THE NATIONAL RESEARCH INSTITUTE
PAPUA NEW GUINEA

SPOTLIGHT

RICE IMPORT QUOTA SYSTEM IN PAPUA NEW GUINEA

ISSUES AND POLICY OPTIONS

Ronald Sofe
Francis Odhuno

www.nri.org.pg
Volume 9, Issue 7

Key Points

- Nearly 98 percent of rice consumed in Papua New Guinea (PNG) is imported. And as the country's population increases, the rising consumer demand for rice creates huge potential for a lucrative rice import business in PNG for the private sector.
- However, controlling the import of rice by allocating import quotas to traders is currently under serious consideration. There is already mounting concern that effective competition in the rice industry might be undermined if only one dominant player gets the largest share of the import quota.
- An optimum method to allocate quotas for importing rice is needed. This should be disclosed in a publicly available policy document. To avoid conflict of interest, import quota allocations should be made to trading companies; no allocation of quota should be made to domestic rice producers.
- PNG is also grappling with challenges of developing its own rice production system. However, a significant number of jobs in the rural areas will be lost if the Government bans other industry players from cultivating the rice crop in PNG, as it intends to do.
- The Government must adopt policies on rice production, an import quota allocation system, and marketing that are not discriminatory, unfair or anti-competitive so rents are not concentrated in the hands of favoured players.

inquire
inform
influence

September 2016

THE NATIONAL RESEARCH INSTITUTE
PAPUA NEW GUINEA

SPOTLIGHT
September 2016

RICE IMPORT QUOTA SYSTEM IN PAPUA NEW GUINEA: ISSUES AND POLICY OPTIONS

By Ronald Sofe and Francis Odhuno

Rice has become a household staple in Papua New Guinea (PNG) today, but it is yet to become an important food crop in the country's agriculture. The main problem has been inconsistent government policy, which is threatening to derail the country's quest for national self-sufficiency in rice supply. The Government has been contemplating granting a PNG-wide monopoly for the production of rice to a 100% foreign-owned entity, Naima Agro Industries, who would also get exclusive protection as an importer of rice.

Both the supposed new rice policy and the agreement signed between the government and Naima Agro Industries have not been made available for public scrutiny. Nevertheless, these proposed policy changes, as reported in the local press, significantly infringes on the interests of competition and consumer welfare. This Spotlight article contributes to the current debate about the looming changes in the country's rice policy; sheds light on the likely implications; and suggests options for allocating rice import quotas.

Production and import of rice in PNG

Anecdotal evidence suggests that rice was introduced in PNG more than 100 years ago. Books, policy documents and public statements from over the years remind us that some of PNG's climatic conditions are very suitable for rice production (Bourke and Harwood, 2012; NARI, 2011; DAL, 2007). And there has been concerted effort by successive governments to promote rice production, especially by smallholder rice farmers, throughout the country (DAL, 2007). But PNG imports still account for nearly 98% of rice demand, suggesting that the rice crop has not been sufficiently integrated into the country's traditional agricultural production system.

Still, in recent years there have been more efforts to promote and assist joint ventures between local and foreign investors to undertake commercial rice production in PNG to complement small-scale producers. The Government has also been promoting the nucleus and 'outgrower' rice production system as part of a targeted private sector development program (NARI, 2011; DAL, 2007). The aim has been to strengthen and expand local production and market share to ensure the country achieves self-sufficiency in rice production. But the results have not been impressive.

Perhaps because rice production is labour intensive, it is seen as commercially less viable for smallholder farmers than other food and cash crop alternatives (NARI, 2011). And while successive governments have made concerted efforts to implore on traditional landowners to free up their rural land for large-scale commercial rice farming, progress has been slow, often due to opposition by the landowners.

Consequently, there have been very low levels of rice production in PNG estimated at two percent of the ever-growing urban and rural consumer demand. This supply gap has created huge potential for a lucrative rice import business in PNG. Who gets the license and the quota to import rice into PNG, and the potential impact on the domestic rice development policy, have been the subject of debate that has recently resurfaced in the media.

