COMMISSION OF THE EUROPEAN COMMUNITIES

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COMMISSION COMMUNICATION TO THE COUNCIL

on participation by the Community in the United Nations Conference for the negotiation of a new International Sugar Agreement

COM(77) 54 final.

Community approach to a new International Sugar Agreement

Object

1. A Community decision is required as to whether and on what basis to take part in the UNCTAD conference to negotiate a new International Sugar Agreement which has been scheduled for 18 April to 27 May 1977.

Background

2. The Community is not a member of the existing Agreement but has participated with observer status in meetings directed towards the preparation of a new agreement.

3. On 18 June 1976 it made a formal statement to the International Sugar Council. In this, the Community declared itself in favour of the principle of participation in a new Agreement, but against the approach to such an agreement contained in the draft then under consideration. It agreed conditionally to take part in further preparatory work, but remained otherwise uncommitted.

4. Since that date the Community has taken an active part in the preparatory work which has preceded the establishment of the draft negotiating text. It has explained in detail, both orally and in writing, its proposals for a system in which market stabilisation would be sought through a maximum and minimum price structure supported by the internationally-coordinated management of national stock levels coupled with appropriate disciplines in extreme price situations. In this approach, which is founded on the GATT MTN negotiating directive, the Community finds itself totally isolated; and it is clear beyond doubt that there is no possibility of the negotiating conference being led to adopt it.

5. The negotiating document which will be before the Conference is a draft prepared by the International Sugar Organisation Secretariat, which is discussed in more detail in paras 15 to 18 below.

6. In these circumstances the Community must now decide whether to take part in the negotiations at all and, if so, by what means to safeguard its interests.

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7. The constraints within which the Community must take its decisions are analysed below.

The Community's internal market organisation

8. The common organisation of the Community's sugar market dates from 1968. In its present form it applies until 1980, when it will be reviewed . It is a complex structure arrived at only with difficulty, and it would be correspondingly difficult for the Community to modify it in any basic respect.

9. Its essential feature is a quota system in two parts : fixed basic quotas (A quotas) and an additional variable element (B quotas). The total of basic quotas was not related to total internal consumption but was fixed with reference to the actual production in a previous reference period. The aim of the additional B quotas was to allow further production to take place in areas best suited to beet growing. The"B" quotas are fixed annually by the Council as a proportion of "A" quotas. The result of the application of this system was and remains a total Community quota-based production which is normally in excess of total internal requirements.

10. In addition, producers have the right to produce sugar (C sugar) in excess of their A and B quotas. All C sugar must be exported by the producers concerned without Community financial assistance, without quantitative restriction and entirely at their own financial risk.

11. The net effect is that export outlets must be sought each year for surplus quota sugar and all C sugar.

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The Community's import obligations

12. The Community's obligations under Protocol 3 of the Lomé Convention, and parallel arrangements with certain other developing countries not party to that Convention, may be summarised as follows.

13. Under these arrangements the countries concerned undertake to supply, and the Community guarantees the purchase and import of sugar totalling some 1.4 million tons (raw equivalent) annually, at guaranteed prices linked to the Community's internal prices. There is no terminal date to the Community's obligation; and the quantity can be reduced only to the extent that the supplying countries concerned fail to meet their supply commitment for reasons other than force majeure. In a situation where the world price is below the guaranteed price the suppliers have every incentive to make sure that this does not happen.

14. These arrangements constitute a very important economic lifeline to the countries concerned at no small cost to the Community.

Draft International Sugar Agreement

15. The draft text prepared by the International Sugar Organisation for the forthcoming negotiations is based directly on the 1968 Agreement.

16. Essentially, it consists of an export quota mechanism to stabilize the price of sugar by regulating the level of supplies coming on to the free market. The system is complicated. A basic export tonnage is negotiated in the agreement for each exporter member as a share of the notional total market. Just before the beginning of each quota year the likely size of effective market demand is estimated, and a corresponding proportionate share of that estimate is allocated to each member as his initial export quota for the year.

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These quotas may be adjusted up or down during the course of the year in function of specified movements of the actual market price towards the maximum and minimum prices fixed in the agreement.

