HOUSE OF LORDS

EU Agriculture, Fisheries, Environment and Energy Sub-Committee

EU Sugar Regime

Oral evidence

Contents

British Sugar plc—Oral evidence (QQ 88-117)

Evidence Session No. 4 *Heard in Public.* *Questions 88 - 117*

WEDNESDAY 20 JUNE 2012

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Lord Carter of Coles (Chairman)
Baroness Howarth of Breckland
Lord Lewis of Newnham
Lord Maclennan of Rogart
Baroness Parminter
Lord Renton of Mount Harry
Lord Whitty

Chris Carter, Corporate Affairs Director, British Sugar plc and **Clare Wenner**, Political Adviser, British Sugar plc

Q88 The Chairman: Mr Carter, Clare Wenner, welcome. We are grateful you have come to give us some evidence today. I am afraid I do have to go through the formality yet again. You have before you a list of interests that have been declared by Committee Members. This is a formal evidence-taking session of the Committee. A full shorthand note will be taken. This will go of course on the public record in printed form and on the parliamentary website. We will send you a copy of the transcript, and you will be able to revise it in terms of any minor errors. The session is on the record; it is being webcast live and will subsequently be available on the parliamentary website. I do not know, Mr Carter, whether you would like to say a few words in opening and then perhaps we can go to the questions.

Chris Carter: Thank you very much, Chairman. It is just a very short statement by way of introduction. Clare Wenner and I represent AB Sugar. That is the sugar division of Associated British Foods plc. AB Sugar has sugar operations in the UK, Spain and northern China, which are beet sugar, but it also has cane sugar operations in six countries in Africa—Malawi, Zambia, Tanzania, Swaziland, Mozambique and South Africa—as well as in southern China. It also owns a refinery in Spain. I just wanted to make that clear. ABF has invested £1.6 billion worldwide in AB Sugar since 2005. The UK sugar industry and British Sugar, which is our operation here in the UK, is one of the most efficient in Europe. It makes an economic contribution of around £1 billion a year and supports 13,000 jobs.

The EU sugar sector, as you have already heard, was radically reformed in 2006. I hope we can delve into that in a little more detail later. The policy framework from this reform continues for a nine-year period until 2015. Last October, the European Commission announced proposals, as part of the CAP reform, to abolish the sugar policy framework or CMO—common market organisation—including the quota system, as soon as it expires in 2015. These proposals are now being debated, both by the European Parliament and by the Council of Ministers, under co-legislative procedure for the first time, before arriving at a final decision, expected probably in early 2014.

I have a short statement about our position, which is very similar to that of the NFU and the developing countries. Despite the competitiveness of our UK industry, we do not support abrupt abolition of the policy framework in 2015, as we believe it would be harmful to UK interests. Instead we support continued but more gradual deregulation, involving extension of the EU sugar policy framework and quota system until 2020. In short, we believe we should learn from the last reform in 2006 and proceed with caution.

Q89 The Chairman: Thank you. We do have a consistent theme from our witnesses today; that is for sure. In the evidence you gave us, you noted that British Sugar responded positively to the 2006 sugar reform in a number of ways, which you helped us with, but you also suggest that the reform has been insufficient to provide a stable and supporting regulatory environment, which you need for further investment. Given how much you have already invested, I would be very keen to understand that. Really, can you explain how you came to that conclusion and which aspects, very specifically please, of the 2006 reform have restricted your freedom and confidence?

Chris Carter: I think there has been a slight misunderstanding here. The 2006 reform was indeed very radical. It involved cuts in European production and support prices of 30 per cent to 40 per cent, and an 80 per cent cut in exports. In just three years, the EU went from the world's second-largest exporter to one of its biggest net importers. Despite that, the underlying policy framework, which includes the quota system, was maintained and, crucially, the arrangements were extended for nine years, not the normal five. That was for a very good purpose, and the reason for that was, because of the radical nature of the reforms, there was a four-year transition period, followed by, effectively, the five-year normal operating period, which we are right in the middle of at the moment.

AB Sugar, as I have already mentioned—British Sugar in the UK—responded to this very positively by investing a great deal of money globally. Of the £1.6 billion I have already mentioned, £200 million has been invested in the last five years in the UK sugar industry and a further £140 million invested in Britain in a very large renewable energy plant that is about to open in collaboration with BP and DuPont at Hull. Although it was radical, the outcome of the 2006 reform did provide a sufficiently stable policy environment for us to invest. Our main concern is that, if the policy arrangements are suddenly scrapped abruptly in 2015, then this will discourage the further investment we need in the industry to make it fully internationally competitive by 2020, which is our prime objective.

Q90 The Chairman: Can I ask if you have stopped investing at this point then, because you do not know what is happening after 2015, or are you on a slight wing and a prayer?

Chris Carter: Of course we have not stopped investing. We have a continuous rolling five-year investment programme, and that continues now, as you would expect. If we have a high degree of confidence about what the arrangements are going to be, that encourages investment. If the confidence of what they are going to be deteriorates, that discourages investment. I should also point out that ABF, like any major plc, cannot speculate on what the policy framework is going to be after 2015. It is not possible; corporate governance and common sense do not allow this. We need to know what the arrangements are and have them confirmed before we can make definitive future plans and have those confirmed—as it were, to start the clock ticking.

Q91 The Chairman: What is the lifecycle of an investment? You are investing now for something that is going to pay back over 10 or 15 years. You must be making an assumption in the period after 2015 as to how the market will work.

Chris Carter: Yes, we are making certain assumptions where we can. In other areas, though, if we feel we cannot look far enough ahead or the policy environment is too uncertain, it is causing delays in the investment programme. Of that there is no doubt. The normal timescale for the investments works something like this: as I have already said, the clock starts ticking when we know what the policy environment is and when the policy is confirmed. In the case of the CAP that is unlikely to be before early 2014. The normal process is then that an investment takes two to five years from instigation to coming on stream. That depends on the size of a project and its technical complexity. In the case of normal de-bottlenecking of factories, that would typically be at the shorter end. More complex projects—renewable energy projects and larger ones—would typically be nearer five than two years. On top of that, we would need to get a reasonable return on investment, as any company would. As you say, an absolute minimum of five years would be needed for that, but it is more normally 10.

The Chairman: Perhaps at the end we can come back to your profitability, EBITDA (earnings before interest, taxes, depreciation and amortization) and margins. That would be an interesting question.

Q92 Lord Renton of Mount Harry: Presumably Associated British Foods produce an annual report; you are a publicly quoted company. I personally would find it very interesting to have a copy of your most recent annual report, and other colleagues might feel the same, just to put us in the total picture. That said, Mr Carter, it is possible to say that what you and NFU are really looking for is protection for another few years. The fact is that you have actually had protection from 2006 to 2015—for nine years—so is it not unreasonable to say that it is time to get out in the world and fight?

Chris Carter: That is a very fair challenge. I should point out that, since 2006, the level of protection, as you describe it, has been hugely reduced. The reform in 2006 was enormously radical. It took out nearly 6 million tonnes of European production and closed 60 per cent of its factories in the current decade. You cannot get much more radical than that. It is also worth pointing out that the current sugar CMO or policy framework arrangements are budget neutral. In fact, in EU terms, they make a relatively modest contribution to the budget of €160 million a year minimum, which is unusual. I would not like you to think that we are operating in a highly protected environment at the moment. It is far less protected than it was before 2006.

To come back to the competitiveness point, from our point of view that is absolutely key. The UK industry has to continue the progress that we have made over the last decade or two, which has been very considerable. We are now regarded as a top-notch industry in Europe, probably one of the best, and increasingly competitive with the best global cane industries as well. We know this because we operate in both. In our view, it is not unreasonable to expect a further five years to complete that transition. We are not expecting and not asking for the quota system to be continued forever—just to make that quite clear as well.

Q93 Lord Renton of Mount Harry: No, but you are asking for it to be continued for another five years.

Chris Carter: We are.

Q94 Lord Renton of Mount Harry: I think it is particularly difficult for you really—I was involved in the 2005-06 talks—because you are the sole producer. If you were in competition with other companies within the UK, it would be easier to give support for continuing protection. I do find it difficult when you are there, just you and the NFU, and you have already had protection since 2006. It is not easy to see why the EU sugar industry should go on being protected in this way. Is that fair or do you think that is quite unfair?

Chris Carter: We need to explore, just for a moment, the way the European market works. The European market is not—it probably never was but it certainly is not now—a UK market. The European market for sugar and related products is very much a European one, so our main competitors, for example, in addition to the refiner Tate & Lyle, which is based in the UK, are very large competitive producers in France, the Netherlands, Germany and Belgium, and we have to compete in a perfectly normal way with them, subject to the English Channel. It is wrong to assume or think that the UK market is dominated by British Sugar or indeed by Tate & Lyle, as we have completely open competition from the continent.

Q95 Lord Whitty: I apologise that I will have to go, but could I just ask the question that I asked the NFU? From your point of view of the market, are you seeing either any significant growth in the bioethanol output from sugar—you have referred to the production facilities—on the one hand and, on the other hand, are you seeing any serious diminution from the health concerns about the traditional confectionery market for sugar and related matters? Just give a context as to what market prospective we are working against.

Chris Carter: It is an excellent question. In the future, sugar should be less viewed as just a product or commodity for the food market and more a source of generalised energy, one route of which is to the food market. In the UK, as you know, we opened the UK's first bioethanol plant at Wissington in 2007. That is from sugar beet. It is relatively small, but it is extremely efficient with very good greenhouse gas saving. I think this is a diversification that we are going to see far more of in the future. Quite a number of our European competitors have done exactly the same.

Beyond that, it is not just bioethanol either; if anybody would like to come to our flagship plant at Wissington, which is one of the innovative leaders across Europe, you will see that we have invested in all kinds of other diversifications. It is truly an integrated biorefinery now, so we are the UK's largest producer of tomatoes and we produce 70 megawatts of extremely high-efficiency—80 per cent efficiency—combined heat and power, which exports 50 megawatts to the grid. We are into pharmaceuticals and a whole variety of other co-products as well. Increasingly, the industry is going to be viewed by the really top producers as an integrated programme of intertwining activities, all of which complement each other.

Lord Whitty: Thank you very much. I am sorry to have to leave you at this point.

Q96 Lord Lewis of Newnham: Perhaps I could just take up this point. You did remark on the fact that at Hull you are investing in a new plant for renewable energy. I know BP at one stage was very concerned with looking at the possibility of producing butanol rather than ethanol. Did anything ever happen with that particular operation?

Chris Carter: Yes, it did. The plant at Hull, as you say, is a joint venture with BP and also DuPont. It is going to produce about 350 million litres of renewable ethanol for the transport market, and it is starting up a little later this summer, as it happens. The initial idea of BP to look at butanol is going on in parallel. There is a pilot plant in operation on the site, at Saltend at Hull, which is examining precisely that at the moment. If the opportunity arises in the future, there will therefore be an option of converting from bioethanol to biobutanol if the costs of production can be made competitive and if the market demand is there.

Q97 The Earl of Caithness: I would be grateful if you could just expand on one sentence in your paper to us. You say there is "surplus capacity sitting idle on the continent, which could be exploited at short notice once quotas are lifted." What is that surplus?

Chris Carter: Up until 2006, I think it is fair to say that the UK industry was set apart from most of our European competitors in how we handled ourselves before the reform. In the UK, we used to have 17 plants. By 2006, we had already reduced that to six. As William Martin explained, we lost a further plant on efficiency grounds in 2007, and another one, York factory, which was highly efficient and pretty large, in 2008 as a direct result of the mandatory restructuring scheme. Up to 2006, there had been very little rationalisation elsewhere in the EU, so we were already running our factories for basically twice as long as the EU average. With the closure of the two extra plants in 2007 and 2008, we now run almost all the way through the year. Most of our European competitors do not do that yet. They are making improvements but they fall well short of that. That means in some countries, and France particularly, they effectively have surplus capacity that they could put into use at relatively short notice, which we no longer have because we have rationalised and restructured so heavily, in the interests of improving our efficiency.

