | 8.56 |

Decreasing agriculture's and farmers' terms of trade....

| Terms of trade | 2019 | 2020 |
|---|--------|--------|
| Agriculture's terms of trade | 112.48 | 102.17 |
| Farmers' terms of trade of food crops subsector | 105.78 | 101.43 |
| Farmers' term of trade of horticultural crops subsector | 102.44 | 101.28 |
| Terms of trade of smallholders estate crops subsector | 94.95 | 104.32 |
| Terms of trade of animal husbandry subsector | 108.05 | 98.08 |
| Terms of trade of fishery/aquaculture subsector | 106.96 | 100.35 |

Source: Statistical Yearbook of Indonesia, 2021 (CBS)

Higher share of food on household consumption expenditure..

| Household consumption expenditure (HCE) | 2019 | 2020 |
|---|-------|-------|
| 1. Food and beverage other than restaurants | 36.70 | 37.89 |
| 2. Clothing and footwear | 3.89 | 3.83 |
| 3. Housing and household equipment | 13.41 | 14.09 |
| 4. Health and education | 7.04 | 7.45 |
| 5. Transportation and communication | 24.84 | 23.07 |
| 6. Restaurants and hotels | 9.47 | 8.93 |
| 7. Others | 4.65 | 4.74 |
| Share of HCE in GDP | 54.22 | 53.91 |

Strategies to increase agribusiness competitiveness

1. Transforming agricultural sector
2. Localize agribusiness
3. Connect to bigger and richer entities

1. Needs for gradual transformation at the on-farm level

- ❑ Transformation of smallholders from primarily subsistence to fully commercialized agricultural production.
- ❑ Structural adjustments need to be done gradually. Support policies have been implemented extensively and for a very long time (such as the case of fertilizer subsidies and price support of rice). It takes a long time for the market mechanism to function efficiently if the policy will be withdrawn.
- ❑ There needs to be a policy component that enables smallholders to respond to emerging market incentives.
- ❑ Smallholders have the potential to become more entrepreneurial and expand their enterprises into other nodes of the value chain if properly supported by agribusiness institutions (Babu and Pinstrup-Andersen, 2009)
- ❑ Key is assisting smallholder farmers to overcome problems of imperfect markets and empowering them to be competitive participants in the market system.

2. Strengthening and improving local agribusiness

- ❑ Locally based agribusiness enterprises are typically small to medium-scale operations in rural areas that either process raw agricultural materials or provide marketing, transport, and other services.
- ❑ Explicitly focusing on the activities that occur after harvest and prior to final sale to consumers.
- ❑ Major investments are required to build the capacity of local agribusiness managers and firms so that they may effectively contribute to the sustainable growth.

Benefits of localize agribusiness

- ❑ Small rural businesses tend to be more intensive in using local resources and labor.
- ❑ Added value that can be captured at the local level will have a multiplier impact on local economy.
- ❑ Improvements in financial, transportation and communication facilities due to the growth of agribusiness can not only be enjoyed by other economic sectors at the local level, but also for providers of these facilities in reaching the wider rural economy.

3. Needs for association with larger and richer entity in national and global value chain

- ❑ Difficult to build a strong and sustainable local agribusiness, if only rely on local talent and resources.
- ❑ Similar to on-farm level, capital and technological problems are also faced by small-scale enterprises in rural areas.
- ❑ At the initial stage, what is needed is how to encourage farmer households to be able to increase the productivity and prices that can be obtained from their business, so that it is difficult to rely on businesses at the local level.
- ❑ It is necessary to connect local agribusiness to national and global value chains through collaboration with multinational and large domestic companies, cooperatives among producers, and individual private marketing enterprises.

Conclusion

- ❑ There are structural problems in the agribusiness system in Indonesia, especially the uneven development between subsystems.
- ❑ Structural problems can hinder the growth and competitiveness of agribusiness system as a whole.
- ❑ Transformation is not only needed at the farm level but also at the downstream of agribusiness.

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1. Statistical Yearbook of Indonesia (CBS) – various years
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