17. Altogether, this is an exceedingly dirigiste system quite incompatible with the existing structure of the Community market.

18. In addition to the quota mechanism , the draft negotiating document contains provisions dealing with purchase commitments, respect of minimum price, and non-purchase from non-members when the market is weak, coupled with minimum stocks and supply obligations related to a maximum price situation. In contrast to the quota mechanism just described, these provisions present no special problems to the Community, since they are broadly in line with the general principles of the Community's own approach.

<u>The attitudes of other countries</u>

- <u>Exporters</u>

19. All the exporters insist on export quotas as the fundamental mechanism for stabilising the free market price of sugar. They seek an agreement which will safeguard their interests when the market is weak; and they see the variable quota mechanism as the only means of guaranteeing them a pre-determined share of the market and of permitting them to programme their production accordingly.

20. None of the exporters will accept a stock mechanism alone - of whatever size or system. They have four main objections : the capital and recurrent costs of carrying the stock; the tendency of a stock to overhang the market and depress the price at all times; the need for a back-up system to protect the price from still further erosion after all stock obligations had been met; the possibility open to wealthy developed countries to meet their stock obligations by a corresponding expansion of production, thus remaining free to export without restraint yet without being in breach of the agreement. Of these objections, the last two are the most entrenched.

21. Within these parameters there are certain variations of approach. A number of countries have indicated a willingness to contemplate a more important role for stocks; in the case of developing countries this has been accompanied by the condition that they should not be required to bear

any corresponding additional financial burden.
A number of developing countries are tending to insist on indexation of the negotiated prices to counter inflation and currency fluctuations during the life of the agreement; and to demand that any growth in the market should be reserved for the growth of their export quotas. Exporters (such as Australia and Brazil) with potential for rapid expansion of production show a greater flexibility of approach to the fixing and adjustment of quotas than countries (like Cuba) which face production difficulties. The same countries have a conflict of interest on whether special arrangement sugar transactions should be excluded from the scope of the new agreement (as they were in the past).

22. Mauritius' original proposal for an international intervention stock backed-up by export quotas coming into force only at the minimum price has been withdrawn in the face of solid opposition from all the other exporters. Mauritius now accepts the basic lines of the draft negotiating text, but has introduced a proposal for the financing of stocks resulting directly from quota reductions : the interest and handling charges on sugar thus stocked would be met from the proceeds of a levy on all imports and exports of free market sugar. This proposal has been met with cautious reserve.

- Importers

23. The importers'group is dominated by Canada and Japan. Both have stated their willingness to accept the exporters' view that the fundamental mechanism of the agreement must be an export quota system. Both have insisted on the need for the quota adjustment mechanism to be much more realistic and flexible than in the past, so as to encourage a shift of trade to efficient producers instead of simply freezing the traditional pattern. Both have rejected the idea of making any financial contribution towards the cost of stocks, and assert the view that their acceptance of price maintenance through export quotas already constitutes a sufficient contribution.
In consequence, the Community's proposals have obtained no support in this quarter, despite the attraction that stocks ought to present to importers as a supply assurance in times of production shortage.

24. The USSR has taken little part in the discussions to date except to make it clear that it is interested only in a quota-based agreement of the 1968 type, with special status for the U.S.S.R. Under the 1968 Agreement

the U.S.S.R.'s substantial imports from Cuba qualified it as an importing member, with a correspondingly substantial vote under the administrative arrangements of the Agreement. The U.S.S.R. concurrently obtained the right to export between 1.1 and 1.25 million tons each year to the free market in addition to any sugar exported by the U.S.S.R. to other Eastern Bloc countries; and at the same time all exports by Cuba to all Eastern Bloc countries were treated as special arrangements, and therefore additional to the Cuban export quota on to the free market.

25. The position of the USA, which is by far the biggest importer of all, remains totally undefined until the Carter administration has time to address itself to the problem of how best to protect American interests.

- Balance of interest between exporters and importers

26. Canada and Japan have said they cannot operate, and therefore cannot accept, obligations to respect the minimum price; in their view it is for the exporters to take care of this. Equally, they will not accept quantitative purchase obligations. They repeat that the quota system itself provides the exporters with all the guarantees they need at the minimum price, and that importer acceptance of this system must be paid for by supply commitments at the maximum price.