Q98 The Earl of Caithness: In fact, France could keep on mothballing those factories for another five years, waiting for the quotas to go, and then you would be in the same position that you are now.

Chris Carter: We would not quite be. The whole point of us asking for five more years is to further improve our competitiveness and get in place the investment we need to do that. We will therefore be in an even better position to hold our own, and we will also consider potential capacity improvement projects, if they are relevant and appropriate at the time.

Q99 The Earl of Caithness: Was it necessary to close York?

Chris Carter: That has already been referred to earlier this morning. Was it necessary to close York under the terms of the EU restructuring scheme? Yes, it was. We had to renounce 165,000 tonnes of UK production. We had no choice about that whatsoever; that was a mandatory requirement of the European restructuring scheme at the time, and we could only get compensation for it, at least at anywhere near a reasonable rate, if we also closed a factory. Effectively, yes, it was completely mandatory, and almost all European companies had to do the same at that point in time.

Q100 The Chairman: The French closed fewer, did they?

Chris Carter: The French closed the ones that they had to close in 2008 as part of exactly the same restructuring scheme. The point in the previous question, which was an excellent one, is that before 2006 they had not closed any at all, whereas we had closed 11.

Q101 The Chairman: Would you have done better not to close and get compensation?

Chris Carter: It is a fair question. The question is: were it not for the restructuring scheme and the terms of the 2006 reform, in hindsight, would we have closed York, which even now would be one of the top-quartile performing factories in the EU? The answer is: we would have had a very different look at it for sure. I cannot say whether we would or would not, but we would have had a very different look at it.

Q102 Baroness Parminter: You have asked for the extension of the quotas for five years. For the record, because no one has said it as yet, do you support the abolition of quotas in 2020 or are we going to face you arguing for a further extension in the future?

Chris Carter: Our position is as stated: we would like to see an extension of the CMO, including the quota system, until 2020. We accept they are extremely unlikely to go on beyond that.

Q103 Baroness Parminter: You do support the abolition of them after 2020.

Chris Carter: We accept that they are likely to be abolished after that point.

Q104 Baroness Parminter: Okay, so you accept but you do not support that. I have two supplementaries to that. It seems to me that you and Mr Martin are both arguing that the UK industry needs to build up its investment to deal with a bullish—I think that is the term you used—European and global market in the future. What argument would you put to counter the view that there are other industries, such as horticulture, that are similarly investing in anaerobic digestion, increasing yields and profitability to deal with the growing market, but will not receive any support and investment in order to deliver that?

Chris Carter: Just to be clear, we are not proposing to invest over the next five to eight years primarily to be able to export on to the world market, although that will be an opportunity after 2020 that I very much hope will be greater than it is at the moment. We are constrained on exports at the moment actually. Our main aim would be to supply competitively our domestic markets in the UK and northern Europe. That would be our main aim.

Q105 Baroness Howarth of Breckland: I want to return to this question of the interprofessional agreement (IPA) and see from your point of view how you value it. It was described as a groundbreaking new contract. Our previous expert did sort of say it is not a cosy cartel, but from the outside world it could rather look like a monopoly and a cartel. I would not have used those words had they not been previously used. Can you explain the benefits of the IPA in the UK, talk a bit about the models that are used elsewhere and how it can actually be justified when you look at many other organisations that are not allowed to run with this sort of partnership?

Chris Carter: The UK sugar industry is unusual in that it is highly integrated. It is integrated right from seed production, genetic breeding of the plant varieties, right through to the final sales of the finished products. That is very unusual. It gives us a number of considerable advantages, and I would say the interprofessional agreement structure is one of those; it forms part of that integrated structure. What it allows us to do is to have a much more focused and closely directed approach to our industry objectives than would normally be the case in a more fragmented industry. For example, we put between £1.5 million and £2 million a year into a joint agricultural research programme. We have an extremely closely organised technology transfer programme and grower support programme to deliver results to our grower suppliers, and we have an extremely close relationship with the NFU, which allows all that to happen.

I guess the acid test of this is: how has the industry performed, both in the UK and internationally? If you look at the last 20 years, it has performed remarkably well. Sugar beet productivity yields have outstripped those of all major UK arable crops by far in the last 20 years, and we have already mentioned that sugar yields in the UK, which are now averaging 11 to 12 tonnes of sugar per hectare, are comparable to those of the very best cane-producing countries, for example Australia and Brazil, and are invariably in the top quartile in the EU. I have to say the best performing areas of the EU are top notch internationally now. I would see the IPA as being a valuable and integral part of that process.

I think also, just to make the point, we have 3,500 to 4,000 supplying farmers and we have one processor—it is called British Sugar plc—in the UK. I think the interprofessional structure ensures a fair balance of interests between those parties.

Q106 Baroness Howarth of Breckland: Could I just ask one other different question? We have heard a little about the developing free trade agreements, which are having an effect in other parts of the world. What kind of effect might that have on our industry in the UK and on any agreements you have?

Chris Carter: The development of free trade agreements, as Barry Newton explained, has totted up about an extra 300,000 tonnes of imports, from next year onwards, in the last couple of years. That is clearly going to affect the supply balance. That is a source of additional supplies on to the European market and it is likely to continue into the future. There is a trade policy wish in the EU to strike bilateral trading agreements, and quite often those include sugar in some part. It will affect the balance; it will increase the supplies. It is already starting to do that.

There are implications, as Barry Newton said, for the developing countries' preferential suppliers—those are the ACP/LDC suppliers—because this was not foreseen at the time of the 2006 review, but it is now happening apace. There are clearly implications for them in that. It also does mean though that, when you combine the new ACP/LDC arrangements, which are completely unrestricted now, with the new free trade agreements and the new additional imports—nearly 700,000 tonnes in to the EU now, effectively, from Brazil—imports to the EU next year are going to be at a level of around 3.2 million tonnes, which is a sizeable proportion of the total consumption of just over 16 million tonnes.

Q107 Baroness Howarth of Breckland: This leads me to the point of my question, which is that, before the agreement, we were a net exporter rather than importer. Would not the freeing up of some of these regulations help us to increase our exports?

Chris Carter: Long term, I very much hope that will be the case. Short term, I am afraid it would not be. There are technical reasons for this, but several other parameters have to be changed in order to free the export constraint that we have at the moment. We are limited to 1.3 million tonnes of exports.

Q108 Baroness Howarth of Breckland: I think we would be quite interested in the answer. If you could write to us about what those reasons are, I think we would be quite interested.

Chris Carter: Yes, I can.

Q109 The Earl of Caithness: You said to Baroness Parminter's question that the maximum transition period is five years and then quotas will go. Do you accept that will also be the end of the IPA?

Chris Carter: Whether you call it an IPA or whether you call it something else, for the reasons already stated, there needs to be some form of negotiating and contractual framework between British Sugar as the sole processor and its supplying farmers. We would prefer to see that in an organised way. We would prefer to see that defined in some way in the legislation, providing it does not inhibit our local freedom and flexibility to negotiate terms that are sensible for UK conditions, which is exactly what we do right now. I think we would prefer to see a system in place that has a degree of structure and allows a fair balance of interests between them.

Q110 The Earl of Caithness: Is that the view of your EU competitors who also have the same cartels?

Chris Carter: Right, when you say "cartel", we do not and they do not have cartels. There is not a cartel between us and the NFU; there is a negotiating structure, the purpose of which, primarily, is to defend the interests of relatively small and fragmented farmers. "Cartel" is a word that is normally used to describe the output sales end, and there is certainly nothing like that in our industry. As I have already explained, we are free to compete with very large international suppliers, as well as European suppliers.

Q111 The Chairman: Could I ask you a question there? On the supermarket shelves in England, what percentage of pure ordinary sugar is supplied by you? In this open market we are hearing, what percentage is imported from France?

Chris Carter: Just over half is supplied by us. About 10 per cent comes in from the continent, and the majority of the rest is supplied by Tate & Lyle.

Q112 The Chairman: What is the basis of that 10 per cent? Is it price competition? Is it some sort of product differentiation? How does that compare with 10 years ago or actually in 2006? Has the market developed?

Chris Carter: Yes, it has. The amount coming in from the continent has sharply increased.

Q113 The Chairman: On what basis? Price?

Chris Carter: On price, competitiveness and availability.

Q114 Lord Renton of Mount Harry: Can I follow up on that? Is there any basic difference in quality or taste between sugar produced by cane, as opposed to sugar produced by beet?

Chris Carter: That is the easiest one to answer: no, there is not.

Q115 The Chairman: We have this question on Africa and southern China. In your paper you explain that AB Sugar has cane sugar operations in Africa and southern China. Can you just help us there on the impact of the EU sugar regime on your operations? You can give us a global perspective on this.

Chris Carter: We have, as I have explained, beet operations in northern China and cane operations in southern China. The answer to that is as simple as the answer to the previous question, which is that there is not really any impact, simply because the two continents are so far away. They operate completely different systems and there is very little sugar trade between China and the EU. In the case of Africa, in contrast, the answer is completely different. Five of the countries we operate in are ACP countries or LDCs. A great deal of investment has been put into those industries in the last five years, over £400 million worth of it, and they have had unrestricted access to the EU market since 2009. As Barry Newton has already explained, their futures are pretty dependent on what happens in the EU. They have local and regional markets as well, and they are pretty attractive in most cases, but nevertheless the EU market is a valuable addition for them and, this year, ACP countries and LDCs are expected to export, in aggregate, 1.8 million or 1.9 million tonnes to the EU market, just to put a number on it.

Q116 The Chairman: In conclusion, is sugar a good business for ABF?

Chris Carter: You would perhaps have to ask the ABF directors that question. I would like to think it is. I think it has long-term potential for industries and companies that are willing to invest and really work hard to become internationally competitive. Our goal is to do that wherever we operate, not just in the UK, so I very much support the contention that it is an excellent business for ABF to be in.

Q117 The Chairman: Could you help us to define what "excellent" would be? In order to do that, would you kindly get us copies of the brokers' reports that are circulated about ABF, which will let us read what the stock market believes the strength of the sugar operation is within that and its profitability? It is unlikely we can break it out, I suspect. I suspect that, like large companies, you publish accounts and have what I would call the statutory accounts, which would tell us very little. We would be very keen to establish how good this arrangement is. It is unlikely we can drill down to the 3,500 farmers that supply these accounts, but I think we could probably do a few calculations about yield per hectare, price and inputs. It would be quite interesting for us just to see whether these arrangements are competitive or not. I would be very grateful if you could supply that. As much segmented information from your accounts as you could give us on that would be enormously helpful.

Chris Carter: We would be delighted. The ABF accounts are actually very full; they are pretty detailed. I will send you copies of them, and we get brokers' reports from time to time, which are semi-public, so we can let you have some examples of those as well, if you would like them.

The Chairman: That would be very helpful. Thank you very much. It has been extremely useful. On behalf of the Committee, thank you both.

