Sugar Preferences – More Harm than Good?[1]

Donald Mitchell[2]
World Bank

December 5, 2005

What to do about preferential market access – or rather, the erosion of such access by multilateral liberalization - is a key issue confronting negotiators in the Doha Round of multilateral trade talks. Many poor countries are fearful that progress in the talks will mean a loss of their preferential access into rich country markets. Sugar preferences are especially sensitive. Countries who receive preferential sugar market access have resisted any attempts to reduce them, arguing that they are of vital importance to their economies. Preferences allow countries with quotas to export to the European Union and United States at prices which are two to three times the world market price. The quantities allowed under these preferential quotas are small (about 1. 6 million tons to the E.U. and 1.1 million tons to the U.S.) and account for only 6 percent of world sugar exports. But, while these preferences may be small as a share of global trade, they are very important to certain countries.

Preferences have also eroded over time, especially to the United States, where preferential import quotas have declined by almost 60 percent since they were introduced in 1982. The European Union has maintained the same level of sugar imports from ACP countries that was agreed in the Lomé Convention in 1975, and allowed 200,000-350,000 tons of additional imports under the Special Preference program since 1995. The EU has recently proposed sharp cuts in sugar prices for both domestic producers and ACP exporters. The ACP countries have expressed extreme dissatisfaction with the proposed EU sugar reform, arguing that the price cuts are too fast, too deep, and too soon. ACP countries are determined to resist changes to their preferences. But is this really in their interests?

Sugar preferences encourage countries with quotas to produce sugar rather than diversify into other agricultural activities which may have higher value and provide more jobs in the long-run—such as fruits and vegetables. A cycle of dependency often builds, as preferences reduce incentives for countries to invest in research on other crops and livestock, causing them to become less competitive in other agricultural activities and thus even more dependent on sugar. High preferences may even harm the very industry they are thought to protect because they reduce the market pressure to adopt improved technology, while countries without preferences must become more productive and reduce costs in order to survive. This can ultimately lead to lower productivity and reduced competitiveness: sugar cane yields in ACP sugar producers with EU quotas fell more than 30 percent relative to other Developing country sugar producers and more than 20 percent relative to other Least Developed sugar producers from 1975-79 to 2000-04 (chart), and the share of world exports by ACP countries fell by half during this period.

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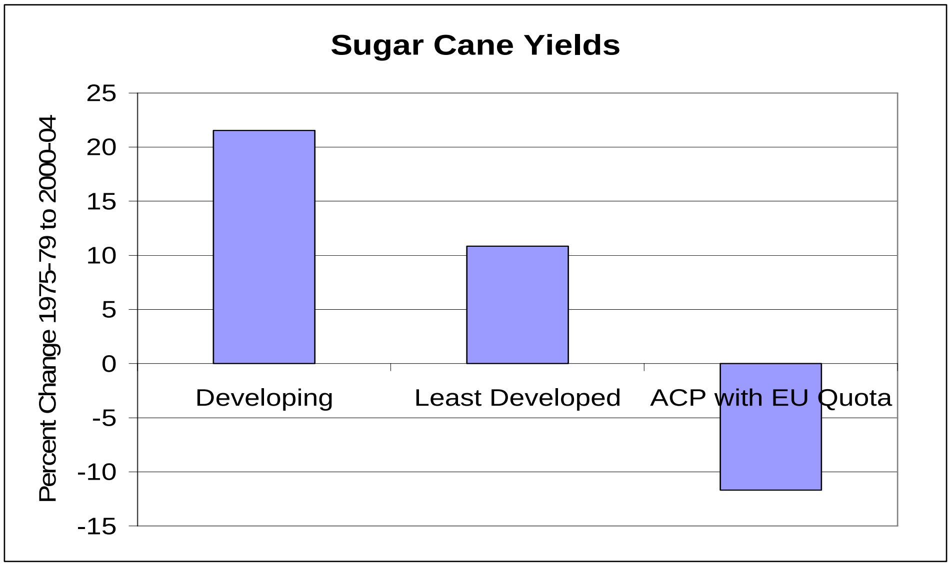
[1] Published in iDM The International Development Magazine, December 2005.
[2] Lead economist in the World Bank's Development Prospects Group.

