EU sugar market update and outlook

8th January 2019

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Portrait of the month

EU28 sugar beet yields are estimated down 15%

As the 2018/19 sugar beet campaign now draws to a close, the final EU28 yield in terms of sucrose per hectare is forecast 15% lower than 2017/18. In 2017/18, the average yield was 12.7 tonnes sucrose produced per hectare whereas after a difficult year including a severe summer drought but a mild November and December, the average yield for 2018/19 is estimated at just 11.0 tonnes/ha.

UK and EU27 publish "no deal" contingency plans – what may they mean for sugar?

Brexit deal or no deal: winners and losers?

Stakeholders	No Deal		Withdrawal Agreement	
	UK	EU27	UK	EU27
Sugar beet growers	😐	☹	😐	☺
Sugar beet processors	☹	☹	☺	☺
Sugar refiners	☺	😐	☹	😐
Sugar traders	☺	☺	😐	😐
ACP/LDC suppliers	☺		☹	
Non-preferential suppliers	😐		😐	
Industrial users	☹	☹	☺	☺
Consumers	☹	😐	☺	😐

With only 80 days to go until Brexit, and no agreement on withdrawal terms yet in sight, the European Commission and the UK Government have simultaneously published "no deal" contingency plans.

What may a "no deal" Brexit look like for sugar stakeholders, sugar traders, sugar refiners, sugar beet processors, sugar beet farmers, and African, Caribbean, Pacific (ACP) and Least Developed Country (LDC) sugar suppliers?

In the event of a no deal Brexit, there could be some very important consequences for sugar stakeholders, some good consequences for some stakeholders, but for others less so, much less so. On page 5, I examine some of these consequences, and I intend to keep readers as fully informed on this issue as possible in during the 80 days until Brexit on 29th March 2019, and hopefully beyond. Moreover, I would greatly welcome your comments and questions.

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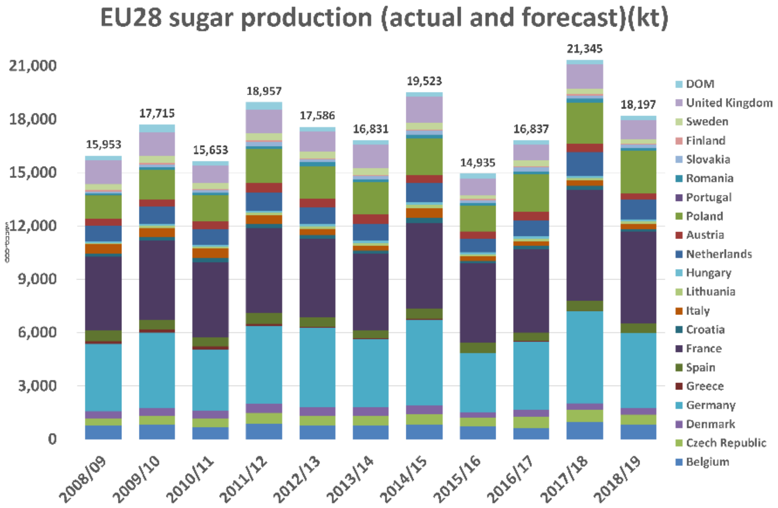
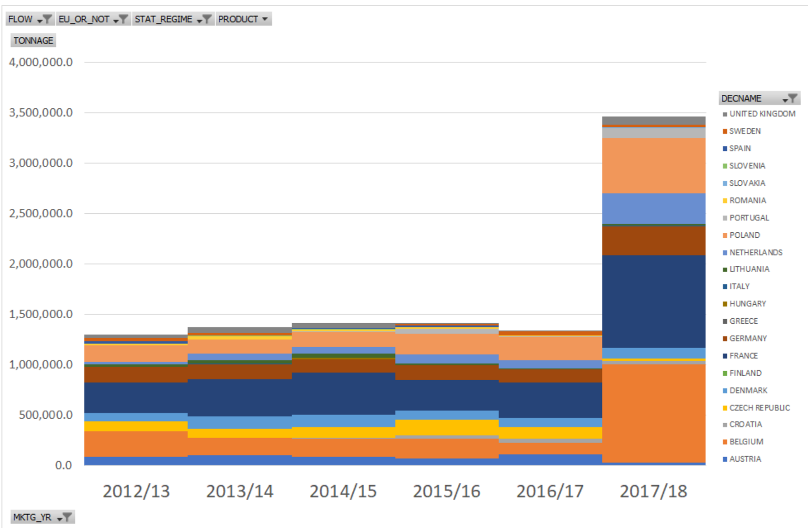
Including sugar produced in the French Overseas Departments (DOM), total EU28 sugar production for 2018/19 is now forecast to be around **18.2 million tonnes** in total after just over 21.3m tonnes in 2017/18. Production is estimated to be very sharply lower in Greece (-77%), Croatia (-39%), Austria (-31%), Romania (-36%) and Finland (-40%), and also significantly lower in Belgium (-170kt), Germany (-950kt), France (-1,100kt), Netherlands (-200kt), Austria (-145kt) and the United Kingdom (-280kt), whilst only three member states are forecast to produce more sugar this year than last: Lithuania (+20kt), Poland (+80kt) and Slovakia (+20kt).