Department for Environment, Food and Rural Affairs (Defra)—Oral evidence (QQ 202-226)

Evidence Session No. 4. *Heard in Public.* *Questions 202 - 226*

WEDNESDAY 4 JULY 2012

Members present

Lord Boswell of Aynho
The Earl of Caithness
Lord Cameron of Dillington
Lord Carter of Coles (Chairman)
The Earl of Courtown
Baroness Howarth of Breckland
Lord Lewis of Newnham
Lord Maclennan of Rogart
Baroness Parminter
Lord Renton of Mount Harry
Lord Whitty

Examination of Witnesses

Rt Hon Jim Paice MP, Minister of State for Agriculture and Food, Department for Environment, Food and Rural Affairs and **Martin Nesbit**, Director, CAP Reform, EU and International, Department for Environment, Food and Rural Affairs

Q202 The Chairman: Minister, good morning. You are very welcome. Also, Mr Nesbit, thank you for coming. Just before we start, we should say that the Committee has been grateful for the performance of your Department in responding to our questions and queries over recent times. It has been a marked improvement and we are very grateful for that. Thank you very much.

Jim Paice: Thank you. I will pass that on.

The Chairman: If I may, I will do the formalities. You have in front of you a list of the interests that have been declared by Committee members. As you know, it is a formal evidence-taking session of the Committee. A full shorthand note will be taken. This will be put on the public record in printed form and on the parliamentary website. We will send you a copy of the transcript and you will be able to review it in terms of any minor errors. The session is on the record. It is being webcast live and will be subsequently accessible on the parliamentary website. Minister, I do not know whether you would like to start by making any general observations before we go to questions, or would you prefer to go straight into those?

Jim Paice: Lord Chairman, I think your questions probably cover all the areas that I would cover in general observations. It is probably just as straightforward to go straight into your questions.

Q203 The Chairman: That is kind. The first is obviously around sugar. The Government's policy is to support the Commission's proposal on not extending the production quota system beyond 2015. In the evidence we have had so far, we have heard arguments from the beet industry and developing countries that the quota system should be extended until 2020 in order to provide an orderly transition before the full volatility of the world market comes into effect. We would like to know how you respond to those arguments and how you consider the concerns surrounding volatility and whether they could be overcome. Adjacent to that, should the Commission retain market management measures in order to protect the market where necessary? Also could you say a little bit about the fact that beet producers are receiving the single farm payment and are protected by a quota—so, that general area?

Jim Paice: Thank you very much, Lord Chairman, and, formally, good morning to my Lords and Ladies. As a matter of principle, I and, you will not be surprised to know, the Government basically dislike the concept of production quotas and, therefore, we support the proposals to abolish them. We supported the abolition of milk quota in 2015 and, in principle, we therefore support the abolition of the beet production quota, which can only lead to artificial inflation of prices and obviously impedes the working of the market. Although it would not have been true 10 or 15 years ago, British beet producers are now among the most efficient in Europe. Our yields have gone up very considerably and, of course, British Sugar's processing capacity is world-leading in its economics.

Obviously we understand that, to expand, as I certainly would wish to see, the British beet-growing industry will require the processing sector to have invested in more processing capacity, whether it is new plants or expansion of existing ones. That takes time and, therefore, the idea that they need time for transition is perfectly valid. Part of me does question whether they will make the commitment to expand until they know when the deadline is, and they will put it off if that deadline is put off as well.

Where I find some difficulty in your question is the comments they have made to you about the exposure to the full volatility of the world market, because that is not what the Commission is proposing. Indeed, that is one of our concerns about the Commission's proposals, which is that it is exposing the internal EU market to full volatility, full competition, but no external competition, because they are proposing to keep external measures, which would mean that countries such as Brazil or Australia or anywhere else would not be competing with either British, French, German or any other European grower. It also brings us to the issue that I know you want to come to in later questions about the cane refineries, because they are not proposing to relax any of the controls on that side of it—the import of raw sugar for further refining. I do not quite understand why British Sugar and the NFU are concerned about that volatility on the basis of the Commission's proposals, because I do not see us in that.

The Chairman: We will come to the cane open-market issues, as you say, subsequently.

Q204 The Earl of Caithness: Can I come on to cane? Before I do, it seems to many of us that it is absolutely ludicrous to talk about new investment when already we have had to close profitable plants as part of the EU sugar regime. There is something very wrong at the heart of the sugar regime if one moment you are saying we have to close plants like they did at York and the next you are saying we need more time in order to invest in new plants. If you could make a further comment on that, I would be grateful.

Coming on to the cane, we have heard a lot of evidence that the cane market is being discriminated against. How would you see the Commission's proposals being changeable into a situation that was more equally balanced between the beet and the cane producers?

Jim Paice: On your first point, my Lord, I think everybody would share your concern but I think, in fairness, in 2006 when the last sugar reforms took place it probably was unlikely that anybody could foresee the very substantial increase in world sugar prices that subsequently took place and which is the cause of today's difficulties as opposed to those difficulties when we were clearly producing massively in excess of European demand. Hence the production cuts that were in place and, as you say, the closure of some very good plants. Clearly, looking backwards, it was the wrong decision, but we have seen this dramatic increase in world sugar prices.

Although it is a volatile market, we do not see any likelihood of significant fall-back, partly because, of course, there are the global markets. There is the link between sugar and ethanol and ethanol, of course, is directly linked to global oil prices. Unless anybody is forecasting dramatic reductions in global oil prices—and I do not see much suggestion of that—then I do not think we will see sugar prices falling back dramatically. I am not suggesting there will not be volatility. We know there is expanding demand—everybody quotes China, but the big developing economies are expanding demand. Therefore, what matters to us is that our own industry, which we now believe can be as efficient as anybody in the world, should have a fair opportunity to compete.

To move on to the cane situation, obviously we are very concerned about the future of the Tate & Lyle factory—it is 800 jobs in east London and not to be ignored—but also about the impact on the former ACP and less developed countries. The Secretary of State for International Development has had a report produced that shows quite clearly that a number of those countries would suffer very considerably were Tate & Lyle to close. We know they are talking about the threats to their business. I would not want to be setting hares running, but I think we all understand that they have had to cut back to about 60 per cent of capacity. Therefore, it is very important to us, in terms of overseas development because of those ACP countries and LDCs, and because of Tate & Lyle jobs, as well as consumer choice.

We have, as you will be well aware, roughly 50:50 cane and beet sugar consumed in this country. If we do not have the cane sugar, then, in the presence of quotas, we will have to fill it with imported sugar that almost certainly will come from other beet producers elsewhere in Europe, probably less efficiently produced than our own. So we need to find a way through the cane dilemma and that is our concern. Having talked, as I did a few minutes ago, about the abolition of quota proposals of the Commission, which we support, our concern is that they are still proposing to keep the tariff barriers, which is what effectively is keeping out the raws from refineries.

It is not the only issue. I think we need to be realistic and say that there are a number of countries, Mauritius being the obvious example, that have stopped exporting raws because they have invested in their own refineries now. Because of the old two-tier market, in Europe or out of Europe, a lot of countries were exporting raws to the UK, into Europe at a high price and buying in refined sugar at a low price on global markets. That has gone, so they are now refining themselves. The overall supply of raws has reduced and I do not think we should argue that they made the wrong decision. Nevertheless, there are many countries that want to continue to produce raws and we believe they should have better access to Tate's factory in London and to other refineries in Europe. That is the angle that we will be working on, as well as the issue of quotas.

Q205 The Earl of Caithness: Do you have any support among other Member States for that view?

Jim Paice: Very little. Interestingly, the only voiced support has come from the Baltics because—and this was news to me—apparently under Russian control they invested in refineries and they were bringing in raws from Cuba, which has all obviously ceased, but the refineries are still there. So there is some support from the Baltics to import raws, but it is not very much support for us, I am afraid.

Q206 Baroness Howarth of Breckland: Minister, you have moved rather into the question about the ACP and LDCs and the difficulties that they might well face. I wonder if I could be presumptuous and ask you a slightly different question about their development and their capacity. It is obviously a very complex picture, geographically, in terms of available markets to some of those countries, with Mauritius having achieved what it has achieved being an example of how it could happen. Do you think that some of the things that may have impeded development have been the way that the Commission has in fact helped the development and the availability of funds to these countries and does the Government have any view about the way the developing countries have been impeded in developing because of the lack of funding through the EU? That is one aspect. The other is: do you think that, because they have a closed market and because of the controls, they are not encouraged in fact to develop their own refineries? What do you think would make a difference to these countries, because I am sure the Government must be concerned about the inconsistency of the policies that they are facing?

Jim Paice: I agree with you, my Lady, that we are very concerned about consistency and I think it is perfectly true that the 2006 reforms, and indeed these ones, did not and do not pay sufficient attention to the needs of developing countries. Indeed, I think these ones almost ignore their needs, and we have seen, as I was just describing, the impact that that has had on our own imports by Tate & Lyle into this country. I certainly agree with you that we have an obligation to find ways to support those countries as they look to decide whether to continue with sugar, what part of the process, if they are going to continue, they continue to do there, and whether to refine or not.

I am winging this slightly without sufficient briefing, but I suspect that quite a number of them do not have sufficient volume to justify refineries of their own. Mauritius, we know, did and, of course, it is always one of our bigger producers. Guyana is another big one, but some of the West Indian islands, I suspect, would not have sufficient capacity to justify a refinery and be competitive. Indeed, some of them do not have ideal sugar-growing competitive conditions anyway. I do not think just helping them to construct refineries is necessarily the most satisfactory way forward and, looking at it from the UK's perspective, it would not do anything to help Tate & Lyle's difficulties.

Q207 Baroness Howarth of Breckland: I suppose the long-term question is: are they going to be dependent forever or what can we and the EU do—because some of these were old colonies—in order to ensure that they can diversify, if that is an appropriate thing to do?

Jim Paice: You will appreciate that I do not particularly want to tread on DfID territory here, but if you go back, as I can, to the banana situation, which was very similar, where we were importing expensive bananas basically to support them, in the end we had to stop doing that. They have survived. They got through it and help was given and I think this would be similar. They were not competitive in global terms of banana production and some of them are not competitive in global terms in sugar cane raws, but others would be and we should help them. I think there is a responsibility, but it would be more DfID's than mine—not that I would not like it—to help them to find ways of diversifying their economy, frankly, to find alternative products and commodities where they can be more competitive, but I entirely believe, strongly, that we owe them that opportunity.

Q208 Lord Whitty: Just on the difficulty of Tate & Lyle, what they said to us was not just about the shortfall in supply from the developing countries but also that one of the perverse effects of a reform that was supposed to rationalise capacity in Europe was that some European beet processors were now setting up additional refining capacity for cane sugar. That seems very perverse given the objectives of the last reform. It also has had a detrimental effect on Tate & Lyle.

Jim Paice: I am obviously not going to argue with what Tate & Lyle said to you, my Lord. I think my initial response is that it just shows what happens when you try to control the marketplace. Businesses respond to it. Yes, I believe that is happening. There is certainly a raws refinery in Portugal, and I believe there are some others.

Q209 Lord Renton of Mount Harry: Minister, I want to pick up on your last point, the difficulty of controlling a market. We are an EU Sub-Committee and we have to produce a report very soon in which we can either say we agree with the idea of continuing the quotas, perhaps up to 2020, or we do not and we think they should go as soon as possible. I think it would be very helpful to us to have your view on this. We have had, in a sense, confusion from the witnesses who have come before us. British Sugar was absolutely certain, as was the NFU, that the quota should stay. Nestlé was equally certain that they should not stay. Would you agree that the retention of quotas looks more likely? I think, from what you are saying, you are not in favour of it yourself, but do you think there is any chance of moving the European Council or MEPs nearer towards your position?

Jim Paice: In a word, my Lord, no. Our view is that they should go and we would support 2015, but I would not wish to put any money on it. In fact, there are a number of countries that do not want to get rid of quotas at all, let alone in 2020, and, as you say, the views of the European Parliament now are equally important. I think the likelihood of them going in 2015 is extremely slim, but from our perspective, because we want to see them go, we will continue to argue that case.

