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Evaluation of CAP measures applied to the starch, sugar and cotton sectors

EVALUATION OF CAP MEASURES APPLIED TO THE SUGAR SECTOR

Short Summary

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This evaluation was conducted by the European Economic Interest Grouping:

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This evaluation covered the ex-post impacts of the 2006 sugar Common market organisation (CMO) reform. It covered the EU-27 but is focused on Finland, France, Germany, Italy, Poland and the United Kingdom, where case studies were carried out.

The analysis was based on the combination of theoretical analysis, quantitative empirical assessment, and qualitative analysis of information collected in the bibliography and from operators and/or managing authorities interviewed.

The main limitation was that some sensitive data (mostly costs of production and restructuring plans) were not made available.

1 CONTEXT

The EU-27 is the world's leader in beet sugar production, with 17.5 million tonnes produced in 2009/10. It used to be the second world exporter of white sugar and has become, after the reform, a net importer of sugar.

The best-suited areas for beet form a "beet-belt" that stretches from the United Kingdom to the east of Poland. Isoglucose is produced from wheat or maize.

The reform was implemented at a time of an unprecedented high level of world sugar prices.

1.1 DEVELOPMENT OF THE SUGAR POLICY FRAMEWORK

Previous to the reform, the sugar sector was regulated through traditional instruments of the Common agricultural Policy (CAP) such as guaranteed prices to support the market, production quotas to limit overproduction or the refunds to export surplus production to the world market. Operators were ensured a stable market with high prices, eliminating competition from imports.

In 2006, the sugar CMO was reform was driven by three main reasons:

- of a great risk of market imbalance: on the one hand, the import concessions awarded mainly through the Everything But Arms initiative (EBA) were expected to lead to substantial increase in imports and, on the other hand, the EU's commitment at the World Trade Organization (WTO) as interpreted following the outcome of legal actions against the EU sugar regime, required a substantial reduction in subsidized exports.
- greater coherence with the CAP framework set in 2003 was to be ensured.

However, the system of quotas as well as of minimum and reference prices were maintained, the reference price and minimum price to growers were reduced progressively and a temporary (four-year) restructuring scheme was established with the aim of encouraging least efficient producers to voluntarily renounce their quotas (the target was 6 million tonnes). Moreover, a decoupled payment for growers was introduced, which partially compensated for the loss of income.

2 MAIN CONCLUSIONS ON THE IMPACTS OF THE REFORM

2.1 THE SUGAR BEET SECTOR

Quantities, yields, location and structure

As a direct impact of the quota reduction as well as of the new limitation on exports, the average volume of beets produced in the EU-27 in 2008-2010 was 19% lower than that of 2003-2005. The restructuring scheme encouraged low-yield growers to give up sugar beet production. As a consequence, the EU annual improvement in yields accelerated, as did the trend of concentration of production in larger farms. These changes were different among Member States and led to further concentration of production in the beet belt, while significant drop in beet quantities occurred mainly in Italy and Spain.

Beet prices and market orientation

According to the limited data collected on beet price, the progressive cut in the minimum price of quota beets was fully applied.

The analysis of market orientation was based on the FADN data analysis, but results are not statistically representative. Due to the decline in the minimum price, the distortive effect of CAP support has greatly decreased. Several indicators confirmed that agricultural production choices are more linked to beet price level; as a consequence, industrial sugar producers' pricing strategy is more linked to alternative crop prices and beet production costs.

Internal competitiveness of the farming sector

The analysis of key components of competitiveness (sugar beet outputs, yields and production costs) and the characteristics of growers who abandoned their beet production showed that the competitiveness of beet production has improved, mainly because the reform led least efficient growers to give up beet production (however, the data were not statistically representative).

2.2 THE SUGAR PRODUCERS

Quota renunciation

The quota renunciations reached 5.8 million tonnes (quotas were 17 million tonnes before the reform).

All sugar companies but one took part in the restructuring scheme. Quotas were largely reduced in Member States located outside the beet-belt, and production stopped in five Member States (Ireland, Latvia, Slovenia, Bulgaria and continental Portugal). France, Germany, the United Kingdom, the Netherlands, Poland and Belgium, Member States located in the sugar belt, accounted for more than 40 % of the decrease in the EU.

Out-of-quota production

Quantities produced outside quotas decreased on average by 1.8 million tonnes. Exports were significantly reduced and were only partially compensated by an increase in bioethanol demand (0.8 million tonnes increase between 2006/07 and 2009/10).

