

SWEETENER USERS ASSOCIATION

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May 4, 2010

The Honorable James Miller
Under Secretary for Farm and Foreign Agricultural Services
U.S. Department of Agriculture
1400 Independence Avenue, S.W.
Washington, D.C. 20250

Dear Mr. Under Secretary:

On behalf of the Sweetener Users Association, I would like to express our appreciation for the Department of Agriculture's announcement of an increase in the raw sugar tariff rate quota (TRQ). Making available an additional 200,000 short tons, raw value (STRV), is a positive first step toward restoring adequate supplies to an extremely tight market.

However, I must also express our members' strong view that the additional TRQ amount announced will be insufficient to supply the market during the balance of this fiscal year. The purpose of this letter is to explain this view, and also to call your attention to certain internal USDA debates about sugar market projections that have, unfortunately, played a part in generating market uncertainty and complicating sugar program decisions.

Sugar Supplies and Stocks in Light of the TRQ Increase

If one simply goes through the mechanical exercise of plugging an additional 200,000 STRV into the April *World Agricultural Supply and Demand Estimates*, assuming that nothing else changes and that the entire 200,000 STRV enters (i.e., there are no shortfalls in filling the quota), the 2009/10 ending stocks-to-use ratio would be just 13.5%, essentially unchanged from 2008/09's very tight stocks, which generated a 35.90 cent per pound average price for wholesale refined beet sugar – the highest fiscal-year average in USDA's records.

That stocks-to-use ratio would be significantly below the range of 14.5%-15.5% historically targeted by USDA policymakers. SUA believes the appropriate target is the upper end of the range, 15.5%. To achieve this stocks level, even assuming that USDA's demand estimates are accurate (a subject discussed more fully below), a further TRQ increase in imports of around 200,000 STRV would be needed. Taking probable shortfalls into account, the TRQ amount would need to be higher than 200,000 STRV.

Because most private-sector analysts dissent from USDA's current estimates of demand, it is instructive to see how some of them assess the need for more imports. Frank Jenkins of Jenkins

Sugar Group wrote on April 23 that “the last two full months of the quota year will be import-starved in the absence of a further increase in the TRQ.” Based on historic patterns of quota entry, Jenkins estimates April-October import needs at 860,000 metric tons, raw value (MTRV), and estimates TRQ availability in the same period at only 524,000 MTRV after Friday’s quota increase. This calculation implies a need for a further TRQ increase of 336,000 MTRV or about 370,000 STRV.

Another analyst, Tom Earley of Promar International, maintains a proprietary supply-demand balance sheet, and on the basis of higher estimates of 2009/10 demand, sees the need for a substantially greater TRQ increase to achieve the ending stocks-to-use range noted above. “My revised numbers would require another 800,000 [short] tons of imports to get to 15.5%,” Earley writes. “There is a wide gulf between the WASDE demand estimates and everyone else.”

Role of Supply-Demand Estimates in Sugar Policy

For most agricultural commodities, USDA’s supply-demand estimates are widely-followed and frequently move markets. These estimates do not, however, normally have a direct impact on farm program decisions. This is because for wheat, corn, cotton and other commodities, both domestic supply management and import quotas have long since been phased out. In prior decades, USDA used its estimates of production and consumption to establish, for example, cotton import quotas or acreage reduction programs for corn and wheat. Present support policies for these commodities, however, no longer rely on the manipulation of supplies by government.

The sugar program is, of course, different. Present policies constrain domestic supply availability through marketing allotments, and offshore supply availability through import quotas. For this reason, accurate, well-understood and robust estimates of supply and demand are of particular importance for all sugar market participants, whether buyers or sellers.

At present, questions and concerns about USDA’s sugar estimates exist among growers, processors, refiners and users. Nor is that all: USDA professionals are themselves divided about how accurate present estimates are, and whether current methodologies for gathering and interpreting data are sufficient for an evolving sugar marketplace.