Domestic disappearance is also forecast lower in the EU28 as a whole this year owing to lower human consumption (estimated down 1.7%) and lower production of bioethanol from sugar beet (not including jus vert).

The outlook for 2019/20 remains uncertain owing to continuing very low EU and world market prices, but for some EU member states (BE, CZ, HR, HU, PL, RO and SK), a temporary waiver to the ill-advised ban on using neonicotinoids (a family of insecticides) to make beet seed pellets in the 2019 planting season may provide some reprieve to the gloomy outlook.

EU sugar exports per Oct/Sep marketing year

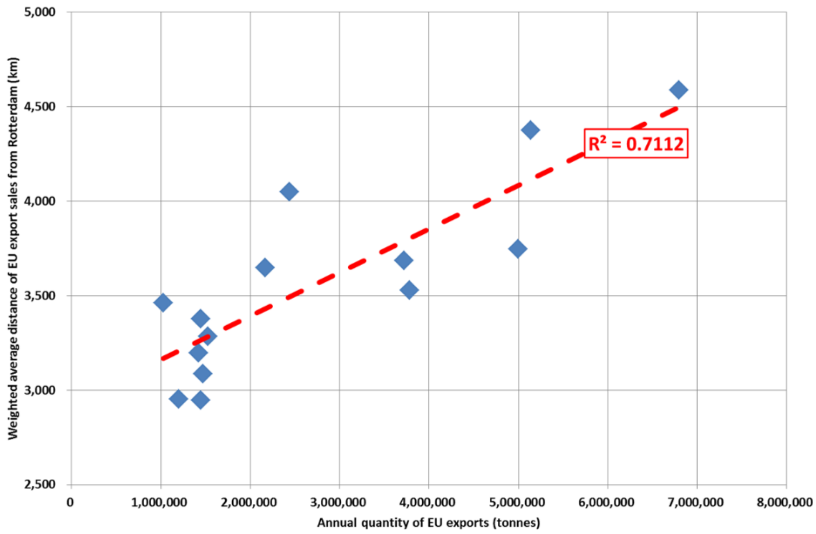


Net EU28 sugar trade surplus expected to reduce by 1.6m tonnes

With EU imports showing some signs of recovery in Q4 2018 but exports sharply lower, the EU's trade balance is expected to move down from a net surplus of around 600,000 tonnes in 2018/19 after 2.15 million tonnes in 2017/18. Key reversals in net trade balance are foreseen in Germany, France, the Netherlands and Austria which may prompt a variety of trade responses, e.g. lower exports to other EU countries, higher imports from third countries and/or an encouragement to plant more beet in the spring of 2019, and most likely a combination of all three.