27. The exporters have made it equally clear that they will not enter into supply commitments (either of price or quantity) at the maximum price except in return for symmetrical commitments by the importers at the minimum price.

28. It is therefore conceivable that agreement, if reached, would only be on the basis of deleting both purchase and supply commitments.

The Community interest in participation in a new Agreement

- Economic factors

29. The economic factors may be summed up in the following terms.

30. Domestic production meets the whole of the internal demand plus an exportable surplus which, depending on weather conditions, may reach the order of 1.6 million tons. Lomé Convention imports amount to 1.4 million tons. The Community therefore currently needs the assurance of export outlets for some 3 million tons per annum if the accumulation of unwanted stocks is to be avoided.

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31. The Community's exports normally take the form of white sugar, refined from beet and from cane.
The external market for white sugar forms part of the world free market to which the new agreement would apply. It is nevertheless a separate component of the market with its own specific limitations. World demand for white sugar is normally of the order of 3.5 million tons.

32. The size of the total free market to be regulated is of the order of 14 million tons. (1975 ISO figure) This includes USA imports of some 4 million tons, and amounts committed under long-term contracts for destinations other than USA of another 5 million tons, leaving only some 5 million tons as the true free market.

33. On the entry into force of a new agreement with export quota provisions, quotas would apply at once. To obtain a quota corresponding to the Community's export needs, as analysed in paragraph 30 above, this would be subject to immensely difficult negotiation. (It may be noted that in the negotiations leading to the 1968 Agreement the Community of the Six sought an export quota of 1 million tons and was offered a quota of 300 000 tons only). To join an agreement on these terms would give the Community the undisputed right to its negotiated share of the market, but would at the same time mean that under normal beet harvest conditions a very substantial tonnage would become unexportable.

34. If the Community remained outside the agreement it would not be subject to this limitation, but neither would it have the corresponding entitlement. The export possibilities open to the Community under these conditions would depend on the extent to which members observed their own rules about respect of the minimum price and abstention from purchase from non-members, and on the extent of membership. Neither of these factors could be quantified beforehand.

35. Whether the Community would be better off (a) inside the agreement with the right to export a specific limited quantity of sugar, or (b) outside the agreement with the freedom to sell all the sugar for which it could find a market, is a question of judgment. In forming such a judgment account would have to be taken both of the likehood that the Community would come under considerable moral pressure not to undercut the market which developing exporters were trying to stabilise through

mutual self-discipline, and of the difficulties for the Community of modifying the amount of domestic sugar produced under its existing system. Finally, account would have to be taken of the likely cost to Community funds of export restitutions on sugar eligible for Community guarantees (ie. all except the C sugar element). This cost would be variable in function of the difference between the world price and the Community price, and of the quantity exported; while the world market price remains volatile this cost is correspondingly difficult to estimate in advance with any degree of precision.

- Political factors

36. The Community's sugar market organisation represents a complex and difficult internal balance, both political and economic. This balance results in the need to be able to export sugar on to the world market, and it is essential to the Community to safeguard its interests in this respect.

37. In recent years the Community has stated on many occasions and in many fora its commitment to the principle of trade expansion and market stabilisation through international commodity agreements. It cannot back down from this commitment now, and in its negotiating stance it must be seen to be adopting a positive and credible position which takes due account of the consensus of views of its negotiating partners in general, of the developing countries in particular, and of the general context of the UNCTAD integrated programme approach.

38. Unfortunately, with its potentiality as a major net exporter, the Community is seen by the exporting members, particularly the developing exporters, as a direct competitor. Their desire for Community membership of the agreement stems directly from their desire to limit Community competition to a tolerable level, and they are unlikely to accept any solution which does not offer the prospect of this result.

Proposal

39. In the light of this analysis the Community should negotiate on the basis of obtaining a special status in the agreement, adapted to the Community's own market stabilisation mechanisms and leaving the other members of the agreement free to adopt the system they prefer. Since special status is accepted for the USSR there can be no objection of principle to this.

