ESRA

Study on Raw Materials in the EU Sugarcane Sector

ESRA

Executive Summary

This study has been produced by the secretariat of the European Sugar Refineries Association (ESRA), which represents the majority of the sugarcane refining industry in the European Union. Its purpose is to present EU institutional stakeholders with the reality faced by our industry, particularly in light of the abolition of EU sugar quotas in 2017. We deemed this necessary for a number of reasons:

> The narrative on sugar in the EU is dominated by the production of white sugar from beet – **our sector's voice often goes unheard as a result.**
> The **global sugar market is complex, and so therefore is our ability to access raw sugar.** What might at first glance appear to be access to raw materials for our sector is often purely theoretical – it is essential that institutional stakeholders be made aware of these nuances.
> The **commercial situation for EU cane refiners has reached a critical point**, with the majority of our former access possibilities having disappeared as a consequence of EU quota abolition.
> The EU is **currently engaged in trade negotiations** with two markets which can provide a lifeline for our sector – Brazil (as part of Mercosur) and Australia. We have already lost an opportunity to gain access to more raw sugar in talks with Mexico – it is crucial that the same mistake is not made again.

The study proceeds as follows:

In a first part, we describe the milestones that have led to the current market situation in the EU, defined by an overabundance of white sugar, and an **unsustainably low white sugar price.** We explain how the primary **cause of this situation is the overproduction of sugar by EU beet producers.** EU refiners have done nothing to contribute to this surplus, and yet must compete in the same low-price market as our beet-producing competitors. What is more, cane refiners do not enjoy access to the supports that have been put in place to help the sugar sector adapt.

Secondly, we show how an indirect consequence of the abolition of sugar quotas has been a **massive reduction in access to raw sugar imports** for EU cane refiners. This is because the former access enjoyed to raw sugar from ACP/LDC countries has been rendered uncompetitive due to the high purchase price of the latter, while access to more competitively-priced sugar from countries such as Brazil and Australia is made impossible as that **sugar is subjected to an import duty.** In both of these cases, the **"refining margin"** (i.e. the difference between the purchase price of raw sugar and the white sugar price in the EU) is rendered so small as to make cane refining uncompetitive.

In a third segment, we zoom in on the ACP/LDC countries to show how **the EU cane refining industry can no longer depend on this source of raw materials** for the bulk of its needs. In this case, the market situation in the EU is but one cause – supply factors in many ACP/LDC countries are also relevant.

Fourth, we put the current EU access to the global supply of raw sugar into context – even when we count "theoretical access" (i.e. where there is preferential access to sugar, but market conditions mean that EU refiners cannot import this sugar and remain competitive), **ESRA members enjoy access to only 2% of the global supply of raw sugar.** This means that our ability to adapt to the new commercial context is severely – and artificially – curtailed.

Lastly, we show how **including duty-free access to raw sugar through TRQs in trade deals** with Mercosur, Australia and others would guarantee a sustainable EU sugar sector across the vectors of security of supply, price, employment, and the production of the sugar itself.

We conclude our dive into the EU cane refining sector by placing all of the above into the current political context, underlining that this is a crucial time to put our message across: without meaningful access to raw sugar through free trade agreements, the survival of our sector is in great peril. The time to act is now.

Introduction

The EU sugar market is in crisis. The 2017 abolition of quotas in the sector has predictably led to freefalling prices, threatening the survival of all but the biggest producers. EU beet growers, insulated from the harsh reality of supply and demand economics for decades, overproduced massively in the first quota-free year, producing far too much cheap sugar for an adjusting market, made even worse by a global surplus and low price level.

For cane refiners, this market transformation has been particularly challenging. Refining of imported raw cane sugar, with its centuries of history and thousands of jobs, is facing existential threat. With our share of EU white sugar production now hovering around 5% (see figure 1), we are often faced with the suggestion that, despite impending market adjustment, we have simply failed to adapt. The implication here is that cane refining has no place in a competitive EU sugar market. We completely reject this notion. There is a simple solution to the current crisis: in this market-oriented EU sugar sector, all cane refiners require to compete and ensure a dynamic, diverse sector is the ability to act like normal market operators. In this paper, we will show how this is currently not the case, and propose fair and feasible ways of addressing this situation.

About ESRA

The European Sugar Refineries Association (ESRA) is the leading voice of Europe's sugar refining industry. Established in 2011 and headquartered in Brussels, the association represents the majority of the full-time cane sugar refineries in the EU.

Our members are full-time cane sugar refineries located in a number of EU Member States. Cane refiners provide consumer choice, competition, food security and a link to global markets, thanks to their use of a different raw material for producing sugar.