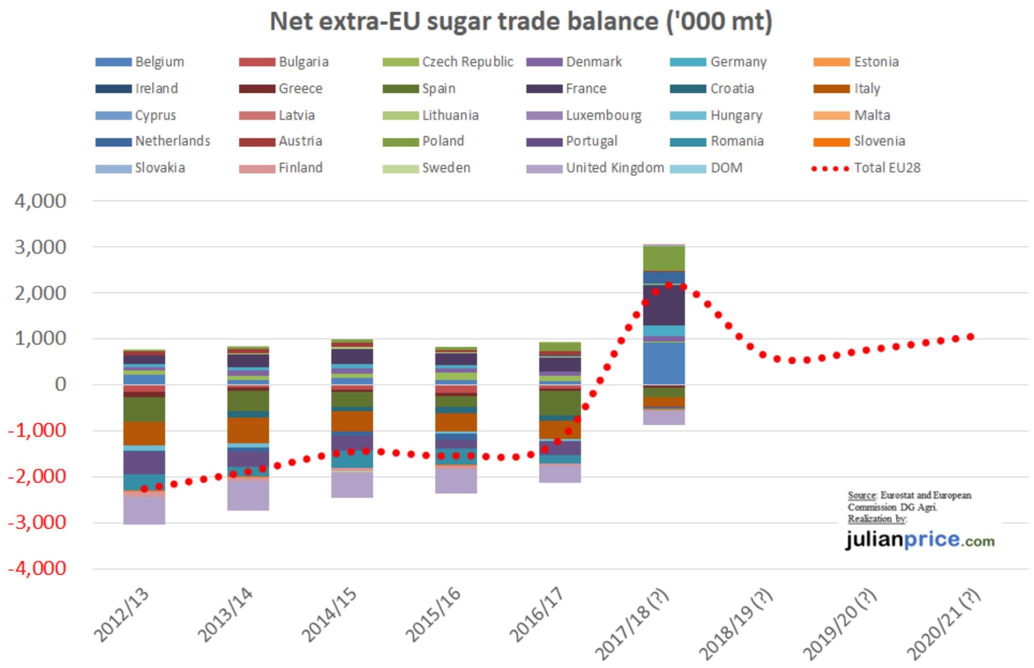
According to preliminary EC TAXUD Surveillance data to mid-December, imports in the 2018/19 reached around 335,000 tonnes, similar to last year, whilst EU28 exports were only 511,000 tonnes, a reduction of 50% compared with the same period in 2017/18. The major destinations for EU exports so far this marketing year were said to be Egypt (20% of the total), Israel (16%), Senegal (7%), Lebanon (4%) and Cameroon (4%), demonstrating the adage that a lower total of EU exports will travel to the nearest markets whilst larger quantities must on average travel further afield.

EU exports: Average distance travelled per annum from Rotterdam



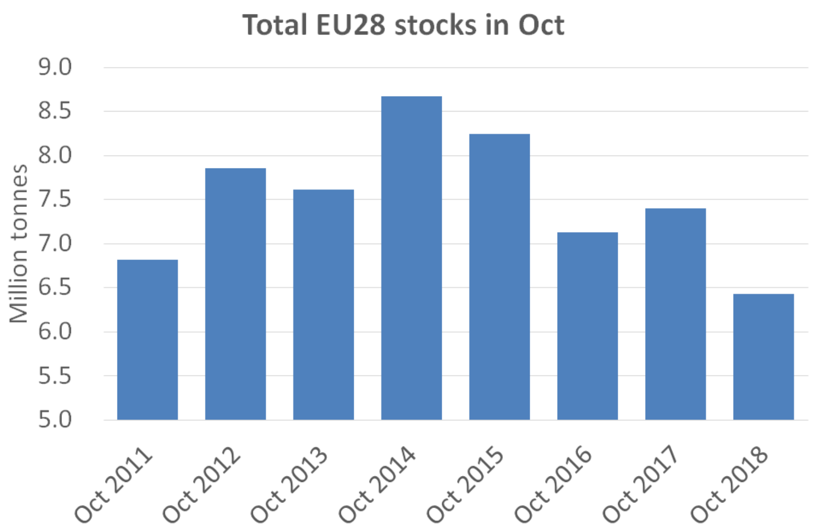
With EU domestic disappearance (consumption) possibly reducing further in the coming years as industrial sugar users reformulate food products to reduce sugar and calorie content in accordance with the recommendations of the health directorate-general of the European Commission (DG SANTE), but tentatively assuming (or hoping) that farm management techniques and the weather will keep aphids and hence virus yellows at bay despite the neonic ban, the EU's trade balance is now forecast to remain positive and perhaps follow a gently upwards path towards a net position of 1m tonnes per annum of sugar (on a *tel quel* basis).

