Getting rid of sugar subsidies: A look to the future after decades of failure

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Executive Summary

Federal government sugar support or subsidies have been part of our national policy since the First Congress of the United States in 1789 legislated a foreign sugar tariff to help fund the fledgling government.[1]

Sugar subsidies, supports or tariffs have existed virtually non-stop throughout our nation's history since this initial act of Congress. From the last half of the 20th Century to today, conservatives have called for an outright end of these subsidies using standard free market language, and we have failed spectacularly.

This failure can be traced to two distinct factors: the heavy agriculture state influence within the Republican Conference in either the Senate or House, and ignoring the impact of a free trade policy on domestic sugar producers.

In the face of this decades long failed strategy, Representative Ted Yoho (R-FL) has introduced a third way to end sugar subsidies that solves both the political and practical problems that have defeated free market efforts. The Yoho plan would be for the United States to end subsidies, but only contingent upon other nations following suit.

Is there a worldwide free sugar market?

Sugar is one of the most subsidized agricultural products in the world. Major producers Brazil, India, Thailand, Mexico and the United States all encourage domestic production of the commodity through a variety of government initiatives. Below is a look at how India, Brazil, Thailand and Mexico play the sugar subsidy game, and the impact it has on the world markets.

India

India is the second largest sugar producer in the world behind only Brazil. In spite of a five year glut on the worldwide sugar market, India's government increased supports for sugar exports with a goal of increasing them from 1.3 million tons in 2013 to an average of 2 million tons in 2014 and 15.

Bloomberg reports that the 2014 exports are projected to have reached the goal, with a 700,000 ton expansion in the just completed October 1-September 30 year. The expansion in exports and overall production in the face of low worldwide prices which in a free market would cause farmers to choose another more lucrative crop has been fueled by expanded Indian government subsidies. These subsidies

[1] The History of U.S. Sugar Protection, Jose Alvarez and Leo C. Polopolus, University of Florida Press, First published November 1990; revised June 2002 and May 2012, page 1 at http://edis.ifas.ufl.edu/pdffiles/SC/SC01900.pdf .

provide mills zero interest loans to pay farmers, and direct cash subsidies to sugar growers to reach the stated export goals. [2]

In March, 2014, the World Trade Organization questioned the government of India's pre-election sugar support program with Australia leading the inquiry. The Times of India reports that Australian representatives pointed out that with India being the third largest sugar exporter, the subsidies "threaten to seriously distort trade."[3]

Brazil

Brazil, the largest sugar producer and exporter in the world, confronted India on its new sugar subsidy program in the October 2013 WTO meeting asking how the country, "…could justify the subsidies since there has been no consensus to extend these special provisions for developing countries," according to FNBNews.com[4].

A World Trade Organization official quoted in the same publication spoke for many countries when he or she said, "In addition to the possibility that India might be violating a commitment, some of these countries said they were concerned that the subsidies would distort world markets by depressing prices, hurting producers in their countries."

India's price support fueled sugar market share grab was a direct threat to the powerful Brazilian sugar producers, who have been promised tax subsidies for exports by the incumbent Administration in Brasilia as they battle for sugar farmers votes with an opponent who is also competing for the industry's votes. [5]

This political gamesmanship of using promises of economic policies designed to make Brazilian sugar more abundant and less expensive on the world market while keeping farmers happy at home has the effect of lowering the international price of the commodity. Brazilian sugar policy matters, because the South American giant dominates the world market with 25 percent of global production and 50 percent of all exports in the world.[6]

Brazil's dominance and influence is so great that Jonathan Kingsman, founder of the eponymous consultancy states in the Financial Times that, "This harvest, the Brazilians will continue to sell at any price and set the world price in the process."[7]

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[2] "Sugar Output in India Seen Jumping as Subsidy Boosts Exports", Pratik Parija and Prabhudatta Mishra, Bloomberg, Mar 27, 2014 at http://www.bloomberg.com/news/2014-03-27/sugar-production-in-india-seen-jumping-as-subsidy-boosts-exports.html

[3] "Export subsidy for sugar questioned at WTO meet", The Times of India, Mar 25, 2014 at http://timesofindia.indiatimes.com/business/india-business/Export-subsidy-for-sugar-questioned-at-WTO-meet/articleshow/32635940.cms .

[4] "Indian sugar exports rise, but WTO members demand removal of subsidies," Libin Chacko Kurian, FNBNews.com, March 31, 2014 at http://www.fnbnews.com/article/detnews.asp?articleid=35244&sectionid=1 .

[5] "Brazil readies fresh aid for sugar and ethanol producers", Wall Street Journal, Paulo Trevisani and Jeffrey T. Lewis, Sept. 10, 2014 at http://online.wsj.com/articles/brazil-readies-fresh-aid-for-sugar-and-ethanol-producers-1410369414 .

[6] http://sugarcane.org/sugarcane-products/sugar

[7] "Brazil's Woes Weigh on Sugar Market," Emiko Terazono, Financial Times, May 26, 2014 at http://www.ft.com/intl/cms/s/0/fa1840bc-e1bf-11e3-b7c4-00144feabdc0.html .

Yet, Brazil's position is weakened by a combination of aging sugar mill infrastructure and a drought that has crimped production making them vulnerable to India's attack on world market share.

Beyond the WTO complaining, Brazil has already responded aggressively through approximately $2 billion worth of loans for growers, mills and ethanol storage facilities. On top of that Brazil currently provides $2.5 billion in sugar subsidies, as well as another billion dollars in various special bailouts and direct subsidies to keep the politically powerful industry well oiled[8].

