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Lessons from the Sugar Protocol Adjustment Measures programme in the Caribbean

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Author: Edited from a study undertaken by Paul Goodison the European Centre for Development Policy Management (ECDPM)

Contact Details: Onze Lieve Vrouweplein 21 – NL-6211 HE

Maastricht / tel: +31 (0) 43 350 29 02 / Email: qd@ecdpm.org

Lessons from the Sugar Protocol Adjustment Measures programme in the Caribbean [1]

Executive Summary:

Assisting firms and producers to adapt to new trade arrangements is one of the many facets of the Aid for Trade (AfT) agenda. This case story relates one such example: the Sugar Protocol Accompanying Measures (SPAM); a European Union (EU) initiative designed to help African, Caribbean and Pacific (ACP) sugar producers adjust to changes in the European sugar import regime. The case story reflects on the initiative as it is currently unfolding in the Caribbean. It highlights the need for such adjustment programmes to be based on an analysis of future and present market trends, and on the leading role the private sector should play in order to take full advantage of AfT initiatives especially when they try to promote value addition and diversification.

The lessons arising from the SPAM programmes are threefold. First, there is a clear need **for a coherent and integrated approach** to meeting the agriculture and food sector adjustment challenges faced. The internal EU experience (i.e the EU Rural Development Programme of the CAP) and other successful programmes in the region (e.g. the EU Caribbean rum programme) strongly emphasise the **need for the whole process to be market-led**, based on a clear understanding of where food and agricultural markets are going and the future role of domestic production within an increasingly liberalised global trading environment.

A second cluster of lessons relates to the **role of the private sector**. SPAM programmes in the Caribbean seem almost exclusively public sector-focused, with little direct engagement from the private sector in the design and implementation of production and trade adjustment measures. This represents a serious constraint on effectively getting to grips with necessary production and trade adjustments. This would appear to require a re-definition of the role of the state away from **directing developments** towards **facilitating** necessary production and trade adjustments in the agricultural and food sector, either within or outside of the sugar sector.

A further tentative cluster of lessons relates to the need for clearer rules on **what can and cannot be supported** in pursuit of the attainment of underlying objectives and **who can and cannot receive support** from the public purse for the implementation of activities designed to achieve these underlying policy objectives. A guidance which serves both to focus the minds of those involved in programme design on the kind of **market-led adjustments** required and to open up the possibility for **directly financing** private sector based production and trade adjustment measures, consistent with broader public policy objectives.

[1] Edited from a study by Paul Goodison entitled "Comparing adjustment support in the agricultural trade and production in the French Overseas Territories and the sugar protocol accompanying measure programme in beneficiary countries."

1- The Sugar Protocol Accompanying Measures in context of EU-ACP relations

The ACP group's access to the EU sugar market traditionally took place under the Sugar Protocol, which formally came to an end on 1 October 2009. Not only did it provide duty-free access to the EU market, it also guaranteed a fixed price as well as country-specific export quotas. These arrangements also gave traditional EU raw sugar cane refiners preferential access to licences to import ACP sugar. This meant that while there were no formal barriers to ACP exporters delivering a range of sugar products, in reality the role of traditional EU refiners in the import process meant that non-raw sugar exports were the exception. Thus, while this situation did guarantee a level of stability to ACP sugar exporters, it also de facto restricted their ability to diversify and move towards higher value added sugars.

The abolition of the Sugar Protocol should be seen in the context of the EU sugar sector reforms, which were intended to close the gap between EU and world market prices. The aim was to establish a reference price acting as a 'safety net', without having it determine market prices on a day-to-day basis. The European Commission (EC) saw the Sugar Protocol arrangement as being incompatible with this new reformed sugar regime: since the price guarantees had been removed for EU farmers they could scarcely be maintained for ACP exporters.

The most significant aspects of the abolition of the Sugar Protocol for ACP sugar producers can be summarized along three points. The first and most important is the phasing out of the guaranteed price that EU importers were obliged to pay to ACP sugar exporters, replaced by an obligation on importers to pay not less than 90% of the reference price up to October 2012. The second is the abolishment of the supply obligations and national sugar export quotas and replacing them with full duty-free, quota-free access opportunities. Finally, while it is clear that ACP sugar suppliers are facing increasingly complex competitive pressures, this reform certainly increases the scope for exporters to find new routes to evolving EU markets that are less dependent on the import preference of traditional refiners, thereby increasing the prospects for the export of more value-added sugars. The ACP sugar sector is therefore facing challenges and opportunities with the new EU sugar regime, challenges and opportunities that should clearly be reflected in the way the adjustment support to the sector is articulated.