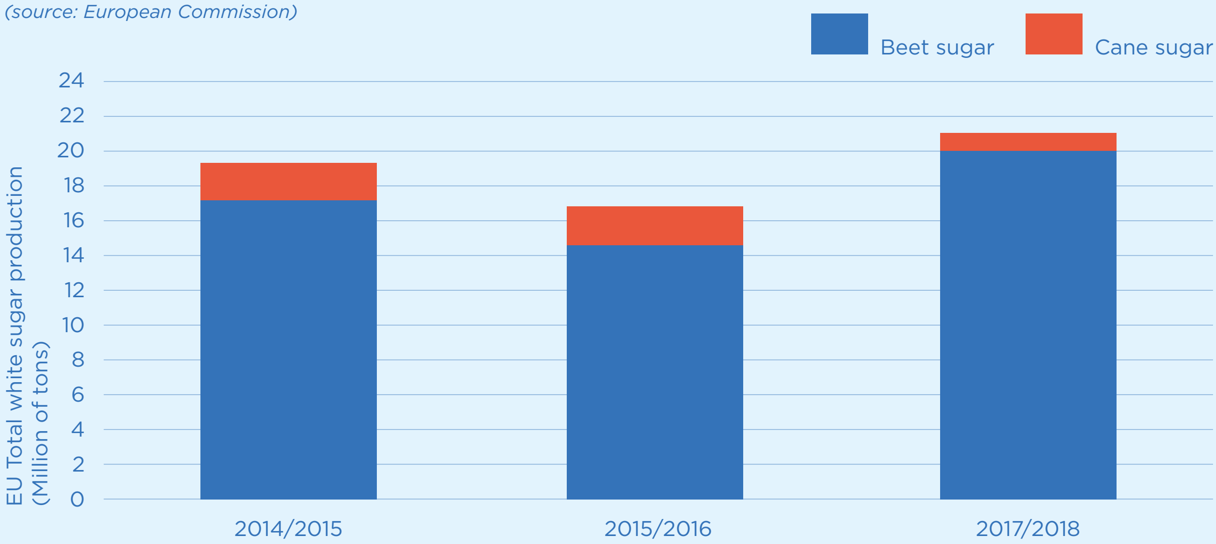
EU cane refiners employ 4,500 workers, mostly in high grade jobs (chemists, engineers, plant operatives) and provide several more jobs indirectly. They have 2,400 active customers ranging from food & drink processors and retail chains to pharmaceuticals.

ESRA members market several types of sugar products derived from sugar cane for a number of different uses and purposes across various different market segments, namely industry and distribution.

EU cane refiners

Source: List of Full-time refiners, European Commission, 2016. ESRA's membership represents the majority of the EU cane refining sector, including Tate & Lyle Sugars (UK), Agrana (Romania), SRB (Italy), Sidul and RAR (Portugal)

Figure 1: Share of cane refiners in EU sugar production
(source: European Commission)



EU sugar reform – a one-way street

With the abolition of sugar production quotas in 2017, the sector became the last major agricultural commodity market to become liberalised, amid promises of a truly market-oriented sugar industry. However, the liberalisation of our sector has been approached in a manner which has exacerbated an already imbalanced market. This is largely a product of political context – as EU sugar policy is subsumed into broader agricultural policy (but not, for example, a food-specific policy), its primary targets are European farmers and beet processors, who operate tightly connected supply chains. Sugar cane production in the EU is negligible, only taking place in some outermost regions – full-time cane refiners are completely dependent on imports from outside the EU. The farmers who produce our raw material thus remain unrepresented in EU policymaking circles, and EU sugar policy is unbalanced as a result.

Figure 2: EU overproduction and the global sugar market
(sources: European Commission, USDA)

Abolition of EU sugar quotas, including minimum prices ↓	In October 2017, the EU stops applying quotas to sugar production, along with abolishing minimum buying prices. This had been foreseen for a number of years.
Massive overproduction of EU sugar beet ↓	EU beet producers, freed from the constraints of quotas, produced over 20 million tonnes of white sugar, an increase of ca. 25% over the previous year.
Depressed EU white sugar prices ↓	Unsurprisingly, this overproduction coupled with the abolition of price controls led to a collapse in white sugar prices, with a record low of €320/tn in October 2018.
Removal of important white sugar premium market ↓	Prior to quota abolition, the EU white sugar price was well above the global average, and thus a large premium market for white sugar. With the EU being the world's 2nd largest consumer of sugar, the removal of this premium market depresses global prices.
Addition to global surplus	The overproduction in Europe added to the already-existing global sugar surplus, further depressing prices in the medium-term.

Figure 2 above shows that the current low sugar price is caused largely by EU policy choices and the actions of European sugar producers – although overproduction in Thailand and India has also had an impact, the combination of the first two factors bears the brunt of responsibility for the difficult situation. However, the ways in which EU sugar market players have been able to adapt to the changed market situation are also driven by EU policy choices, and in this case, the approach has been remarkably imbalanced, as shown in the Table 1.