Proposed rice import quota system

Currently, rice imports into PNG are not subject to quota. In keeping with its commitment to the General Agreements on Tariffs and Trade (GATT) following Uruguay Round negotiations, the country implemented a tariff reduction program that removed quantitative restrictions on rice imports. As a result, rice, which is primarily sourced from Australia, Thailand, Vietnam, and Malaysia in bulk quantities for milling and packaging in PNG, is also imported free of customs duty (PNG Customs Service, 2012 p.66). And the window has been open to any private sector player wishing to import rice into PNG.

It is not clear whether the Parliament has approved the country's proposed new rice policy that would take these privileges away from the private sector. The Department of Agriculture and Livestock (DAL), in a recent media notice for a stakeholder consultative meeting (Post Courier, 2016a), suggests that there is a new rice policy that guarantees exclusive rights to the Government to directly import rice into PNG. The Government is also expected to issue two types of import quota permits to rice importers in accordance with the policy guidelines.

The first is the Quota Rice Import Approval Permit, which entitles a permit holder to import rice during a given period of time with privileges of tax concession and reduced import duties. The only requirement is that the importer pioneers into large-scale mechanised and irrigated commercial rice farming. The second is the Standard Rice Import Approval Permit, which will be granted to an importer who does not engage in large-scale commercial rice farming, and may attract higher tax and levies without preferential treatment.

While details of the policy and permit allocation remain unclear, the proposed arrangements are disconcerting. There are concerns that allocating 80% of rice import quota to a pioneer investor will hold PNG's domestic rice policy at ransom (Post Courier, 2016b). It is likely that the preferred pioneer investor granted the largest import quota will have no tangible investment in the country's domestic rice value chain.

Yet it is still claimed that the proposed introduction of the quota system is part of the national rice policy aimed at promoting and boosting local rice crop production to achieve self-sufficiency and food security. It may be asked why the duty waiver should be in relation to rice imported by only one preferred pioneer investor. This is because, ideally, there should be no case where import quota is allocated to domestic producers of like goods. Ordinarily, any import duty waiver should be on imported machinery and other inputs to be used in domestic rice production.

While preferential treatment to the pioneer investor will damage the currently underdeveloped local rice production system, allocating the remaining 20% import quota to the rest of the traders will likely create imbalance in the country's rice market share.

The unending rice policy debate

The debate on rice production and the rice market in PNG seems never ending. Proponents of large-scale rice farming as projected in the supposed new rice policy base this support on the prospects of local rice production and greater self-sufficiency for food security. While this is a patriotic and noble cause, it is not clear how practical and feasible it would be to commercially operate large-scale rice projects in the country. Indeed, structural and chronic problems and the high costs of doing business are not in question. Recent research shows that, among others factors, the high capital cost of establishing irrigated rice farms and the high production cost per tonne remain severe constraints to the sustainable development of PNG's rice industry (Bourke and Harwood, 2012, pp 171).

During the 2005 Independent Consumer and Competition (ICCC) rice pricing review, the National Research Institute (NRI) strongly argued for the market to be liberalised and not dominated by a single player, which was, and still is, Trukai Industries. Since then, gains have been made through entries of other competitors in the rice industry.

In 2012, Naima Agro Industries, an Indonesian-owned company, proposed a rice project in the Central Province and asked for exclusive rights for the production, import and distribution of rice in PNG. This provoked different views from the public and business community.

The NRI argued, as it did in 2005, that despite the intentions of being a major agricultural project, the proposed monopoly by the developer had the potential to undermine benefits of competitive market enjoyed by the public (Gumoi and Nao, 2012). The country's consumer watch dog, ICCC, has also warned the Government against deals that will create a monopoly rice producer with access to a quota to control rice imports (ICCC, 2015 p.51).