Total EU28 sugar balance ('000 tonnes)	**2012/13**	**2013/14**	**2014/15**	**2015/16**	**2016/17**	**2017/18**	**2018/19**	**2019/20**
	actual	*actual*	*actual*	*actual*	*actual*	*provisional*	*forecast*	*forecast*
Beginning stocks	2,397	3,231	2,573	4,029	1,928	2,174	2,423	1,459
Fresh production	17,586	16,831	19,523	14,935	16,837	21,345	18,197	19,031
Imports from non-EU	3,561	3,256	2,867	2,953	2,517	1,309	1,440	
Exports to non-EU	1,300	1,369	1,415	1,413	1,333	3,460	2,058	
Overall trade balance	**-2,261**	**-1,887**	**-1,453**	**-1,540**	**-1,185**	**2,151**	**618**	**780**
Domestic disappearance	19,013	19,376	19,519	18,577	17,776	18,944	18,543	18,251
Ending stocks	3,231	2,573	4,029	1,928	2,174	2,423	1,459	1,459



EU28 stocks in October 2018 are reported lower even than in October 2011

At the end of October 2018, total EU28 stocks were reported by the European Commission to amount to 6,432,000 million tonnes (of which stocks at the refineries amounted to 283,000 tonnes), lower even than in October 2011 when total stocks amounted to 6,822,000 tonnes (of which 437,000 tonnes were held by the refiners) and EU domestic sugar prices reached above 700 €/t. It remains the case that there is no correlation whatsoever between EU stocks and domestic sugar prices, but with stocks so low, it must surely be a signal for domestic market prices to move higher than the 320 €/t reported for October 2018.



Amid low sugar market prices, the EU may support Australia and Brazil in their WTO challenge to Indian export subsidies at a high level meeting on 29th January 2019

At the EU Agriculture Council meeting in October 2018 and on the basis of a note from the Italian delegation urging the Member States to recognize that deregulation of the of the EU market has led to a "crisis" and calling on the Commission to take the "necessary measures needed for balancing the market in the short and medium term", it was decided by agriculture ministers that a "high level meeting" should be convened in Brussels to discuss the dire sugar market situation. The high level meeting will likely include senior agriculture officials and possibly secretaries of state of the governments of the member states. At the Commission's management committee at the end of December, it was announced that the high level meeting would be held on 29th January 2019. The high level meeting is expected to discuss production costs in the EU in order to better understand supply and profitability, arable crop rotations which could be adversely affected by lower beet areas, voluntary coupled support (VCS) for sugar beet growers in the eleven Member States where VCS is authorized, and contractual relations between beet growers and processors in light of the natural monopsony faced by EU beet growers.

The meeting is also expected discuss India's transport subsidies and the WTO challenge. The Commission is being urged to support Australia and Brazil, and the expectation is that the EC will indeed formally support the WTO challenge.

BREXIT: "no deal" contingency plans – what may they mean for sugar?

What may a "no deal" Brexit look like for sugar stakeholders, sugar traders, sugar refiners, sugar beet processors, sugar beet farmers, and African, Caribbean, Pacific (ACP) and Least Developed Country (LDC) sugar suppliers?

On 19th December 2019, the UK and the EU27 simultaneously published "unilateral contingency plans" for no deal Brexit. They were published perhaps because both sides really do want to avoid no deal and hence that this is a means by which heads may, at long last, be banged together and minds concentrated. The gamble for the EU27 seems to be that London will eventually accept indefinite duration of the "backstop" because the consequences of a no-deal Brexit may be considered intolerable. On the other hand, London seems to be gambling that the EU27 will agree to time-limit the backstop for much the same reason. But if these gambles fail, then these contingency measures may mitigate for each side the most severe consequences for both sides of British withdrawal from the European Union without a Withdrawal Agreement.