Furthermore, EU beet sugar producers have access to an important adaptation measure which is largely closed to cane refiners – export markets. In the past year, almost all major EU sugar producers have expanded their operations to refocus towards exports, a lucrative business now that EU prices are so low, and bearing in mind Europe's proximity to high-value markets in North Africa and the Middle East in particular. All in all, exports increased from 1.35m tonnes in 2016/17 to 3.35m tonnes in 2017-18 – a 150% increase. For cane refiners, this opportunity is largely ruled out, as raw materials must first be imported – the addition of an extra shipping leg means that even when these raw materials are duty-free, practice remains largely unprofitable.

Table 1: EU policy aiding adaptation to sugar quota abolition

Beet producers	Cane refiners
Direct CAP support (voluntary coupled support)	No CAP support
Indirect CAP support (direct payments)	
Potential private storage aid	Cane refiners ineligible for private storage aid
Massive increase in volume of raw material	Existing restrictions to global market exacerbated by low EU sugar price (CXL and majority of ACP/LDC sugar rendered unprofitable)
Reduction in price of raw materials	

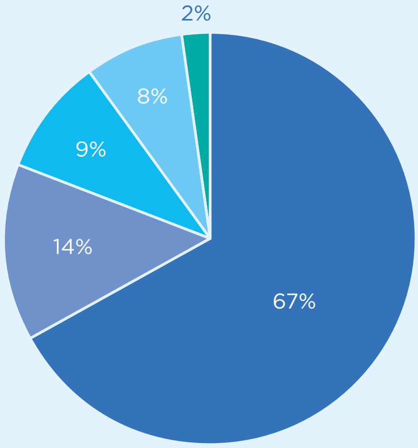
Indirect consequences of quota abolition: a collapse in access to raw sugar

Historically, cane refiners had access to raw sugar through a number of sources, as shown in Figure 3. The bulk of imports (average 67% 2012-16) came from Africa-Caribbean-Pacific countries and least-developed countries (ACP and LDC) through the Everything But Arms (EBA) agreement as well as under Economic Partnership Agreements (EPA). This important source being duty- and quota-free, it made up the bulk of raw sugar imports. This was despite the fact that purchase prices for raw sugar from these countries are sometimes amongst the highest on the market – cane refiners could absorb these high purchase prices due to high white sugar prices in the EU.

Imports also came from two important producers under the CXL quota – 14% provided by Brazil, and 9% by Cuba. In these cases, imported raw sugar was subject to an import duty of €98/tn. Combining this with lower purchase prices and high EU white sugar prices, these were still profitable sources of raw sugar for EU refiners.

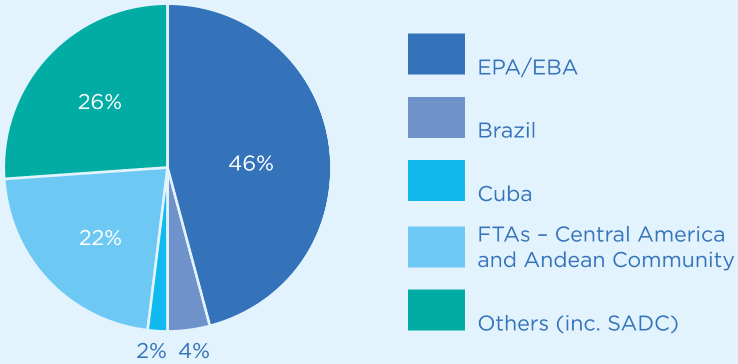
Following the conclusion of free trade agreements with the countries of Central America and the Andean Community in 2012, these also became important provides of EU raw sugar needs, albeit restricted by tariff-rate quotas (TRQs). These allowed the import of sugar with no duty attached, but again due to higher EU sugar prices, did not displace ACP/LDC suppliers completely.

Figure 3: Sources of EU raw sugar (average 2012/2016)



Total import: 2.3m tonnes

Figure 4: Sources of EU raw sugar (2017/2018)



Total import: 0.961m tonnes

(source: European Commission)

However, the diversity of sources available in the years 2012-16 is no longer our reality in a post-quota world. While theoretically, EU cane refiners still has access to these sources of raw sugar, market realities render them almost meaningless.

In the case of ACP/LDC countries, a massive amount of the supply has been ruled out as the raw sugar often costs more than EU white sugar prices – evidently, this makes the import and refining of this raw sugar commercially impossible.

For sugar sourced through the CXL tariff-rate quotas (TRQs), the imposition of the €98/tn duty means that this has also been ruled out as a source for European cane refiners. Indeed, in marketing year 2017/18, these TRQs remained almost entirely unfilled. Even in the case of a discounted TRQ with Brazil – where the duty is temporarily reduced to €11/tn due to the EU accession of Croatia – less than half of the 55,000tn TRQ was filled. The CXL tariff was EU cane refiners only access to the Brazilian market.

