Source: MSF Sugar – Tablelands Mill

FEB 2019

SUGAR POLICY INSIGHTS

INSIDE

AUSTRALIAN Sugar Milling COUNCIL

WHERE NEXT FOR AUSTRALIAN RAW SUGAR?

In January, ASMC released an independent report that showed sugar manufacturing in Queensland directly and indirectly contributes more than $4 billion in economic activity. The sector underpins more than 22,500 jobs and supports a large number of businesses and communities in regional Queensland, predicted to be a key 'battleground' in the upcoming federal election.

Australian sugar manufacturers and exporters however face a number of short and longer term threats including ever deeper economic cycles and real price decreases, cost increases and increasing global competition.

To navigate this challenging environment, the industry urgently needs to come together to develop a revitalisation strategy.

A first step must include a cold hard look at the data, which highlights some fundamental failings that must be collectively addressed by all industry sectors.

In this edition, we explore these fundamentals in more detail and begin to quantify the scale of the challenge ahead.

FROM THE CEO
by David Pietsch

In this election year, the sugar industry needs a combination of vision and progressive industry and government leadership if it is to fulfil its potential as an economic powerhouse, delivering jobs and growth for regional Queensland.

The Australian Sugar Milling Council's (ASMC) election priorities are firmly focused on the political leadership needed to remove red-tape, challenge the market-distorting subsidies employed by competing countries, and to support industry revitalisation.

Raw sugar manufacturing's federal election priorities:

- Commit to ongoing trade liberalisation efforts including WTO action against Indian sugar subsidies
- Removal of counter-productive marketing regulations
- Actively support the industry to develop a strategy to revitalise its future

We seek a continuation of the strong, bipartisan leadership shown on trade policy liberalisation and market access negotiations. The Australian Government, in partnership with ASMC and CANEGROWERS, has led the way in prosecuting our WTO case against subsidised sugar, particularly from India, and this leadership must continue and intensify in 2019.

In December the federal government released its review into the Sugar Code of Conduct. The review made six recommendations that drew strongly from ASMC's own submission. While not calling for the complete removal of the Code as ASMC argued, the review team nevertheless recommended significant reform, including removal of contested components of the Code, and the need for greater focus on industry strategy to drive the industry forward. Disappointingly, the current government baulked and left two of the six vital recommendations on the shelf.

The sugar industry urgently needs a revitalisation strategy to secure its future – one that encourages investment in diversified revenue streams and differentiation – and this can only come with decisive industry and government leadership to help it get there.

REVITALISING THE SUGAR INDUSTRY
by David Rynne, Director of Economics, Policy and Trade

Global raw sugar prices have fallen in real dollar terms on average 2 percent per annum since the 1970s (Chart 1). Deteriorating terms of trade (output prices relative to input prices) is a common feature of competitive commodity markets and requires concerted industry and government effort in response. Our biggest competitors – Brazil and Thailand – are pursuing multiple strategies whereas Australia has no plan, and no supporting policy framework.

Assuming constant commercial cane sugar (CCS) values, sugar prices, and exchange rates, this means milling revenues (i.e. production and productivity for these purposes) need to grow more than 2 percent per annum to improve profitability, competitiveness and resilience.

PRODUCT DIVERSIFICATION IS NEEDED

Despite the potential, the Australian sugar industry has not been able to substantially diversify its revenue base, mitigate risk and create arbitrage opportunities and there remains no real policy framework in place to support diversification.

In 2017, 90 percent of the almost $2 billion in revenues earned by the Australian sugar manufacturing industry were derived from raw sugar production - of which 85 percent was sold into a highly competitive and distorted global raw sugar market. In the same year, only 5 percent of revenues were derived from molasses, 3 percent from ethanol and 2 percent from co-generated power.

In comparison, Brazil can readily switch between sugar and various forms of ethanol production and Thailand is investing actively in value-added bio-product innovation and manufacture. Furthermore, both countries have supporting diversification strategies and policies in place.