This uncertainty comes at a cost. The job of policymakers who must make decisions about the TRQ and domestic allotments becomes more complicated, and fraught with uncertainties and risks. Of course, by definition, no system of predicting the future will produce a perfect match with what eventually happens. But there are better and worse ways of making predictions, and when it becomes clear that even the experts are confused about the derivation and meaning of market-moving numbers, it is time for a thorough review.

Yet program decisions cannot wait on such a review. Therefore, in our recommendations below, we stress that in an imperfect world, USDA needs to assume that the signals being sent by current near-record prices are an accurate reflection of the situation in the market – and that therefore the Department takes more risk in withholding supplies from the market than in making them available, and should immediately proceed with a further TRQ increase while it ensures the integrity of its statistics.

Sources of Uncertainty in USDA's Supply-Demand Estimates

USDA wrote in the April 13, 2010, *Sugar and Sweeteners Outlook* that “[m]any observers believe [USDA’s demand estimates] to be unrealistically low.” This statement is accurate. In the WASDE, USDA projects 2009/10 domestic deliveries to be 3% below 2008/09. However, total domestic deliveries through February 2010, as reported in *Sweetener Market Data* (also a USDA publication) are up 5.5% compared to the prior year. Most private-sector balance sheets likewise feature higher total domestic delivery estimates than found in the WASDE.

The *Outlook* purports to explain this discrepancy through a discussion of two factors:

1. Traders supposedly imported some sugar from Mexico which they then sold to U.S. cane refiners for further refining, rather than to an end user as USDA normally assumes. These cane refiners, as required by regulations, reported the subsequent refined sugar sales as a delivery, but the same sugar had previously been (mistakenly) counted as a direct-consumption import, i.e., imported sugar that USDA assumes to be sold directly to an end user and that is counted as a delivery.
2. “Refiners’ losses” is a category that compares (a) the quantity of domestic and imported raw sugar melted with (b) refiners’ reported sales of refined sugar to end users (converted to raw value). In theory, this number should be close to zero over time, but the *Outlook* notes that the number may be a *negative* 200,000 STRV for 2009/10. This alone should be sufficient to cause further inquiry, since it means that refiners “found” 200,000 STRV more than they imported or purchased from cane processors. Promar International, however, has pointed out that previous years’ “refiners’ losses” have been positive numbers, raising (but not answering) the question whether reporting time lags or inconsistencies across fiscal years might be an explanatory factor.

The *Outlook* combines the two factors and arrives at an estimate of deliveries for human consumption that is close to the WASDE number. But the calculation again begs the question why *actual* reported deliveries for the fiscal year to date are up 5.5%.

The marketplace, it need hardly be said, appears to believe the actual reports of deliveries rather than USDA economists’ estimates. Wholesale refined sugar prices remain at levels *higher* than they attained in 2005/06 after two major refineries were closed by Hurricane Katrina. Moreover, retail (grocery store) consumer prices in February set an all-time record. If price is the intersection of supply and demand, the market is telling USDA, with breathtaking clarity, that sugar supplies are tight and demand is relatively strong.

Recommendations

These considerations lead us to respectfully submit the following recommendations for your consideration:

1. Immediately increase raw and refined sugar TRQs by up to 800,000 STRV, in recognition of continuing strong deliveries and the need to increase stocks, not only for the balance of this fiscal year but for next year as well. If USDA is concerned that this amount could be excessive, we recommend reinstating the tranche system that was used in the 1990s to stage the availability of TRQ sugar.
2. Devote significant internal resources to identifying and resolving the major statistical issues and anomalies in the WASDE sugar balance sheet, carrying out any necessary surveys, consulting with industry stakeholders, and providing a transparent, straightforward explanation of USDA's estimates and how they will be used.
3. Broaden USDA's internal process of gathering input for the WASDE numbers, ensuring that all responsible and relevant USDA agencies are represented on the interagency committee that prepares the estimates.
4. Assess whether additional methods of gathering information, including enhanced reporting, are necessary in order to assure the integrity of USDA estimates.

As always, SUA appreciates the opportunity to provide information and suggestions that will, we hope, be helpful to you in the difficult job of administering the sugar program. We will be happy to discuss this letter further with you and your colleagues.

Sincerely,



Perry Cerminara
Chairman