Recent media reports, however, suggest that the issue has resurfaced, with the possibility that a greater share of import quota will be allocated to the pioneer investor. It is understood that the proposed national rice policy will grant pioneer status to the person willing to invest over US$2 billion in a highly mechanised large scale (100,000 ha) rice irrigation scheme(s) that will produce over 300,000 tonnes of rice by 2030 (ICCC, 2015 p.52)

Anecdotal evidence reveals that the Government has already approved Naima Agro Industry Ltd.'s investment plan for the K7 billion (US$2.2 billion) rice venture in Central Province (Post Courier, 2016c). While this confirms that the threshold level needed to obtain the pioneer status has already been met, there is no evidence that the project has got off the ground. Still, it is critical that the Government devise and disclose an optimum method that it will use to allocate import quotas.

Economic implications

Allocating greater import quota share and granting free import duties, tax concessions, and preferential treatment to a single pioneer investor sets a dangerous precedent. It has detrimental impacts on rice growers, suppliers, and consumers.

Import quota is a protectionist trade policy that restricts imports but benefits the trader at the expense of the consumer. Experience has shown that imposing quotas on imports has a prohibitive effect on competition through creating more market power for the trader who accesses greater import quota share.

Under the Quota Rice Import Approval Permit, the Government has based access to import licence on the requirement to invest substantially in commercial rice farming. Rice importers opting to trade under this permit must have the capacity and economies of scale to viably invest in the project. In principle, the rice quota system that is based on this pre-requisite and grants a trader exclusive and excessive access to imports is anti-competitive in nature. This goes against the spirit of the promotion of competition under the Independent Consumer and Competition Commission Act 2002 (the ICCC Act).

Under the Standard Rice Import Approval Permit, on the other hand, there will be restricted access to rice imports. The permit holder is obliged to acquire only a certain proportion of quota over a given timeframe and will be subjected to normal import duties and tax. This is discriminatory, unfair and irresponsible and increases the effect of market distortion in the rice industry. This also goes against the spirit of the National Small and Medium Enterprises (SME) Policy where the objective is to promote SMEs in various production sectors, inclusive of rice production, to enhance income creation and employment generation for Papua New Guineans.

Level playing field and optimal allocation of import quotas

At a recent Parliament sitting, a concern was raised on the dangers of the looming monopoly in the rice market if the pioneer status is granted to a lone investor (Loop PNG, 2016). With special privileges and entitlements, the Quota Rice Import Approval Permit has the potential to crown the pioneer individual or company as the legislated monopolist in the rice market.

Moreover, the advantages – tax concession, import duty waiver and preferential treatment on quota allocation – accorded to the legislated monopolist-cum-pioneer investor potentially enhances its ability to capture all the available rice market. Later, it may exercise its market power to constrain quota allocation and effectively deter new entry and expansion of existing traders with long histories in the country.

In a monopolistic market, consumers will be left with limited product choices – although the Government might argue that there are already a number of rice varieties to choose from. But consumers will also be faced with a higher price to pay as opposed to a market that has proven to be on level playing field. PNG's experiences of monopolies in the delivery of crucial goods and services have been dreadful. A monopoly trader emerging in the rice industry is therefore a dangerous prospect, especially with rice fast becoming a staple food throughout the country; the cost of survival for many households will increase.

To avoid this pitfall, access to import quotas should be open to all industry participants. There are two optimal methods of allocating import quotas. One is through regular auctions to avoid entrenching the privilege of importing rice to one or a select few companies on a long-term basis. But auctions may not be appropriate in the PNG case – perhaps because the market is already dominated by a few likely highest bidders.

The alternative, to be fair, is to allocate import quotas in proportion to the size of the local operation of the potential rice importers. There is some evidence of effective competition among importers and retailers in the country, with Trukai Industries leading the share of the market and supporting development of the local rice industry (Business Advantage PNG, 2015). Allocating import quotas according to the size of local operation will promote competition and fair trading in rice products. However, there should be some free quota allocated on a first-come-first-served basis for new entrants (with no performance history) to the market.

