Implications for the ACP of Current Projections for the EU Sugar Markets

Summary

The abolition of EU sugar and isoglucose production quotas will have far reaching effects on the EU sweetener market with this carrying import price and import demand implications for ACP sugar exporters, particularly those with a high exposure to the EU market. However the effects on individual ACP exporters will be strongly influenced by the strategies adopted by EU sugar companies, which since 2005, have been restructuring, diversifying and globalising.

The integration of some ACP suppliers into single corporate controlled supply chains potentially raises important regulatory issues. EU policy initiatives to strengthen the functioning of supply chains could hold lessons in this regard, particularly where the distribution of economic power along the supply chain is such as to create opportunities for abusive practices within the supply chain.

Projected Price Effects

According to the December 2014 EC's "Prospects for Agricultural Markets and Incomes in the EU 2014-2024", "*the abolition of sugar and isoglucose quotas in 2017 has far-reaching impacts on the sweetener market*"[1]. The EU sugar price is projected to decline towards world market price levels until average price premiums of only between 12% and 18% are obtainable. This process of price decline is already underway, with EU sugar prices having fallen on average around 32% since the highs of the summer of 2012.

Despite a projected recovery in prices in 2015, the trend of declining sugar prices is expected to resume before the formal abolition of production quotas, but with a sharp decline in 2017 (-16.1%) and much smaller declines in 2018 and 2019 (-0.5% and -2.0% respectively). EU sugar prices will then follow world market prices. "*Lower white sugar prices are expected to be transmitted to the sugar beet price, which is expected to dip under 25 EUR/t after quota abolition*".

Projected EU and world market prices of sugar 2013 -2024 €/tonne and € and % difference between EU & world market

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
EU price	679	723	600	495	543	496	416	414	406	415	424	427	444	458
World price	440	392	355	350	375	396	374	351	345	352	360	382	397	410
EU premium	54%	84%	69%	41%	45%	25%	11%	18%	18%	18%	18%	12%	12%	12%
€ premium	+239	+331	+245	+145	+168	+100	+42	+63	+61	+63	+64	+45	+47	+48

Source: 'Prospects for EU Agricultural markets and income 2014-2024', December 2014, Table 7.16

Projected Production and Consumption Effects

Despite these price trends, after initial marginal declines, EU sugar beet production is projected to average some 0.7% above the 2016 production level. More significantly the average volume of sugar beet being converted into sugar in the eight years after reform is projected to be 5% higher than the average volume converted to sugar in the final four years in the run up to the reform. According to the EC this is the result of higher sucrose yields being achieved, as sugar beet production relocates to regions where the highest yields are attainable.

Significantly, abolition of isoglucose production quotas will see the share of isolgucose in the sweetener market double between 2016 and 2018 (from 3.6% to 7.3%), before reaching fully 11.6% of the total sweetener market by 2024. The increase in the volume of sugar beet being directed towards sugar production, along with the contraction in

[1] EC, 'Prospects for EU Agricultural markets and income 2014-2024', December 2014, http://www.lafranceagricole.fr/var/gfa/storage/fichiers-pdf/Docs/2014/Commission-081214.pdf

consumer demand for sugar (linked not only to increased use of isoglucose but also to an overall decline in consumption of sweeteners), will carry important trade implications.

EU production and consumption of sugar and Isoglucose (million tonnes)

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Sugar														
Production	18.0	16.4	15.3	17.6	15.8	16.1	16.5	16.6	16.7	16.8	16.8	16.9	16.9	16.9
Consumption	18.2	18.1	18.0	17.7	18.3	17.7	18.5	17.2	17.2	17.2	17.0	17.2	17.1	17.0
Isoglucose														
Consumption	0.7	0.7	0.7	0.7	0.7	0.7	1.3	1.4	1.5	1.6	1.8	1.9	2.1	2.2
% sweetener	3.6	3.6	3.5	3.6	3.5	3.6	6.5	7.3	7.8	8.5	9.4	10.1	10.9	11.6

Source: 'Prospects for EU Agricultural markets and income 2014-2024', December 2014, Table 7.16

Projected Trade Effects

While the early stages of sugar sector reform turned the EU from a net sugar exporter into a net sugar importer, this final stage of reform seems likely to periodically turn the EU back into a net sugar exporter. By 2024 it is projected that the EU will be largely self-sufficient in sugar production.

