UNITED STATES SUGAR REGIME

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INTRODUCTION

Good morning. I would first like to thank the Government of Cuba for agreeing to host the second FAO International Sugar Conference, and I would like to say that it is indeed an honour for me to address this distinguished group of Conference participants and speakers. Thanks also for travelling to Havana from sugar producing and consuming countries throughout the world. Please note that throughout this presentation I will refer to the United States Sugar Regime as United States Sugar Policy.

This paper will provide a brief overview of United States sugar policy prior to the Uruguay Round, domestic support measures of the United States Sugar Program, and current United States sugar policy within the context of the North American Free Trade Agreement and the Uruguay Round.

UNITED STATES SUGAR POLICY PRIOR TO URUGUAY ROUND

Current sugar policy in the United States has evolved from policy instruments established in the late 1970s, when the United States Congress passed an emergency loan programme to insulate sugar producers from the dramatic price fluctuations of the world sugar market. This emergency amendment was eventually incorporated into 1981 Farm Bill legislation as an 18 cents per pound price guarantee loan for raw cane sugar. Further protections for sugar growers were added in 1982 through a country-by-country import quota system, allocated according to historical percentages.

The 1985 Farm Bill added a no net-cost provision to the basic price support concept. This provision required that administration of the Sugar Program incur no cost to the Federal government. Thus, the United States Department of Agriculture (USDA) received a Congressional mandate to administer support mechanisms to maintain internal raw cane and refined beet sugar prices at high enough levels to avoid forfeitures of loans, which would violate the no net-cost provision.

Australia successfully challenged the legality of the United States sugar import quota under the GATT in the late 1980s. As a result of this case, United States sugar import quotas were converted to a Tariff Rate Quota (TRQ) system. A two-tier low/high duty system was implemented to replace the absolute country-by-country quotas, with all country percentages or allocations remaining the same under the Tariff Rate Import Quota.

A minimum import quota of 1.13 million tonnes was established as a result of the Uruguay Round. Restrictions on sales of domestic sugar, called marketing allotments, were also established to protect the GATT-mandated minimum quota access. If surplus domestic supplies of raw cane and/or refined beet sugar threatened the minimum quota volume, cane millers and beet processors were required to restrict sales of sugar on a pro rata company by company basis. Marketing allotments were implemented on two occasions during the mid-1990s, and were eliminated from the 1996 Farm Bill, leaving the Tariff Rate Quota as the only supply control mechanism available to USDA.

SUGAR AND CORN SWEETENERS

Any discussion of the development of United States Sugar Policy since the late 1970s must also refer to the relationship between sugar and corn sweeteners in the United States. Sugar supplied virtually all of the sweetener demand in the United States until the introduction of high fructose corn sweeteners in the late 1970s. High fructose corn sweetener rapidly displaced sugar in liquid applications due to substantially lower prices, and by the late 1980s the conversion of the domestic beverage industry to corn sweeteners was virtually complete. This substitution led to widespread rationalization of the sugar industry throughout the United States, resulting in a 75 percent decline in sugar imports under quota.

Price supports under the United States Sugar Program provided, and continue to provide, a favourable price umbrella for corn sweeteners. Expansions in corn sweetener production facilities were inevitable as food and beverage manufacturers in the United States continued to substitute the lower cost sweetener for sugar in as many applications as technically feasible.

Today, corn sweeteners comprise the major part of total consumption of caloric sweeteners in the United States. For calendar year 1998, total United States consumption of caloric sweeteners was 19.4 million metric tonnes, of which corn sweetener comprised 54 percent and refined sugar 43 percent. The relationship between sugar and corn sweeteners in the United States is an important one not only for the price umbrella provided by the Sugar Program, but also as a basis for understanding currently contentious NAFTA sugar and sweetener trade issues between Mexico and the United States.

The potential for significant corn sweetener substitution of sugar in the Mexican beverage market is one of the driving factors behind current trade disputes. Substitution either through substantial volumes of exports from the United States as well as Mexican corn sweetener production would most likely result in the rationalization of the Mexican sugar industry. Anti-dumping duties on imports of United States corn sweeteners levied by Mexico over the past few years should be viewed as a means to delay potential substitution until ongoing United States-Mexico sugar trade negotiations are completed or the NAFTA is fully implemented, whichever comes first. The NAFTA provisions for sugar trade between Mexico and the United States will be discussed after a brief review of domestic support tools.

UNITED STATES SUGAR PROGRAM SUPPORT MECHANISMS

The United States Sugar Program utilizes two primary tools to support internal sugar prices and control total sugar supplies. The first tool is a loan programme which establishes a minimum price guarantee to cane millers or beet processors with no price guarantee to United States cane refiners. The loan price guaranteed to cane millers for raw sugar has been constant since 1985, while the loan price to beet processors has increased only slightly over the past six years. The loans rates function as a price floor to determine effective market prices for both cane and beet sugar.