It is in this context that the European Commission (EC) declared in 2005 that it recognised "the likely needs of Sugar Protocol countries to adapt to the new market conditions to be created by the reform of the EU sugar regime", and that it was "committed to accompanying this adaptation process[2]". The Sugar Protocol Accompanying Measures (SPAM) was then conceived as a fund to help the ACP sugar sector adjust to new market access realities. The SPAM programme can therefore be understood as an AfT initiative that falls within the WTO's Task Force on Aid for Trade category of "trade related adjustment, including*:* supporting developing countries to put in place accompanying measures that assist them to benefit from liberalized trade"[3]. This case story reflects on how these trade adjustment funds are being operationalised in the Caribbean region, with a particular focus on the role that the private sector should play in leading the process, and on the centrality of a market-led approach. By doing so it tries to shed light on concerns surrounding the "lack of private-sector involvement" already present in the WTO's Task Force on Aid for Trade recommendations, and to come up with a set of lessons useful for the design of other AfT programmes.[4]

2- Objective pursued

The SPAM programmes can be seen as a tool to "facilitate, implement and adjust to trade reform and liberalisation", with the particularity of assisting the ACP sugar sector with reform in a third market, namely the European Union.[5] It therefore clearly falls in the WTO Task force on Aid for Trade's categorisation of an aid for trade programme. Its stated goals are:

1) to enhance the competitiveness of the sugar and sugar cane sector;
2) to promote the economic diversification of sugar dependent areas, for example by redirecting current sugar production towards the production of bio-ethanol and other non-food applications of sugar;

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[2] Commission Staff Working Paper SEC(2005) 61.
[3] Document WT/AFT/1
[4] Ibid
[5] Ibid

3) to address broader impacts generated by the adaptation process.

Crucially, the EU regulation covering the SPAM states that the multi-annual adaptation strategy also need to take into account "*present and future market conditions*[6]". This last point is critical in order to ensure that the overarching goals of adjustment, competitiveness, diversification and mitigation of adverse social effects can be achieved.

3- Design and Implementation

Under the SPAM emphasis is placed on establishing a clear adaptation strategy, which is then operationalised through the establishment of a multi-annual indicative programme at the national level and the deployment of funding within the framework of annual action plans. Overall sector budget support is the preferred method of disbursement. The option of pursuing restructuring and/or diversification within agriculture and/or outside of agriculture is opened to beneficiaries of the SPAM programme.

4- Problems Encountered

The need for further strategic market analysis

When comparing the EU financed SPAM programmes in the Caribbean with similar programmes in the region such as the EU's own rural development policy in the French overseas territories of Martinique, Guadeloupe and French Guyana and the EU Caribbean rum programme, it is interesting to note that a sound strategic marketing analysis is one of the key elements in determining the overall direction of the adjustment. These programmes have at heart a basic vision of where the agro-food sector is going. Without it, it is unlikely that adjustment to the new trade regime for EU sugar imports will be successful.

As pointed out above, the DFQF access now granted to ACP sugar producers presents them with an opportunity to climb the value added ladder, notably by moving to increasingly differentiated, quality products. With the abolition of the import licensing procedures that kept it at the bottom of the value chain, the ACP sugar sector has an opportunity to diversify and move away from strictly raw sugar production. The growing taste of European consumers for higher quality food products "luxury purchase" further reinforces the rationale for shifting production away from undifferentiated "bulk" production towards quality products (see box 1). It is this crucial strategic market assessment that should guide the way SPAM funds are operationalised.

There should accordingly be a distinct bias in SPAM funded programmes towards investments which follow market trends and evolving consumption patterns, with the aim of shifting patterns of production towards serving growing "luxury purchase" markets both within Europe and globally. The opposite side of this coin is the discouragement of investment in renewal of patterns of production which serve traditionally protected markets, where competition will intensify in the era of agricultural trade liberalisation.

The *need for a more active involvement of the private sector*

The strong tendency towards delivering SPAM programme support in the Caribbean in the form of sector budget support or general budget support potentially gives Caribbean governments considerable discretion over how to deploy the financial assistance provided. Providing financial assistance in this form also potentially provides for the swift deployment of such funding, once specific policy conditionalities have been defined and met.

[6] Regulation (EC) No. 266/2006 article 4.2.

Box 1: Underlying Market Trends in the EU: The Defining Context for Restructuring

According to the United States Department of Agriculture (USDA), there are now two distinct components to the EU market – "**necessity purchases**" and "**luxury purchases**". "Necessity purchases" are those products where purchase decisions are made exclusively on the basis of price considerations. For "luxury purchases", in contrast, purchase decisions are not primarily based on price, but on some perceived "quality" attributes of the product. It might be organic or artisanal produced, or it might be a "fair trade" product or respect animal welfare standards, or have some particular geographical designation of origin to which a particular value is attributed. Whatever the non-price reasons which drive the purchase decisions, this type of EU consumer is willing to pay more, often substantially more, for the "luxury purchase" product compared to the "necessity purchase" product.