Structure

41% of the 179 factories operating in 2005/06 closed during the transition period. Yet, the reform mainly accelerated the ongoing restructuring process: it contributed to speeding up the closure of factories with low capacities (in Poland mostly) and medium capacities (up to 12 000 t/day).

Price

The reform contributed to a decrease in in-quota prices through the fall in the reference price. However, since November 2009, the EU price has well remained above the reference price because of very high world prices. The variability of in-quota sugar prices has increased as a result of the decrease in the reference price giving operators more freedom to adjust prices to the market situation.

2.3 THE ISOGLUCOSE SECTOR

The reform gave isoglucose producers the opportunity to increase their quotas without fees, as well as to renounce quotas. In the EU-25, 0.3 million tonnes of quotas were distributed for free while 0.2 million tonnes of quotas were renounced. As a result, the isoglucose quota increased from 0.5 to 0.6 million tonnes. Half of the existing isoglucose production units were dismantled because, (1) quotas were considered by the operators as insufficient to maintain cost-effective production in a context of low sugar prices and (2) the restructuring fund was a source of immediate cash flow. As a result:

- The average quantities processed per site have increased by 44%;
- The share of isoglucose in EU quotas has increased from 2.9% to 4.5%;
- Production is now concentrated in 9 Member States, compared to 15 before.

2.4 REFINERS

Under the previous CMO and the Sugar Protocol with ACP states and India, full-time refiners benefited from guaranteed raw sugar supplies at a guaranteed price. The new framework, resulting from the CMO reform and the progressive replacement of the Sugar Protocol by the Economic Partnership Agreements and Everything But Arms agreements (EPA – EBA), has enhanced competition in the European market between EU beet sugar and imports of raw or refined cane sugar. With decreased EU quota production, imported sugar (raw or white sugar) was expected to gain market shares. A three-year transition period (2006/07 to 2008/09) and transitional aid to full-time refiners were implemented to prepare refiners for the new context.

Structure and geographical distribution

Thanks to the change in the institutional framework, and to prepare for a context in which the EU should increase sugar imports:

- The number of full-time refiners has gone from 7 to 11;
- Full-time refineries capacities have increased by 58%[1];
- Four beet processing plants have started refining raw cane sugar, adding additional new capacities.

[1] Estimation based on the declarations of refineries and on the basis of an utilisation standard of the equipment.

Refining structures appeared in Member States where there was no activity before, e.g. Denmark, Italy and Spain.

Supplies

After the transition period, supplies of raw cane sugar in the EU-15 reached an all-time low of 1.4 million tonnes in 2010. Indeed, the attractiveness of the Community market now depends on the price gap between the EU and other markets. When the price conditions are not in favour of the European market, producers from EPA-EBA countries might find it more advantageous to export to neighbouring markets rather than the EU.
Moreover, European companies have increased imports of white sugar from ACP states (e.g. Mauritius and Swaziland), as a strategic response to the reform.

Contribution of the transitional aid to the restructuring of the full-time refiners

No data were provided by authorities. According to the interviews, the transitional aid contributed both to lessening negative impacts on margins by covering operating costs of the refineries, and to restructuring the plants.

2.5 MARKET BALANCE

Before 2006, the market was highly regulated. In 2005, the upcoming changes were obvious drivers of risk of oversupply, which the new CMO aimed at limiting.

Unexpectedly, because of the high level of world sugar prices, import flows needed to meeting EU demand did not occur in 2009/10 and 2010/11, and a 1-million-tonne deficit cumulated. As a consequence, market price in the EU remained at a much higher level than that of the reference price, and stocks were at their lowest level at the end of 2009/10.

In 2011, temporary measures were taken by the Commission to ease the tight situation in the market, and stocks were partly replenished at the end of 2010/11 (500 000 tonnes of out-of-quota sugar release on the quota market and import duties reduction). So even though the new CMO had been designed to limit the risk of oversupply, it was possible to deal with the deficit situation due to high world prices.

2.6 COMPETITIVENESS OF SUGAR PRODUCERS AND REFINERS

Competitiveness of production activities

Concerning sugar producers, the reform has stimulated improvement in the main factors of achieving competitiveness: increasing the average campaign length, labour productivity, sugar production per hectare and average production per factory. As this improvement has not been equal between Member States, the reform has contributed to increasing the competitiveness gap that existed among Member States before the reform.

Concerning full-time refineries, because of the combined effects of a decrease in supply flows and an increase in production capacity, the utilization rate of capacity has deteriorated to a level where full-time refiners are less competitive.