As far as the British beet industry is concerned, I have said to British Sugar and to the NFU that that is our view. I believe it is in the long-term interests of British beet growers because I would like to see us be able to expand production, which we cannot do while we have quotas. I would like to see either British Sugar or another start investing in further capacity, because we can certainly grow more beets in this country competitively. If we are going to see a decline in imports of cane sugar in any form, which seems to be the way the land is lying, then I would far rather we were producing our own sugar than having to import from elsewhere in Europe where they are no more competitive but we were tied up with quotas.

We know that some other European countries like France have a quota massively in excess of domestic consumption, which they have to export, and they will export it to us if there is a hole in our market. We have managed to resist that so far, but if we have a decline in cane sugar, I would rather we filled it ourselves than import it from somebody else because we were constrained from producing it ourselves. I think that is completely wrong. That is why, in principle, we wish to see quotas go.

Q210 Lord Renton of Mount Harry: I think most probably the EU Common Agricultural Policy will extend them to 2020.

Jim Paice: That would be my estimate, yes.

Lord Renton of Mount Harry: There is not much we can do about it.

Jim Paice: As I know you fully appreciate from your own experience, my Lord, we have to keep on with our position, otherwise it could get even worse. What we certainly want is a commitment to end them in 2020, if not before; whereas, as I say, there is quite a strong voice that does not want to end them at all and I certainly would not want that to gain supremacy. I would far rather a commitment for 2020 than no commitment at all.

Q211 Lord Lewis of Newnham: Is there going to be any consideration of the basis on which the quotas have been allocated? We have the present situation. Let us make the pessimistic assumption that it does go forward as you are saying. Will there be a review of the quotas themselves? After all, we have included a new group of countries in the EU and they must have an influence on that. It does seem to me that the questions you are asking in part will not be solved but could be alleviated and helped by reconsideration of the quota system itself as a whole.

Jim Paice: I will defer to Martin Nesbit in a moment, if he has further information, but my understanding is that there is absolutely no proposition of recalculating the basis of quotas. The new Member States were given quotas as part of their accession arrangements and, while I might have some agreement with you that I do not think they are very fairly distributed at the present time, there is nothing on the table, no proposition, as far as I am aware.

Q212 Lord Lewis of Newnham: Do we know the basis on which the allocations are made or were made in the initial stages? It does seem to me these could have changed. This is really what I think I am asking.

Jim Paice: Go on, Martin.

Martin Nesbit: If I can just add on this, obviously the Commission has not proposed a reallocation of quotas because the Commission's position is that it wants quotas to end. Obviously our hope is that the ineluctable logic of the UK's position in favour of the Commission's proposal will start to sway other Member States and I am officially obliged to be more optimistic on that than the Minister, but if we ended up in a situation where quotas were continued, I think at that point there might then be a discussion about what sort of basis there should be for allocation and whether the existing basis for allocation needed to be in some way adjusted.

Q213 The Chairman: Thank you. I think perhaps we can leave the rather depressing subject of sugar, by the sounds of things. Perhaps just one question before we do leave sugar though. Do you have a sense, Minister, of what these existing arrangements, particularly the tariff and things, add to the cost of consumers' price of sugar in this country, the pack on the supermarket shelf? What about if we were to totally liberalise sugar and accept the volatility that would accompany it? Is there any sense of this?

Jim Paice: I am afraid I cannot give you any estimate of that, Lord Chairman, and I think you have put your finger on it by talking about the volatility. In the last couple of years there would have been periods where it could have gone up, when the world price was higher than the internal European market. As I understand it, that is not the case today, but I do not think it would be much cheaper. Those days are behind us, unless world prices collapse considerably, but for a long while, as you rightly say, the price of sugar was being held up by tariffs and quotas and the consumer was paying for that. I suspect that in today's price it is not very significant.

The Chairman: Thank you. Let us go on to Common Agricultural Policy (CAP) reform.

Q214 Lord Whitty: You have been very frank and slightly depressing about the prospects on sugar. Can we move to the wider issue, on which you have also set out fairly scathing comments on the European Parliament's position? Could you perhaps outline your main concerns on the way in which the CAP reform prospects are going and perhaps, as you have done on sugar, give us an outline of the politics as you see it between the Member States?

Jim Paice: I will try, my Lord. The CAP reform, of course, covers a whole range of propositions, everything from the single market and the issues of market support through to the future of the direct payment, the rural development programme and so on. I am very conscious that what I say is being noted but I think I would say that the only thing that unites all 27 Member States is the fact that we do not like the Commission's proposals, which is why we—the British Government, myself and my colleagues—have spent a great deal of time working with other like-minded Member States to come forward wherever possible with alternatives around which a majority can coalesce.

Let me quickly canter through the key issues. The area where I think most progress has been made was the Commission's proposals to define an "active farmer", which was to be based on the proportion of their income obtained from European aid as opposed to other sources of income—nothing to do with farming. I think it is true to say that has been universally condemned and effectively dropped. What will take its place is slightly less clear, but it looks like being based on a negative list, a list of the types of business, such as airports for example, who might not be able to claim CAP funds in the future. Our position is we would prefer the whole basis not to be on the type of business but on whether they were farming. It does not matter what sort of business it is; if they are farming actively then that should be the guiding principle.

On the second issue, the big one obviously is the greening proposals, the 30 per cent of the single farm payment, where there has been widespread criticism of the Commission's proposals. It is very complicated, and one of the guiding principles that we have adopted and virtually every other Member State adopted is that, early in March last year, I think, we wrote to the Commission urging simplicity. We are not seeing too much sign that that was heeded, although the Commissioner certainly defers to the need to be simple. I will come back to one of those points.

On the greening proposals, he is very committed to what I call the three-legged stool approach of crop differentiation, permanent pasture and ecological focus areas. There are a number of options now on the table being considered. One is a menu-based approach. Another, which we favour, is the idea of greening by definition. We would like to see membership of our stewardship schemes be an automatic entitlement passport into the greening premium in the single farm payment. I hesitate to prophesy, but I think we shall get something close to what we want in that. I suspect the Commission's proposals will still be part of the endgame, but one way of demonstrating that you will have an ecological focus area might be that you are in a stewardship scheme.

We have the somewhat emotive issue of capping and whether there should be a lid on the amount of money going to the largest farms. We have continually opposed that. Previous governments have opposed it in previous rounds of the CAP when it has come up. We believe it to be anti-competitive and we believe that it would simply encourage the fragmentation of units, which is not necessarily desirable. We have a blocking minority on that at the moment. On this occasion I am more optimistic than Martin is about whether that blocking minority will hold.

Then there is the proposal for young farmers. We are quite happy with the concept of helping young farmers, but we think Member States should have flexibility as to how they should do it because we think simply making a top-up to their single farm payment to a limited number of entitlements is not going to help, certainly in the UK context, at all. Then there is the proposal for a top-slice for what we call less-favoured areas, which is going to be called "areas of natural constraint". Frankly, we are very unsure as to how that top-up would work and who would get it and how it would be allocated. We are not averse to it but, like a lot of other things, we think it would be more simply accommodated in pillar 2, as I think we have made clear in our evidence to you.

Then we move across to the issue of the rural development programme, where it is still quite hazy what precisely the Commission is proposing. The biggest challenge of all is that we do not have a clue how much money we might get. The Commission is saying they will not produce any estimates of what each country's allocation will be until late this year—therefore, we assume, until probably close to if not the resolution of the multi-annual financial framework for the whole of the EU, which will settle the CAP budget. That is why we have pushed very hard to have the option of moving up to 20 per cent from pillar 1 into pillar 2, if we need it, to fund our pillar 2 commitments in terms of stewardship schemes, but also our other proposals in helping to improve farm competitiveness.

I am sorry, my Lord; it is quite a long answer but, as you will have gathered, the crystal ball is extremely murky and I am not, on this one occasion, going to start to guess how it is going to end up. We are still a long way from settlement.

Q215 Lord Cameron of Dillington: Good morning, Minister. As you know, I am a farmer and I have already declared my interests as such in this context. As a farmer I have become more and more convinced that the CAP, at least pillar 1 as you have just mentioned, is not very helpful for the competitive position of EU agriculture. There are all sorts of add-on costs that occur as a result of it. First of all, let me say that I am not asking for more money for risk management. This is predicated on the belief that pillar 1 would be reduced and we could get some funding alternatively allocated into some form of risk management. One of the issues that farmers have to put up with is extreme volatility of prices. Already in some of the developing countries of Africa, they have insurance schemes on cost of inputs. In their original proposals the Commission put forward some suggestions that this might be an alternative solution, some sort of way forward, but it does not seem to have come to anything. No one else seems to be talking about it and developing it and I am just wondering whether you thought there was any future in this idea as a system of trying to level out some of the volatility for farmers.

Jim Paice: I think it is a very difficult area to address, my Lord, because there are so many different possible solutions, if indeed one is looking for solutions. There is an argument that says volatility is a feature of the global market so we should learn to live with it. Larger farms in the UK, through the use of futures and things like that, or maybe through a co-operative that uses the futures markets, have been able to address that risk and that volatility issue. There are proposals, as you know, for the crisis reserve to be used in ways involving things like the income stabilisation tool, akin to what I believe they have in Canada. We have big questions about whether it fits with WTO anyway, but also we think it would be very bureaucratic.

Many of the proposals that are coming from Member States we are convinced would breach WTO green box issues and the Commission has made it clear there would have to be a very strong political consensus if we were going to go down that road. There is the use of Article 68, whereby Member States could retain 5 per cent to 10 per cent as coupled measures for specific purposes, which, in an ideal world, we do not particularly want. We do not want to see any coupling continue. We certainly do not want to see a reversion of coupling. Some Member States want to see re-established coupling for commodities where coupling has already ceased, but the idea of 5 per cent to 10 per cent for specific reasons, such as happens in Scotland for the Scottish calf scheme, we can be relaxed about. That is another form of risk management.

As far as we are concerned, we are open to other suggestions, but we have not yet seen any particular proposals that readily seem to be simple, workable and fit within the WTO. I think that is the reality. Do you want to add to that, Martin?

Martin Nesbit: Yes. I think the sorts of mechanisms that the Commission has proposed in the rural development regulation would be decided on by individual Member States and regions as they work up their rural development programmes. You would tend to get a little bit of thought about how they would be used a bit further down the line, rather than a sort of EU-wide discussion on exactly how that should be designed. As the Minister has explained, we have some concerns about some of the proposals in the risk management toolkit that the Commission has put forward, but the scope for using rural development funding to help farms and groups of farms manage their own risk, making use of private sector insurance mechanisms, for example, is potentially a direction that looks worthwhile and worth encouraging.

Q216 The Earl of Caithness: Minister, I would like to return to direct payments. You commented quite a lot on that in reply to Lord Whitty's question, but how do you respond to the EU Parliament rapporteur's suggestion that farmers who are holding certificates under national regional environmental certification schemes should be automatically entitled to a greening payment?

Jim Paice: As long as there is some element of environmental equivalence to those schemes then we support it. That is effectively what we are asking for to be able to use stewardship, but it is important. I had a meeting with all the CAP stakeholders and the environmental lobbies are, understandably, concerned that those national or regional schemes are of genuine, reasonably high-quality greening standards and not just some easy passport to the premium.

Q217 The Earl of Caithness: Two more questions, please: do you think that enough attention is being paid to farmers who have already done greening measures rather than encouraging farmers to take up new greening measures, because that is very hard on those who have already done it? Secondly, with regard to the less-favoured areas that you mentioned, are the Scottish Ministers happy with the position in Europe?