EU Sugar Trade Projections 2011-2020 (million tonnes)

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Sugar Imports	3.6	3.9	3.7	3.0	3.1	2.7	1.89	1.91	1.89	1.91	1.91	1.90	1.91	1.91
Sugar Exports	2.2	1.5	1.5	1.6	1.5	1.5	1.5	1.3	1.4	1.5	1.7	1.8	1.8	1.9

Source: 'Prospects for EU Agricultural markets and income 2014-2024', December 2014, Table 7.16

This does not mean the EU will no longer import sugar. Imports will still take place, but will be 51% below the peak level of imports in 2012, which reached some 3.9 million tonnes. EU sugar exports after falling to a low of 1.3 million tonnes in 2018 are projected to reach 1.9 million tonnes by 2014

According to the EC analysis "*there will be ample need for imports in certain periods and certain regions*". It is maintained "*the most competitive trade partners with free access to the EU markets will therefore continue to supply it, while others can divert part of their sugar to sugar deficit regional markets (e.g. in Africa)*."

The Corporate Dimension

According to the EC, in preparation for sugar production quota abolition EU sugar companies may try and gain market shares by running down their privately held stocks of sugar. Recent corporate market re-positioning efforts within the EU reflect wider processes of corporate adjustments which are underway. This involves mergers and acquisitions both within the EU and globally (including in the ACP).

Many ACP-EU sugar supply chains are now vertically integrated within corporate structures. These range from the acquisition of Belize Sugar Industries milling operations by *American Sugar Refiners* (ASR), which had previously acquired the sugar interests of *Tate & Lyle* (including the Thames raw cane sugar refinery), to the acquisition of a 50% share in the Southern African sugar giant *Illovo* by Associated British Foods (ABF), the owners of *British Sugar*, the sole UK sugar beet processor.

The example of ABF/Illovo provides a vivid illustration of the kinds of policy and regulatory challenges which are emerging. Illovo, is Africa's largest sugar producer with agricultural investments and factories in six countries (South Africa, Swaziland, Zambia, Malawi, Tanzania and Mozambique), where it "*produces raw and refined sugar for local, regional, European and world markets from sugar cane supplied by its own agricultural operations and independent growers*". Since 2006 Illovo has invested extensively across its operations to expand sugar production and processing capacity to take advantage of preferences on the EU market.

In support of their operations in Southern Africa, *British Sugar* and *Illovo* have jointly established a sugar trading company, *Mitra*, which "*supplies a range of European*

Refineries with raw sugar for refining as well as direct consumption customers with specialty and refined sugars". *Mitra* sources its sugars primarily from LDC/EPA countries but also from all countries with market access arrangements to the EU[2]. In addition, "*AB Sugar owns a 42.5% share in the Czarnikow Group*", which has a "*commercial involvement in physical transactions in excess of 8 million tonnes of sugar each year*" (10% of sugar traded annually).

In addition, within Europe, ABF has expanded its raw cane sugar processing capacity both at its beet processing plants in the UK (at Newark, with a potential capacity of 120,000 tonnes and at Cantley, with a potential capacity of 230,000 tonnes) and since 2009 through its acquisition of *Azucarera*, the Spanish sugar business of Ebro Puleva. This saw the commissioning of a refinery at Guadelete (the site of a former beet factory, decommissioned as part of the EU sugar sector reform process) with a capacity to process 100,000 tonnes of beet and 300,000 tonnes of raw cane sugar, which Illovo was contracted to supply. In addition in 2012/13 Azucarera's beet plants reportedly processed 95,000 tonnes of raw cane sugar.

This means sugar cane grown in Southern African ACP countries on *ABF/Illovo* owned estates and by smallholder out-growers, is processed at *ABF/Illovo* mills, and is potentially traded by *ABF/Illovo* owned companies and potentially refined by *ABF/Illovo* owned companies, before the finished product is marketed by *ABF* in Europe.

Similar issues related to the functioning of the sugar supply chain arise with reference to the Belize-EU trade, where ASR owns the mill, operates sugar trading operations and owns the EU refinery at which Belize sugar is processed.

It is unclear how the process of market price formation for sugar will occur within such supply chains. This is an increasingly important issue since in recent years widely differing prices have been obtained for individual consignments of ACP sugar exported to the EU. This raises important issues about the functioning of ACP-EU sugar supply chains, for in the new context scope exists for abuse of the dominant market position which these companies hold.

Avoiding Being Left Out in the Cold

While the increasingly close intra-corporate linkages along ACP-EU sugar supply chains raises new policy and regulatory challenges, more fundamental market challenges are likely to be faced by ACP sugar suppliers which are not part of these closer intra-corporate relationships. This is particularly the case for the state owned sugar industries in Fiji and Guyana, which have largely maintained their supply relationship with the traditional refiner (*Tate and Lyle Sugar*- TLS), whose commercial prospects post quota abolition are a source of concern.