40. The Community's status should be that of exporter, with exclusion of the Community's preferential sugar imports from the net export calculation on which votes in the agreement would be based. This would be a mirror image of the USSR special status as importer with inclusion of her special arrangement imports from Cuba for the purposes of vote entitlement calculations.

41. The Community would accept no export quota obligations. It would, however, be prepared to negotiate a commitment to contribute to the stabilisation of the world sugar market, through mechanisms compatible with its own market organisation, parallel to the commitments accepted by other exporters. The mechanisms envisaged for this purpose would be broadly of the type described (mutatis mutandis) in paragraphs 13 to 15 of the GATT negotiating directive (doc. I/40/1/75 (CoS 4) rev.1 of 24 April 75).

42. As indicated in para 18 above, the other economic elements of the draft negotiating document (on minimum stocks, supply and purchase commitments, respect of minimum price, provisions against purchases from non-members) present no particular problem, in the sense that they are not out of line with the Community's existing GATT negotiating directive.

43. The Community's proposal is one which can be justified as capable of producing the required result without imposing unacceptable modifications on the Community's market organisation. It would represent a considerable step by the Community towards a compromise solution. At this juncture the Community should not be willing to pay too great a price to achieve a settlement which may be beyond reach for other reasons.

<u>Participation in the negotiations</u>

44. It is to be noted that arrangements would need to be made to enable the Community as such to participate in the negotiating conference.

<u>Community negotiating directive</u>

45. The Community's existing negotiating directive is directed specifically to the conduct of the GATT multilateral negotiations. The members of the International Sugar Agreement having decided to negotiate in an UNCTAD context, a formal adaptation of the Community directive is required in this sense. In addition it needs to be adapted in the sense of paras 39 to 42 above. A directive to this effect is annexed to the Recommendation for a Council decision at Annex A.

Recommendation for a Council Decision concerning the negotiation of a new International Sugar Agreement

Council Decision of .....

authorising the Commission to take part in the negotiation of a new International Sugar Agreement

THE COUNCIL OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Economic Community, and in particular Article 113 thereof;

Having regard to the recommendation of the Commission;

Whereas the Community has declared that it supports the principle of setting up a new International Sugar Agreement and of participating in it;

Whereas an International Conference will be held in Geneva from 18 April to 27 May 1977 within the framework of UNCTAD for the negotiation of a new International Sugar Agreement;

Whereas the Community should take part in these negotiations, which involve the common commercial policy;

HAS DECIDED AS FOLLOWS :

Sole Article

The Commission is hereby authorised to participate in the negotiation of a new International Sugar Agreement.

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The Commission shall conduct the negotiations within the framework of the annexed directive and in consultation with the Special Committee provided for in Article 113 of the Treaty.

Done at Brussels,
For the Council

The President

Annex to Council Decision of ...

Negotiating Directive
for
International Sugar Agreement

Introduction

1. Following the relevant Council decision of June 1976, the Community has taken part in the preparatory work towards a new International Sugar Agreement, conducted in the framework of the existing Agreement.

2. The Community's proposals in this context have been directed towards the negotiation of an agreement to coordinate national stockpiling policies on the lines laid down in Section II of the directives for the GATT multilateral trade negotiations (Council document 1/40/1/75 (CoS 4) rev. 1 of 24 April 1975). Those directives exclude the possibility of accepting export quotas.

3. The consensus reached by all the other participants in the preparatory work is that the new Agreement should follow the general lines of the International Sugar Agreement 1968 : that is, it should be based on export quotas, supported by certain other disciplines at the level of predetermined maximum and minimum prices. A conference to negotiate such an agreement has been convened by UNCTAD for the period 18 April to 27 May 1977.

4. In order to enable the Community to participate in these negotiations in a positive spirit but without compromising the essential characteristics of its own internal market organisation, the Council authorises the Commission to negotiate at the UNCTAD Conference on the basis that the Community is prepared to participate in an agreement of the type described in para 3 above provided it is accorded special status. Under the terms of that special status the Community would undertake stocking obligations which would parallel the export quota adjustment obligations undertaken by the other members of the agreement; but it would not itself accept any quota obligations.