Jim Paice: I will take the first one first, if I may, on the situation with the greening and people who have already done the work. As you may recall the Commissioner came to the NFU AGM in February and referred to British farmers as the champions and said he does not wish to penalise the champions of the environment, a point that we keep reminding him of as we try to get our arguments across for including entry level. I think that is right. I was challenged yesterday by the RSBP, I believe, that if we simply did that it would not lead to any additionality in terms of greening. I made the point, and I think—I would say this, wouldn't I?—it is a good point; do not forget 30 per cent of English farmland is not in stewardship. If the incentive that you had your greening premium of 30 per cent encouraged that extra 30 per cent of English land to go into stewardship, that to me is a massive addition, and I think that would be it.

I am, though, very concerned about the Commissioner's proposals for the ecological focus areas of 7 per cent because it is not at all clear what he is talking about 7 per cent of. When he has been challenged in debate he has said, "Well, many people have hedges or ponds or things like this", but they are not eligible acres. Of your land that you declare and claim on, that does not count. So is he saying it is 7 per cent of your claimable land, which would be effectively reintroducing a form of set-aside, which he has said he is not trying to do? If it is to include all those natural features, then it seems to me very unequal that a farmer who has those natural features may automatically meet his 7 per cent while others who have not may have to do something quite radical in order to do so. That is one reason why we see that as a serious problem.

On your second point about Scotland, indeed all the devolved authorities, we meet with them regularly. Most of them come to each Council meeting and we go through the agenda and try to agree the lines that the British Minister, myself, or the Secretary of State are going to use. I am not going to pretend to you that we agree on everything. Obviously one area where there is not agreement is the size of the overall budget. We always make the point, quite rightly, that the budget will be settled by heads of government. It will not be settled by Agriculture Ministers. When we get down to the detail of the CAP then largely there is a lot of common ground. There are one or two areas where there are nuances of difference, but, in principle, we are largely in agreement. On the greening issue, I think we are all speaking with the same voice.

Q218 Lord Renton of Mount Harry: Could I, for a moment, Minister, go on about CAP and the coming seven years? Is it right that the CAP will continue to have the same percentage of the total EU budget as now, or will the CAP just get the same figure as now although the total will be going up?

Jim Paice: You mean in the proposals as opposed to—

Lord Renton of Mount Harry: In the proposals as at the moment, yes.

Jim Paice: Yes. The British Government's view is that the proportion and actual spend should fall considerably and that that reduction should focus on—

Lord Renton of Mount Harry: I was really focused on the proposals as one—

Jim Paice: As far as the proposals are concerned, the proposition is that the CAP should be frozen in real terms. That would be in cash figures. What that meant as a share of the total EU budget, I assume, is that it would fall, but Martin—

Martin Nesbit: It would be a declining proportion of the overall EU budget as proposed by the Commission.

Jim Paice: A declining proportion, but the same in cash terms.

Q219 Lord Renton of Mount Harry: Does that not mean, though—this is very simplistic—that as there are now many more countries within the EU than there used to be, money to individual countries such as ourselves or France or Germany is bound to fall, the actual figure?

Jim Paice: I think you are right. I need to qualify that by, of course, pointing out that in the Commission's proposals there is this element of convergence where the Member States with the lowest levels of payment on a per hectare basis would be converging with the mean, or with 90 per cent of the mean. What they are saying is that every country getting less than 90 per cent of the average for the whole of the EU would see an increase above their normal allocation, so that their rate per hectare would go up and, equally, those at the top would see their rate come down.

The UK is on 90 per cent. The convergence criteria would make virtually no difference to the UK. The wider point you raise though, which is about how far can you spread the money, effectively, I think is very important because even if you accept the Commission's proposals, which is a real-terms freeze, that means a decline obviously over the seven years in reality. I just feel very strongly that the farming industry needs to understand that this is the trend. It has happened over the last seven years, and it will continue to happen.

That is why our position is that we would far rather see a proactive policy that says, "Over the next X years the single farm payment is going to be declining at a certain rate to be decided and this is the way the future is going". The world market is changing; there are great opportunities out there. We should be using the CAP to help farmers equip themselves and be competitive for that global demand that we all know is rising, rather than arguing about whether we should get an extra pound or two a hectare this year, and we have to freeze the budget because we need the income. We all know they need the income today, but we believe the day will dawn when they will not need it, or much less, and we should be planning for that day rather than just letting it happen.

Lord Renton of Mount Harry: This seems to be extremely realistic and very necessary.

Jim Paice: I entirely agree with you.

Q220 Lord Renton of Mount Harry: This is a smaller question. Could you elaborate for us on the progress in negotiating the new pillar 2? I have a question to ask you: are you able to assure us that its focus on a competitive, sustainable and innovative agriculture will be maintained? That is perhaps making the rose blush.

Jim Paice: The answer is yes in terms of our intent. The British Government's view is that pillar 2 is the far more important pillar. It is far better value for money for the taxpayer. It targets payments at specific activities, whether it be care for the environment—and, as you know, in England 18 per cent of the money goes into that, through stewardship predominantly—or what are currently axes 1 and 3 of the RDP (Rural Development Programme), which are about competitiveness, innovation and socioeconomic activities. Basically, what the Commission is proposing is to abolish the three axes and to say that within a set of criteria that they list, which is roughly similar, Member States can spend what they like. There has been a debate about whether there should be a *de minimis* of 25 per cent on the environment. That is not yet resolved.

So, overall, we are reasonably happy with pillar 2 in that regard. Where we are not happy is on the issue, as I touched on earlier, about how much we get in the allocation, because our allocation is one of the lowest in the whole of the EU and it is entirely based on historic spend a very long while ago. The Commission is proposing a more objective set of criteria, but they are pretty woolly, and we cannot get much of an indication of what it would actually mean. Lord Whitty referred earlier to the European Parliament's reports. What worries us is that the rapporteur reporting on this aspect is proposing that they should stay on an historic allocation basis, which we would strongly oppose.

Q221 The Earl of Courtown: We are now turning toward farm advice. Our innovation report[1] wanted to place it at the core of boosting innovation in EU agriculture and recommended in particular that the advisory service be extended beyond cross-compliance. You are opposed, I think you were saying, to suggestions by the European Parliament's rapporteur that the advisory service be extended to new topics such as in relation to modernisation, competitiveness, innovation and market orientation. Why is this disagreeable to the Government at the moment?

Jim Paice: I am going to be honest with you, my Lord. I do not know because when I read this brief I asked myself the same question, if I am brutally honest. I will expand on that a little bit. I am very concerned that we have a plethora of advice and a plethora of small pockets of government money—I mean there is lots of private advice but we also have lots of different pockets of government money, including the Farming Advice Service (FAS)—and I have to admit I have not yet met a farmer who has ever used it. That may be unfair, but I am concerned that we are not maximising the gain from this. I think farmers get confused about who to go to for this, that and the other. One of my hobby-horses in the Department is to try to pull together and rationalise our advice.

I think we discussed this in previous sessions with this Committee, but we have seen the demise of FWAG (Farming and Wildlife Advisory Group). We have the campaign for the farmed environment, which we have recently extended. We have the FAS. They are not exactly duplicatory in any respect, but there is a lot of overlap. You have Natural England's own advisers and the RPA (Rural Payments Agency) inspectors, who inevitably give some advice off the record, so to speak. I just feel we can do better and that is what I want to do. I think what is behind the comments about the Farming Advice Service is that that is a pretty definitive set of things from the European level end, and I would rather we had the flexibility to devise our own ourselves, but to put together these pockets of money to maximise the benefit.

Q222 The Earl of Courtown: I do not have the declaration to make now, but I used to be involved in property advice to farmers and estate owners and, unless you could offer the whole picture, it was a waste of time going down that route at all.

Jim Paice: I think I ought to defer to Martin to give you the official answer.

Martin Nesbit: I was just going to say that the Minister has described exactly the rationale behind our position on the farm advisory service. It does not make much sense to set in concrete at European level the rules that govern how farm advice should be delivered effectively across the EU. It is much better to design it at Member-State regional and local levels in ways that work for the farming interests concerned.

[1] 19th report (2010-12): *Innovation in EU agriculture* (HL Paper 171) http://www.publications.parliament.uk/pa/ld201012/ldselect/ldeucom/171/171.pdf

Q223 Baroness Howarth of Breckland: Just a supplementary on that: although I can see that it does not need to be set at European level, when we did our inquiry into innovation in agriculture one of the messages that came out loud and clear was that there was a real need for one trusted advice source. The Farming Advice Service were seen as people that the farmers could turn to for advice. The way that innovation was transferred through the chain, from experiments through to the farmer, was by having these bits of advice. Has the Government thought through, since we did that report—and you talk about pulling it together—having that trusted source of advice that the farmers were clearly asking for when we undertook our report?

Jim Paice: Yes, we have moved forward. If my memory serves me right, since that report my friend and colleague Lord Taylor of Holbeach has joined the Defra team and he is leading this forward now and has the bit between his teeth on the subject. It is an issue he did a lot of work on when we worked together in opposition. The whole issue of knowledge transfer from the leading-edge research and innovation to getting it into the farms is something that he is grappling with. I am not at liberty to make announcements that have not yet been made, but I can assure you that we are taking it very seriously. He is working very hard on things to do such as monitor farms and demonstration farms. Obviously, as you rightly suggested, it links into the on-farm advisory side as well. So watch this space, but I can assure you that we are grappling with it.

Q224 Baroness Parminter: You will be aware, Minister, from our recent report on the freshwater policy[2] that we supported the inclusion of specific elements of the Water Framework Directive into cross-compliance, specifically extraction and discharge, or unauthorised extraction and discharge. It seems to be that the Government's view is that the total removal of the Water Framework Directive is a useful clarification, citing lack of specificity. I think my question is: is the Government's position that they would like it included if there were specifics around the Water Framework Directive and, to that end, have either our Government or indeed any other Member States made any specific proposals to that end?

Jim Paice: I think the answer to your question, my Lady, is yes. If the Commission was far more clear and specific about what basic measures they expected to be put into cross-compliance, then we would certainly be very much more interested. It is being done through the Water Framework Directive expert group on agriculture, which we co-chair, as you probably know, and if they do put forward some positive proposals then clearly we will give them the attention that they deserve. I cannot say whether we would support them in the absence of knowing what they would be, but we are not averse to supporting them if that is justified. As to how much work is being done on it, I do not know whether Martin can add to that. As I say, it is being dealt with through the expert group. It is not an issue that has been discussed at Council level, I am afraid. Martin, do you know any more?

Martin Nesbit: Not much further detail, no. Obviously the timescale for that expert group's work is going to be a relatively longer timeframe than the negotiations on the CAP, partly because Member States are still discovering exactly what the implications of the Water Framework Directive are as they work through implementation in their own context. The difficulty that many Member States had with what the Commission proposed for cross-compliance there was that it was, in a sense, badly drafted legislation. It simply said that

[2] 33rd report (2010-12): *An Indispensable Resource: EU Freshwater Policy* (HL Paper 296) http://www.publications.parliament.uk/pa/ld201012/ldselect/ldeucom/296/296.pdf

future rules will be designed at some unspecified point in the future on some unspecified basis. So we would prefer a separate proposal to sort that out.

Jim Paice: It is probably worth making the point that, of course, a number of issues related to water and the issues within the Water Framework Directive are already in cross-compliance. It is not that that cross-compliance would just ignore anything to do with water. That is not the case. As I am sure you know, there are a number of issues already covered, such as buffers and things like that.

Q225 Baroness Howarth of Breckland: This may be a real invitation for you to be able to say what you think about some of the issues in relation to the CAP.

Jim Paice: That implies I have not!

