

REPORT NO. 463

**INCREASE IN THE DOMESTIC DOLLAR-BASED
REFERENCE PRICE FOR SUGAR FROM US\$358/TON
TO US\$566/TON**

The International Trade Administration Commission of South Africa herewith presents its Report No.463: **Increase in the Domestic Dollar-Based Reference Price of Sugar from US\$358/ton to US\$566/ton.**



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Siyabulela Tsengwe
CHIEF COMMISSIONER

PRETORIA

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INCREASE IN THE DOMESTIC DOLLAR-BASED REFERENCE PRICE OF SUGAR FROM US\$358/TON TO US\$566/TON

Synopsis

The South African Sugar Association (SASA), on behalf of its members, applied for an increase in the dollar-based reference price (DBRP) for sugar from the existing US\$358/ton to US\$764.34/ton. SASA's request is that the DBRP be substantially altered from the current methodology used to determine the variable tariff formula, and instead be based on the domestic sugar industry's own cost of production and desired return on investment.

Using the world sugar price of US\$440.40/ton as at 3 January 2014 and at an exchange rate of R10.47 to the US\$, SASA's request would result in a specific duty of 339c/kg (equivalent to 66% *ad valorem*).

As reason for the application, the applicant submitted that it needed a fair level of protection, based on the importance of the South African sugar industry in the South African economy and its contribution to sustainable socio-economic development. It submitted that increasing imports affect the financial sustainability and competitive position of the domestic sugar industry.

The Commission considered four scenarios in making an appropriate tariff determination. Before considering the four scenarios, the Commission firstly considered an appropriate, evidence-based distortion factor in the global sugar market, due to subsidies. The Commission drew on information obtained from a report by Patrick H Chatenay, prepared for the American Sugar Alliance, titled: "Government support and the Brazilian Sugar Industry", dated 17 April 2013. It was found that the Brazilian sugar industry benefits from US\$2.5 billion per annum of direct and indirect government incentives, representing 7% of the price of Brazilian sugar.

The above distortion factor was decided on as it was evident from the latest LMC data, specific to the sugar industry, that the average world sugar price has, since the Commission's last review, increased to such an extent that it now exceeds the average world cost of production. In the last review, the Commission determined that the difference between the weighted average global cost of sugar production and the much lower average global sugar price was indicative of the distortion in the global sugar market. In determining an appropriate current distortion factor, the LMC data was not helpful and the Commission instead relied on the above-mentioned report on the Brazilian sugar industry.

The Commission determined that the current freight rate and other costs to import sugar from Brazil, the main source of imports into SACU, to a port in South Africa, amounts on average to US\$31/ton.

The Commission then considered the following variable tariff formula scenarios, taking into account a distortion factor of 7% in the average world price and ocean freight costs of US\$31/ton:

Scenario 1:

Based on a 10-year average world sugar price of US\$390/ton

Over the last ten years, the average world sugar price was US\$390/ton. Applying a distortion factor of 7% (US\$27/ton) and transport costs of US\$31/ton, the domestic reference price would be US\$386/ton.

Using the price calculations as at 3 January 2014, no duty will be triggered as the price on the day (US\$440.40/ton) was higher than the domestic reference price of US\$386/ton.

The 10-year average world reference price was used by the BTT as a benchmark price. However, a ten year average was found by the Commission to be too long a period to account for structural changes in the global sugar market and rising price levels. In the case of the variable tariff formula for wheat, the Commission found that a shift in this parameter was required to account for recent structural changes. The Commission decided on a five-year average world wheat price that properly reflected prevailing circumstances in the global wheat market.

Scenario 2:

Based on a 5-year average world sugar price of US\$509/ton

Over the last five years, the average world sugar price was US\$509/ton. Applying a distortion factor of 7% (US\$36/ton) and transport costs of US\$31/ton, the domestic reference price would be US\$514/ton.

Using the price calculations as at 3 January 2014, a specific duty of 77c/kg (equivalent to 15% ad valorem) will be triggered, equal to the difference between the price on the day (US\$440.40/ton) and the higher domestic reference price of US\$514/ton.

Although the 5-year average is consistent with the methodology followed on wheat, the Commission took the view that a DBRP of US\$514/ton would just fall short of adequately supporting the sugar industry in relation to current costs of production.

Scenario 3:

Based on a 4-year average world sugar price of US\$558/ton

Over the last four years, the average world sugar price was US\$558/ton. Applying a distortion factor of 7% (US\$39/ton) and transport costs of US\$31/ton, the domestic reference price would be US\$566/ton.

Using the price calculations as at 3 January 2014, a specific duty of 132c/kg (equivalent to 26% ad valorem) will be triggered, equal to the difference between the price on the day (US\$440.40/ton) and the higher domestic reference price of US\$566/ton. Given the peculiar circumstances of the sugar industry as these relate to the cost of production and the industry's price-competitive position vis-à-vis landed cost of imports, a four-year average world reference price was found to be an appropriate benchmark price.

Scenario 4:

Based on a 3-year average world sugar price of US\$625/ton

Over the last three years, the average world sugar price was US\$625/ton. Applying a distortion factor of 7% (US\$44/ton) and transport costs of US\$31/ton, the domestic reference price would be US\$638/ton.

Using the price calculations as at 3 January 2014, a specific duty of 207c/kg (equivalent to 41% ad valorem) will be triggered, equal to the difference between the price on the day (US\$440.40/ton) and the higher domestic reference price of US\$638/ton. Due to price instability over the short term (world sugar prices have since fallen steeply below the 3-year average world price), the Commission found that, in this instance, a 3-year average world reference price was too unstable to serve as a longer-term world reference price. A domestic reference price of US\$638/ton would overprotect the industry and have an inflationary impact.

The Commission could not support the applicant's request for a radically altered formula, to be periodically updated, based solely on the domestic sugar industry's own production cost and desired return on investment. Spiralling cost and price increases and investment returns would be automatically accommodated through a higher tariff on imports, completely isolating the domestic industry from import competition. In effect the industry would be setting the tariff. Such a system would not be conducive to competitiveness and would have a significant inherent cost-raising impact downstream with unintended consequences for food security as well as the tariff-setting process and methodology for other commodities such as wheat and maize. In addition, the level requested by SASA would disadvantage the large industrial manufacturers using sugar as an intermediate input, constituting more than 60% of the domestic sugar industry's downstream clientele.

A DBRP as suggested by SASA could lead to unintended consequences by encouraging industrial users to consider less costly imported substitutes for sugar, such as high fructose cassava syrup or artificial sweeteners.