Comparing sugar producers and full-time refineries, the ratio between the potential industrial margins[2] showed: a) a loss of competitiveness of sugar producers during the first four years of the reform, mainly because of the contribution to the restructuring fund during the first three post-reform campaigns, and b) a loss of competitiveness of the refineries in 2010/11, which is related to price increase for raw sugar imports due to elevated world market prices.

Competitiveness of commercial activities

The competitive system of the sugar industry is oligopolistic. Furthermore, as a direct effect of the reform, there is a wider differentiation of prices and companies increasingly used them to improve competitiveness.

And in some Member States such as Greece and Italy that have stopped a significant proportion of their sugar production, less efficient local industries could have a competitive advantage in their own market, compared to more efficient but more distant competitors thanks to lower transport costs.

Companies' profitability and global competitive position

The level of concentration could be taken as an indicator of the effectiveness of the measures fostering competitiveness which have been implemented by the companies.

At a country-system level, quite a relevant growth in concentration could be measured, in particular in France and Germany.

At the company level, the structure was and has remained in a situation of relative unbalanced oligopoly[3], but the profit margins of the sector's leading companies are likely to have grown slightly after the reform.

2.7 PREVENTING NEGATIVE SOCIAL AND ENVIRONMENTAL IMPACTS

The analysis has been limited by the lack of data: only six detailed restructuring plans were made available. Therefore, these conclusions should be treated with great caution.

Social aspects

The closure of 41% of sugar factories inevitably led to considerable job losses (from 50 000 employees in 2005/06 to 28 000 in 2009/10 according to the data of the European Committee of Sugar Producers). At least half of these jobs would have been lost even without the reform, as restructuring is in an ongoing process in the sector.

Although the Council regulation laying down the sugar restructuring scheme addressed the issue of limiting negative social impacts, very limited requirements, beyond national legal frameworks, were imposed: except in Italy, companies received the restructuring aid subject only to the obligation of presenting a social plan[4] and to complying with their respective national labour market legislations. Yet, according to the interviews, the existence of restructuring aid received by the companies weighed in the negotiations between the company and the employees. But it is

[2] The potential unit margin represents the level that the actual production costs must stay under in order for a factory to make a profit, therefore rendering the company competitive.
For sugar producers, it is calculated as the difference between the average EU price of white sugar net of the temporary restructuring amount and the average EU purchase cost beets. For refiners, it is the result of the difference between the average EU price of white sugar and the CIF implicit price of raw sugar for refining (NC 1701 11 10) imported from ACP states.
[3] Oligopoly in which market power of the biggest three companies is unbalanced.
[4] Granting the restructuring aid to the sugar companies was conditioned by presentation to the authorities of a restructuring plan, including social plan detailing the actions planned in particular with respect to retraining, redeployment and early retirement of the workforce concerned.

difficult to assess to what extent the restructuring aid contributed to compensating the employees affected beyond national labour legislation.

Environmental aspects

The authorities did not consider the closure of sugar factories as a source of significant negative environmental impacts. The Council regulation went beyond existing minimum obligations by requiring a full dismantling of all the production facilities and restoring good environmental conditions in order to benefit from the highest amount of restructuring aid. No additional measure was taken at Member-States level.

2.8 EFFICIENCY AND SIMPLIFICATION OF THE COMMON AGRICULTURAL POLICY

Efficiency

The reform can be considered overall efficient since it was effective with limited costs. Previously, costs were borne mainly by the consumer through the high market prices. Under the new scheme, the cost of the market measures was practically eliminated, and the loss of farmers' income caused by decrease in minimum beet prices was partially compensated by introduction of decoupled support.

Simplifying the Common agricultural Policy

In part, the reform contributed to simplifying the CAP, as it eliminated some market measures.

Nevertheless, to maintain production quotas and a reference price system combined with a greater liberalisation of the sugar trade arrangements is complex and requires additional monitoring and decision-making from the authorities.

2.9 RELEVANCE AND COHERENCE

At the time of the reform, the main issues of the sector were the upcoming risks of unbalanced market and the fact that the CMO did not make the sector very market-oriented. The analysis of each one of the objectives of the reform showed that they were relevant with regard to the needs of the sector.

The coherence of the diversification aid with the rural development policy was good.

The 2006 reform was in line with the principle of the 2003 CAP reform, as it laid down a transition path towards a less distortive CMO and a more market-oriented sector.

Because of the ruling by the WTO Panel and the EBA Initiative, the EU had to reform its sugar regime which entailed significant reduction of its production capacities. At the same time, the restructuring scheme contributed to improving the competitiveness of the sector; this is, in the long run, coherent with the Lisbon Strategy in favour of “growth and jobs”.