While there have always been differences in prices paid based on quality considerations, with the process of CAP reform bringing down the price of basic commodities, this price differential has increased significantly. According to the EC commissioned ***Scenar 2020*** study, which looked at the future of agriculture in rural areas of the EU up to 2020, the underlying demographic trend in the EU will see no expansion of overall demand for food and agricultural products in the coming period. However, as EU citizens become more affluent, patterns of food consumption will change, with consumers increasingly favouring high quality products and convenience foods. As a consequence, in the face of a progressive liberalisation of imports of agricultural products (increasingly feasible in the context of the shift away from price support to income support), it is expected that prices of undifferentiated agricultural commodities ('necessity purchases') will fall in the coming years in the EU[7]. In contrast the demand for "luxury purchase" products will show a marked increase due to "*a shift to quality ("luxury") and convenient products (e.g. ready meals)*" in European consumption patterns. Against this background, there will be "*an increase in value rather than an increase in the volume of food consumed*[8]". This represents the longer term trend on EU markets. A trend which is fully taken into account in the design of EU production and trade adjustment support instruments established under its expanding rural development programmes.

However, this public sector-focused aid deployment approach also needs to ensure that production and trade adjustments are market-led. Under the SPAM programme there is a strong emphasis on working through the public sector, both in terms of diversification measures and sugar and agricultural sector focused activities. While this may be a logical choice when dealing with state-run sugar industries (as in Guyana and Jamaica), or when focusing on support to wider economic diversification (St Kitts and Nevis and in large part Trinidad and Tobago), it would appear key to also take into account the important lessons both from previous sector-based restructuring support programmes in the Caribbean (in the banana and rum sectors) and the EU's own internal experience of food and agricultural sector restructuring in preparation for trade liberalisation.

The most important lesson in this regard is that production and trade adjustments need to be market-led and in large part private sector-based[9], if they are to effectively respond to the challenges faced in an era of accelerating agricultural and food product trade liberalisation (see box 2).

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[7] This is despite the recent increases in EU food prices. What is noticeable about these EU food price increases is that they are far less pronounced than the global increases in food prices, given the higher starting point for EU food prices. Price declines in the EU will thus be relative to the traditionally high prices which African exporters have enjoyed under long standing preferential trading arrangements.

[8] See the full text of the study at: http://ec.europa.eu/agriculture/agrista/2006/scenar2020/final_report/scenar2020final.pdf

[9] With the notable exception of Guyana, where a commercially orientated state run company is seeking to address these challenges in a coherent and integrated fashion.

This would appear to be an area where a change of approach to the SPAM programme could be considered, especially in those countries where Caribbean governments are seeking to maintain production within the sugar value chain and/or support diversification within the agricultural sector. Under these programmes there appears to be a need to explore how to devolve more responsibility for the design and management of production and trade adjustment initiatives down to the private sector (including all forms of private enterprise at the primary production and secondary processing levels), within a clear policy framework for deploying "pump priming" public funding to stimulate dynamic market-led, private sector based adjustments. Again the example of the EU Caribbean rum programme is illuminating in this regard.

5 – Factors for success/failure

A certain number of factors can be identified for the lack of strategic vision and the little amount of engagement with the private sector in SPAM financed programmes in the Caribbean. It is far from clear whether this situation is a product of:

1- the capacity constraints of private sector bodies in the Caribbean and the consequent limits on their ability to lead the production and trade adjustment process;
2- the administrative constraints faced by the EC in managing the deployment of assistance to private sector bodies which leads them to favour easily managed instruments such as general budget support and sector budget support;
3- the regulatory constraints on the deployment of EU public funding in support of private sector based production and trade adjustment initiatives, which states that a "grant may not have the purpose or effect of producing a profit for the beneficiary";
4- a Caribbean state-led approach to economic development, instead of a state facilitated philosophy of continuous economic adjustment to a dynamically changing production and trade environment;
5- a combination of a number or all of the above.

Box 2: The Case of Belize and Luxury Purchase Sugars

Under the Belize National Adaptation Strategy four priorities were identified: Support to a Sugarcane Production Improvement and Rehabilitation Programme; support for improvement of the "Sugar Belt" Road Network; support for an Enterprise Development Programme; support for a Policy Development Capacity Building and Training Programme. The first long-term priority area was seen as being "***strategic support to the farmers and institutions of the sugar industry that will improve competitiveness and contribute to a stable and sound physical environment in sugar-dependent areas***". This was entirely consistent with on-going industry efforts to develop supplies to a "luxury purchase" component of the EU market, namely the market for "fair trade" sugar.