The Commission found Scenario 3 (DBRP of US\$566/ton), the most appropriate model for a revised domestic reference price for sugar. The reference price of US\$566/ton yielding an immediate duty equivalent to 26% ad valorem, sufficiently accounts for the structural changes in the global market since the last review, and corresponds to the existing price disadvantage experienced by the domestic industry. This reference price of US\$566/ton is consistent with one of the major reasons cited by SASA for this application that the aim is to have a “fair level” of protection.

The Commission also considered that an increase in the duty on sugar would have an impact on downstream industries and consumers.

In arriving at its recommendations and in light of the foregoing, the Commission considered the information at its disposal and the comments received. The Commission also took the following factors into account:

- The rising level of imports into the SACU and erosion of market share of domestic producers. On average, imports constituted approximately 7.6% (including SADC) of the total SACU market from 2009 to 2012. However, provisional data indicates that imports have increased from 7.6% to 18.6% of the SACU market. This spike in import volumes in the latter part of 2013 seems to coincide with the movement towards the finalisation of this investigation and once the new tariff dispensation is implemented this is expected to normalise;
- The suppressed domestic sugar price as a result of distorted global market prices;
- The domestic sugar industry’s considerable levels of production, employment and investment; and
- The competitive position, including the cost and price structure, and the level of price disadvantage experienced by the domestic sugar industry vis-à-vis foreign producers.

The Commission also considered that the notional sugar price is not set in a market but is a self-regulated price set by the sugar industry, comprising the growers and the millers, at the beginning of each year. General inflation levels dictate the price, regardless of cost increases or import competition.

Unlike the other tariff scenarios considered by the Commission, the price-impact analyses suggest that the domestic reference price recommended below, yielding an immediate duty of 132c/kg, equivalent to 26% ad valorem would not have a considerable price-raising effect, but would remove the price disadvantage experienced by the domestic industry and lead to increased production levels and profitability.

In view of the above, the Commission recommended that the DBRP for sugar be increased to US\$566/ton as follows:

Domestic reference price = World reference price + distortion factor – transport costs

i.e. US\$566/ton = US\$558 + US\$39 - US\$31

Using the price data as at 3 January 2014, a specific duty of 132c/kg (equivalent to 26% *ad valorem*) will be triggered using a DBRP of US\$566/ton.

In light of the foregoing the Commission decided to recommend that the domestic Dollar-based reference price for sugar be increased from US\$358/ton to US\$566/ton based on the 4-year average London No. 5 settlement price of sugar of US\$558/ton, plus an adjustment for the distortion factor evident in the international sugar market of US\$39/ton, less the average ocean transport cost of sugar to a South African port of US\$31/ton.

The initial duty on sugar will be calculated as the difference between US\$566/ton and the price of sugar on the London sugar exchange on 3 January 2014, which amounted to US\$440.40/ton at an exchange rate of R10.47 to the US\$ as follows:

Reference price	
RSA domestic reference price	US\$566/ton
Minus: London No. 5 settlement price of sugar on 03 January 2014	US\$440.40/ton
Dollar duty on sugar	US\$125.6/ton
Rand duty on sugar	132c/kg

Adjustments to the level of protection will be based on quantum movements in the world reference price as follows:

The difference between the 20 trading day moving average London No. 5 settlement price and the established domestic reference price for sugar will be calculated daily. If the 20 trading day moving average of the No. 5 settlement price shows a variance of more than US\$20/ton from the previous trigger level for 20 consecutive trading days, a new duty will be calculated. The resulting Dollar duty will be converted to Rand, based on the Rand/Dollar exchange rate prevailing on the day that the adjustment is triggered.

THE APPLICATION AND TARIFF POSITION

(i) The application

The South African Sugar Association (SASA), on behalf of its members, applied for an increase in the dollar-based reference price (DBRP) for sugar from the existing US\$358/ton to US\$764.34/ton.

As reason for the application, the applicant submitted that it needed a fair level of protection, based on the importance of the South African sugar industry in the South African economy and its contribution to sustainable socio-economic development. It submitted that increasing imports affect the financial sustainability and competitive position of the domestic sugar industry.

The application by SASA was published in the Government Gazette on 20 September 2013 for comment by interested parties. As part of the consultative process, ITAC engaged extensively with interested parties throughout the investigation.

These parties consisted of representatives from the SACU primary and secondary industries, importers, retailers, the National Agricultural Marketing Council (NAMC) and the Department of Agriculture, Forestry and Fisheries (DAFF). Representatives from the primary and secondary sugar industries, the Association of South African Sugar Importers (ASASI), as well as the downstream manufacturers of products containing sugar e.g. the Beverage Association of South Africa (BEVSA), Tiger Brands Limited, Snackworks (Pty) Ltd, and the South African Chocolate and Sweets Manufacturers Association (SAC SMA), made oral presentations to the Commission at its meeting of 10 December 2013.

ii) The existing dollar-based reference price (DBRP)

The current tariff dispensation for sugar, termed the variable tariff formula for sugar, was introduced by ITAC's predecessor, the Board on Tariffs and Trade (BTT), in September 2000. The domestic reference price was calculated as follows:

Domestic reference price= World reference price + distortion- transport costs
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Based on the prevailing price data, this particular dispensation was deemed to better suit the circumstances surrounding the production and trade of sugar than the normal *ad valorem* import duties that are in place for most other products. The reason for this was that swift reaction is required due to the high frequency of the peaks and troughs evident in the price cycle of this commodity. The formula also accommodates exchange rate fluctuations.

The Board considered that the then average long term (10 year average) international price for sugar on the London Sugar Exchange of US\$300/ton (the world reference price) was distorted to such an extent that it could not be accepted as a fair reflection of a normal world price for sugar. Guided by the results of various studies regarding the effects of market intervention on the price for sugar, the Board concluded that in order to establish a fair benchmark for a sugar pricing model, the long term average world reference price for sugar should be adjusted upwards by 20 per cent or US\$60/ton, to factor in distortions in the international sugar markets.

The Board also considered that over and above tariff protection, the industry also benefitted from natural protection, in that sugar is an expensive product to transport. It was found that ocean transportation costs add an additional protection of US\$20/ton to US\$70/ton per ton to tariff protection (at 1999 prices).

In view of the above, the Board recommended a dollar-based reference price system in terms of which the domestic reference price for sugar should be the long-term average world reference price calculated at US\$330 per ton, after adjustments, to provide for an average transport cost of US\$30 per ton to allow for the natural or geographical protection that South African producers enjoy and the price-suppressing effects of interventionist policies in some major sugar-producing countries.