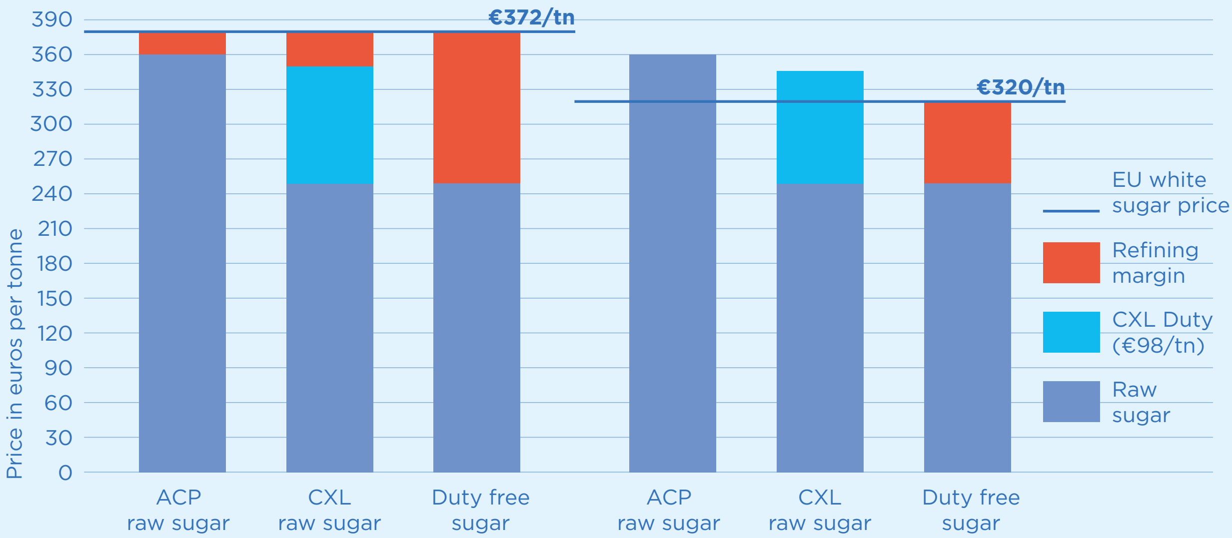
As Figure 4 shows, two parallel phenomena can be observed. On the one hand, the volume of raw sugar imported into Europe has already seen a drastic decrease, coming in at less than 1m tonnes, compared to a 2012-16 average of 2.3m tonnes. While this is evidently a problem for our sector, an even more important change is that seen in the composition of imports. While EPA/EBA imports made up almost 70% of our sector's imports in 2012-16, this has already been reduced to 46% in 2017/18, and will likely reduce even further for the marketing year 2018/19. Furthermore, CXL imports have gone from 23% of our imports to just 6%, and may even approach zero in 2018/19.

By contrast, the portion of ESRA members' raw materials arriving through duty-free free trade agreements has grown dramatically. From 10% on average in the years 2012-16, this source of raw materials now accounts for almost at least 40% of our total resources. This is clear evidence that these duty-free FTAs are the only viable source for our industry moving forward.
This reality is presented in the Figures 5 and 6, which show two different scenarios since the abolition of sugar quotas. In February 2018, when the EU white sugar price had already fallen to €372/tn, the "refining margin" (i.e. the difference between the cost of white sugar and raw sugar) had already been reduced to a negligible amount. This was the case for ACP/LDC sugar (based on average import prices of €360/tn) and CXL quota sugar (based on the baseline of a world raw sugar price of €250/tn). Bearing in mind that the refining margin must account for costs (including shipping, human resources etc.) before profit is even considered, this is evidently unsustainable, and only duty-free, competitively priced sugar could allow cane refiners to function normally. Figure 6 shows how desperate the situation had become by October 2018 – at

this point, neither ACP/LDC sugar nor CXL sugar was even theoretically capable of supplying our industry, as in both cases, the costs of the raw materials were higher than the EU white sugar price. Here again, duty-free sugar through FTAs with competitive suppliers is the only possible option.

Figure 5: Refining margin for raw sugar - February 2018

Figure 6: Refining margin for raw sugar - October 2018



ACP/LDC raw sugar – an increasingly scarce resource

As stated above, ACP/LDC sugar imports have already seen a dramatic drop since quota abolition. However, one might argue that this situation is temporary, and that ACP/LDC suppliers can again become the primary source of raw materials for EU cane refiners, thus providing an ample supply of duty-free, quota-free sugar. We submit that this assumption is false, and does not take into account movements within ACP/LDC sugar markets, which already show a pivot away from the EU as a major export market.

