Discussion

TRADE DISPUTES IN AN UNSETTLED INDUSTRY: MEXICAN SUGAR

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Shwedel has provided a comprehensive review of the Mexican sugar industry and the current trade situation between Mexico and the United States. Following are some perspectives of someone who has spend a number of years in the industry in California.

Shwedel made the point that sugar is a commodity for which the rules are unresolved under NAFTA. Back in 1993, I was informed there was a side letter to the NAFTA that set out the rules for trade in sugar. I reported this to the California Beet Growers Association (CBGA) membership in my annual report that year. Later it was learned that the Mexican government and sugar industry had differing opinions. Shwedel reviewed these and the other circumstances which led to the current situation in sugar trade. The bottom line is that the U.S. and Mexican sugar industries are currently awaiting negotiations by their governments on sugar trade rules between the two nations.

There are similarities between the Mexican and U.S. sugar industries. Both have governmental policies to protect their industry, both have highly efficient producers and both have inefficient producers, and they have similar internal sugar prices. The sugar issue is clouded because it concerns not only sucrose produced from beet and cane but also HFCS from corn. In the United States, HFCS entered the market with a vengeance in the mid 1980s. This low-cost sweetener took its market share, and sales of sucrose plummeted. U.S. sugar factories closed, and imports of foreign sugar declined. The U.S. government took no action to limit the sale of HFCS, unlike Europe and other countries that discouraged its production and sale through tariffs, legislation, and regulation. Today in the United States, caloric sweetener consumption is about 65 pounds of sugar and 62 pounds of HFCS.

Since 2000, three U.S. beet processing plants have closed, not because of HFCS but because of a poor sugar economy. Two of these were in the state of California and one in Washington state. There has also been closure of a cane refinery or two in the South, and the Hawaiian industry has declined in production.

Tate & Lyle, a worldwide processor of sugar and sweeteners, has divested themselves of their Domino refineries to Florida cane producers. They are also in negotiations with their beet growers who produce for Tate & Lyle's Western Sugar operations in the Midwest for those growers to purchase the plants and operate them as cooperatives. To date, this effort has not been completed due to financing problems.

The largest processor/marketer of sugar in the United States, Imperial Sugar, has recently emerged from bankruptcy on the backs of their former shareholders who lost all their equity in the bankruptcy. In an action to reduce their debt, Imperial sold their Michigan Sugar operation to beet growers in Michigan who are currently operating it as a co-op. Imperial has sold other assets, and I'm certain they will sell other facilities in time to put their balance sheet in order. The two plants that closed in California also belonged to Imperial, which closed the factories and put the land on the market because the potential sale of the land would give the company a higher return than operating the factories. To date, the property has not been sold, and the company has reduced the price of the real estate. I do not foresee that sugar processing will start again since growers cannot operate the plants profitably.

Currently, there are 27 beet processing plants operating in the United States. If Western Sugar (Tate & Lyle) is able to finalize their deal with their beet growers, only five factories out of 27 will be operated as proprietary businesses; all the others will be cooperatives. This puts all the risk of growing and processing sugar on the farmers.

On the cane side of the business, because of low margins, producers in Florida are vertically integrating, either by purchasing refineries or installing refineries on their raw cane mills. One producer-miller in Florida

has joined a beet sugar marketing co-op to jointly sell their refined sugar. Millions of dollars are being expended to improve the efficiency of the beet and cane industries in the U.S. through these consolidations.

In Mexico, as Shwedel pointed out, the government has expropriated 27 out of 60 cane mills because they faced large and mostly unpayable debts to the Mexican government. The Mexican government has announced their intention to resell these mills to private industry over a period of some 18 months. Industry sources believe that not all the 27 mills will continue to operate; some smaller units will consolidate with larger plants that have underutilized crushing capacity.

Unlike Mexico, the United States is not self-sufficient in sugar production. This past year, for instance, it is estimated that about 84 percent of consumption came from domestic production, about 12 percent came from foreign countries, and the remaining four to five percent came from stocks and other sources.

Shwedel showed that Mexico is self-sufficient in sucrose and has roughly 600,000 metric tons to export. Sugar exported to the world (dumping) market will be sold at below cost of production for most mills in Mexico. Sugar that is exported to the United States is sold at a premium of nearly three times the world price. The Mexican industry and government must be careful not to take action to disrupt this price or they also will suffer from lower pricing.

This export figure is compounded when HFCS is added to Mexican production. To combat the inroads of HFCS and to protect domestic producers and the Mexican treasury from exposure to low sugar prices for their expropriated plants, the government has recently placed a 20 percent tax on sodas sweetened with HFCS. This has further complicated the negotiations over the sweetener trade between the two countries. However, in the last few days, this tax has been suspended for an indeterminate time, in an attempt to speed up the sugar negotiations between the countries.

Because of the potential oversupply of sucrose, there must be rationalization for both the Mexican and U.S. sugar industries. In the United

States, rationalization has occurred and is occurring by eliminating those plants or firms that cannot compete. The U.S. government has not acted to help individual plants or firms. The Mexican government should provide rationalization of their expropriated mills or incentives for ethanol production. If those mills cannot compete in the current trade arena, they certainly will not be able to compete as trade is liberalized between the countries. Having said that, the social and political implications of downsizing the Mexican industry must be recognized. There are also implications to the development of an ethanol industry in Mexico since that country's petroleum industry is controlled by the government monopoly, PEMEX.

From a strictly California perspective, California producers look forward to the time their industry could supply sugar to the border towns of Mexicali, Tijuana, and Tecate. There are several million customers in those towns. The California plants are closer than the Mexican-produced sugar. Sugar prices in the border towns are close to U.S. prices, and economists report the industry is price competitive.

Shwedel raised the issue of the Free Trade of the Americas (FTAA) initiative. Other than NAFTA, international sugar agreements should supercede regional trade agreements. Sugar is a commodity produced by over 50 major supplying countries and another 50 less important producers. The WTO should continue to reform sugar trade. Sugar economists tell us that the sugar industry in the United States is price competitive. If this is true, then in a level playing field it can compete. However, there are many factors that do not allow the world sugar playing field to be completely level. Shwedel raised the question about post-Castro sugar trade with Cuba. It seems that any Cuban imports to the United States would fall under the WTO tariff rate quota.

I don't envy the negotiators as they try to forge sugar trade rules between the United States and Mexico. It is a very complicated and difficult problem, and it's going to take some time to resolve the differences. There must be patience and creativity from both the U.S. and Mexican industries as this process moves forward.