Protection for the industry was then calculated as the difference between the domestic reference price of US\$330/ton and the reigning moving average London No. 5 price (world reference price), where the world reference price was the 20-day moving average daily settlement price for No.5 White Sugar as traded on the London International Financial Futures and Options Exchange. Adjustments to the tariff were triggered when the 20-day moving average of the London No.5 price showed a variance of more than US\$20/ton for 20 consecutive trading days from the London No.5 price at which the previous adjustment was triggered. The amount of the difference was converted to Rand at the R/US\$ exchange rate on the day an adjustment in the tariff was triggered. The sugar industry therefore enjoyed tariff protection when the international sugar price dipped below US\$330/ton.

The customs duty for sugar is reflected in Part 1 of Schedule No.1 in the Customs Tariff as a variable specific duty.

Since the introduction of the variable tariff formula for sugar in 2000, ITAC maintained the use of the variable tariff formula for the determination of the customs duty on sugar, but reviewed the dispensation in 2009, through an adjustment to the world reference price, the distortion factor, and transport costs.

The Commission, in its last investigation regarding the DBRP for sugar, recommended in Report No.308 of 2009, an increase in the DBRP for sugar from US\$330/ton to US\$358/ton.

The Commission found adequate justification for amending the then existing sugar pricing variable tariff formula as follows:

The world reference price was adjusted from the previous 1987/88-1998/99 average to the 1998/99-2007/08 average price of US\$256/ton.

The Commission recommended a larger adjustment for the distortion factor than what was recommended by the BTT in 2000. The Commission based its decision on the rationale of measuring the difference between the long term (10-year) weighted average cost of producing sugar (for all sugar producing countries) and the actual average world sugar price over the same 10-year period as published by Landell Mills Commodity Studies (LMC). The difference between the world sugar price and the average cost of sugar

production was regarded as the distortion factor. A calculation of the average distortion factor using a 10-year average yielded 58%.

The Commission further recommended a larger adjustment for the average transportation cost from other sugar producing countries, to a South African port, from the previous US\$30/ton as recommended in 2000 to US\$46/ton, mainly due to significantly higher fuel prices.

The system would yield protection to the SACU industry when the reference price fell below US\$358/ton. As per this variable tariff formula, the customs duty for sugar has been duty free since 09 April 2009.

The existing tariff position for sugar reads as follows:

Current tariff position for sugar

Tariff heading	Tariff subheading	Description	Statistical unit	Rate of duty			
				General	EU	EFTA	SADC
17.01		CANE OR BEET SUGAR AND CHEMICALLY PURE SUCROSE IN SOLID FORM					
1701.1		Raw sugar not containing added flavoring or colouring matter:					
	1701.12	Beet sugar	Kg	Free	Free	Free	Free
	1701.13	Cane sugar specified in subheading Note 2 to this chapter	Kg	Free	Free	Free	Free
	1701.14	Cane sugar	Kg	Free	Free	Free	Free
1701.9		Other:					
	1701.91	Containing added flavoring or coloring matter	Kg	Free	Free	Free	Free
	1701.99	Other	Kg	Free	Free	Free	Free

(Source: SARS)

The WTO bound rate for South African sugar is 105% ad valorem.

Under the SADC Trade Protocol, a provision for rebate of the full duty in terms of Schedule No. 4 to the Customs and Excise Act, 1964, exists with respect to raw or refined sugar imported from non-SACU SADC Member States. (Rebate provision under item 460.04/17.01/01.04).

At the time of the WTO negotiations, Uruguay round, South Africa's level of bound rates for agricultural products was deemed high. Subsequently, South Africa agreed to the introduction of Minimum Market Access rebates for certain agricultural goods, which allows

for a specific percentage of lower rated duty imports calculated as a percentage of the bound rate.

iii) The requested reference price

SASA's request is that the DBRP be substantially altered from the current methodology used to determine the variable tariff formula, as described in the previous sections, and instead be based on the domestic sugar industry's own cost of production and desired return on investment.

Using the world sugar price of US\$440.40/ton as at 3 January 2014 and the rate of exchange of 10.47 on the day, SASA's request would result in a specific duty of 339c/kg (equivalent to 66% *ad valorem*).

INDUSTRY AND MARKET

The world market

Sugar is produced in more than 100 countries and global production exceeds 120 million tons a year. The biggest producers globally are Brazil (18.6%), the European Union (13.7%), India, and China.

The largest sugar exporters are Brazil and the European Union, followed by Australia and Thailand. Africa, excluding Egypt, accounts for 5.7% of world production, 14.9% of imports and 7.7% of exports. South Africa is the only significant African player (1.8% of world production).

Approximately three quarters of sugar production is consumed in the countries of production. The balance is traded in the international sugar market, generally at prices below those supported by economic fundamentals. The distorted world sugar prices arise from interventionist measures adopted in a number of sugar producing countries. These measures, which have the effect of artificially increasing the supply of sugar to the world market, include producer and export support programs, market access constraints such as preferential quotas and special market arrangements, and are supported by high import tariffs.

SACU Market

The table below reflects the estimated size of the SACU sugar market:

Size of SACU market

Year 1 April - 31 March	Total quantity of SACU sales (Tons)	Total value of SACU sales (Million R)	Annual rate of increase in terms of (1) quantity (2) and value	Percentage share of applicant's sales to total SACU sales in terms of volume & value	Percentage share of imports and Swaziland's sales to total SACU sales in terms of volume & value	Imports quantities (Tons), percentage growth and percentage of SACU sales in tonnages
2009/10	1 922 682	8 451.50	0.6% / 9.0%	78.00%	28.00%	102 049 / -25% / 5.0%
2010/11	1 932 574	9 165.10	0.5% / 8.4%	79.50%	20.50%	84 819 / -17% / 4.4%
2011/12	2 106 865	11 203.40	9.2% / 22.2%	82.00%	18.00%	116 838 / 38% / 5.5%
2012/13	2 097 522	11 855.70	0.4% / 5.8%	77.80%	22.20%	160 000 / 37% / 7.6%
2013/14 (Estimate)	2 141 129	12 095.00	2.1% / 2.0%	79.10%	20.90%	

The total SACU market for the 2012/13 period is comprised of sugar supplied by South Africa (78%), Swaziland (14.4%), SADC producers who have quotas under the SADC Sugar Cooperation Agreement (1.6%) and all other imports (6%).

The SACU sugar market is shared by Swaziland and South African sugar producers according to the industry agreement of March 1998 between the Swazi and South African sugar industries. The agreement is aimed at establishing fair market access for producers through the maintenance of equal export obligations. In terms of this agreement South Africa and Swaziland share the SACU market in a 81.3:18.7 ratio.