EU27-UK trade:
In its communication dated 19th December 2018, the European Commission (EC) has confirmed that all UK trade will be treated as trade with a "third country" and hence that import and export formalities and controls will apply in all bilateral trade in goods and services, and that WTO Most Favoured Nation (MFN) customs duties and other charges will be charged. In the case of sugar, the MFN import duties to be applied on <u>both</u> sides of the UK/EU27 border would be 419 €/t for white sugar and direct consumption raw sugar and 339 €/t basis 96 polarization for raw sugar for refining, although the charge would presumably be the sterling equivalent of these euro amounts.
The EC further confirms that the UK will be disconnected from Customs IT systems, and hence that the UK will not be able to ensure the correct tax collection and to fight against fraud, hence the need for a "hard" border with all that that entails, e.g. customs checks, etc. Nevertheless, the EC will

prepare for UK accession to the Convention on a Common Transit Procedure. The EU will only guarantee basic connectivity of transport links as demanded by international agreements such as the 1968 Vienna Convention on Road Transport, but road hauliers from the UK will temporarily be allowed to carry goods to the EU until 31st December 2019. UK-registered airlines will be allowed to operate point-to-point flights from the UK to EU airports only until 30th March 2020 and they won't be allowed to take passengers between EU airports. UK train-drivers will not be allowed to drive trains in the EU, even Eurostar trains.

On the UK side, the UK has stated it would have the option in WTO rules to apply smaller tariffs below the MFN bound rates. Several scenarios could be envisaged, e.g. maintain the MFN tariffs in €/t, or complete liberalization, or the UK opening Autonomous Tariff Quotas for specific quantities of specific goods likely to be in short supply. The objective would be to minimise disruption, and any measures taken would be temporary, the UK states. It seems unlikely that sugar *per se* would be in immediate short supply after a no deal Brexit, however, equally vital are process chemicals, e.g. CO_2 gas, and packaging materials. Supply chains for sugar from factories to industrial users and supermarkets, and from industrial sugar users to supermarkets, are said to be so highly optimized that stocks of finished goods are only sufficient for a few days, maybe a few weeks at most.

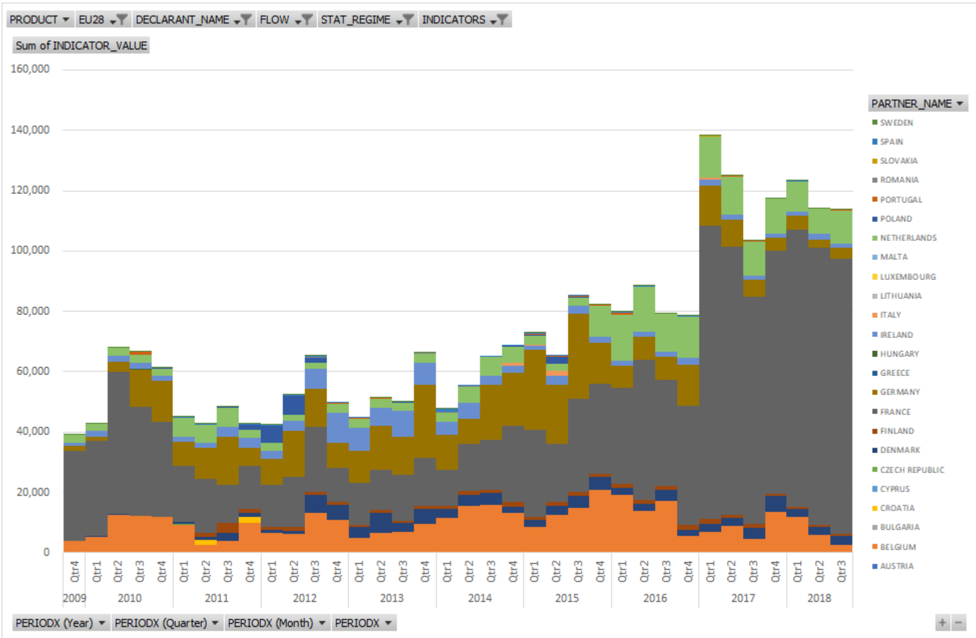
Trade agreements with third countries:
The UK is already a full member of the World Trade Organization (WTO) and negotiations are ongoing to "rectify" the UK's share of the EU's Uruguay Round tariff schedules (see: Sugaronline's EU report of 9th August 2018).