Moreover, many ACP countries no longer produce enough sugar to meet their own demand and now rely on imports from the world market while exporting their own production to the EU or U.S. Thus, sugar preferences have not led to strong vibrant sugar sectors despite the high prices. Instead they have encouraged stagnation, lack of diversification, and probably contributed to the loss of market share.

Yields of ACP sugar producers with EU Quotas have declined relative to countries without Quotas



Source: FAOSTAT.
Note: Developing countries and Least Developed countries exclude ACP countries with ACP quotas.

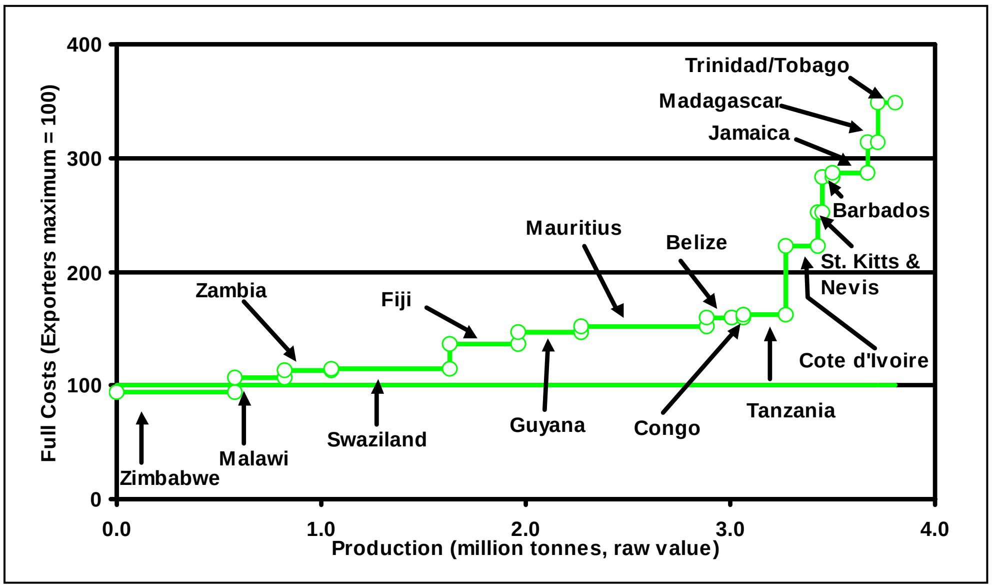
Even the benefits of preferential exports may be overstated because production costs in many countries with preferential market access have increased to the point where exports are no longer very profitable. According to an LMC International study, about half of ACP producers have production costs at least 50 percent higher than the world's leading free market exporters (chart). Mauritius, the largest preference holder to the E.U., is in this category. Jamaica, which also has large preference quotas to the E.U. market, has production costs which are nearly equal to the prices received from exports to the E.U. and above the prices received for exports to the U.S. St. Kitts & Nevis, another Caribbean sugar producer with preferences has recently announced plans to close their industry because they cannot export profitably.

What's more, consumers in countries with sugar preferences are often harmed by government policies that protect domestic sugar producers from lower cost imports. Retail sugar prices in Jamaica, for example, are about double the prices which consumers would pay if not for high protection to domestic producers. Ironically, Jamaican consumers pay higher retail sugar prices than consumers in the EU, to which most of

Jamaica's sugar is exported, according to the London-based International Sugar Organization.

If sugar preferences cause more harm than good, how should countries with preferences approach the Doha Round negotiations? Rather than resisting change and using scarce negotiating coin to fight for something of declining value, a better approach could be to negotiate for assistance from the international community to restructure agricultural sectors and jump-start agricultural research systems. Investments of this kind could help to release preference-receiving countries from their sugar dependency and make them competitive in other, higher-value and more rapidly growing export commodities. Aid for trade is also available to help countries undertake trade-policy reforms that will help them take advantage of new market opportunities.

ACP Sugar Production Costs Are High Relative to Other Exporters



Source: LMC International & Oxford Policy Management, 2004. Note: Data is the average raw sugar production costs for 2000-2002 f.o.b. basis.