According to the Swaziland Sugar Association (SSA), Swaziland's sugar is largely sold to two main markets: SACU and the European Union, almost in a 50:50 split. Other preferential markets exist in COMESA and the United States, but have not been utilised in recent years owing to the relatively lower returns in those markets contrasted with a high-priced unlimited access to the EU market.

Swaziland's access to the EU market is on the basis of the duty-free quota-free market access provisions of the Market Access Regulation (the interim instrument prior to the enactment of Economic Partnership Agreements). This has provided Swaziland with an avenue to sell unlimited quantities of sugar to (a higher-priced market in) the EU, essentially diverting sales from the low-priced regional and US markets. Through this access arrangement, Swaziland's exports to the EU have increased from 153 250 tons in 2006/07 to the 360 000 tons forecasted to be sold in 2013/14.

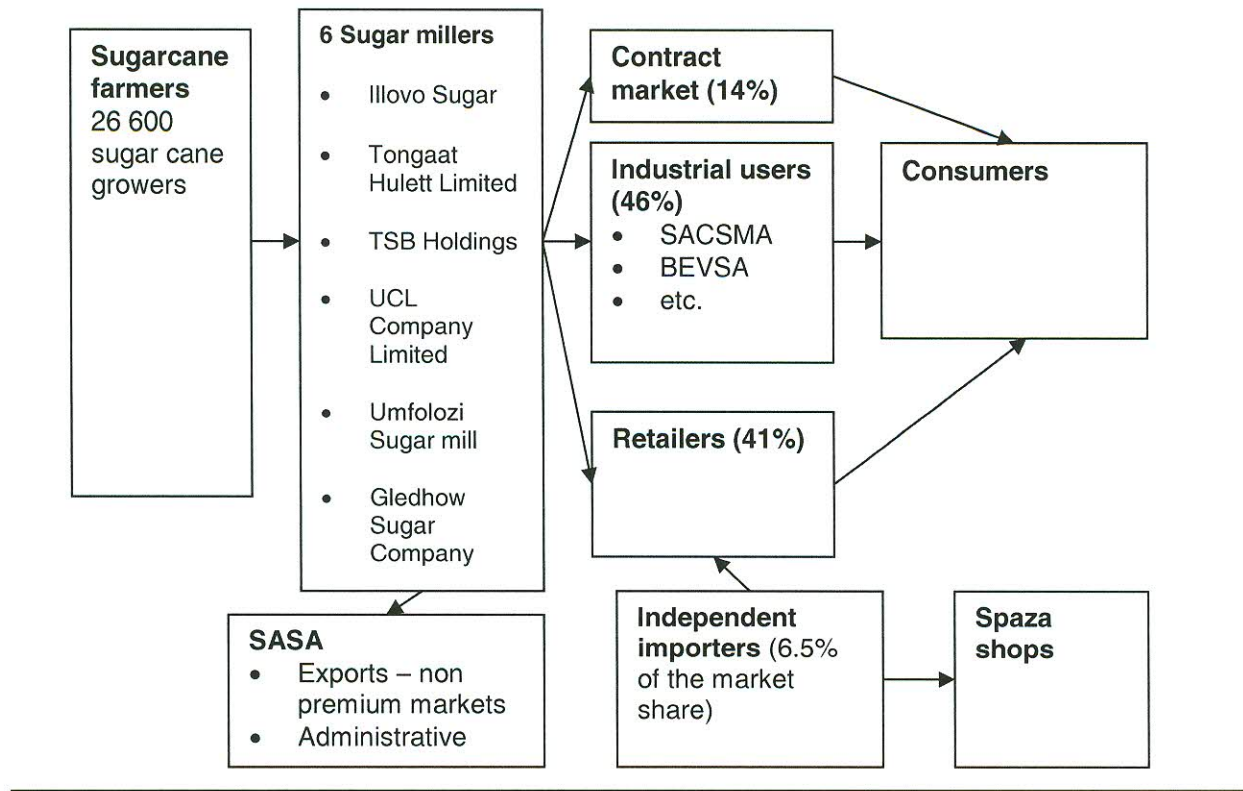
The US market is accessed under the tariff rate quota (TRQ) system governed by the US Sugar Programme under the Farm Bill of 2002.

The world market is the residual or "dumped" market which takes all the remaining sugar.

The South African sugar industry does not enjoy any preferential sugar market access agreements.

The South African sugar value chain is presented in Figure 1 below:

Figure 1



South African sugar is produced from sugarcane by approximately 26 600 registered sugarcane growers who annually produce on average 22 million tons of sugarcane from 14 mill supply areas. Approximately 25 200 are small-scale growers, of whom 11 600 delivered cane last season, producing 9.35% of the total crop.

There are approximately 1 400 large-scale growers (inclusive of the 323 black emerging farmers) who produced 83.2% of total sugarcane production. Milling companies with their own sugar estates produced approximately 7.5% of the crop. This percentage of the total crop produced by the miller-cum-planter estates has decreased in recent years and is likely to continue to do so as the companies promote more black farming development.

The applicant submitted that, on average, the South African sugar industry processes 22 million tons of cane in a season resulting in sugar production of 2.2 million tons (valued at approximately R12 billion per annum).

Four of the fourteen South African mills are owned by Illovo Sugar Ltd; four mills are owned by Tongaat-Hulett Sugar Ltd; and three mills by TSB Sugar RSA Ltd. UCL Company Ltd, Gledhow Sugar Company and Umfolozi Sugar Mill each operate one mill. Two of the TSB Sugar RSA Ltd mills are located in the Mpumalanga province and the remaining mill in the KwaZulu-Natal province.

Three of the South African sugar mills are known as "white end" mills and produce their own refined sugar. Raw sugar produced by TSB Sugar RSA Ltd is exported via the sugar

terminal in Maputo. Raw sugar produced at the remaining mills is routed to Durban where it is either refined at the central refinery of Tongaat-Hulett Sugar Ltd or stored at the South African Sugar Association's sugar terminal, prior to export. According to the applicant, diversity is the key factor in today's highly integrated sugar milling operations and the mills produce a range of other products such as ethyl alcohol and furfural and its derivatives, although these activities are outside the industry partnership.

The members of the South African Sugar Millers' Association are:

- Illovo Sugar Ltd, which operates four sugar mills in South Africa, one of which has a refinery and two have packaging plants. It has three cane growing estates and produces a variety of downstream products.
- Tongaat-Hulett Sugar Ltd, which operates four sugar mills in South Africa, two which have packaging plants, a central refinery in Durban which has its own packaging plant, various sugar estates and an animal feeds operation.
- TSB Sugar RSA Ltd, which operates three sugar mills, two of which have refineries, a packaging plant, sugar estates, cane and sugar transport, and an animal feed division.
- UCL Company Ltd, which operates a sugar mill, a wattle extract factory, two saw mills, a number of mixed farms and a trading division.
- The Gledhow Mill, which is owned by a black empowerment group that bought the mill from Illovo Sugar Limited in 2004.
- Umfolozi Sugar Mill (Pty) Ltd, which bags high quality VHP brown sugar for sale into the industrial and retail markets.