Conclusion

The press has recently reported on PNG's rice market but the absence of local production data and the opacity of the new rice policy have prevented meaningful research and analysis of the issues raised. Nevertheless, the implications of the proposed rice import quota system as gleaned from the press are discriminatory, unfair and anti-competitive. A competitive market is good for an efficient outcome and allocation of economic resources. But the Government's proposed import quota allocation system will frustrate competition and create an inefficient rice market in the country. By promoting anti-competitive trade practices through the proposed unfair import quota policy/system, the Government will be violating World Trade Organization (WTO) trading rules; it cannot be argued that rice is a "sensitive commodity" in PNG so as to convince the international community about this move.

Yet the role of the Government is to promote an environment that is conducive for strong private sector competition. The Government should focus on removing barriers to the growth of a competitive rice market. Rather than supporting a yet-to-be-established foreign entity to unfairly compete against the existing vibrant private rice firms in the market, the Government should consider splitting the annual rice import quota into two parts.

80% of the rice import quota should be allocated to the existing industry players on a pro rata basis based on their past performance. The remaining 20% of the import should be allocated to new market entrants on a first-come-first-served basis and then to the existing companies who have exhausted their quotas. Applications for import approval and import quota allocation should not be refused, if they satisfy the prescribed conditions.

To avoid conflict of interest, import quota allocations should be made to trading companies; no allocation of quota should be made to domestic rice producers. In any case the preferential treatment – tax concessions and import duty waiver on farm machinery and other inputs – should not be misinterpreted; they are designed to promote local economic production of rice for domestic consumption with a view to reducing the importation of rice.

References

Bourke, R. M. and Harwood, R. (2012). *Food and Agriculture in Papua New Guinea*. Canberra: ANU Press.

Business Advantage PNG (2015, July). Trukai investing tens of millions to produce Papua New Guinea grown rice. Retrived from www.businessadvantagepng.com/trukai-investing-tens-of-millions-to-produce-papua-new-guinea-grown-rice/ (Accessed 15 Aug 2016).

Department of Agriculture and Livestock (DAL) (2007). *Agricultural Development Plan 2007–2016 Volume 1: Policies and Strategies Part 2*. Port Moresby: DAL.

Independent Consumer and Competition Commission (ICCC) (2015). *2015 Rice Industry Pricing Review*. Port Moresby, Independent Consumer and Competition Commission.

Gumoi, M. and Nao, L. (2012). Creation of monopoly in rice industry detrimental to people's overall welfare. *National Research Institute Spotlight,* 6 (1). Port Moresby: National Research Institute.

Loop PNG (2016, August). PM O'Neill clarifies rice pricing. Retrived from www.looppng-sb.com/content/pm-o'neill-clarifies-rice-pricing (Accessed 17 Aug 2016).

National Agricultural Research Institute (NARI) (2011). 'Rice Stakeholder Workshop Report'. Lae, 22–23 November 2011.

PNG Customs Service (2012). *Customs Tariff Act of 1990: Papua New Guinea Customs Import & Export Tariff 2012 Edition*. Port Moresby. PNG Customs Service.

Post Courier (2016c). "Government approve K7bn rice plan in Central Province." 8 April 2016 (p. 3).

Post Courier (2016b). "Notice to Current Rice Importers in Papua New Guinea." 1 August 2016 (p. 25).

Post Courier (2016a). "Legality of rice monopoly questioned." 16 August 2016 (p. 20).

About the authors

Ronald Sofe is a Research Fellow in the Economic Policy Program at PNG NRI. Dr Francis Odhuno is Program Leader and a Senior Research Fellow in the Economic Policy Program at PNG NRI.

The National Research Institute (NRI), PO Box 5854, Boroko, NCD 111, Papua New Guinea. Telephone +675 326 0300; Facsimile +675 326 0213.
Website: www.nri.org.pg; email: nri@nri.org.pg

NRI is an independent statutory authority established by an Act of Parliament in 1988 and confirmed by the IASER (Amendment) Act 1993.