Australian Sugar Milling Council

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Committee Secretary
Joint Standing Committee on Foreign Affairs, Defence and Trade
PO Box 6021
Parliament House, Canberra ACT 2600

Sent by email: jscfadt@aph.gov.au and Andrew.Dawson.Reps@aph.gov.au

Dear Committee Secretary

The Australian Sugar Milling Council (ASMC) welcomes the opportunity to make a late submission to the Joint Standing Committee on Foreign Affairs, Defence and Trade inquiry into access to trade agreements by small and medium sized enterprises.

ASMC is the peak body representing six milling companies who collectively own and operate 20 sugar mills in Queensland. Our members account for over 95% of national raw sugar production and produce more than 99% of Australia's raw sugar exports.

Consistent with the Committee's objective of identifying ways Government can improve the efficacy of FTAs and Australian trade in general, our submission focusses on:

- The significant socio-economic contribution of the milling sector and emerging threat of low global sugar prices
- The strong demand fundamentals for global sugar
- The industry's competitive and comparative strengths in burgeoning markets
- The overly complex regulatory settings that control how Australian sugar is marketed
- The dual imperative for the Australian government to pursue both offensive and defensive trade strategies
- What industry is doing to maximise its export revenues
- Recommendations for improving the marketability of Australian sugar.

The Australian sugar industry's socio-economic contribution

The Australian sugar industry is a vibrant and vital contributor to Queensland's rural and regional economy but is currently under threat from low global prices.

In 2017/18 Australia's 24 sugar mills generated total revenue of $2 billion from export and domestic sales of raw and refined sugar, domestic sales of electricity made from the bio-mass known as bagasse, and domestic and export sales of molasses.

Specifically, the milling sector in 2017/18:

- Employed more than 4,000 workers directly and paid approximately $360 million in wages

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- Purchased around $1 billion in goods and services from more than 3,000 Australian businesses in operational expenditures (to maintain or make current mills more efficient) or capital expenditures (expand to improve capacity or diversify revenue streams).
- Purchased around $1 billion in sugarcane from around 3,000 cane farming businesses to produce milled raw sugar and refined white sugar.

In the context of this inquiry, Australia's sugar mills and refineries would be considered medium-sized advanced manufacturers.

Caused by subsidised over-supply, global raw and white sugar prices are currently depressed, and approximately 30% below the cost of producing raw sugar (of which Australia is a low cost, quartile 1 global producer). A continuation of these prices beyond the 2018/19 season is likely to place growers and mills under considerable financial strain.

The global demand fundamentals for sugar remain strong

Despite the increasing attention to the role of sugar in the modern diet, the demand fundamentals for sugar remain sound. Whilst demand is slowing, it is still expected to increase in aggregate and per capita terms over the next ten years.

Recent analysis by Copersucar[1] indicates:

- World sugar consumption per kilogram, per capita, per year (kg/capita/year) has grown each year since 2009 and is currently at a global average of 23. From lowest to highest the most sugar consuming regions on a kg/capita/year basis are China (11), Africa (15), India (21), Asia others (23.5), North America (25), Europe (34) and Latin America (38)

- World sugar consumption is expected to increase around 2% per annum on average over the next ten years. Calculated on GDP and population growth forecasts, and from lowest to highest, forecast growth rates are Europe (-0.4%), Latin America (1.2%), North America (1.3%), China (1.8%), India (2.1%), Asia (2.6%) and Africa (3.5%).

Australian sugar's competitive strengths

Australia's competitive strength is the high-quality of its raw sugar supply, the freight differential due to our proximity to burgeoning markets – especially in Asia, and the tariff concessions earnt through preferential trade deals.

Raw sugar is produced and sold in 'brands' with specified quality standards (sucrose content as measured by polarisation or pol, moisture etc). Typically, the higher the pol, the higher the premium (and total returns) paid by the global market.

Australia competes for market share against countries like Brazil, Thailand, Guatemala, India and Mexico. With the exception of Thailand who produces lower pol raw sugar, on a

[1] Mr Paulo Roberto de Souza at the February 2018 Dubai Sugar Conference (full presentation is available upon request)

like-for-like (quality or pol) basis, Australian raw sugar shipping costs are lower into Asia when compared to these competing suppliers.

