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Sugar Update

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Report Highlights:

On March 6, 2013, the Economic Coordination Committee of the Cabinet (ECC) approved an inland freight subsidy and the Federal Board of Revenue (FBR) lowered the federal excise duty on domestic sugar sales to facilitate the export of up to 1.2 million tons of sugar. The decision looks politically motivated and could have repercussions on the future availability of stocks and result in higher domestic prices.

General Information:
GOP to Subsidize Sugar Exports

On March 6, 2013, the Economic Coordination Committee of the Cabinet (ECC) approved an inland freight subsidy of Rs 1.75/kg ($18/ton) for the export of up to 1.2 million tons of sugar. Previously, the ECC announced that the export quota for MY 2012/2013 (Oct.-Sep.) would be 895,000 tons, however, at that time no freight subsidy was considered. Additionally, to provide increased incentive to export, the Federal Board of Revenue lowered the federal excise duty on domestic sugar sales from 8.0 percent to 0.5 percent, contingent on each mill's exports up to its government allocated export quota. This means that for every ton of sugar exported, the mill will receive a reduction in the excise tax on an equivalent volume sold domestically, up to its export quota. Furthermore, millers will receive, retroactively, the reduction in excise taxes paid on exports made to date. These concessions were granted at the request of the Pakistan Sugar Mills Association (PSMA) based upon a plea that large production surpluses, high input costs, and increased international competition caused a significant reduction in sugar mill profits.

Domestic Production and Cash Flow Scenario

According to Pakistani sugar millers, the current domestic price of sugar is approximately Rs 50/kg ($510/ton) FOB Karachi, which is in tandem with international market prices at around $537/ton. Pakistan's production cost of sugar, however, is reported to be approximately Rs 63/kg ($642/ton). The Ministry of Commerce (MOC) concluded that sugar mills are facing "financial duress", resulting in severe cash shortages, which has limited the mills' ability to pay farmers during the current crushing season. Thus, the MOC successfully argued that government intervention was necessary to ease the sugar industry's financial hardship.

Will Pakistan Have to Import in MY 2013/2014?

Pakistan's MY 2012/13 (Oct-Sep) sugar production is estimated at 4.7 million tons in addition to1.3 million tons of beginning stocks, making for a total MY 2012/2013 sugar supply of 6.0 million tons. In MY 2012/13, consumption is estimated at 4.4 million tons, exports are now targeted at 1.2 million tons of sugar, resulting in a precariously low level of ending stocks at 400,000 tons, enough to supply Pakistani consumer demand for only 40 days. This is compared to a total average annual ending stock of approximately 1 million tons over the past five years, sufficient to meet three months worth of consumption needs.

According to commodity traders and market analysts, the ECC decision is misguided as it could seriously erode stocks, depending on the rate of exports, and ultimately lead to higher domestic sugar prices. How much prices will rise will depend upon how much stocks are reduced and how much of the reduced excise tax savings is passed onto the consumer. Furthermore, if the rate of export is not closely monitored, Pakistan could find itself depleting its stocks to where imports are needed to fill gaps in demand – a politically damaging proposition. Since October 2012, Pakistan has exported approximately 500,000 tons of sugar leaving up to another 700,000 tons to be exported under the new policy. According to Pakistani commodity traders, there is enough demand for the additional 700,000 tons given current low international prices. However, an unknown wild card is the amount of sugar in the market from other suppliers such as India. According to trade sources, India is looking to liberalize its sugar industry to reduce its excess supplies. Possible export destinations for Pakistani sugar include the Middle East, Bangladesh and Northern Africa.

Politically Motivated Decision with WTO Implications

The GOP's decision to provide the transport subsidy and reduced excise tax is being heavily criticized as a politically motivated move by the government to garner support from the sugar industry in the upcoming elections. The approximately Rs 2.1 billion ($20 million) in transport subsidy to sugar mills would adversely impact consumers, and add to the government's shaky finances.

If the export target is attained, it would be the first time in Pakistan's history to export over 1 million tons of sugar; its previous record set at 628,000 tons in MY 1997/98. The government's efforts to increase the competitiveness of Pakistani sugar in the international market by means of providing direct payments to millers for export could be a violation of its WTO obligations under the Agreement on Agriculture (AOA).

FAS Islamabad is monitoring the impact of this new sugar policy and will update the PSD table, if necessary, in the Sugar Annual report due in April 2013.