Baroness Howarth of Breckland: We have had a look at the European Court of Auditor's report and you described some of the elements of the expenditure in the CAP earlier on as "murky, to say the least". I think that was your phrase. Ultimately, as you know, this Committee would like to see a simplified CAP that drives sustainable innovation. How confident are you that we are going to get that?

Jim Paice: The honest, direct answer to your question is that I am not very confident. The Commission's original proposals were, in my view and most countries' views, extremely complicated. They would have made life much worse, not just for farmers but for paying agencies, governments, auditors and the rest. As I said in my earlier remarks, the Commissioner himself, though, keeps on about how he is providing simplification. I think I said I was going to come back to him. The area where he talks about it that I omitted to mention is his proposals for a small farmer scheme, whereby farmers whose claim would be less than €1,000 would just get the €1,000 basically as of right without having to comply with the greening criteria or any cross-compliance criteria. He says that that is a form of simplification and I can accept the argument that for those farmers it is, but it is not simplification of the system that we would all like to see.

The problem is, as I said at the beginning, that the fact that most Member States cannot agree on the way forward, other than we do not like what he is proposing, leads me to expect that more of his original proposals will remain at the final stage than perhaps we initially thought, unless we can get very clear majority agreement on alternatives. If that is the case, then I feel it will be more complicated. Anything that changes today's single farm payment system, and so many of the proposals do, will be a complicating factor both for farmers and for the payment agencies. I should add that the Rural Payments Agency is actively involved in discussing with Martin's team the impact of all the various proposals, so we take that into account in our responses.

Q226 Lord Lewis of Newnham: Could I just ask the Minister a question? You referred earlier to the ethanol situation from sugar. Where exactly are we standing as far as this is concerned? Is the use of sugars as a whole for the production of ethanol in any way whatsoever related to quotas?

Jim Paice: No, it is outside the quota system.

Lord Lewis of Newnham: So this is a production line that would be in addition to any other sugar that is used.

Jim Paice: Yes. There is very little of it in this country, my Lord. The only British Sugar factory, in Norfolk, currently produces—I do not think it is ethanol. It is another one of the alcohols from sugar.

Lord Lewis of Newnham: Butanol?

Jim Paice: No. It will come back to me, but basically this country's production of ethanol from sugar, as opposed to grain—

Lord Lewis of Newnham: Yes, wheat.

Jim Paice: Yes, wheat. But from sugar it is very, very limited. My point was that in Brazil, the world's biggest producer, they can easily switch, whether to push sugar into the sugar market or into ethanol and, because the world price of ethanol is closely linked to the world price of oil, that links them to the sugar market—that was the point I was trying to make—rather than the domestic one.

The Chairman: That is perfect timing, bang on 12.15 pm. We have had you for an hour. Thank you very much, Minister.

EPA/EBA London Sugar Group—Oral evidence (QQ 52-71)

Evidence Session No. 2 *Heard in Public.* *Questions 52 - 71*

WEDNESDAY 20 JUNE 2012

Members present

The Earl of Caithness
Lord Cameron of Dillington
Lord Carter of Coles (Chairman)
Baroness Howarth of Breckland
Lord Lewis of Newnham
Lord Maclennan of Rogart
Baroness Parminter
Lord Renton of Mount Harry
Lord Whitty

Examination of Witness

Barry Newton, Chairman, EPA/EBA London Sugar Group

Q52 The Chairman: Mr Newton, you are very welcome. Thank you for coming to see us today. We are looking forward to what you have to say. If I may, I will deal with the formalities. You should have in front of you a list of interests that have been declared by Committee members. This is a formal evidence-taking session of the Committee. Full shorthand notes will be taken and they will of course go on the public record in printed form and on the parliamentary website. We will send you a copy of the transcript, and you will be able to revise it in terms of any minor errors. The session is on record, and it is being webcast and will be subsequently available on the parliamentary website.

I wonder if we can go to the questions. I think you have had some preparation for this. If I may, I would like to take the first question. It is this: in the papers that you very kindly sent to us and which were very interesting, you made reference to the interplay between free trade agreements, economic partnership agreements and the "Everything But Arms" initiative. Could you set out for us in greater detail how you consider the reform process needs to take these three factors into account?

Barry Newton: Yes, Lord Chairman. First of all, I apologise on behalf of my Ambassador colleagues in Brussels, who have not been able to be here today. They did ask me to pass on their apologies to you; they have been committed to other things, not least in Vanuatu with the EU ACP Council.

Very briefly, the "Everything But Arms" agreement, which was introduced by Pascal Lamy in 2001, I think, introduced a complete change to the structure of the EU market. It was one of the main reasons given by the Commission for reform, as it wished to remove the incentive of the very high prices in the European Union for the least-developed countries to invest heavily and disturb the balance of the market. The 2005 reform also took account of the problems that were introduced by the WTO challenge to the preferences given to a number of old established suppliers to the EU—mainly to the UK market—that had been attached to the Lomé and then Cotonou conventions. Reform would replace the present arrangements with Economic Partnership Agreements (EPAs), which were regional and would meet the requirements of the WTO. These EPAs were meant to provide, for the members who signed up to them, conditions and results, which if not exactly the same as the former protocols would give benefits at least as great in the round.

We then have the Free Trade Agreements, which are coming in now in the last few years, and subsequent to the reform and which we believe are in danger of creating a further instability in the market. These were not foreseen in any of the figures that were put out at the reform time, and we now have approximately 300,000 tonnes' commitment to the Central American and the Andean countries, with further activities taking place in discussions with India and Mercosur. One can argue whether these are going anywhere in the short term but, nevertheless, there is a problem that we see in the market balance that would be created by these unforeseen increases of quotas—they would be quotas—and tariff-rate quotas attached to it. It is in that regard we see the problem that, not only as you discussed last week—the issue of the coherence with the CAP, which is an internal regime, and the development activities—but there is the problem of the activities of the Trade Director General, which has an impact on all of this as well. We believe this coherence is not being properly addressed. Does that—

The Chairman: I think that does it. Perhaps we can come back to that, because some other questions will fit with that. Maybe we can come back at the end and try to tie these all together.

Q53 The Earl of Caithness: In following on from what you have just said, after the reforms of 2006 and the massive premium that was reduced, what has happened in the way of restructuring within the ACP countries to find alternative markets or to diversify?

Barry Newton: It is a very varied response, as you might expect from such a wide range of countries. However, one of the specific intentions of the finance that had been offered, the accompanying measures finance, was to provide a basis that, together with other money from other development institutions, would provide an impetus to further an accelerated response to the change in the markets, specifically the price. One of the offers in the Economic Partnership Agreements was to offer duty-free quota-free, which, for some countries that had a low access under the old protocols, enabled them, as the Commission put it, to make up for the price drop by increased access to the market, which presumes that the market price is going to continue to be attractive, albeit at a lower level.

The problem with the market price of course is that we have had several years of difficult growing conditions—these are climatic issues as much as anything else—where the high price, perhaps for some countries, has not been enough to generate a surplus to help in the investment programme. The biggest problem I think most of us have had, and I exclude Mauritius from this, which has done rather well, is that the money that is coming from the accompanying measures has been tied up in such red tape that Belize, the country I represent, for example, has only received 16 per cent of the cash allocated for the period 2007-10. Others are in a similar position. It is partly caused by the fact that the ability of the EU to provide the money is curtailed by having to separate countries that are eligible to receive budgetary support finance, in which the money can be disbursed very quickly, and other countries that have to go through all the project activities that bedevil banana finance and is still bedevilling sugar finance. It is a nightmare to get the money.

Let me give you an example that gets to the heart of what has been done. A number of us were already involved in activities to improve efficiency. This has been going on for some time, because the reform was signalled as long ago as 1992, and a lot of countries have been engaged in doing that. It involves productivity; it involves expansion; it involves a number of things, but access to the market is part of that. In Belize, our diversifications were first of all into activities within the sugar industry. We spent US$60 million on a co-generation facility, which now provides 20 per cent of the grid.

Q54 Lord Renton of Mount Harry: Can I just ask: what does that mean, a co-generation facility?

Barry Newton: The sugar cane plant, when crushed, leaves a residue that is called bagasse. It is a fibrous residue, which traditionally has fired the boilers of the plant. It has always had a certain amount of ability to generate electricity for surrounding housing. However, with a major investment in the change of the design of the boilers, we have been able to put in higher pressure boilers and steam generation, which has got alongside the sugar factory a major power plant, which generates electricity that goes into the grid and has replaced the import of Mexican oil. That $60 million was contingent on growth in the supply of cane, which was to be generated by the accompanying measures being given to the farmers to replant their fields and improve their productivity. We are running several hundred thousand tonnes of cane short because of the delays in the finance. We are not in any problem, but it is back to the old problem that, unless the sugar industry is profitable, there is no diversification because, if we have to stop producing sugar cane or reduce it, the generation—whether of ethanol or power—is affected. One cannot go without the other.

Q55 The Chairman: In that specific example, there is the accompanying measures finance that did not run. Exactly what happened in that case? Just describe in detail what actually happened.

Barry Newton: Well, nothing.

Q56 The Chairman: But where did the responsibility for the nothing lie? I think that is what we would like to establish.

Barry Newton: There was an action plan put in for every country in 2006.

Q57 The Earl of Caithness: The action plan was required by Brussels, was it?

Barry Newton: Yes, it was. It was specifically required in order to be eligible to receive accompanying measures. That was in April 2006. The first allocation was a small amount of money that was left over from the previous seven-year budget of the EU, and then a significant amount more money, approximately €1.2 billion, was allocated for the remainder of the period, which was meant to end in 2013, which is the expiry of the current budget.

My Lord Chairman, the problem then was that the EU requires each year for a multi-annual budget to be agreed. It seems that in discussions, with whom we are not sure, the allocation of money suddenly shifts more to building roads and consultancies than releasing what we thought was a priority, which was to establish some revolving funds for the farmers to receive cash that they repay over the period to keep the fund going. So far that fund has not yet been set up. It was agreed several years ago and then has fallen foul of a desire by the main delegate of the EU, based in Jamaica, that it needed an international financial institution to be an intermediary between the EU and the Belize Government. The International Financial Institution they finally agreed to appoint, the Caribbean Development Bank, has then spent with the EU about a year arguing as to who will have responsibility for the proper spending of the funds. That is the sort of bureaucratic problem that we face. As a small country, it is very difficult.

Certainly one could argue, and I would not deny, that perhaps the Belize Government departments have faults. It is a small country with a difficulty in having people who can deal with some very efficient and quite pressing people from Brussels and more from the delegations, but we are not getting a proper discussion. From our point of view as the miller, we are a private sector company and are told we are not eligible for any money from the EU, because we are private sector. Therefore, we can only sit at the side—comment, help, but not get involved in any of the discussions.

Q58 Baroness Howarth of Breckland: My question you have answered, but for those of us who are new to this situation, it looks an extraordinary bureaucratic muddle with a failure to target where the money should go. This is the first question we came up with: if this money is there, why is it not being targeted and why is the investment not happening that actually leads to the kind of factories you were describing? To cut to the chase, if you were making recommendations to the Commission—and we will be writing recommendations in our report—what would they be in this area?

Barry Newton: My recommendation to the Commission was to try to be more helpful to and understanding of the smaller countries. They do not have the resources to meet the very stringent conditions, sometimes, that are laid down for contracts, even the contracts for roads. As an industry, we would say, yes, there are proper uses of the funds for roads because, without the roads being in a decent state, you cannot transport the product. However we would think that the highest priority should have been to increase the productivity of the cane farmers because, without that, their costs are not going to go down to the level that is required for the future viability of the industry, which we believe is certainly fundamentally sound. It is this holding back and the lack of priority of what we believe are the right things to do first. They ought to be more helpful. Lord Mandelson, when he was Commissioner, said that after him there would be a long line of development experts coming in to help. I do not recall seeing anybody coming in to help; they are coming in to criticise most of the time.