Since the modification of import licensing arrangements as part of EU sugar sector reform, (*TLS*) has faced difficulties in securing access to sugar exported by traditionally preferred suppliers. Given the capital costs of beet processors are covered by their beet operations, EU beet and raw cane sugar co-refiners are able to offer better prices to traditional raw cane sugar suppliers. This has generated a situation where *TLS* is "operating at 65% of its 1.4 million to 1.5 million tons capacity at its factories in London and Lisbon."[3] This saw the launch in 2012 of the TLS convened "Save our Sugar" campaign. *TLS* maintains that "*if current and proposed EU policies continue to unfairly restrict access to raw sugar, cane refiners will not survive as part of the supply mix in Europe's sugar sector*". This could carry serious implications for Guyana and Fiji's sugar exports, unless new, secure routes to markets, which maintain traditional price premiums, can be found.

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[2] ABSugar, 'Our Group: Mitre Sugar Ltd', http://www.absugar.com/Our-Group/Mitra-Sugar-Ltd

[3] Sugaronline.com, 'Tate & Lyle wants end to duty on raw sugar imports', 26 November 2013, http://www.sugaronline.com/home/website_contents/view/1223816

There would now appear to be an urgent need for both *GUYSUCO* and the *Fiji Sugar Corporation* to begin seriously exploring their options in this regard. In the case of Fiji this may need to extend to exploring the scope for a joint venture arrangement with a suitable EU beet co-refiner for the toll refining and joint marketing of substantial volumes of "fair trade" certified and labelled sugar for industrial and direct consumption use.

Issues Arising

- **Strengthening the Functioning of ACP-EU Sugar Supply Chains**

The EU sugar sector has a relatively poor record in avoiding abuse of dominant market positions. This was most recently illustrated by the fines totalling €280 million imposed by the German Federal Cartel Office on three major German sugar companies for collusion on prices and market division[4]. 2014 also saw complaints emerging from *The Real Good Food Company* (24% owned by the Mauritian company *Omnicane*), the owners of the UK's largest independent bagger of sugar *Napier Brown*, over the pricing and supply practices of *British Sugar. RGFC* maintained *British Sugar* was abusing its monopoly position, however the regulatory authority in the UK declined to pursue the case, citing the burden of its existing case load.

This nevertheless suggests a need to strengthen the regulatory framework for the functioning of ACP-EU sugar supply chains. This potentially constitutes an important area for policy initiative on the part of the ACP. This could build on the EC's existing initiatives to strengthen the functioning of agricultural supply chains in sectors where scope exists for abuse of a dominant market position. This could provide a new focus unction for the Brussels based ***ACP Sugar Group***.

This issue reaches beyond trade with the EU, for companies such as *ABF* and *ASR* are well placed to tap into expanding demand for sugar in Asian markets. However given the scope for intra-corporate trading on the basis of non-transparent prices, it is unclear to what extent this would be likely to benefit competitive ACP sugar producers (e.g. those in Southern Africa). Getting to grips with strengthening the functioning of sugar supply chains could thus have far wider implications

- **Getting to Grips with Domestic Revenue Distribution Issues**

As sugar prices on the EU market fall and as the volume of EU sugar imports declines, the importance of non-sugar sales revenues will increase in many ACP countries. In some ACP countries extensive investments are underway in exploiting the full potential of sugar cane processing by opening up a multiplicity of new revenue streams. The growing importance of some of these non-traditional revenue streams to corporate earnings, raises important issues related to the pooling of proceeds from sales of sugar cane based products and their division between growers and millers.

Traditionally only revenues from raw sugar and molasses were pooled prior to division between growers and millers. As earnings from sales to the EU fall post 2017, these 'division of the proceeds' arrangements may need to be revised. This is particularly so since the revenue effects of the completion of EU sugar sector reforms will be compounded by growing price pressures on sugar markets across Southern and Eastern Africa, as regional markets become more attractive to regional producers.

This agricultural trade alert is produced for the Ramphal Institute by Dr Paul Goodison of GDC-Partners. Briefings and alerts on these and other international development issues and policy responses available to Commonwealth and ACP governments and private sector operators will be published regularly on this site.

[4] Food Navigator, 'German sugar companies fined €280m for price fixing', 19 February 2014 http://www.foodnavigator.com/Business/German-sugar-companies-fined-280m-for-price-fixing