5. This directive does not define in advance the precise line of action for the Community to follow in the detailed aspects of the negotiations. For obvious tactical reasons it would be inadvisable for the Community to reveal its proposals in detail until the negotiations have reached the point where these would have the maximum effect. The directive must, however, be sufficiently clear to enable the Community to embark on the negotiations with

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a clear idea of its objectives.

6. This directive will have to be defined more precisely as the negotiations develop.

Directive

A. Aim, scope and relationship with the GATT multilateral negotiations

7. The agreement should constitute a framework for multilateral cooperation to ensure the expansion of trade on a stable world market. The purpose of the agreement would be to

- achieve price stabilisation,
- ensure the continuity of supplies to importers and of outlets for exporters,
- take due account of the interests of developing countries.

8. In order to be completely effective the agreement should involve the major producing and consuming countries. If the agreement is concluded before the conclusion of the GATT multilateral negotiations the net balance of advantages and obligations arising out of it shall be taken into account in the final balance to be struck in connection with the GATT negotiations.

B. Mechanisms

9. Market stabilisation should be sought through the introduction of a minimum and maximum safeguard price provision including obligations linked to extreme price situations.

10. A minimum and a maximum price would be fixed in the Agreement defining a price bracket within which operations would normally take place. These prices, which would be fixed for a given period, would be subject to review in the light of long term market trends.

11. If market prices fell to the fixed minimum of the bracket, the importing countries would be obliged to obtain their supplies from exporting

member countries, which in turn would be obliged to respect this minimum price and refrain from selling on more favourable terms to non-member countries.

12. If market prices reached or exceeded the level of the maximum price of the bracket, exporting countries would undertake to give priority to supplying importing countries which were party to the Agreement with the quantities traditionally imported by them at the maximum price level.

13. The Community would accept no export quota obligations. It would, however, be prepared to negotiate a commitment to contribute to the stabilisation of the world sugar market, through mechanisms compatible with its own market organisation, parallel to the commitments accepted by other exporters. The mechanisms envisaged for this purpose would be broadly of the type described (mutatis mutandis) in paragraphs 13 to 15 of the GATT negotiating directive referred to in paragraph 2 above, and of which the text is reproduced in footnote (1) below for reference.

14. For the purpose of calculating the number of votes to which the Community would be entitled in the college of exporters under the administrative provisions of the Agreement, all its exports would be taken into account, including those exports corresponding to the quantity of imports into the Community under Protocol n° 3 of the Lomé Convention and parallel special arrangements.

15. A specific provision to enable the Community as such to become a party to the agreement would also be required.

C. Functioning of the Agreement

16. The functioning of the mechanisms described above implies that a body responsible for the continuous surveillance of the market situation should be set up under the Agreement to work, where necessary, with international organisations.

(1) Text of paras 13-15 of GATT Directive

"13. In order to achieve greater market stability, national stocks should be set up and managed on the basis of rules laid down in the Agreement. These rules should therefore define the minimum and maximum amounts which the body could stockpile in order to meet the objectives of the Agreement. They should also determine the allocation of these stocks.

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(1) 14. If market prices reached a percentage laid down in the Agreement of the minimum price of the bracket the member countries would undertake with due regard for other market factors to stockpile fixed quantities of [sugar] within the agreed maximum amount in a co-ordinated manner.

15. If market prices reached a percentage laid down in the Agreement of the maximum price of the bracket, the member countries would arrange for appropriate quantities to be taken from their stocks and placed on the market in a co-ordinated manner."

Annex : Financial Implications

1 The present proposal, which relates only to the negotiating stance to be adopted by the Community, has in itself no new financial implications.

2. These would only arise from a future Council decision as to whether or not to participate in a new International Sugar Agreement, after its terms had been negotiated.

3. The financial implications of such a future decision would be related to

(a) a judgment as to whether the overall cost of the Community's sugar policy would be less costly inside or outside the Agreement; and

(b) the obligation to make an annual contribution to the administrative budget of the International Sugar Organization, if the Community decided to join. On the basis of the current scale of contributions, this could reasonably be estimated at not more than £ 44 000 per year.