Swaziland, which is the only other sugar producer in the SACU, has three main sugar cane growers, namely Simunye planters, Mhlume planters and Big Bend planters. The cane growers are aligned with their respective millers – i.e. Simunye mill, Mhlume mill and Ubombo mill. Presently, the industry has approximately 485 growers spread across the areas where the mills are based. Of these, 456 are smallholder quota holders (340 are individual growers while the 116 are grouped into farmers associations, with a total membership of over 5 000 individuals).

SSA submitted that Swaziland's sugar production (in tons per annum) has grown from an annual average of 200 000 tons in the 1970s to a forecast of 660 000 tons in 2013. The growth has been supported by natural expansion of existing schemes as well as the entry of new growers (mainly smallholders in farmers associations) through the two large irrigation projects, namely the Komati Downstream Development Project in the north of the Lowveld and the Lower Usuthu Smallholder Irrigation Project in the south of the Lowveld.

SSA submitted that current total production forecast at 660 000 t/annum is projected to generate revenues in excess of R4billion/annum.

The SADC Sugar Cooperation Agreement consists of two components, namely market access and areas of cooperation. The market access component allows non-SACU SADC surplus sugar producing countries, exposed to depressed world market prices, the opportunity to share in the growth in the SACU market. The cooperation component enables cooperation in the areas of research, training, small holder development, infrastructure (including export facilities), customs administration and developments in the

rest of the world, with the ultimate objective of creating an integrated and internationally competitive SADC sugar industry.

The SA sugar industry is governed by the Sugar Act of 1978 and Sugar Industry Agreement (SIA) of 1994. The Sugar Act, inter alia, administers a single channel export system for South African sugar and sets a fixed proceeds sharing formula for the share of proceeds to be paid over by millers to growers, calculated in terms of the recoverable value price for cane.

The majority of the substantial profits generated by South African milling companies are made in other SADC countries where they have invested in sugar cane growing and milling due to the preferential access to premium markets that these countries enjoy.

The Sugar Act is currently under review. The main objective of the current review of the Sugar Act is to establish a regulatory framework for sugar production and marketing that will promote optimal competition and participation in the domestic sugar industry, whilst also recognising that some level of formal intervention is needed to allow the industry to maintain its participation in the international sugar market.

SACU is a sugar surplus region. This is a latent source of price pressure. In addition, the region has a competition legislation which prevents market sharing arrangements. According to the applicant, this reduces the ability of sugar suppliers to prop up prices. A second source of pressure is imported sugar from Brazil and India. A third source is the sugar inflow under the SADC Sugar Cooperation Agreement.

Production and sales

The actual production of sugar by the applicant is shown in the table below:

Actual production of applicant

Year (1 April - 31 March)	2010/11	2011/12	2012/13	2013/14 (Estimate)
Production Capacity	2 700 000	2 700 000	2 700 000	2 700 000
Actual Production (Tons)	1 919 116	1 832 438	1 967 684	2 194 000
Sales volume (Tons)	1 919 116	1 832 438	1 967 684	2 194 000
Sales Value (Million R)	8 547.5	9 546.7	10 754.8	11 794.9

(Source: SASA)

As can be seen in the table above, the applicant's total sugar production decreased, in terms of volume, by 4.5% from the 2010/11 to 2011/2012 season, increased 7% from the 2011/12 to 2012/13 season, and is estimated to increase by 11.5% from the 2012/13 to 2013/14 season.

In terms of sales, the applicant's sales values increased by 12% from the 2010/11 to 2011/2012 season, increased 13% from the 2011/12 to 2012/13 season, and are estimated to increase by 10% from the 2012/13 to 2013/14 season. From the table above it can also be seen that the Applicant's sales value increased by 26% from the 2010/11 to the 2012/13 season.

Production factors

Imported inputs included in sugar production from farming to refining the final product vary from farmer to farmer and mill to mill, however, in broad terms they include the following:

- Fertiliser;
- Fuel;
- Herbicides;
- Tractors;
- Spares;
- Cane Loaders;
- Bale Loaders;
- Laboratory equipment and chemicals;
- Refining and filtering chemicals; and
- Milling plant, machinery, equipment and spares.

Initial planting costs are high but these are spread over a number of harvests. New plantings are done via vegetative propagation, which usually takes place in September/October. Cane harvesting occurs between April and December when it is delivered to the sugar mill.

According to the applicant, the age of cane varies between 11 months and 24 months depending on harvesting cycles and geographic location (cooler inland areas generally have older cane). Certain mill areas are only suitable for dry land and supplementary irrigation, and others are fully irrigated. Much of the land on which sugarcane is grown is steeply undulating and is therefore only suitable for a crop such as sugarcane which is not replanted annually therefore effectively conserving soil.

SASRI (The South African Sugar Research Institute) and SMRI (The Sugar Milling Research Institute) strive to improve cane varieties and growing conditions, and factory operations, equipment and processes, respectively. These institutes provide applied research solutions, consulting, training and routine analytical services to the growers and mills to ensure the sustainability of the South African sugar industry. These institutes collaborate widely with other organizations around the world to keep abreast of the latest technologies applicable to the manufacture of sugar, and other technologies that may be applied in the industry to improve efficiencies and reduce costs. In addition to the work undertaken by these institutes, individual milling companies also fund and undertake research which is particularly relevant to their operations. Contact with foreign sugar milling companies provides benchmarking opportunities and for the exchange of information relating to developments in sugar manufacturing techniques.

Employment and Investment

The SACU sugar industry employs more than 100 000 people and has invested a considerable amount of capital. It has many linkages to other sectors of the economy and is of particular importance as far as economic development in rural areas is concerned.

The South African sugar industry has various levels of interventions that are aimed at skills development and empowerment. SASA's Shukela Training Centre, established in 1974

and funded by the millers and growers, is the preferred provider of agricultural and engineering skills development to the sugar industry. While the agricultural training is more sugar industry focused towards sugarcane growing, the engineering training is provided more broadly to both sugar industry and non-sugar industry interests. The Centre is accredited with the relevant Sectorial Education and Training Authorities.

On the sugar cane farming side, there is also an accredited learnership program available, and funds are usually sourced from the Sugar Industry Development Fund to support small-scale grower attendance at these courses where required.