In February 2008 a major breakthrough was achieved in this programme with Tate & Lyle announcing its decision to convert its granulated white cane sugar brand to "fair trade" sugar by the end of 2009. A further 22 products will subsequently be converted to "fair trade", until 100% of Tate & Lyle's retail cane sugar range is "fair trade". Belize is to be the main source of supply for Tate & Lyle, which plans to buy between 50,000 and 100,000 tonnes of sugar from Belize in the first year, paying a premium of $ 60 per tonne. While this will bring additional benefits to 6,000 smallholder farmers, in the short term there are substantial costs associated with this strategy related to compliance and certification to "fair trade" standards, ensuring full traceability of "fair trade" sugar and investing in milling capacity to ensure quality and expand supply to meet demand.

However, under the 2007 annual action plan fully 70.9% of the €9 million allocation was devoted to a road sector programme and the bulk of remaining funds being devoted to government orientated capacity building measures. Only a mere €50,000 was allocated to a study to looking at the institutional strengthening of sugar cane farmers organisations. No funds were earmarked to assist producers in investing in adjusting production to effectively serve the new "luxury purchase" market opportunities which had been created by the Belize Sugar Associations partnership initiative with Tate and Lyle. Yet here again this is the kind of production and trade adjustments routinely support with direct financing under the EU's Axis 1 rural development interventions.

Whatever the cause, if food and agricultural sector production and trade adjustments are to be successfully supporting in the Caribbean, it is apparent that this reluctance to engage with the challenge of deploying public funding in support of market-led, private sector-based trade and production adjustment initiatives will need to be overcome.

Against this background, what tentative lessons can be drawn from the SPAM programme beneficiaries in the Caribbean, and what do these lessons imply for the design of AfT programmes at large?

6 - Lessons Learned

The first tentative cluster of lessons relates to the need for a **coherent** and **integrated approach** to meeting the agriculture and food sector adjustment challenges faced. The internal EU experience strongly emphasises the need for the whole process to be market-led, based on a clear understanding of where food and agricultural markets are going and the future role of domestic production within an increasingly liberalised global trading environment. The approach to supporting market-led production and trade adjustments then needs to combine instruments which address **human resource constraints**, **physical infrastructure constraints** and **marketing constraints** on pro-active responses, with interventions combining both **private sector-led** and **public sector-led** initiatives, depending on what is most effective in delivering the necessary production and trade adjustments.

Under the SPAM programme the drawing up of the national adaptation strategy was intended to provide the framework for a coherent and integrated approach. However, the market-led dimension of such strategies is not always clear. This means that on occasion, there appears to be an absence of a clear vision of the end objectives to be attained through the national adaptation strategy. Even where there is a clear market-led orientation to the national adaptation strategy, this is not always reflected in the multi-annual indicative programme established.

A second cluster of lessons relates to the role of the private sector. SPAM programmes in the Caribbean are almost exclusively public sector-focused, with little direct engagement with private sector led production and trade adjustment initiatives. While the state focused approach is understandable in sugar industries which are state controlled, in other countries it represents a serious constraint on effectively getting to grips with necessary production and trade adjustments. Certainly there would appear to be a need to move beyond the public sector in engaging with production and trade adjustments in SPAM programme beneficiary countries. Outside of those countries where sugar sectors are entirely state controlled, this would appear to require a re-definition of the role of the state away from **directing developments** towards **facilitating** necessary production and trade adjustments in the agricultural and food sector, either within or outside of the sugar sector.

In the context of the SPAM programmes in the Caribbean countries, this suggests a need to provide considerable support to **strengthening agricultural producer organisations** where there is held to be a long-term future for sugar production or other forms of agricultural production. In countries where there is deemed to be no such future, then there would appear to be a need for establishing structures to encourage locally relevant restructuring, diversification and social adjustment initiatives.

A further tentative cluster of lessons relates to the need for clearer rules on **what can and cannot be supported** in pursuit of the attainment of underlying objectives and **who can and cannot receive support** from the public purse for the implementation of activities designed to achieve these underlying policy objectives. A guidance which serves both to focus the minds of those involved in programme design on the kind of **market-led adjustments** required and to open up the possibility for **directly financing** private sector based production and trade adjustment measures, consistent with broader public policy objectives.

7- Conclusion

This case story sought to assess the various ongoing trade adjustment support programmes taking place in the Caribbean sugar sector under the SPAM. It identified the need for strategic analysis of the evolution of the agro-food sector in Europe, and the need for more direct involvement of the private sector. Both of these issues are critical to ensure the efficiency of the adjustment support process.

The lessons of this case story are, at first glance, widely valid for other AfT programmes. AfT cannot operate in isolation from market realities. Programmes should follow market trends and favour production and re-conversion in promising sectors, such as the luxury food purchase sector in Europe. This in turn requires working in close cooperation with the concerned producers in the design of programmes, strengthening producer organisations when necessary. Working with the private sector also entails that AfT initiatives should equipped with the right tools do to so, notably by a clearer definition of what kind of modalities are acceptable to directly finance private sector based production and trade adjustment measures.