The second support mechanism is the Tariff Rate Import Quota (TRQ), annually established by USDA to ensure that domestic prices remain above loan rates plus interest (no net-cost provision). The TRQ is a two-tiered duty, with the lower tier subject to nominal or zero duty. Quota-holding countries are given preferential access and sell into the United States market at the internal price for raw sugar. Import quotas on refined and speciality sugars are also in place, but the volumes are not as significant as the raw sugar import quota. A brief discussion of both the loan programme and the tariff rate quota system is presented below.

LOAN PROGRAM

Sugarcane millers or sugarbeet processors in the United States are eligible to receive price guarantees through loans administered by USDA. These loans essentially function as the effective price floor for raw cane sugar and refined beet sugar in the United States. Loan rates are adjusted for each producing area to reflect regional transportation costs.

The 1996 Farm Bill negotiations resulted in two types of loan programmes for millers and processors, non-recourse and recourse loans. The new Farm Bill determined that non-recourse loans, previously the only type of loan offered by the Sugar Program, would only be available for that crop year if the TRQ is established at or above 1.36 million metric tonnes. Non-recourse loans allow a cane miller or beet processor to place sugar under loan at the guarantee price of 18 cents per pound for raw cane sugar and 23.90 cents per pound for beet, with sugar the only security for the loan. Thus, if market prices decline to below loan rates, the government has no recourse but to accept the sugar instead of cash payment of principal and interest.

If the TRQ is established below 1.36 million metric tonnes, millers and processors are eligible for recourse loans, which essentially function as commercial bank loans, require cash repayment and essentially remove effective price support from the market. Non-recourse loans and the option to place sugar under loan as the necessary collateral tends to support internal market prices.

TARIFF RATE IMPORT QUOTA (TRQ) UNDER URUGUAY ROUND

The TRQ allows for the import of an annually established quantity of raw sugar at preferential duties, with second tier or high tariff rate duties on any ex-quota imports. As such, the Tariff Rate Import Quota (TRQ) is the primary form of border protection in place to support domestic sugar prices through restrictions on imports.

The TRQ is established through an intergovernmental working group comprised of representatives of many United States Government agencies. USDA determines an appropriate import volume for the upcoming fiscal year, requests comments from industry, and typically announces the TRQ prior to the beginning of the new fiscal year. Many factors determine the import quota volume, including USDA forecasts of sugar supply and demand, non-quota imports and NAFTA provisions. USDA then reviews the import volume in order to either allocate additional quantities for release to the United States Trade Representative (USTR) or cancel a certain percentage of the originally established import volume.

USDA announced this year’s quota level in early November at 1.36 million metric tonnes, allowing 1.13 million metric tonnes for initial allocation to quota-holding countries. USDA establishes and announces the import quota level in any given year, while USTR announces the country-by-country tonnage allocations. Forty countries around the world receive TRQ allocations based on historical trade to the United States. The top three quota holding countries are the Dominican Republic, Brazil and the Philippines, which combined hold slightly over 43% of the quota volume, or almost 481,000 metric tonnes. The top ten quota-holding countries after the top tier listed above include Australia, Guatemala, Argentina, Peru, Panama, El Salvador and Colombia. These countries account for close to 70% of the quota volume, or approximately 717,000 metric tonnes. Imports under the TRQ are dependent on annual supply/demand factors, but have increasingly declined due to expansions in domestic production and increased ex-quota imports.

The United States also restricts access for refined sugar and related products with Tariff Rate Quotas. The refined sugar quota is 60,000 metric tonnes, with 25,000 metric tonnes of this quota allocated to Mexico in order to fulfil NAFTA obligations. Under the NAFTA, the United States is to provide market access for raw or refined sugar from Mexico, in conjunction with Mexico’s net surplus producer status.

UNITED STATES SUGAR POLICY AND THE NORTH AMERICAN FREE TRADE AGREEMENT

The NAFTA sugar provisions mandate complete liberalization of sugar and sweetener trade between Mexico and the United States by 2008. NAFTA provisions stipulate that all tariffs on mutual trade be phased out by the end of the fifteen-year implementation period. Mexico is to align its tariffs on third country trade with United States tariffs over the first six years.

For all the years of the agreement, Mexico receives a preferential duty-free quota of 7,258 tonnes. However, this preferential access increases if Mexico’s sugar consumption (including high fructose corn sweetener) is less than sugar production for two consecutive years, resulting in net surplus producer status. Mexico became a net surplus producer in 1994 according to these criteria, and has remained a net producer to date. Net producer status has increased Mexican quota access to the

United States sugar market to 25,000 metric tonnes for the first six years of NAFTA. Quota access will increase to 250,000 tonnes as of October 2000 and remain at that level until 2008 if net surplus producer status is maintained.