Through co-generation upgrades and expansions, and changes to steam on cane usage, internal analysis shows that the milling sector has significant potential to increase the amount of power it exports to the grid. Furthermore, there is significant potential to expand ethanol production with the right policy and commercial incentives.

Whilst we continue to assess global and domestic market demand for bio-products this is an emerging and promising value-add opportunity for the industry. There are potentially significant environmental benefits from displacing fossil fuels from the electricity/fuel energy mix and removing non-biodegradable plastics from circulation.

IMPROVED SUGAR AND CANE PRODUCTIVITY AND ACREAGE EXPANSIONS ARE ALSO KEY

Increased production can be achieved through improved cane and sugar yields and cane area expansions.

Cane productivity gains are critical to improve:

- The economics of increasingly marginal new cane acreage
- Profitability to encourage new farm and milling investments, and
- Australia's global competitiveness relative to suppliers like Brazil and Thailand who are aggressively improving their competitiveness.

PAST PRODUCTION AND PRODUCTIVITY PERFORMANCE HAS NOT BEEN ADEQUATE

A review of the industry's past performance reveals that 2 percent production and productivity gains per annum have not been achieved.

ABARES data reveals[1] that from 1974 to 2018 cane and sugar production has increased, but short of the required 2 percent. Cane production recorded a 1.5 percent per annum increase over this period and sugar increased 1.6 percent per annum. The growth was driven mainly by cane area growth (hectares) (1.2 percent increase per annum) and to a lesser extent, cane yield growth (0.3 percent increase per annum).

Significant improvement in cane yields has been stymied by onsets of disease (orange rust and smut) resulting in the removal of better performing varieties from production. Expansion of the area under cane has been hindered by water availability and affordability (electricity costs and access charges), urban encroachment and substitution to other crops.

"Australia has not been able to diversify revenues, increase cane and sugar production or productivity sufficiently to offset the (real) price fall of raw sugar."

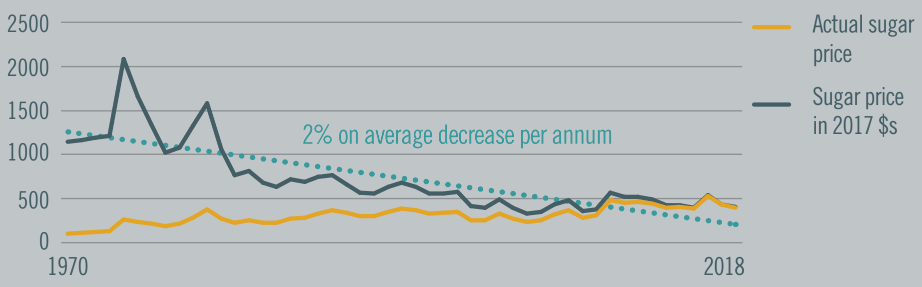
REQUIREMENTS TO OFFSET 2 PERCENT REVENUE LOSSES PER ANNUM

Looking at sugarcane specifically, Table 1 summarises the increases in cane acreage or yield (this could be achieved as a combination) that would need to be achieved in each growing region by year 10 of a 10 Year Strategy to offset the 2 percent annual decrease in sugar prices.

NEXT STEPS

ASMC plans to meet industry stakeholders and government over the coming months to stimulate development of a revitalisation strategy, including a discussion on how diversification (ethanol, co-generation and other bio-products) and increased cane acreage and improved yields can be best achieved.

CHART 1: RAW # 11 SUGAR PRICE ACTUAL AND REAL ($A) 1970-2018



SOURCE: USDA (PRICES), ABS (CPI), ATO (FOREX)

TABLE 1: AGGREGATE INCREASES THAT OFFSET A 2 PERCENT PER ANNUM PRICE DECLINE

REGION	CANE ACREAGE (HA)		CANE PRODUCTIVITY (T/HA)	
	2017	2026	2017	2026
Northern	84,429	100,900	82	98
Herbert/Burdekin	125,878	150,436	104	125
Central	105,140	125,652	72	86
South	46,096	55,089	83	99
Queensland	**361,543**	**432,078**	**87**	**104**

SOURCE: ASMC MEMBERS AND INTERNAL ASMC ANALYSIS

1 ABARES, Agriculture commodities and trade data, rural commodities – sugar

Indonesia in Focus

Indonesia is a close neighbour and an important market for Australia's agricultural commodities, including raw sugar. It has a long history as a sugar producer, but increasingly depends on raw sugar imports to satisfy demand from its fast-growing population.