Another example was that there was a hurricane not long after the start of the accompanying measures, and money was disbursed quickly by the EU for the Government to spend in assisting people who had been hit by the hurricane. It was not well administered internally—it was rushed—but the EU came in and decided that it had not been done properly and demanded the money back. I do not think they have received all of it back, but it is now being used as the reason why Belize is not able to handle money properly anywhere else. It is frustrating.

Q59 The Earl of Caithness: Can I just follow that up? Do you think there was a misunderstanding between what you anticipated the EU doing and what the EU anticipated you doing?

Barry Newton: I do not think there was a misunderstanding in the discussions we had in Brussels with the senior people at DG Development. One of the confusions that I get concerned about is knowing to whom the delegate reports in Brussels. The delegate is part of the foreign service, and that has been enshrined now under Baroness Ashton, but the various directorates general seem to operate independently. The collegiate style only comes back at a very high level. It is not an easy thing to trace the way through as to whom you might be approaching for help.

Q60 Baroness Howarth of Breckland: Is there a conflict between democracy and achievement, if you can understand what I mean by that? The countries themselves are wishing to disburse funds, but they do not necessarily see the same priorities that you or the EU might?

Barry Newton: I do not think there should be a problem there, because the action plan was very clear as to what the priorities were, how much of it was to be spent from EU funds and how much had to be found by the independent parties. I do not think it is a problem of democracy, because it was made very clear in discussions in Brussels with the Commission—and I was there when the UK was in the presidency and Minister Beckett was in the Chair—that the plans belonged to the governments. It is not always clear as to whether the administration of these funds then supports that.

Q61 Lord Whitty: Can I just follow up with a quick one on that and then go into more general questions? We can take them both together. One is: is there a significant differential impact of the plans on different ACP countries and LDCs? You mentioned 16 per cent of these funds got to Belize. That is my first question, and then my other question is broader. It is understandable that the ACP countries see what has been quite a traditional market, do not wish to lose it and did not wish to lose it fast when the reforms came through, but is it not also true that the bigger pressures on the least efficient sugar producers are not really from changes in the EU regime but because there is domination in the global cane sugar market by Brazil and, to some extent, the larger African countries? In other words, is this not really your biggest problem, although it must be a very irritating one?

Barry Newton: You are right: of course there are different effects across the countries. We are quite a diversified group of people and the group I represent is 30 countries, of which 28 are effectively suppliers and have supplied in the past three years. Mauritius has done extremely well; it has a well-organised society and government, and seems to have had a constructive relationship with its delegate. They have done very well and made a major transformation. There are not many others that have done that, and the amounts of money were, of course, it has to be remembered, allocated on the basis of the previous protocol supply figures. Some of the countries, such as the newer countries in Africa in supply to the EU, like Zambia and Mozambique, therefore had relatively small amounts of these accompanying measures, so the amount that impact had on them was not so great. Equally, they are also now run by some of the biggest of the South African groups, so that the funding is not so much of a problem for them and they have very good, well-run conditions for producing low-cost cane. The people who perhaps have had the biggest problem in integrating it all have been some of the smaller countries, and I think that is an administrative issue.

Back to your last question, I think that the problems for the older countries, the smaller countries, when traditionally a high proportion of their supplies have come to Europe and to the UK in particular, are much more to do with the EU than the world price, because they have not really been affected by the world price directly in the past. It is what happens in Europe and their traditional supply routes that has been and still is a major problem.

Just to explain, there are two significantly different groups in broad terms. There are the countries that were old suppliers to the UK. When the UK came into the EU in 1974, they had the protocol. These are countries that are, for the most part, small populations that rely entirely on exports. Belize has 300,000 people. Guyana, one of the bigger countries, has 750,000 people. These are not countries where diversification is easy. Their whole economies were set up in order to supply the metropolitan country. Goodness knows, I have been involved in I do not know how many different schemes to find diversification, but they have found nothing as good as sugar for the large rural element of their populations to do. 300,000 people is not the basis for any industrial activity, and Belize now has a good banana industry; it has a good sugar industry; it has a good citrus industry. It has shrimp. It has three forms of tourism—the eco-tourist, the ship tourist and the reef tourist. It is not easy to find a broader diversification than that, but we rely very heavily on the maintenance of a market in the European Union. If we were reliant on the world market, we would be reliant on a very fragile forecast of prices. This is a market that traditionally goes up and down in big swings. It is in one of its upswings now; it will go down. I hear evidence that Brazil's costs are inexorably going higher. I am not sure I believe that. I think Brazil's currency will have a big impact on that. I believe Brazil has failed to invest in the last few years, but I believe also that they are capable of turning that around. I would not buy into the fact that Brazil's costs are going to remain high. It would be a dangerous thing. Anybody who forecasts the world sugar market price endangers their reputation.

Q62 Lord Renton of Mount Harry: Listening to you, Mr Newton, today, having been in this when we talked about it in 2005, one slightly despairs because one feels that it should all have been worked out by now somehow and, obviously from what you are saying, it has not been. Just touching on a country like Jamaica, for example, it obviously is presumably not nearly as much at risk as Belize, because they have large tourist possibilities as well. I take it that, probably in their case, sugar is not that important, whereas you are saying it is for some of the other countries.

Barry Newton: I think that there is a danger of assuming that GDP figures are the only things that really matter on this. One of the things that Jamaica, St Kitts and a number of the other islands face is the significant difference that already exists between the urban and rural populations. St Kitts' costs had risen to a level where it could not sustain remaining in sugar, and they felt that getting compensation, the safety net funding, would enable them to survive. In discussing this with the ambassador in Brussels, she has said that they did not anticipate the degree of problems that have come up through removing from the rural economy jobs, which women could do part-time in some of the areas around it and which other people could do, pushing more people into relatively small cities to find jobs and/or relying on tourism, which is not easy and does not have deep roots financially in any of these economies. It is a big problem, which is why we talk about the fabric of society with sugar, particularly because of its ancient roots, in many ways, despite the unpleasantness of slavery connotations. It is very important in those rural areas, more than we really understand.

The fact is that, although it has taken a long time so far to get this thing moving, I do not believe it should take long to kick-start it. What has happened since is we have had a number of other economic and financial shocks, which were not anticipated at the time in 2006, are eating into the amount of money that was allocated, and now will require less to be done for the same amount of disbursement. If all of the money, the €1.2 billion, is disbursed effectively, it will have an impact. There are not many countries of which I would even question whether or not they are spending it effectively on efficiency. Clearly when you give it to governments that are in some financial difficulty, the Prime Minister and the

Minister of Finance will be very pleased to accept money and disburse it to their economy in the best way they see fit. That is their privilege. It is up to them then to satisfy the EU that they are spending it wisely, because otherwise, they will claw it back.

Q63 Lord Renton of Mount Harry: Thank you. Perhaps I can just take you on to the question of future reform. Basically you say that the rationale for keeping the quota is strong because, above all, without the quota instability would increase further. Going on from that, what alternatives do you see to addressing price instability? Are there other ways of doing it without retaining the EU quota system, in your view?

Barry Newton: I have not found one, my Lord. It is a serious problem. The instability is counter to what the EU decides it wants in this. One of the points, if I could read a quotation from what was said in the staff working paper in the 2006 reform, was that production quotas would be phased out "once imports and production levels had stabilised". This is clearly not the case now, and any predictions that you look at say this is not going to happen by 2015. The OECD and the FAO are forecasting greater instability in prices, and the more that we bring it nearer to world price impacts, the worse it is going to get.

There was also to be "a non-disruptive end to quotas at a date to be defined". That was only said by the Commission in 2011. In statistical terms, it has to be understood that the sugar regime is not and never has been a production-limiting regime; it is a marketing tool to manage the markets to achieve stability. This is now coming counter to the views of some of the people in the Commission that, somehow, free trade is the objective, not a means to an objective. It is of great concern. At the moment, the average amount of out-of-quota sugar over the past three or four years has amounted to in excess of 4 million tonnes. That sugar does not go into the food market. The regime was designed to direct quantities of sugar into the food market. There has always been some production that went into ethanol, into industrial use and other things, and the system at the moment has two major tools: one is withdrawal of quotas if there is too much coming on to the market; and the second is private storage, which can happen during a crop. Nobody wants to put sugar into private storage if, the following year, there is going to be an even bigger surplus. The credibility of this requires there to be definitions of the amount of sugar that can be withdrawn and put on the market later.

You will hear from the NFU about their view on this, but we believe, from our side, that unless we have the controls of the quota system, we are not just in competition with world prices and other things; we would be in direct competition with a large amount of sugar on the market coming from the beet industry. Inevitably, with the prices in the food market generally being higher than in the other markets for sugar, it would be perfectly understandable for beet producers to attack that market first. We are a long way away from the market. We are small and we feel that this would be a difficult thing for us. We believe, and I also think the beet producers believe, that there is room in this market for both of us. It was, after all, structured in 2006 to provide a greater amount of imports into it than it had ever had before.

The fact that we have not achieved those numbers yet is due to a number of factors, not least because, as has often been unstated, 700,000 tonnes of the supply was expected to come from swaps, because the world price was expected to be lower than the European price. Therefore, Brazilian sugar coming into East Africa could be put into the domestic market and the domestic production could come to the EU. That did not happen; the price does not allow it. 500,000 tonnes was intended to come from Sudan but, for reasons that are not surprising, they have not yet achieved the levels of production expected and a great deal more has been consumed locally than anybody anticipated. 1.2 million tonnes is a very large lump out of the predicted amounts. We are nowhere near the predictions that came out in the 2005 reform, and yet we are now talking about continuing that reform without understanding, or sitting back and looking at, how it might be modified to achieve its ultimate objective. We think it is far too soon and it is not based upon solid evidence. Unfortunately, we are hampered by the fact that the Commission does not put in writing its reasons for suddenly rushing to the front of their objective, which is to get rid of the quotas. It is quite wrong to say these were anticipated before. It is quite to wrong to say that simply because there was a date on it, it must be done—since 1968 there has always been a date on the end of the regime. It moves in packets of years and has then been renewed. We did not expect it to end in 2015, and we do not believe it should.

Q64 Baroness Parminter: In terms of mitigating the impacts of reform, would you support a transitional period between 2015 and any future date for the reform of quotas? If you did, what date would you set? Do you have any suggestions for any other mechanisms that could ease the transition for the effects on any of the ACP LDCs?

Barry Newton: We are in a transitional period at the moment. That is what we have been told. I am reluctant to put a date on this, because of the conditions that we have seen in the past five years. In fact, it is only three years since the last part of the big price cuts, so it is an even shorter period than is being suggested as the full impact of the price cuts did not come in until the end of 2009. We then had a year of reasonable stability, and then the price hikes and the supply shortages impacted on the market. I would be very reluctant to fix a date. At the moment, I support the view that a reasonable period to have as a minimum would be the end of the next financial perspective, 2020. It seems a long time ahead for a lot of people but, as I explained, I do not think we have gone anywhere near the end period of improving the efficiencies. We certainly, and I believe the beet industry too, feel we would like to spend far more time and more investment to achieve the improvements in productivity, both in the field and in the factories, that would allow us to be competing more openly in world markets after that period. They do not believe they have reached the end, and we certainly do not believe we have reached the end, of the reform in our own industries. At the moment, we would say 2020 and I believe that Monsieur Dantin, in his recent report, has suggested that there should be a report introduced in 2018, which would then inform everybody as to what has happened and what the conditions have been over the period. A decision will be made then as to whether 2020 is still the right period.