The main export destinations for Australian sugar millers are currently Japan (0.6 million tonnes), South Korea (1.5 mt) and Indonesia (1 mt) where it is made into white sugar. Australia's competitive advantage into these markets has been improved over the years by preferential trade deals. For example, the tariff concessions achieved through TPP-11 and the proposed AUD$18.35 per tonne reduction in the Japanese tariff on high-pol (98.5-99.3 pol) has a number of economic and strategic benefits including:

- Consolidates Australia's competitive position against alternative suppliers.
- The required shift to higher pol supply and higher volumes may lead to domestic handling and refining efficiencies and higher price premiums.
- By virtue that importers and distributors of sugar are typically large Japanese corporations assists with lowering counterparty risks and costs.

How Australian sugar is marketed

The export marketing of Australian sugar is regulated under the Queensland *Sugar Industry Act* (the Act) and the Federal Code of Conduct (the Code). Under both, growers can exercise through Grower Economic Interest (GEI) provisions, control over who markets a portion of the sugar that is manufactured by the mills they supply cane to (i.e. the former single-desk being Queensland Sugar Limited, and the millng companies). Today, around half of the raw sugar that is exported is marketed by QSL and the rest by milling companies.

As outlined in ASMC's recent submission to the review of the Code, these regulations are a disincentive to investment, may have lowered revenues and have increased transaction costs (finalization of cane supply agreements, GEI calculations and payments) and risk impost (e.g. indemnification of third party pricing agents). ASMC is seeking full repeal of these provisions in the Act and the Code.

The Australian sugar industry's trade interests are both offensive and defensive

With a relatively small domestic market[2], access to the export market and buoyant, market driven global prices to sell the remaining 3-4 million tonnes of raw sugar production is vital. Despite around 180 million tonnes of raw sugar consumption globally, Australia competes in a relatively small traded market of around 65 million tonnes per year. Countries that import raw sugar in this market either have refineries that do not have any or enough domestic raw sugar supply.

Due to the significant sizes of sugarcane acreages and the high number of people employed, sugar is a 'sensitive' product meaning countries commonly subsidise cane and sugar production (often resulting in domestic surpluses that are exported and that depress global prices) and/or try to protect their domestic sugar industries against more competitive imports.

Through preferential trade agreements that reduce tariff and non-tariff barriers to trade and provide for expanded quota access, the Australian sugar industry looks to government

[2] Australian consumes around 1 million tonnes per annum

to open up new, and consolidate existing trade arrangements to diversify market opportunities and increase demand for Australian sugars and overall returns (offensive interests). As critical is the need to work with like-minded countries to hold countries who flaunt their WTO obligations to account (defensive interests).

ASMC's priorities are to consolidate relationships with our loyal trading partners (Japan, Indonesia and Korea) as well as diversify risk and gain access to additional, premium earning markets. The United States (3 mt pa requirement), China (5.3 mt pa requirement) and the European Union (and UK) (2.5 mt pa requirement) are examples of markets Australia has been servicing for many years but new, improved policy settings are sought.

The Australian sugar industry failed through the Aus-US FTA and more recently through TPP-12 negotiations to achieve improved market access to the highly lucrative US market. In the US, where the federal government implements a number of complex domestic and import supply controls, the raw sugar price is around US25c/lb or AU$765/tonne. This is more than double the current global export price of AU$367/tonne. Currently supplying around 100,000 tonnes per year, or 3% of US total raw sugar import needs, Australia continues to look for opportunities to increase our duty free access to the US market.

Further opportunities include the upcoming review of the China-Australia FTA, the EU-27-Australia FTA and a post BREXIT deal with the UK. Under World Trade Organisation (WTO) rules, Australia is allowed to export a very low, and non-commercial volume of 9,925 tonnes to the EU-28 (EU-27 plus UK) at a prohibitive €98 per tonne duty. The EU-27's total raw sugar import requirement is currently close to 1 million tonnes. The upcoming EU-27 FTA negotiations presents an opportunity for Australia to improve the quantum of duty free access. Australia's access to China is also limited and we compete for around 2 million tonnes of access and a tariff currently set at 95%.