One notable change is the decision by ACP/LDC producers to focus on regional or domestic markets, as can be seen in the case of Malawi, Cambodia, Kenya, Jamaica, and Mozambique – all of which were once important sources of EU raw sugar imports. These producers are making these decisions for a number of reasons:

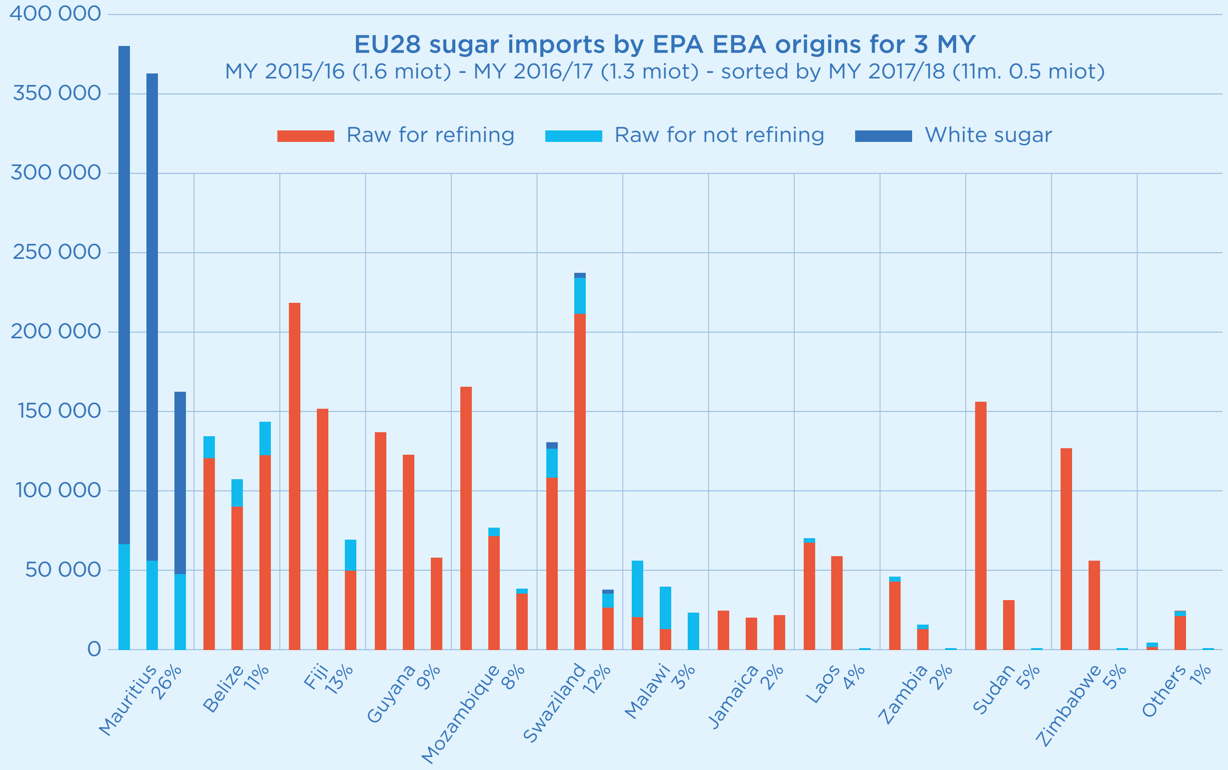
(i) On the one hand, the biggest drivers of demand for sugar on the global market are located in developing countries – it makes sense for these producers to follow that demand, and to grow domestic markets. This can be seen for example in Cambodia, which is focusing its attention on the Chinese market, and Kenya, which is working towards meeting domestic demand.

(ii) Secondly, focusing on domestic markets allows these producers to move up the value chain. A good example here is Jamaica, where the former situation was to export its raw sugar while importing white sugar to meet domestic/regional demand. The country's agriculture ministry rightly highlighted the irrationality of this approach.

Incidentally, a key rationale of the EU's Economic Partnership Agreements with APC/LDC countries is to foster regional demand, and the movement of ACP/LDC producers towards full value-chain production is perfectly aligned with this objective.

The shifts outlined above are indeed backed up by hard data, as outlined in the table, produced by the European Commission, which shows the collapse in ACP/LDC imports, almost without exception:

Figure 7: Collapse in ACP/LDC imports
(source: European Commission)



This is not to say that ACP/LDC countries cannot form part of the import mix for EU refiners in the future – indeed, some may even remain competitive despite very low EU white sugar prices. However, there is absolutely no reason to believe that this supply source can ever provide the EU's raw sugar needs in the same way it did before quota abolition.