The applicant submitted that each milling company promotes its own skills and development programs to empower staff members. The milling companies are the major funders of the Sugar Milling Research Institute, which was established in 1949. It provides state-of-the-art training for sugar technologists. The training ranges from initial courses in sugar manufacturing to intensive courses in sugar engineering and technology.

The industry acknowledges the importance of access to education for the children of small-scale growers and supports bursaries for worthy children in science, engineering and technology through the Sugar Industry Trust Fund for Education. Tertiary education bursaries are available in science and engineering from the same fund.

According to SSA, in Swaziland, the sugar industry also provides social services (i.e., education, health care, housing, water, sanitation, recreational facilities, etc.) of above-average national standards. The social services contribution is very important considering that the sugar industry is located in the rural sector which houses more than 70% of the population where the supply of government services is inadequate and in most cases of low quality. In addition to own employees and their dependents, neighboring communities also have access to the social services provided by the sugar industry.

Trade data

Total sugar imports decreased, in terms of volume, by 43% from 2008 to 2009, but increased by 15% from 2009 to 2010, increased further by 39% from 2010 to 2011, and increased again by 44% from 2011 to 2012. Overall imports increased by 30% from 2008/2009 to 2011/2012.

In 2012, 86% of sugar imports originated from MFN countries, 13% originated from SADC, 1% of imports came from the EU and 0.22% from EFTA countries. Imports from Brazil constituted 87% of MFN imports.

Imports from Brazil decreased, in terms of volume, by 21% from 2008 to 2009, decreased further by 36% from 2009 to 2010, then increased by 91% from 2010 to 2011, and increased further by 12% from 2011 to 2012. Overall, imports of sugar from Brazil, in terms of volume, increased from 2008 to 2012 by 9%.

On average, imports constituted approximately 7.6% (including SADC) of the total SACU market from 2009 to 2012. However, imports increased during 2013 from 7.6% of the SACU market to 18.6% of the SACU market, based on provisional data.

THE COMPETITIVE POSITION

South Africa's position in terms of global ranking of the lowest cost cane sugar producers on total field and factory cost, is as set out in the table below:

Table: Lowest Cost Cane Producers Ranking, 2011/2012

Rank	Total Ex-Factory Costs	Total F.O.B. Stowed Costs
1	Nicaragua	Nicaragua
2	Guatemala	Guatemala
3	Brazil (C.S.)	Thailand
4	Colombia	Brazil (C.S.)
5	Malawi	Colombia
6	Thailand	Honduras
7	Zimbabwe	El Salvador
8	Zambia	South Africa
9	Swaziland	Zimbabwe
10	Honduras	Swaziland

Source: LMC, 2012

As can be seen above, the latest figures for the 2011/2012 season compiled by Landell Mills Commodity Studies (LMC) reveal that South Africa ranks 17th globally in terms of raw cane sugar ex-factory costs out of over 80 cane producers, and 8th globally in terms of F.O.B. (Free on Board) costs out of a sample of the ten lowest cost developing country cane producers.

The drought (2009/2010 – 2010/2011) seasons played a role in recent years in slightly reducing the industry's competitiveness, as most capital costs are fixed whereas cane supply and mill capacity utilisation rates fall during drought as a result of impact on production. To strip out the effects of the drought, a slightly longer time period should be examined. LMC figures averaged across 2008/2009 to 2011/2012 ranks the industry as amongst the top 10 most competitive in terms of raw cane sugar ex-factory costs, right up until the impact of the drought occurred. This is illustrated in the table below:

Table: Lowest Cost Cane Producers Ranking, 2008/09 - 2010/2011

Rank	2011/12	2010/11	2009/10	2008/09
1	Nicaragua	Brazil (C.S.)	Brazil (C.S.)	Brazil (C.S.)
2	Guatemala	Ethiopia	Colombia	Nicaragua
3	Ethiopia	Nicaragua	Nicaragua	Malawi
4	Brazil (C.S.)	Guatemala	South Africa	Guatemala
5	Colombia	Thailand	Guatemala	Ethiopia
6	Malawi	Paraguay	Paraguay	South Africa
7	Thailand	Colombia	Swaziland	Swaziland
8	Paraguay	Malawi	Ethiopia	Colombia
9	Peru	Zambia	Malawi	Bolivia
10	Zimbabwe	Swaziland	Thailand	Peru
11	Zambia	South Africa	Australia	Australia
12	Swaziland	Bolivia	Peru	Thailand
13	Honduras	El Salvador	Bolivia	Paraguay
14	El Salvador	Zimbabwe	Brazil (N.E.)	Brazil (N.E.)
15	Bolivia	Honduras	Zambia	El Salvador

Source: LMC, 2012

The current tariff dispensation for sugar, termed the variable tariff formula, establishes a domestic reference price that is used to calculate the price support or level of duty for sugar. One of the factors considered by the Commission in determining the variables of

the formula is the price advantage/disadvantage between domestically produced sugar and the landed cost of imported sugar.

According to information at the Commission's disposal, the notional price for sugar for the 2014/15 period has been set at R6 637/ton. The notional sugar price is a self-regulated price set by the sugar industry. The price is closely aligned to annual increases in the consumer and producer price indices. When the existing notional price for sugar is compared to the landed cost of imported sugar, the South African sugar industry experiences a price disadvantage.

COMMENTS FROM INTERESTED PARTIES

The Swaziland Sugar Association supported the application for an increase in the DBRP, stating that the DBRP must be at a level that guarantees effective protection of the SACU sugar industry. This protection is justified for a number of reasons such as distortion in the global sugar markets, sensitivity to the sugar industry in SACU and the need for a positive tariff in negotiations with third parties. It was submitted that the sugar industry continues to be threatened by escalating sugar imports into SACU that could significantly affect economic growth, employment, human development and Swazi economic empowerment. It further requested that the DBRP be reviewed every year to accommodate developments in international prices and/or the distortion levels.

The Ministry of Trade and Industry of the Republic of Namibia submitted its objection to the application stating that it supports the views forwarded by Matrix One-Two-One Commodity Market (Pty) Ltd, that commented on behalf of the Namibian private sector, stating that the SADC Protocol's aim was that no sugar industry within SADC should suffer injury, but with the long term objective to establish full liberalisation of trade in the sugar sector in the SADC region after the year 2012.

The Ministry of Trade and Industry of Botswana objected to the application stating that the increase in the domestic DBRP would have a negative effect on the sugar downstream industries, and that prevailing restrictions or conditions in the SACU market should be removed to allow Botswana to import cheap sugar from other sources.

