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Future Effects of the U.S. Sugar Program
Impact on Industrial Users

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The current version of the Farm Bill passed in both houses of Congress contains legislation which industrial users oppose, and represents a reversal of many years of efforts to reform the least market-oriented of all U.S. farm economy support programs. The 2002 Farm Bill provides for:

- The elimination of the 1 cent forfeiture penalty to the CCC.
- Re-establishment of the no-net cost feature of the program by authorizing a Payment -in-Kind program.
- Re-introduction of marketing allotments in an attempt to regulate domestic production.

These provisions virtually guarantee higher prices to industrial users induced by artificial shortages, as well as stagnant growth in the marketplace for domestically produced sugar containing products. Users will continue to move operations offshore, closing domestic factories with a loss of manufacturing jobs, and seek to develop products that minimize the use of sugar.

Background – A History of Sugar Reform during the 1990's

Before stating the objectives of a user-oriented policy, a brief history of sugar reform will be reviewed.

In the 1990 Farm Bill markup, the Downey amendment sought to reduce the loan rate by 2 cents per pound from 18 cents to 16 cents per pound. The amendment failed to pass in the House by a vote of 150-271, but not before over $30,000 in contributions to 61 different members of Congress was pledged just four days before the vote by the Southern Minnesota Sugar Cooperative PAC. [1]

In 1995, Rep. Dan Miller from Florida introduced legislation to eliminate the Sugar Program. He convinced the Rules Committee to allow one hour of debate on the issue. The amendment lost by nine votes – 5 people who had ***co-sponsored the legislation*** changed their votes, and voted against the amendment! [2]

Reforms did emerge in the process, however. The "no net cost provision" (to the taxpayer) - which prevented the CCC from accumulating sugar stocks under forfeiture, and was institutionalized by shrinking the import quota and/or the imposition of domestic marketing allocations, was not included in the 1996 bill.

The repeal of the "no net cost" provision was also underpinned by the authorization of **recourse loans** for sugar for the first time, but only if the raw sugar Tariff Rate Quota was set below 1.5 million short tons. U.S.D.A. then proceeded to set the quota above the 1.5 million ton limit (allowing for non-recourse loans only), but proceeded to "hold back" at least 100,000 tons in quota tranches as a "reserve for market conditions". Industrial users watched in disbelief as the Administration violated not only the spirit but the letter of the law, in order to circumvent a process for the benefit of the growers that is common practice for individuals and the business community: when one draws on a credit line, one pays back the loan.

This administrative dilemma was resolved in the fiscal 2001 Agricultural Appropriations Act, which amended the 1996 Farm Bill to eliminate the trigger for non-recourse loans.

However, the combination of a record domestic sugar beet crop in 1999/00, non-recourse loans and the lack of the no net cost provision led to the forfeiture of over 750,000 tons to the CCC, at a substantial cost to the taxpayer. A PIK program was established to trade the stocks back to producers in an exchange for a reduction in new crop acres, and re-marketing of CCC stocks has occurred in a semi-commercial fashion. The conversion of white and raw sugar values caused by the record beet crop also contributed to the bankruptcy declaration of Imperial Sugar.

The sugar program self-destructed under its own weight. Rather than recognize the valid exertion of inevitable market forces on domestic sugar prices, the current legislation regresses to tighter supply management controls to support the price of sugar.