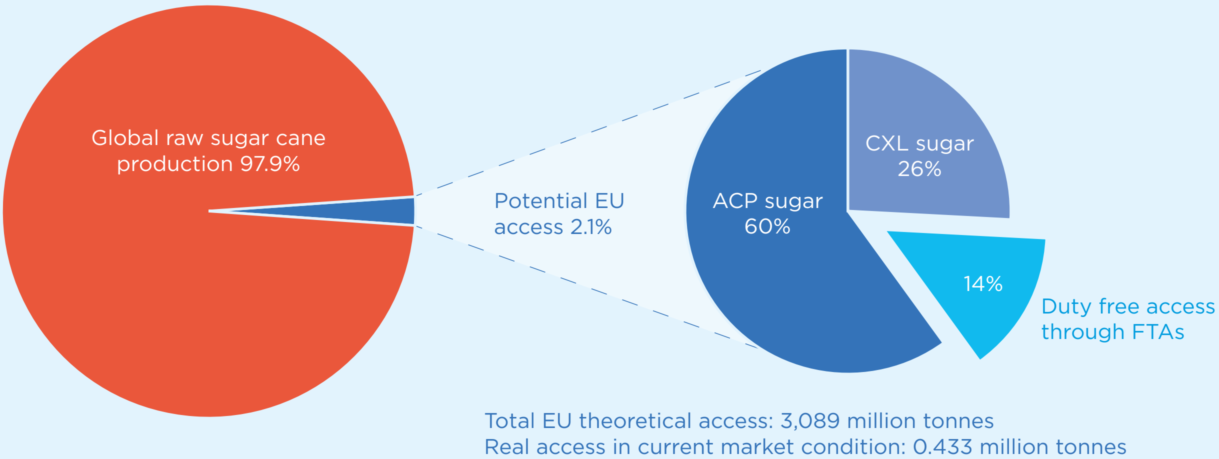
Lack of access to global supply

The European Commission rightly advises all participants in the EU sugar sector that they must adapt to the changes inherent in the reform of the industry. Indeed, the cane refining sector has already adjusted to this by diversifying our product offer, as well as by operating below our full capacity. What institutional stakeholders seem to forget, however, is that the market liberalisation in the EU is an incomplete process. While EU domestic producers do indeed now operate without production quotas or minimum prices – and can thus export freely as a result – they are still protected by the restrictive access taken by the EU towards raw sugar imports. This is shown clearly in Figure 8, where it can be seen that EU refiners are currently restricted to less than 2.1% of the global raw sugar market.

However, this table needs to be read in a more nuanced manner – this is "theoretical access", as it includes both ACP/LDC sugar (where we have taken the record amount of 1.865m tonnes) and CXL sugar. As described above, these sources are currently closed to EU refiners due to the low EU white sugar price – and are likely to remain so. Thus, the real access to the global sugar market is a paltry 0.3%.

Cane refiners must ask the question: how can we adapt to market liberalisation when we are not permitted to act as rational market participants?

Figure 8: Effective EU access to the global market in raw sugar
(sources: European Commission, USDA)



FTA access to raw sugar from Mercosur, Australia providing for a sustainable EU sugar sector

The future sustainability of the EU sugar sector is dependent on the survival of the cane refining sector. This is because of a number of factors:

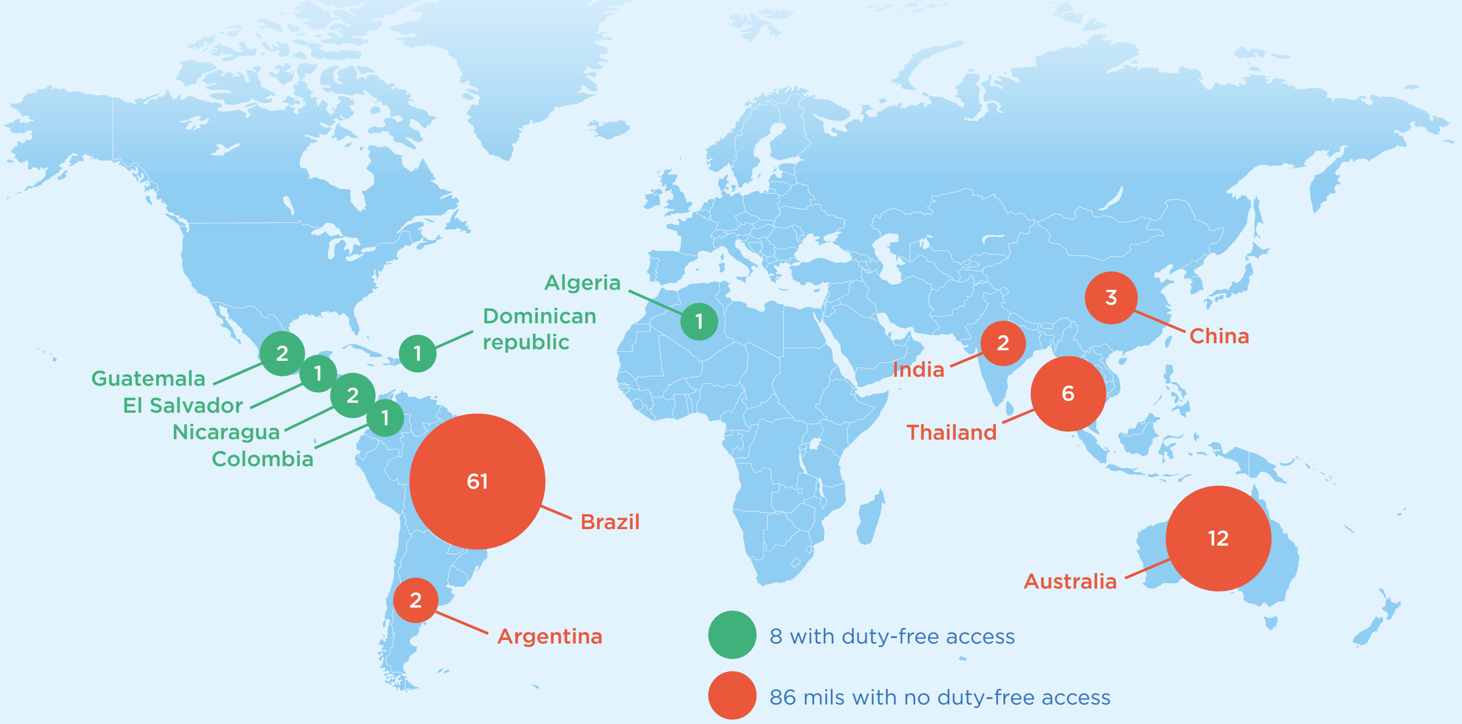
Sustainable supply
While it is likely that the EU will remain a surplus market in sugar for the foreseeable future, it would be unwise to restrict EU sugar production to the sole source of EU sugar beet. Although sugar beet has improved in reliability and yield in recent years, it cannot match the certainty provided by access to the global cane sugar market, which accounts for 80% of global sugar production. Indeed, in the past, many beet processors added refining capacity in order to benefit from imported raw cane sugar. However, much of this has been mothballed, making full-time refiners such as the members of ESRA the only reliable remaining connection to the global cane sugar supply. Beet output is also susceptible to changing weather conditions, as was seen with the drop in output resulting from the drought conditions of 2018.