The NAFTA tariff schedule declines rapidly over the length of the agreement in order to fully liberalize the two markets. The lower NAFTA tariffs plus sharp declines in world prices encouraged Mexican ex-quota sugar exports to the United States this past year. The high-tier tariff for raw sugar (96 polarity) is reduced from 13.60 cents per pound to 12.09 cents per pound as of calendar year 2000. The corresponding tariff for refined sugar (100 polarity) declines from 14.42 cents per pound to 12.81 cents per pound.

Declining NAFTA tariffs and high internal prices in the United States have resulted in substantially increased amounts of Mexican ex-quota sugar entries at the high duty. There are no price-based safeguards on sugar exports from Mexico, unlike the special safeguards the United States has in place under the WTO. USDA is currently projecting non-TRQ imports for 1999/2000 at 450,000 tonnes, with a large amount of this volume potentially sourced from Mexico. Recent declines in United States domestic raw sugar prices may slow the pace of ex-quota exports from Mexico, but if Mexican refiners need to export their exportable surplus beyond the current quota access, internal prices in the United States are an attractive alternative over near term world market prices. The result is further diversion of trade as increasing Mexican exports to the United States ultimately pressure the Tariff Rate Import Quota. And, this pressure is in place even prior to the upcoming increase in Mexico's quota access.

The United States government must determine whether or not the additional Mexican access is to be included within or in excess of the current minimum TRQ of 1.13 million metric tonnes, and the final rule over NAFTA trade is the GATT accord. Most importantly, the resolution of this issue will establish a precedent for any future bilateral sugar trade agreements with the United States.

UNITED STATES SUGAR POLICY AND THE URUGUAY ROUND

The Uruguay Round did not result in substantial reform of the United States domestic sugar supports or sugar trade policy. The underlying structure of the United States sugar market remains basically unchanged despite the reworking of a system in accordance to URA commitments.

The Uruguay Round objective of tariffication was easily fulfilled by the United States because a Tariff Rate Quota system had already been established. The GATT two-tier duty allowed preferential access to quota-holding countries at nominal or zero duty, while the initial high duty tariff was established at 17 cents per pound. The United States agreed to lower the high tier duties by 15% over the six-year implementation period, with the high tariff to decline to 14.45 cents per pound next year. However, the United States included some protection components in the calculation of the base tariff level, effectively increasing the base from which the tariff reductions would be applied. The United States under the WTO has the right to invoke an additional form of border protection, called special safeguards, in the event of rapidly declining prices or import volume surges. To date, the United States has not invoked its special safeguard rights for sugar.

No reductions in domestic support measures were undertaken as the Blair House Accords between the United States and the European Community resulted in an agreement that no reductions in domestic support prices would be part of the URA negotiations for sugar. Furthermore, negotiations for reductions in export subsidies were not at issue because the United States has never subsidized refined sugar exports

IMPLICATIONS FOR FUTURE UNITED STATES SUGAR POLICY

Record levels of domestic production, increased ex-quota sugar imports from Mexico and import leakage in the form of sugar syrups or finished sugar containing products have all contributed to recent downward price pressures for both refined and raw sugar in the United States. Furthermore, the sharp declines in world sugar prices have lead to increased import leakage, either through quota circumvention, low priced sugar syrups or high duty entries.

All of the above factors are seemingly pressuring the domestic support mechanisms currently in place. The postponed announcement of this year's TRQ is an example of the dynamics at work in the United States sugar market. USDA understood that domestic market fundamentals would have called for a quota at the GATT-minimum. However, under current legislation, any announcement below 1.36 million tonnes would have resulted in recourse loans, essentially removing USDA's ability to support domestic prices.

USDA announced the TRQ after unusually lengthy discussions with other United States Government counterparts at a level, which seemed artificially high given past supply control targets and stocks-to-use rations. Yet announcing the quota at the 1.36 million metric tonne level ensures that cane millers and beet processors are eligible for non-recourse loans at the guaranteed loan price. Although too early to determine thus far this year, the sharp declines in domestic raw sugar prices indicate that forfeitures of sugar under loan, particularly raw sugar, may be likely. Florida sugarcane processors last faced a similar market scenario in 1985, when sugar under loan was forfeited to the United States Government. The sugar was stored by the Commodity Credit Corporation and eventually sold to China at 4 cents per pound, less than 25% of the price guaranteed to the growers.

CONCLUSION

United States Sugar Policy has continued to provide a price umbrella to the corn sweetener industry, and encouraged significant expansions in domestic sugar production. United States raw sugar prices have declined significantly over the past few months and are below loan rate levels, despite the policy tools in place to support internal prices.

These recent market developments signal the serious challenges currently facing most sugar producers in the United States. The challenges faced by the United States and Mexican market in regard to NAFTA liberalization are formidable for both countries and will form the precedent for further hemispheric trade pacts, such as the Free Trade Agreement of the Americas. And, in regard to the URA and future trade talks, there continue to be significant concerns about the future direction of United States Sugar Policy reform.