For ACP and LDC sugar suppliers, the UK Taxation (Cross-border Trade) Act 2018 already enables the UK to put in place a UK unilateral trade preference scheme for developing countries. In the first instance, the UK confirms in its contingency plan that it intends, subject to agreement with ACP partners, to provide the same level of preferential access as provided by the current Economic Partnership Agreements and, no matter what, to maintain tariff free access for LDCs. For other trade agreements, UK Ministers and officials are said to be engaging regularly with partner countries, including with South Africa, with the intention that the effects of new bilateral agreements will be identical to, or substantially the same as, the EU agreements they replace, and to bring these into force as from Brexit day (29th March 2019) or as soon as possible thereafter. One of the most difficult issues far from being addressed concerns rules of origin, notably cumulation of origin, e.g. for EU imports, both UK content and content processed in the UK from materials originating third countries, including LDC countries, will be considered as non-originating. Another question arises from a no deal Brexit further to a joint agreement between the UK and the EU27 (See: COM(2018) 312 final) to divide the ACP Sugar Quota between the EU27: 71.2% or 921,707 tonnes, and the UK: 28.8% or 372,993 tonnes w.s.e. It remains unanswered as to whether all seventy ACP countries may be entitled to a share of the UK ACP sugar quota or if not, what would be their individual shares (e.g. their original Agreed Quantities?).

EU27 to UK sugar trade flows:
If the UK and the EU27 fail reach agreement before 29th March 2019, it would seem that the EU27 will lose a market in the UK for around 500,000 tonnes per annum of sugar (a quantity which has been growing strongly since 2009 – *see graph below*), whilst the UK would lose a market in the EU27 for 80,000 tonnes per annum of sugar, of which around 40,000 tonnes per annum is exported to the Republic of Ireland (about 45% of total Irish imports). Meanwhile, in a no deal scenario, the ACP and LDC countries may have the opportunity to supply these "missing" 500,000 tonnes to the UK in place of the EU27, no doubt much of it as raw sugar for refining. However, as discussed above, the terms of ACP and LDC access for sugar post-Brexit remain very much for further discussion and agreement. Meanwhile, sugar trade contracts must presumably be "caveated" accordingly.

Quarterly imports from the EU27 to the UK (tonnes, Q4 2009 to Q3 2018)

(Source: Eurostat)