Policy Goals: A User Perspective

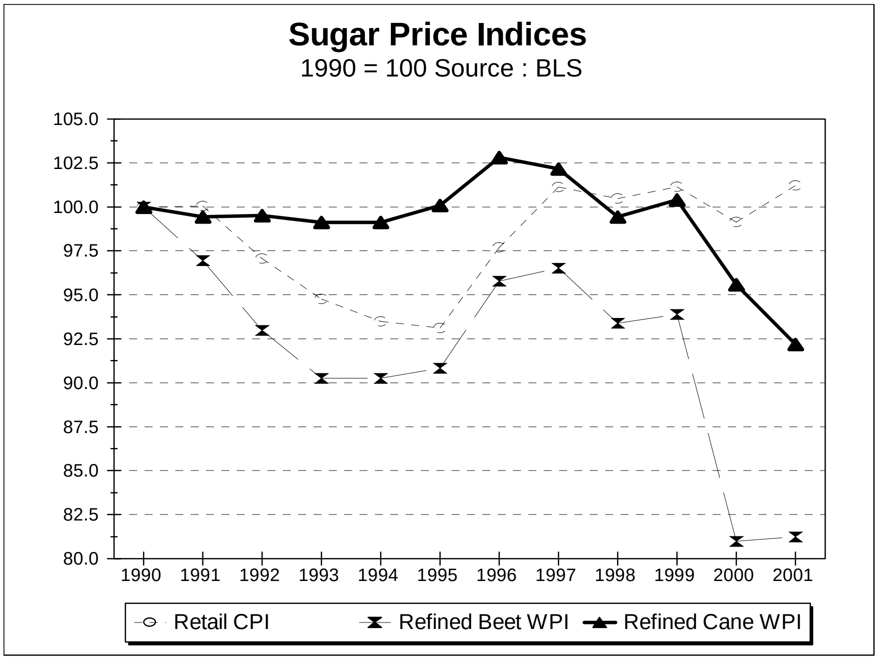
Users seek an adequate and reliable supply of sweeteners at a competitive cost. We are opposed to restrictive trade barriers, domestic supply/marketing controls, and diversion programs. We believe that efficiency and competition rather than government barriers and subsidies should determine the structure of the domestic and global sweetener markets. There is no economic reason why the government should support the price of sugar any differently than it supports any other industry or commodity.

We are not opposed to supporting farm incomes of sugar growers in the United States. That is a transfer payment decision made outside of the marketplace. We are opposed to supporting farm incomes by insuring non-competitive prices through restrictive measures such as import quotas and domestic marketing allotments. Users would prefer consistency with other commodities in which farm incomes are supported by marketing loans or loan deficiency payments.

Proponents of the measures set forth in the 2001 Farm Bill seem to oppose the user position on two major fronts : (1) "Pass Through" – the notion that consumers will not benefit from lower prices paid to growers; any cost saving will not be passed on by industrial users to the final consumer. (2) The access users seek to more competitive prices is based on world sugar values which are viewed as the "world dump market" – those values are low because predominantly subsidized production is sold into the world market as a residual.

Pass Through

The chart on the following page demonstrates some notion of pass through in retail sugar prices from the wholesale level. The relationship breaks down in the latter part of the series, but lags need to be examined further to see if retail sugar prices fell in the second half of 2001. [3]



When one examines the relationship between wholesale sugar prices and price indices for sugar containing products, there appears to be very little relationship. The user community responds to this in 2 ways. First, consumer value may be enhanced in ways other than unit price, including new product introductions, advertising, increased distribution, and increased portion size. Second, the CPI for these items is urban based. Although it is beyond the scope of proof in this paper, we believe pass through in the form of lower unit prices may be occurring in mass merchandising outlets which are not typically located in urban areas. Practical experience suggests that this retail channel is extremely competitive for branded food companies, and mass merchandisers have grown dramatically in importance in the distribution of branded products over the last several years.

The “World Dump Market”

World sugar prices are governed by the cost structures of the efficient producers, not by “dumping” of residual sugar.

In the September 2001 “Sugar and Sweetener Situation & Outlook”, Stephen L. Haley or ERS/USDA summarizes a study by LMC International on the range of production costs for categories of sugar. [4] In examining the data for comparison, one notes that U.S. producing regions are below the world averages in all categories – raw cane sugar, the white value equivalent of cane sugar, and refined beet sugar. Efficient producers of domestic beet sugar rival the lowest cost producers in the world.