Thailand

Thailand is the second largest exporter of sugar in the world, and their new military government has plans to immediately and dramatically expand production by opening up new state-owned land for sugar production and encouraging some rice producers to change crops. Given the small size of farms[9] and inefficiencies that define the Thai industry, such expansion is likely being fueled by government programs, which in the past have included preferential loans, production quotas, government-set domestic prices and import tariffs. The Rakyat Post reports that the government hopes that these actions would increase refined sugar production by 800,000 to one million tons above the estimated ten million tons of sugar projected to be produced in the 2014/15 year.[10]

While the new government is pushing more farmers into sugar production, the experience of the previous, displaced Thai leaders in attempting to manipulate both rubber and rice production has made them wary of the distortions caused by rapidly increasing rates of subsidization and state-run purchasing programs. Bloomberg quotes Thai Agriculture Minister and Cooperatives Petipong Puengbun Na Ayudhya as worrying, "We don't want to use taxpayers' money to disrupt the free, commercial system." He continued by noting, "It's easy to buy stockpiles but difficult to sell them at the right time and the right place. In the long run, this isn't going to work."[11]

Mexico

Twenty percent of the Mexican sugar industry is owned by the Mexican government creating the ultimate government subsidy – immunity from needing to produce a profit. To assist the rest of their domestic sugar industry, the government provides subsidies for them to export sugar and government loans with debt forgiveness features built into them.

And in August of 2014, the Mexicans have been found by the U.S. Department of Commerce to have engaged in unfair trade practices as their subsidized sugar exports to the U.S. collapsed the sugar market putting U.S. growers at risk.

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[8] "Brazil Escalates Sugar Arms Race with India," American Sugar Alliance, April 10, 2014 at http://www.sugaralliance.org/brazil-escalates-subsidy-arms-race-with-india-4824/ .

[9] http://www.fao.org/fileadmin/templates/est/meetings/sugar_fiji_2012/Rangsit_Hiangrat_-_Thailand.pdf

[10] "Thailand Aims to be Sugar Giant", The Rakyat Post, August 29,2014 at http://www.therakyatpost.com/business/2014/08/29/thailand-aims-sugar-giant/ .

[11] "Thailand Halts Buying Crops as Junta Seeks Sales," Supunnabul Suwannakij, Bloomberg, October 2, 2014 http://www.bloomberg.com/news/2014-10-02/thailand-shifts-away-from-buying-crops-as-junta-tackles-gluts.html .

Various penalties and actions are scheduled to be finalized by the Department in early 2015 designed to offset the export subsidy advantage created by Mexican government actions.[12]

U.S. politics works against the current anti-sugar subsidy strategy

Free market supporters depend upon a coalition of fiscal, faith voters and national defense hawks to achieve legislative majorities and accomplish reforms that cut the size and scope of government. A simple look at the 2012 presidential electoral map reveals that many of the states that support limited government candidates and elect conservative Members to Congress also are rural with a heavy presence of agriculture.

The pernicious effect of the farm support programs begun under FDR, is that many of the free market members of Congress from these states face extreme political cross-pressures when it comes to agricultural subsidies as a whole. This sense that if one agricultural subsidy is eliminated, the rest are in jeopardy creates an extremely high political wall for free market supporters to scale. In fact, combined with the reality that there is not a free sugar market, it is the reason that frontal assaults on sugar subsidies in Congress have failed time and again.

What can be done?

Ultimately the current free market argument against sugar subsidies devolves down to an argument that a Member of Congress should not care if every domestic sugar producer is driven out of business costing hundreds of thousands of jobs. This has proven time and again to be a losing argument as it reinforces the fears of every farm state conservative that their constituent interests could be in the cross hairs next.

If however, the sugar markets could be made substantially more free at the international level, then free marketers have a chance to make a legitimate case that the U.S. government should eliminate subsidies and let domestic sugar producers succeed or fail based upon their own initiative, hard work and business acumen.

So, how can conservative free market supporters change the international subsidy equation? The answer is found in a relatively simple proposal by Representative Ted Yoho (R-FL).

Yoho's proposal known as zero for zero is bold in that it takes the first step by eliminating U.S. sugar subsidies. However, the subsidy elimination is triggered by the agreement of other major sugar producers around the world to do the same.

With pressure already mounting on the World Trade Organization to take action due to India's massive export subsidy increase, Brazil's increased vulnerability to losing market share, and the new Thai

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[12] "Commerce Says Mexico Is Subsidizing Exports of Sugar into U.S. Market," Rosella Brevetti, BNA, August 28, 2014 at http://www.bna.com/commerce-says-mexico-n17179894232/ .

government’s seeming openness to market-based commodities production, now is the time for free market conservatives to change tactics.

Representative Yoho eliminates sugar subsidies, but he doesn’t unilaterally disarm making our domestic industry vulnerable. Instead, he gives our trade representatives a powerful weapon to change the international sugar wars forever. Under the Yoho approach, our trade representative will be fighting to eliminate sugar subsidies from a position of strength, able to encourage other countries to take the same bold approach.

This refreshing action and argument disrupts the normal trade dispute narratives about how much subsidization is too much, into substantive discussion about the transformation of international sugar markets into a free market model.

After decades of failure, zero for zero is a chance for conservative free market supporters to finally move the ball toward ending sugar subsidies, and then expand this approach to other agricultural commodities.

Conclusion

Ultimately, conservatives face a simple choice. We can continue on the current failed path, spitting out red meat sound bites that get people excited, but ultimately fail, or we can embrace Representative Yoho’s plan that gives a future free market oriented American administration the horsepower to help build an international free sugar market.

The question is whether free marketers want to keep losing, or do they finally want to change tactics and put themselves in a position to win?