Comments were received from some of the major South African industrial users who use sugar as an ingredient in their respective industries. The companies, namely, Ceres Fruit Juices (Pty) Ltd, the Beverage Association of South Africa (BEVSA), the South African Chocolate and Sweets Manufacturers Association (SACMSA), XA International Trade Advisors representing [Snackworks, a division of National Brands Limited (NBL)], Heinz Foods South Africa (Pty) Ltd, the COTI Chocolate Manufacturers (Pty) Ltd, Cape Cookies, Halewood International SA, Bokomo Foods, a division of Pioneer Foods, Coca-Cola South Africa, and the South African Fruit Juices Association (SAFJA) objected to the application for an increase in the DBRP on sugar stating that an increase in the DBRP for sugar would directly increase their input costs, thus affecting the production of products containing sugar.

Supplementary comments were also received from six importers of sugar, namely, Sugar on Tap, Akila Trading (Pty) Ltd, Matrix One-Two-One Commodity Marketing (Pty) Ltd, Flava Foods CC and River Edge Trading 4 (Pty) Ltd. The companies submitted that an

increase in the DBRP of sugar to the requested level would eliminate all imports and putting their companies out of business.

Comments objecting to the application were also received from two shipping companies, namely, Nicholson Shipping SA and MOL South Africa (Pty) Ltd. objected to the application indicating, inter alia, that should the duty be granted, consumers would be put under pressure as the price of white sugar has increased over the past six years.

Comments objecting to the application were also received from the following retailers: Shoprite Checkers and Wheels Cash and Carry cc, citing, inter alia:

- The right of everyone to food in terms of the provisions of the Constitution;
- The proposed increase would not benefit the consumer;
- The increase would increase the level of inefficiency of SASA's members and diminish broad based economic empowerment;
- Millers would maximize profits; and
- The depreciation of the Rand sufficiently protects the industry.

Although comments objecting to the application by SASA were received from various interested parties, there was acceptance by these interested parties, especially those that appeared before the Commission, that there was a need to adjust the current DBRP given the passage of time since the last review, but not at the level requested by SASA.

Support for the application was received from the following entities: HF Stegen cc, River North Farm (Pty) Ltd, Nampak Sacks, Clariant SA (Pty) Ltd, KZN Oils, Natal Associated Colliers (Pty) Ltd, Felixton Cane Growers' Association, Sucrotech (Pty) Ltd, Jelcane Farming, Jubane Petroleum (Pty) Ltd, Reka Trade 1216 cc, Buckhaw Brow Farm, Imperial Managed Logistics, Torquay Cane Estates, Waltons (Pty) Ltd, River North Farm (Pty) Ltd, Unitrans Supply Chain Solutions (Pty) Ltd, The Sezela Cane Growers' Association, Nutri-Flo, Maidstone Grower Council, Noodsberg Local Grower Council, Umzimkulu Local Grower Council, Aveton Farm, Trader Vic (Pty) Ltd, Farmers Agri-Care (Pty) Ltd, Tufbag (Pty) Ltd, Amatikulu Local Grower Council, Illovo Eston Local Grower Council, NCR Consulting cc, The Donnybrook Trust, Umfolozi Cane Growers' Association, Mpumalanga Cane Growers Association, Maidstone Planters Association, Liquid Nutrient Technologies (Pty) Ltd, Desdale Estates (Pty) Ltd, Barloworld Logistics, SGX Logistics, IT Dynamics, Rutherford Farm, Bearing Man Group, Thulumisindo Trading Enterprise, Benard Mbewe Enterprise, SBU Madlokovu Trading Enterprise cc, Mr. Lindiwe Hlubi, M & G Farming cc, Standard Sidings, AFROX, Bell Equipment Co. SA (Pty) Ltd, Umshwathi Agricultural Union, Inglebrook Farm, The Sugar Manufacturing and Refining Employers' Association, Action Bolt (Pty) Ltd, Bruce Prentice Trading cc, CAL Marketing Services cc, Leitch Landscapes (Pty) Ltd, MSA Africa, FTS Safety, Imbali Services, uFundiSA Training, Matriarch Equipment cc, Brocklee Farms, Ellesmere Sugar Estate cc, SAPPI Paper & Packaging, Coastal Farmers' Co-operative Ltd, LR Plastics (Pty) Ltd and Soreyten Farm.

The main reasons for support from the above entities revolved around issues such as that the companies are directly dependent on the sugar industry for their businesses and that mill closures would lead to significant job losses in farming as well as in supporting industries.

TARIFF DETERMINATION

The Commission considered four scenarios in making an appropriate tariff determination. Before considering the four scenarios, the Commission firstly considered an appropriate, evidence-based distortion factor in the global sugar market, due to subsidies. The Commission drew on information obtained from a report by Patrick H Chatenay, prepared for the American Sugar Alliance, titled: "Government support and the Brazilian Sugar Industry", dated 17 April 2013. It was found that the Brazilian sugar industry benefits from US\$2.5 billion per annum of direct and indirect government incentives, representing 7% of the price of Brazilian sugar.

The above distortion factor was decided on as it was evident from the latest LMC data, specific to the sugar industry, that the average world sugar price has, since the Commission's last review, increased to such an extent that it now exceeds the average world cost of production. In the last review, the Commission determined that the difference between the weighted average global cost of sugar production and the much lower average global sugar price was indicative of the distortion in the global sugar market. In determining an appropriate current distortion factor, the LMC data was not helpful and the Commission instead relied on the above-mentioned report on the Brazilian sugar industry.

The Commission determined that the current freight rate and other costs to import sugar from Brazil, the main source of imports into SACU, to a port in South Africa, amounts on average to US\$31/ton.

The Commission then considered the following variable tariff formula scenarios, taking into account a distortion factor of 7% in the average world price and ocean freight costs of US\$31/ton:

Scenario 1:

Based on a 10-year average world sugar price of US\$390/ton

Over the last ten years, the average world sugar price was US\$390/ton. Applying a distortion factor of 7% (US\$27/ton) and transport costs of US\$31/ton, the domestic reference price would be US\$386/ton.

Using the price calculations as at 3 January 2014, no duty will be triggered as the price on the day (US\$440.40/ton) was higher than the domestic reference price of US\$386/ton.

The 10-year average world reference price was used by the BTT as a benchmark price. However, a ten year average was found by the Commission to be too long a period to account for structural changes in the global sugar market and rising price levels. In the case of the variable tariff formula for wheat, the Commission found that a shift in this parameter was required to account for recent structural changes. The Commission decided on a five-year average world wheat price that properly reflected prevailing circumstances in the global wheat market.