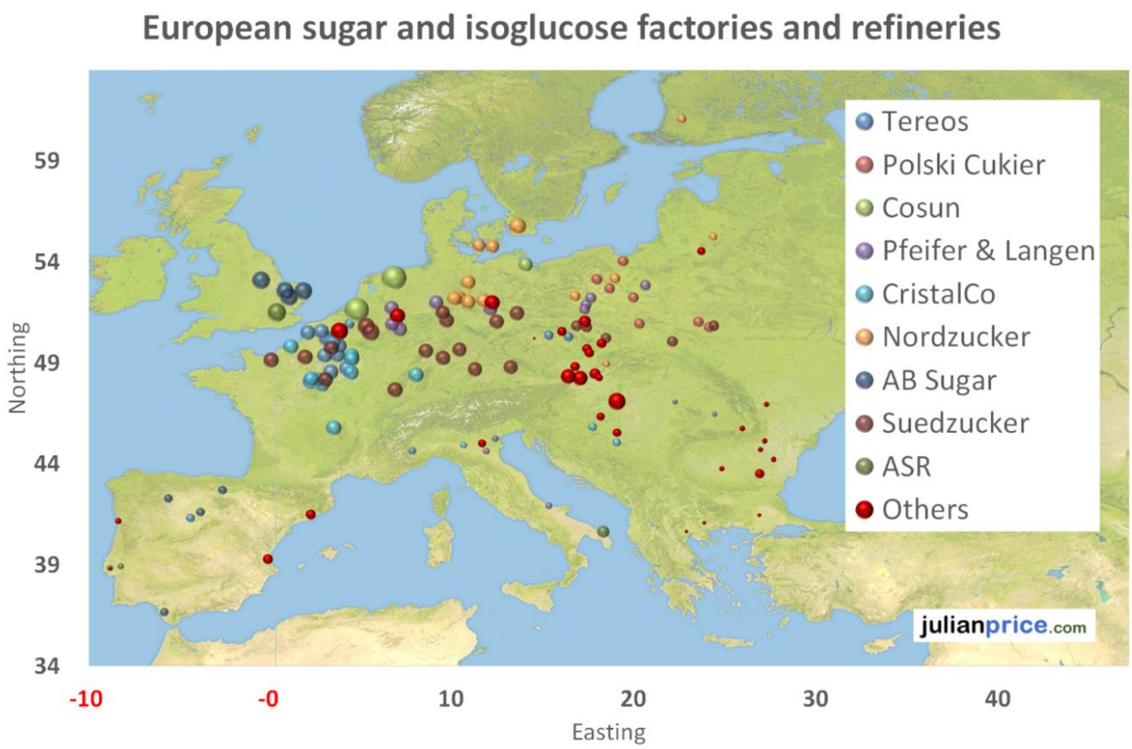


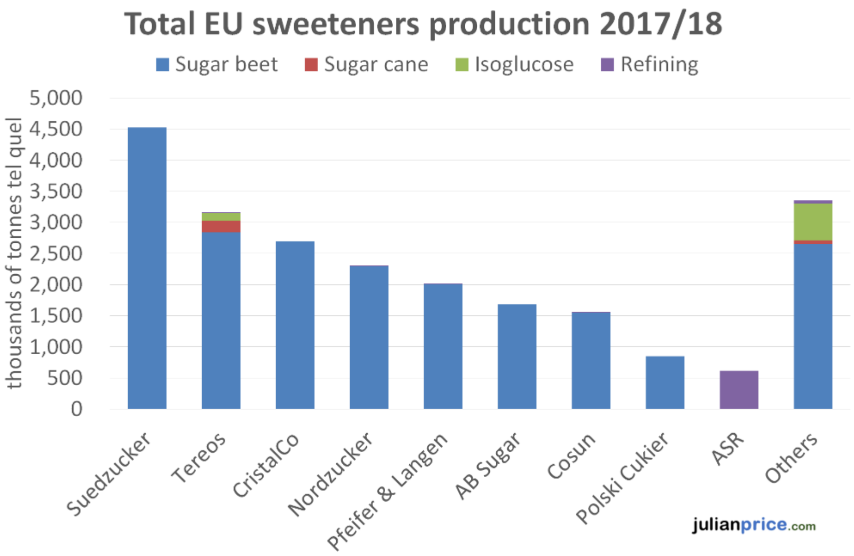
Under the terms of the Withdrawal Agreement, were it to be ratified, the contingency plans published on 19th December 2018 would not be necessary. This is because under the terms of the Protocol on Ireland/Northern Ireland (also known as the "backstop"), the UK would remain part of the Customs Territory of the EU after the end of the transition period ending 31st December 2020 until a "subsequent agreement" takes the place of the backstop. Under a subsequent agreement, e.g. a Free Trade Agreement, provisions for trade in sugar and sugar-containing products between the EU and the EU27 could be negotiated which may be different to the current arrangements under the Customs Union and Single Market.

But until then, under an agreed Brexit, it would probably be largely "sugar business as usual". When would "then" be in this case? It is the indefinite nature of the backstop and the consequent asymmetry in negotiating hands for a future UK/EU27 Free Trade Agreement that is very largely preventing the UK Parliament from ratifying the Withdrawal Agreement including the backstop. The EU have flat out refused to put a definite time-limit on the backstop and it still seems that the UK House of Commons will not agree to an indefinite backstop.

The matter will be put to a vote in the House of Commons by 14th January 2019, but it remains to be seen if this will resolve the impasse one way or another.

The future trading environment for sugar and sugar-containing products between the UK, the EU27, the ACP, the LDC and other the sugar trading partner countries, that is whether we're going to have to live with the contingency plans or we will have the Withdrawal Agreement, transition period, backstop and all, will probably remain unknown until a few days before Brexit on 29th March 2019.





NB: 2017/18 data, i.e. before the announcement of the merger of Hrvatska Industrija Secera.

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