Sustainable pricing
With the EU set to remain a surplus market, and one in which low white sugar prices predominate, it is illogical to state that raw sugar imports would be capable of depressing EU white sugar prices. Barring a massive, highly improbable drop in global raw sugar prices, EU cane refiners will never be able to undercut beet producers, as the refining margin is already extremely small. What is more, as all viable future sources of raw sugar are controlled in volume by TRQs, cane refining simply could not have a significant effect on the wider price level due to its small share of the market. However, were a lack of competition to lead to higher white sugar prices in Europe, cane sugar access could act as a control of sorts on EU prices becoming too high, as sugar imports could displace some domestic production were prices to rise to an unreasonably high level. Put simply, the connection to the global market through cane refining (and indeed through the potential import of white sugar from ACP/LDC countries) is healthy for the EU sugar sector.

Sustainable employment
The simplest argument of all that cane refiners put forward to decision makers is this – our sector current supports up to 4,500 jobs for EU citizens. At the moment, starved of supply, our industry may well disappear, and all of these jobs – many located in some of the most economically depressed parts of the EU – will disappear with it.

Sustainable sugar
Last of all, we can look beyond the three vectors of sustainability mentioned above and instead zoom in on the product itself. Worldwide, the sustainability of sugar production is guaranteed through the rigorous certification standards and practices employed by Bonsucro. As Figure 9 shows, EU cane refiners currently have access to only 5 sugar mills which export Bonsucro-certified raw sugar. This not only means that we are unable to contribute to the overall sustainability of the EU sugar sector, it also means that our ability to orient our adaptation towards consumers' taste for sustainable produce is severely limited.

Figure 9: EU access to sustainably produced sugar – locations of Bonsucro-certified mills
(sources: Bonsucro)



As the map shows, ESRA members currently enjoy duty-free access to only 5 Bonsucro-certified mills which export raw sugar (2 in Guatemala, 2 in Nicaragua and 1 in El Salvador through the EU-Central America FTA). Certified ACP members (1 in Algeria and 1 in Dominican Republic) and those covered by the EU-Andean Community FTA (1 in Colombia) export white sugar only.

Conclusion

At the time of writing (early 2019), European Commission officials were engaged in negotiations with their counterparts from both Mercosur and Australia. Furthermore, negotiations may (re-)open with Thailand in the foreseeable future. For our sector, these negotiations are a last chance to secure access to the raw materials that we desperately need to keep our businesses alive. Unfortunately, we have already missed a chance to secure better access in the negotiations between the EU and Mexico, which concluded in 2018 and yielded a very disappointing result for EU refiners – a small TRQ with a duty of €49/tonne attached. For ESRA members, the attachment of this duty means that Mexico is effectively blocked from becoming a source of the raw materials we so desperately need.

As this study has shown, the changed EU market in which we now operate means that our access to the global supply of raw sugar is even more severely restricted than in the past. We believe this can be resolved, and provide some conclusions below on how this can be achieved. But first of all, we would like to remind stakeholders what we are not asking for:

> We are not asking decision-makers to impose any kind of restrictions on domestic sugar production in the EU. Indeed, we hope for a fully liberalised sector in which we can join our beet processing colleagues in a truly competitive market.
> Although we have outlined the existence of supports for sugar beet production in Europe, we are not calling for their elimination. We understand the complexities of EU agricultural policy and the need for balanced regional and rural development. Rather, we think it important to point out that subsidies of EU sugar through coupled support, and the potential for supports such as private storage aid, are a reality: EU sugar producers should accept and acknowledge this in their communications with stakeholders.
> We are not seeking to abandon ACP/LDC sugar imports. Should ACP/LDC prices become competitive for ESRA members, there is no reason why we would not use these sources of raw materials. However, the current market situation simply does not allow us to import from these partners.
> We are not asking for unlimited access to the global sugar supply. We understand that our supplies will always face some limitations due to political sensitivities in the EU sugar sector.