A further issue that needs to be resolved is the continuing risk that Australian raw sugar exports to Japan can exceed allowable pol limits and incur additional costs. Under the Japan-Australia Economic Partnership Agreement (JAEPA), Japan provided a number of tariff concessions to support raw sugar imports less than 99.3 dry polarisation. If imports exceed 99.3 dry polarisation very high customs duty and tariff penalties are applied (~AUD $220/t). The issue is that despite the raw sugar being tested in Australia as consistently below 99.3 under universally accepted testing protocols, Japanese Customs on a number of occasions have determined the sugar to be in excess of 99.3. Consistent with the good will exhibited by both countries in finalising the JAEPA, Australian raw sugar exporters are seeking to engage the Japanese government to ensure that polarisation testing is aligned, proficient, and repeatable. At present, under the current protocol of strictly interpreting the dry pol standard, and in order to ensure compliance, Australian sugar producers must prepare special cargoes for the Japanese market, reducing efficiencies, limiting optionality and raising costs.

On the defensive side, a significant concern is the increase in government interventions in sugar producing countries. Common government interventions include import quotas and tariffs, direct payments to growers, export subsidies and domestic cane and sugar price support. These interventions have multiple impacts, but commonly they incentivise excessive production, global oversupply and depressed global prices. This means that the most efficient and low cost sugar producers like Australia lose money – compromising viability and new investment. Countries who are members to the WTO enjoy certain entitlements but are also under certain obligations. It is imperative that governments are fully transparent with the cost and type of assistance being provided and meet their obligations under the WTO. If inconsistencies are identified, there needs to be effective dispute regimes in place to hold countries to account.

ASMC continues to advocate and work with DFAT and DAWR and like-minded global producers to advance global trade liberalisation in the global sugar industry. ASMC is currently calling on the Australian government to pursue diplomatic and potentially WTO action against India and Pakistan who are currently in contravention of their WTO entitlements.

Developing an Industry Trade Strategy

Over the coming months, the Australian sugar industry will commence development of a 20 year trade policy and market access (TP&MA) plan with the following features:

- A 20-year time horizon with progress clearly defined at the end of the first five years.
- A set of TP&MA outcomes, limited in number but comprehensive in scope, that can realistically be achieved and that would deliver maximum benefits for the industry.
- Extensive use of analysis of what is possible and the benefits of achieving the outcome via a combination of expert views (both from industry leaders, government and technical experts) and economic analysis that provides insight into where the greatest pay-offs to effort exist.
- For each outcome in the Plan, clearly defined KPIs indicating attainment of the outcome or satisfactory progress — with separate sets of KPIs defined for a 5-year time horizon and a 20-year horizon.

Recommendations to improve the global marketability of Australian sugar

(1) ASMC seeks repeal of those provisions of the Act and Code that regulate who can market sugar (the so-called marketing choice) and the right of a third party to control decisions usually vested between commercial entities (the so-called pre-contract arbitration provisions). Repeal would reduce risk and encourage greater investment as well as improve marketing efficiencies.
(2) A further escalation of Australian Government representations to the Indian Government, and to canvass support from like-minded sugar exporting nations, including Brazil, to pursue action against India at the WTO.
(3) Seek to re-negotiate access opportunities into China and the US and an ambitious duty-free quota into the EU-27 and the UK post BREXIT.
(4) For the Australian Government to work with the Australian sugar industry as it develops its Industry Trade Strategy over the coming 12 months. The strategy will use quantitative and qualitative analysis to identify market opportunities most likely to maximise export revenues over the coming five years. Over time, ASMC would seek to align our commercial and policy advocacy efforts to these identified markets.

For further information on these matters please don’t hesitate to contact Mr David Rynne, Director – Policy, Economics and Trade on david.rynne@asmc.com.au and via 0431 729 509.

Yours sincerely

David Pietsch
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