However, the lowest cost beet producers are over 4 cents per pound more expensive than low cost producers of refined cane sugar. This claim (which I believed to be very obscure at the time) was first imparted to me as a student in a Principles of Economics Class in 1974.

Perhaps the worst irony of the last 15-16 years of the protectionist domestic sugar program has been the destruction of a very efficient cane refining industry in the United States for the benefit of domestic raw sugar growers and the more costly process of producing refined sugar from beets. The program continues to deny access to low cost efficient producers of raw sugar such as Australia and Brazil, both of which align their domestic prices with world values.

Users do not contest the need for sugar reform in the European Union, and its system of subsidized exports from inefficient producers; however, current anti-dumping laws should address the entry of this sugar into the United States.

In comparison to other commodity markets, the world sugar market cannot be characterized as "residual". Roughly 26 % of the world crop (excluding the EU) is imported / exported, compared to corn at 17% [5], wheat at 19% [6], and rice at 6% [7]. The percentage of world crop traded in sugar is exceeded only by tropical commodities, such as cocoa and coffee. Furthermore, the trading volume and open interest in the NYBOT # 11 Raw Sugar contract exceeds most other agricultural commodities, including soybeans and wheat. Regular market participants accept that the key price determinant is the supply and demand situation for Brazilian sugar, a dominant low cost producer, not the "residual dump market".

Impact of the 2001 Sugar Program on Industrial Users

Marketing allotments backed by a PIK program all but assure high prices and stagnation of supply growth. The user community accepts the inevitable trend toward the global marketplace for its products, in spite of the implicit denial by domestic suppliers.

The U.S. Census Bureau estimates that imports of sugar confectionery grew nearly 72% between 1996 and 2000; 40% of all non-chocolate confectionery could be imported in 5 years. The loss of 1,100 manufacturing jobs at the Brach plant in Chicago, 150 to 200 at Bob's Candies in Albany, Georgia, and most recently, at least 600 jobs at the Kraft facility in Holland, Michigan to the province of Quebec are indicative of the industrial user response to programs which support input costs at non-competitive levels. [8] Although supporters of the sugar program allege the job losses are due to wage rates rather than competitive sugar prices, the Kraft case appears to refute this assertion – total labor compensation in Canada has grown 11% faster than in the U.S.A in the last 9 years. [9] Given the choice to expand production, replace assets, or consolidate capacity, a more restrictive sugar policy leads those decisions to foreign venues.

Several years ago, a veteran industry participant once addressed industrial users stating "Users and consumers will never change sugar policy – you cannot win because you do not represent a constituency". Taken literally, perhaps he was accurate in his assessment .Unfortunately, for the entirety of the domestic sugar industry, he was incorrect – users and consumers vote with their dollars in the marketplace, and to the extent that the resources of labor and capital are transferable, industrial users will vote with their feet as well.

Endnotes and References

1. Center for Responsive Politics. “The Politics of Sugar – The 1990 Farm Bill”

2. Watzman, Nancy .Center for Public Integrity. “Interview with Congressman Dan Miller”, *Investigative Reports – The Buying of the Congress – Transcript.* August 5, 1997.

3. Bureau of Labor Statistics. All data restated to 1990 as the base year.

4. Haley, Stephen L. “U.S. and World Sugar and HFCS Production Costs, 1994/95-1998/99,”*Sugar and Sweetener Situation and Outlook Report.* E.R.S. / USDA, SSS-232, September 2001.

5. ERS / USDA. Feed Yearbook. FDS-2001, April 2001.

6. ERS / USDA. Wheat Yearbook. WHS-2001, March 2001.

7. ERS / USDA. *Rice Situation and Outlook*. RCS-2001, November 2001.

8. Young, Jason. “Sweet Relief? ,” *Candy Business.* May / June 2001.

9. Bureau of Labor Statistics. Total Labor Compensation in Manufacturing, 14 Countries. August 2001.

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