All ESRA is asking for is the chance to compete in the EU sugar sector, through the provision of meaningful access to raw sugar.

The only way this can be achieved in a manner that is fair to our sector is through the inclusion of duty-free access to raw sugar through EU free trade agreements with raw sugar exporters.

If we fail to gain access to raw sugar, there will be no more discussion, as our sector will cease to exist. To avoid this scenario, EU negotiators must remember that, when it comes to sugar, it is a mistake to approach these talks from a purely defensive point of view.

We are EU stakeholders too, and we need EU negotiators to remember this. We need them to stand with us in these talks, and to fight for the access that can save our historic industry from an almost certain demise.

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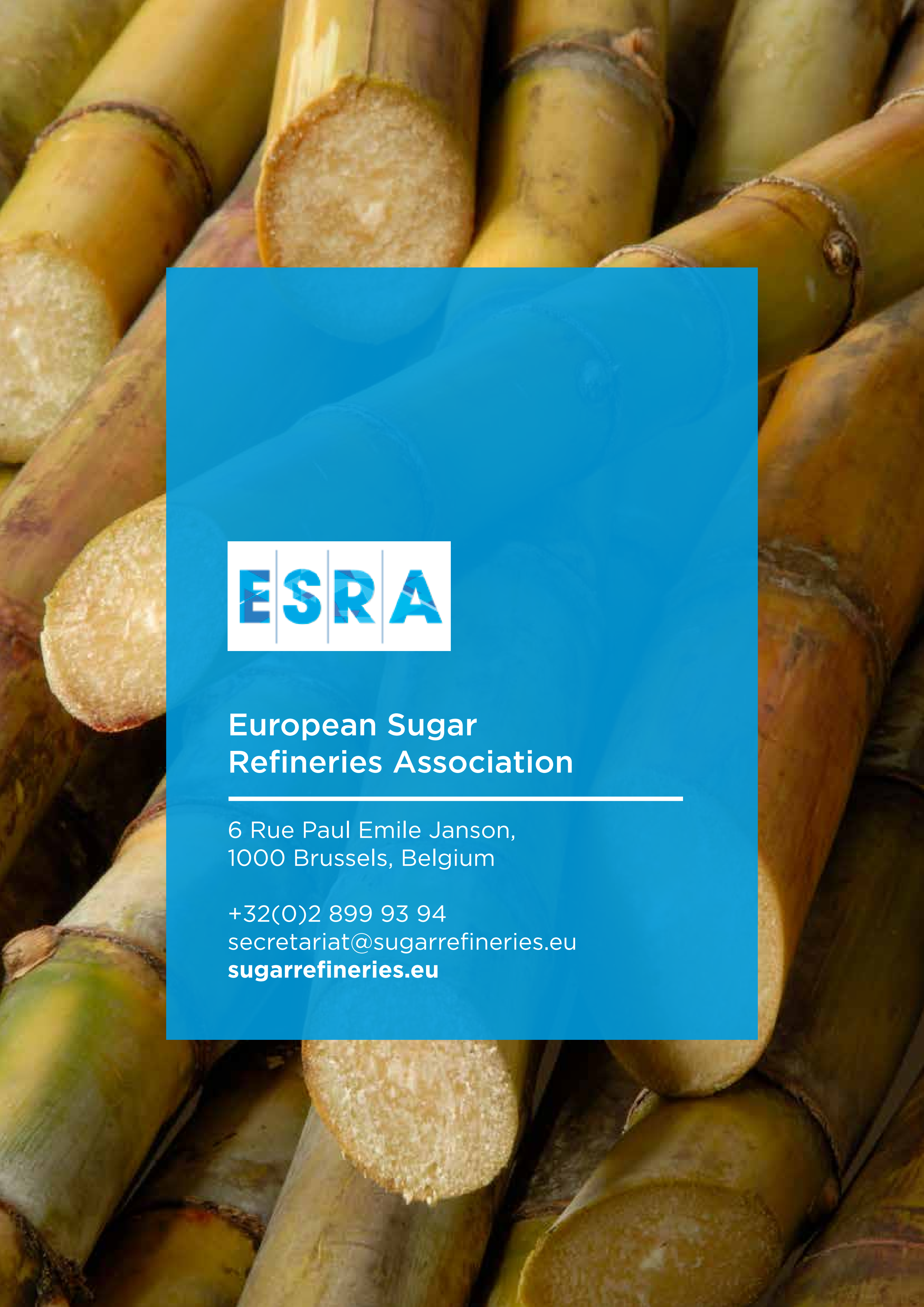

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