Scenario 2:

Based on a 5-year average world sugar price of US\$509/ton

Over the last five years, the average world sugar price was US\$509/ton. Applying a distortion factor of 7% (US\$36/ton) and transport costs of US\$31/ton, the domestic reference price would be US\$514/ton.

Using the price calculations as at 3 January 2014, a specific duty of 77c/kg (equivalent to 15% ad valorem) will be triggered, equal to the difference between the price on the day (US\$440.40/ton) and the higher domestic reference price of US\$514/ton.

Although the 5-year average is consistent with the methodology followed on wheat, the Commission took the view that a DBRP of US\$514/ton would just fall short of adequately supporting the sugar industry in relation to current costs of production.

Scenario 3:

Based on a 4-year average world sugar price of US\$558/ton

Over the last four years, the average world sugar price was US\$558/ton. Applying a distortion factor of 7% (US\$39/ton) and transport costs of US\$31/ton, the domestic reference price would be US\$566/ton.

Using the price calculations as at 3 January 2014, a specific duty of 132c/kg (equivalent to 26% ad valorem) will be triggered, equal to the difference between the price on the day (US\$440.40/ton) and the higher domestic reference price of US\$566/ton. Given the peculiar circumstances of the sugar industry as these relate to the cost of production and the industry's price-competitive position vis-à-vis landed cost of imports, a four-year average world reference price was found to be an appropriate benchmark price.

Scenario 4:

Based on a 3-year average world sugar price of US\$625/ton

Over the last three years, the average world sugar price was US\$625/ton. Applying a distortion factor of 7% (US\$44/ton) and transport costs of US\$31/ton, the domestic reference price would be US\$638/ton.

Using the price calculations as at 3 January 2014, a specific duty of 207c/kg (equivalent to 41% ad valorem) will be triggered, equal to the difference between the price on the day (US\$440.40/ton) and the higher domestic reference price of US\$638/ton. Due to price instability over the short term (world sugar prices have since fallen steeply below the 3-year average world price), the Commission found that, in this instance, a 3-year average world reference price was too unstable to serve as a longer-term world reference price. A domestic reference price of US\$638/ton would overprotect the industry and have an inflationary impact.

The Commission's determination of an appropriate DBRP

The Commission could not support the applicant's request for a radically altered formula, to be periodically updated, based solely on the domestic sugar industry's own production cost and desired return on investment. Spiralling cost and price increases and investment returns would be automatically accommodated through a higher tariff on imports, completely isolating the domestic industry from import competition. In effect the industry would be setting the tariff. Such a system would not be conducive to competitiveness and would have a significant inherent cost-raising impact downstream with unintended consequences for food security as well as the tariff-setting process and methodology for other commodities such as wheat and maize. In addition, the level requested by SASA would disadvantage the large industrial manufacturers using sugar as an intermediate input, constituting more than 60% of the domestic sugar industry's downstream clientele.

A DBRP as suggested by SASA could lead to unintended consequences by encouraging industrial users to consider less costly imported substitutes for sugar, such as high fructose cassava syrup or artificial sweeteners.

The Commission found Scenario 3 (DBRP of US\$566/ton), the most appropriate model for a revised domestic reference price for sugar. The reference price of US\$566/ton yielding an immediate duty equivalent to 26% ad valorem, sufficiently accounts for the structural changes in the global market since the last review, and corresponds to the existing price disadvantage experienced by the domestic industry. This reference price of US\$566/ton is consistent with one of the major reasons cited by SASA for this application that the aim is to have a "fair level" of protection.

FINDINGS

In arriving at its recommendations and in light of the foregoing, the Commission considered the information at its disposal and the comments received. The Commission also took the following factors into account:

- The rising level of imports into the SACU and erosion of market share of domestic producers. On average, imports constituted approximately 7.6% (including SADC) of the total SACU market from 2009 to 2012. However, provisional data indicates that imports have increased from 7.6% to 18.6% of the SACU market. This spike in import volumes in the latter part of 2013 seems to coincide with the movement towards the finalisation of this investigation and once the new tariff dispensation is implemented this is expected to normalise;
- The suppressed domestic sugar price as a result of distorted global market prices;
- The domestic sugar industry's considerable levels of production, employment and investment; and
- The competitive position, including the cost and price structure, and the level of price disadvantage experienced by the domestic sugar industry vis-à-vis foreign producers.

The Commission also considered that the notional sugar price is not set in a market but is a self-regulated price set by the sugar industry, comprising the growers and the millers, at the beginning of each year. General inflation levels dictate the price, regardless of cost increases or import competition.

The Commission also considered that an increase in the duty on sugar would have an impact on downstream industries and consumers. Unlike the other tariff scenarios, the price-impact analyses considered by the Commission, suggest that the domestic reference price recommended below, yielding an immediate duty of 132c/kg, equivalent to 26% *ad valorem*, would not have a considerable price-raising effect, but would remove the price disadvantage experienced by the domestic industry and lead to increased production levels and profitability.

In view of the above, the Commission recommended that the DBRP for sugar be increased to US\$566/ton as follows:

Domestic reference price = World reference price + distortion factor – transport costs

i.e. US\$566/ton = US\$558 + US\$39 - US\$31

Using the price data as on 3 January 2014, a specific duty of 132c/kg (equivalent to 26% *ad valorem*) will be triggered using a DBRP of US\$566/ton.

RECOMMENDATION

In view of the foregoing the Commission decided to recommend that the domestic Dollar-based reference price for sugar be increased from US\$358/ton to US\$566/ton based on the 4-year average London No. 5 settlement price of sugar of US\$558/ton, plus an adjustment for the distortion factor evident in the international sugar market of US\$39/ton, less the average ocean transport cost of sugar to a South African port of US\$31/ton.

The initial duty on sugar will be calculated as the difference between US\$566/ton and the price of sugar on the London sugar exchange on 3 January 2014, which amounted to US\$440.40/ton at an exchange rate of R10.47 to the US\$ as follows:

Reference price	
RSA domestic reference price	US\$566/ton
Minus: London No. 5 settlement price of sugar on 03 January 2014	US\$440.40/ton
Dollar duty on sugar	US\$125.6/ton
Rand duty on sugar	132c/kg

Adjustments to the level of protection will be based on quantum movements in the world reference price as follows:

The difference between the 20 trading day moving average London No. 5 settlement price and the established domestic reference price for sugar will be calculated daily. If the 20 trading day moving average of the No. 5 settlement price shows a variance of more than US\$20/ton from the previous trigger level for 20 consecutive trading days, a new duty will be calculated. The resulting Dollar duty will be converted to Rand, based on the Rand/Dollar exchange rate prevailing on the day that the adjustment is triggered.

[08/2013]