In 2017 the Australian government negotiated a 3 percent reduction to the previous 8 percent import tariff for Australian raw sugar imports. Since coming into force on **4 October 2017***, the same low **5 percent tariff** applies to imports of both Australian and ASEAN (Association of South East Asian Nations) raw sugar, particularly from Thailand.

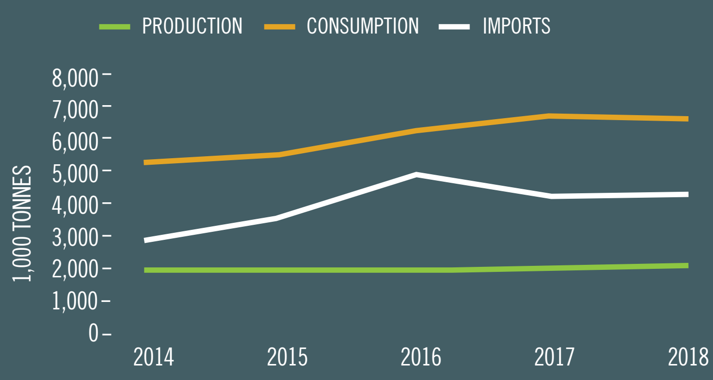
In 2018, a three year duty free access regime negotiated by Brazil came to an end. Therefore, building on our strong bilateral relationships, our raw sugar exporters are well positioned to supply this burgeoning market.

*Required a tariff schedule change under the regulations of the AANZFTA (ASEAN Australian New Zealand Free Trade Agreement).

At a Glance

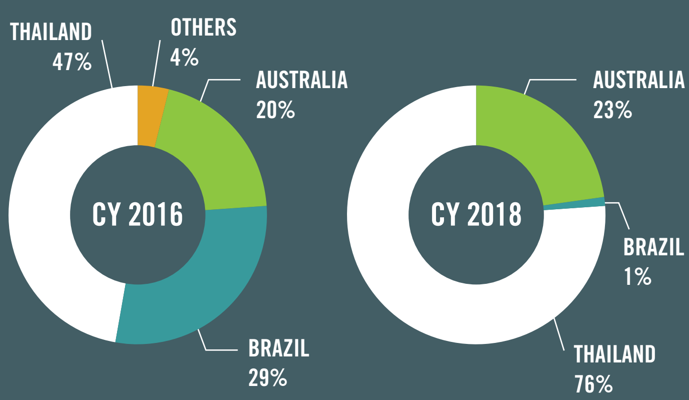
- Population over **263 million**
- Consumption increased **3.4 percent year on year** since 2008 (to approx. 25kg per capita)
- **Largest importer of raw sugar in the world** overtaking China in 2016
- Highly regulated market with initial import quota set in January 2019 at **2.83 million tonnes**
- Raw sugar imports mainly for **industrial uses** (beverage and food manufacturing)
- Thailand and **Australia well positioned to fulfil import demand** due to advantageous 5 percent tariff plus freight differentials
- Australian market share up from 20 percent to **23 percent** 2016 to 2018

INDONESIAN SUGAR MARKET



SOURCE: USDA

ORIGIN OF INDONESIAN RAW SUGAR IMPORTS



SOURCE: OLAM SUGAR RESEARCH, BLOOMBERG

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About ASMC

Established in 1987, the Australian Sugar Milling Council represents Australia's raw sugar manufacturers and exporters. Our aim is to be a leading voice for change to create opportunities for a more profitable and sustainable sugar industry.

KEY FOCUS AREAS

Trade policy | Social licence | Advocacy | Revitalisation | Research strategy