Europe's cane sugar refiners – what is fair competition?

A personal perspective on the EU sugar sector by Tate and Lyle's Gerald Mason

Casual observers of Europe's sugar market may be perplexed by the current situation. White sugar prices in Europe have risen 36% in 12 months, leaving them at a 40% premium to world prices. At the same time, Europe's cane sugar refineries must pay increasingly high import duties through a series of European Commission auctions.

Even then, the raw material they can access is insufficient to run their plants. All of this despite global availability of sugar growing and prices falling. How did Europe's sugar market get into this predicament and how do we extricate ourselves?

The key issue is that the current Common Market Organisation (CMO) for sugar is based on an EU forecast from 2005 that cane sugar imports from Least Developed Countries (LDC) and African, Caribbean and Pacific (ACP) countries would almost double by 2012/13 to 3.5 million tonnes.

This is important as these countries benefit from preferential access to the EU sugar market so are exempt from the otherwise punitive fixed import duties of €339 per tonne for cane sugar for refining and €419/t for refined sugar. These fixed duties are designed to prevent imports from other countries by effectively doubling the market cost of the sugar.

The problem for Europe's sugar market, and its cane refiners, is that the forecasts for duty free imports from LDC and ACP counties have not been realised. For this marketing year, 2011/12, the Commission forecasts imports of 1.8mt – a full 1.5mt below the 3.3mt forecasted in 2005.

The lack of imports from preferential suppliers means that Europe's cane sugar refiners cannot access the raw material they need – cane sugar for refining – in the volumes that are necessary to run their European plants and supply the needs of their European customers.

The reasons for the import deficit are numerous, but one thing is clear: sugar from the LDCs and ACPs is not being exported to other, more lucrative, markets. This criticism, levied as world sugar prices climbed to record highs in recent years, has no basis in fact. *International Sugar Organisation* data clearly shows that cane sugar exports from these developing countries to all markets have fallen since 2005.

Notwithstanding the overly optimistic original forecast of imports, the reasons for the shortfall in imports are almost all structural. Production is in decline in a number of preferential supplying countries, a tragic fact given the importance of the industry in many of these small and vulnerable economies, and a trend which we should be seeking to reverse.

Meanwhile, growth in others is well behind the EC forecast due to multiple obstacles. The financial crisis has restricted access to capital for investment, whilst the EU's disbursement of funds for sugar accompanying measures is slow. Where sugar production is growing, much of the additional supply is consumed by the producers' own growing populations. This leaves Europe with a structural sugar deficit as sales from the other two models – beet sugar and isoglucose – are limited by quota. To solve the problem, the EC has invoked its powers, giving them the possibility to respond to the shortage of sugar at their own initiative through the Management Committee procedure.

If current and proposed policies continue to restrict access to raw materials, cane refiners will not survive

It would be reasonable to assume that a policy response to a shortage of sugar resulting from a shortfall of ACP and LDC imports would be to make good those imports from other cane sugar suppliers, and that this new supply would be made available free of import duty. This would fulfil the basic assumptions that the legislation was based around. However, this response was not adopted and indeed, for many months, there was no response at all.

Instead, choice and implementation of a solution has been mired in political debate. It has been clear since 2009 that cane imports were not growing as forecast and were not meeting demand.

Unfortunately, the political nature of the debate meant that the issue was not addressed until it caused a market crisis in late 2010. By then cane refineries had to cut back or even stop operations due to insufficient raw material and their customers found other supplies were often simply unavailable. Prices have been on an upward trajectory ever since.

The solutions ultimately adopted have also been unfair for cane refiners. Despite the shortage stemming from insufficient imports of cane sugar to meet demand, let alone Commission import forecasts, the largest solution to date has been to effectively increase quotas for beet sugar.

This means that beet processors are allowed to market more than their quota in the EU, whilst cane refiners face a shortage of raw material forcing them to close factories and reduce their workforce. For any sophisticated manufacturing industry, where a high proportion of costs are fixed, lack of raw material is economically unsustainable.

In value terms, the solutions have also been unfair to cane refiners. Extra access to imports has most recently been through a series of tenders, where cane refiners and other importers are forced to bid against each other for access to extra raw material and against imports of white sugar from non-EU refineries.

The theory is that this allows the market to determine how the deficit should be filled. In practice, it means that refiners are forced to pay a much higher price for their raw material than their main competitors in the beet sector, who do not face the same regulatory costs.

Until 2015, with imports unlikely to grow significantly from the ACP and LDC, these ad-hoc and political solutions are likely to be repeated every marketing year. Cane sugar refiners will continue to make the point that as a European manufacturing business they deserve fair access to raw material.

In practice, this means that either LDC and ACP countries supply the forecast volumes or, if they cannot, then the shortfall should be made good from other sources that can supply, and to make that supply free of import duty.

Post-2015 brings a new challenge. With the Commission proposing to abolish quotas for beet and isoglucose, cane refiners are left in a precarious and unfair position in which they still face limitations on access to raw material. But if the European Parliament and Council instead decide to maintain quotas for beet and isoglucose, cane refiners nevertheless need an automatic mechanism to ensure their fair raw material needs are met.

If current and proposed policies continue to restrict access to raw materials, cane refiners will not survive as part of the supply mix in Europe's sugar sector. Their disappearance would be regrettable but understandable if they were uncompetitive in a market sense. But this is not the case. Cane refiners are being driven out of business by policy choices that prevent a level playing field among beet, cane and isoglucose producers.

There is no doubt that finding a fair legislative balance between the three very different European models of sweetener manufacturing will be difficult. Yet, it is mandatory if Europe wants to build an agricultural and food manufacturing sector that is globally competitive and provides high quality products, choice and competition for its consumers.

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