I do not accept that sugar has to change simply because milk has changed. The dairy industry is very different. Farmers are financially penalised for producing more milk than their quotas. Nobody is penalised for producing more sugar, but the fact is that, as efficiency improves, you will get these spurts of supply. It is not anything that is done deliberately to create over-supply, but the consequences of the over-supply are harmful to everybody. At the moment, the tools exist for this to be ameliorated by the Commission in managing it. 2020 to me would be a reasonable view to look at the time if it has worked or has not. We have seen in many other markets major problems that were not foreseen a few years ago, not least in financial markets. Times are changing fast.

Q65 Baroness Howarth of Breckland: I hear what you say, but is that only a reasonable thought if we are clear that there is some movement? From what you say, movement seems to be difficult because of the bureaucratic impact of the way the Commission deals with issues. If, by 2018, nothing has happened, is it then reasonable to continue with this same programme to 2020? How do you actually make sure that the movement takes place and we are not facing 2020 with the same situation? It seems to me that some of these countries are not being helped to become efficient and to improve their industries by simply leaving them as they are, without very targeted help to actually improve their production, or is that a totally naïve view?

Barry Newton: No, not at all, but I think you have to separate what the accompanying measures are supposed to be doing to help this situation, what is being done by the industries themselves anyway and also what is happening in the market generally. What I am talking about, in response to Baroness Parminter's question, is to determine what should happen in the market. The market is important, because investment in efficiency is something that we are very intent on doing; it should be done by the industries themselves with the assistance of the accompanying measures, and if the accompanying measures do not appear, we intend to go on doing it as much as we can. But to get the money to make the investment, we have to persuade banks that we have a market where we can sell our sugar at a reasonably remunerative price, so the market comes first in all of this, as far as I am concerned. Without that, we will not get money from the banks, whether or not that is to get money in support of the accompanying measures, which are not meant to be the sole source of funding for improvements of efficiency. A lot of us will continue to invest in efficiency as much as we can, and that is a decision we will make every year in one way but against strategic planning targets in others. We have every intention, certainly in Belize, of reducing our costs of production to the 15- to 16-cent level. That requires volume, and volume requires productivity from the farmers, possibly expansion in area, further investment in the milling facilities and, possibly, in support of our financing, the co-generation and maybe ethanol, maybe not. Ethanol for export is a tricky thing, as far as I am concerned, but there are other things we can do. In the northern Belize area, we do actually occupy 30 per cent of the national population and there is nothing else of significance apart from minor food crops.

Q66 Baroness Howarth of Breckland: Could I ask just one other provocative question? Is it not more appropriate that it might be seen as overseas aid, as against the sugar market? I can hear what you say about women in some of these countries, the need to actually keep stability and the fabric of society. Those are all phrases you have used, but that is not a lot to do with the market; it is to do with maintaining a society. I just wonder what that balance is about.

Barry Newton: Without the market at a reasonable price, you have not got anything to spend on social activities unless you are begging for aid and become mendicants rather than producers. It is not an attractive thing and not something that we aspire to. Unfortunately some of the smaller islands, with the loss of bananas and sugar, because of their history and the geography of the islands, are inevitably slipping into an inability to produce effectively in any of these markets. The markets are not going to be providing them with a price that enables them to stay in production irrespective of efficiency but, for a number of others, there is the scope for considerably greater efficiency to be invested in. That is something that a number of us are doing and will continue to do. The accompanying measures will be helpful but, from our perspective, they are not critical. The market is far more critical to all of us. In the stability of it all, we need a stable premium price that is "reasonably remunerative to efficient producers". Those are the words that were in the Commonwealth Sugar Agreement and which still apply today. The "efficient producer" is an important part of the "reasonably remunerative". You cannot get a price that will just be paid for nothing at all, but it is price inelastic as a product.

From our point of view, we also need to have access to the EU market because we are very small. Eighty per cent of the use of sugar, roughly, goes into what we call industrial use, not into the chemical industries but into soft drinks, cakes and chocolates. Only about 20 per cent is seen on the table, so we need access to some very large buyer chains, which is very important to us as well. It is an integrated system that has worked very well. We have accepted the reform, as it took place in 2005, but we believe it just has not been tested properly to see how you might take it to the next stage. Unfortunately, Doha now seems to be dead in the water, but that is a different issue.

Q67 Lord Cameron of Dillington: Good morning. You have already touched on this question throughout your evidence, but I was just wondering whether you could expand a little bit on the differential effect of the 2006 reform on the various ACP countries and LDCs. You have highlighted mostly the large versus small in your evidence so far. I was just wondering whether it goes broader than that, with geographical positioning and so on. I was just wondering whether you could expand a bit on that, please.

Barry Newton: Yes. Strangely enough, the large and small is also like a separation of the old and the new, in the sense that the newer countries in south-east Africa, which have become very efficient, with large plantations of irrigated cane, well controlled, have largely come from areas that were developed just pre- or post-independence, which were set up for import substitution with fairly large capital funds from CDC in some cases, Tate & Lyle on their own in the case of Swaziland and in Zambia, and the larger South African companies as well. These are the countries that have the bigger populations and whose exports have suddenly become more important to them. We do not know whether that is going to continue, and a lot depends on the growth of consumption in some fast-growing populations. I think they are at 3 per cent per annum in some of the countries. That requires continuing investment simply to stand still.

The other countries that I referred to tend to be those smaller countries that have been the countries supplying sugar for 300 years or more, from the small islands of the Caribbean for example. Fiji is more recent but is in a similar type of arrangement, and Mauritius also, but Mauritius has developed a much more efficient and integrated industry than many others. I am not sure historically why that is, but it certainly has avoided a lot of the political hiccups that a number of the other countries in the group I referred to have. I am pleased to say that Belize and Barbados still have currencies that are, as they were 20 years ago, at two to one to the dollar. That affects us in one way, because we are fighting against countries that have devalued by huge amounts, and therefore LDCs can gain more but, frankly, if we devalued, I think we would still be in the same position because we import so much. That is part of the food security angle as well. Food security is talked about as if the producers do it, but we also need income to be able to provide food security for the imports, which are essential as well.

That is the broad difference between the countries, but each one of them is also slightly different. A lot of the countries that are referred to in Africa—Malawi, Zambia, Zimbabwe—have extremely long routes to the coast before they get into marine freight to Europe. None of us in the ACP group receive a Single Farm Payment and we do have very long costly routes to the market. That is a fact; we are not asking for Single Farm Payments, but there is a difference. Therefore, the market price to us is more important than it is to the European farmer. It is very important to the European farmer. I do not deny that, but it is an added complication.

Q68 Lord Cameron of Dillington: My next question is actually about co-ordination. Again, you have mentioned the lack of connection between DG Development, Trade, Agriculture and so on. It is about the co-ordination that you are finding within Europe and how the policies overall affect you and the differential it makes. For instance, the CAP reform is just coming up again; what difference do you think that is going to make to you?

Barry Newton: We discussed the fact that the reform itself is changing the market and it is the drive for the common market organisation, which we believe is not the most essential thing to do. As far as Trade is concerned, we have always found them perhaps the most difficult to integrate into the three groups. Development tends to be reactive to what has happened in, say, CAP and other things. Certainly on this occasion, they have been, because the Accompanying Measures finance has been a huge amount of money relative to European Development Fund (EDF) funding. It has far swamped the amount that comes out of EDF.

The question for Trade is that Trade has an objective that has been clearly stated: they are trying to increase the free trade areas that they wish to reach treaties with, in order to increase exports of EU goods. The Trade Commissioner seems to regard domestic agriculture as something he can give away in return for these free trade areas. From our point of view, we are very concerned and very angry, in many ways, that the treaties that have been signed, which required them to consult with us on anything that affects the long-standing preferences signed at the economic partnership agreements and at Cotonou, are being ignored. The economic partnership agreement that CARICOM signed a number of years ago now requires the Commission, very clearly, to have prior consultation with us on anything that affects the preferences of the major products, which are sugar, bananas, rum and rice. That does not take place. Commissioner De Gucht goes his own way and they pretend they have had consultations, when all they have had is an occasional meeting in which they inform us what they are doing. It is distressing.

Perhaps our governments are not screaming enough, but if they continue to enter into new free trade agreements, sugar is always a part—and when you look at the trade groups they are talking to, it is bound to be a part. One of them suggested to us they did not know what they were going to discuss until they got into negotiations. It is very disingenuous when you are dealing with some of biggest sugar producers in the world, who want access to the market and have stated so. That is being given away and it will increase what we regard as the potential, if not probable, structural surplus in this market, and the structural surplus will bring downward pressure on prices inevitably. Who loses the most? The impact assessment has made it very clear it expects the ACP to lose more than anybody, and I think that is probably true, if a structural surplus exists. At the moment, there is too much concentration on the fact that there is a deficit because of low supplies. That is not, in my view, the problem. Looking forward, there is a structural surplus.

Q69 Lord Renton of Mount Harry: How would you describe this structural surplus?

Barry Newton: The amount of quota or allocations is greater than the ability of the market to absorb it. The EU market is static. We hear figures that there is some consumption growth, but it is pretty negligible. The only way consumption is growing in the EU is when another country comes into the EU and, very often, it brings the same amount of production as it does consumption, so there is really no great amount. The previous reform took figures of between 5.5 million and 6 million tonnes out of the supply to the food industry but, if there are no quotas, the whole of any extra production is there in the market and consumption has not gone up. We also have, without quotas, isoglucose, which is the corn syrup type of supply. Inulin and isoglucose will increase. At the moment, they are restricted on quota as well as sugar going into the food market. If the free-trade area agreements are bringing 300,000, and if Brazil and Mercosur, if not this year but in a few years' time, have a trade agreement, they are bound to want sugar. India is bound to want sugar. With both of them being very big suppliers in the world market, the instability will again start to rise and fall in a way that would mean that we would not be bankable to the European bankers.

Q70 Lord Cameron of Dillington: Just going back to the European situation for a moment, it is obvious that DG Agriculture and DG Trade, for instance, with 27 members, are going to be focused on their members and what they want, rather than what you outsiders necessarily feel, but DG Development ought to be more focused on what you need. You are saying that DG Development is not pulling its weight because it is too focused on a reactive agenda rather than a long-term agenda.

Barry Newton: Yes, I agree. To some extent, a number of them believe, as one of them told me one day, there must be something else you can do other than sugar, without knowing anything about it—"There must be something else." That is an attitudinal thing. A lot of the academic economists seem to believe that diversification must be easy; it is not. The smaller the country is, the more difficult it becomes. That is something that I think has to be debunked. DG Development's role normally is a relatively small amount of money to help, and it is in the aid sector. It is not usually involved in things that affect trade developments, but they are important in it all. They ought to be arguing, from their remit, with Trade and Agriculture as to what the impact of this is. The Lisbon Treaty has a very clear need for policy coherence, and there are reports on it. I would have thought it should be done before the event rather than after the event.

Q71 Baroness Howarth of Breckland: I would just have you comment at the end about the structure of the cane and beet industries because, in a previous inquiry that the Committee undertook in 2005, we heard that suppliers felt restricted by the limited refining possibilities in the UK, and in particular being locked into Tate & Lyle, the one big refiner. Can you offer any comment on the extent to which the current structure of the EU beet sugar industry and the cane-refining industry, with further years of reform, is more favourable or not to the ACP/LDC producers? That is the question I was given, but really what we want to know is whether or not the countries that you are talking about are going to find it beneficial or not in relation to the structure of the industry.

Barry Newton: Again, I think we are very varied on this. The ownership of refineries is rather more complex than is sometimes thought, especially since there was a release in the 2005 reform from January 2010 that the importers could supply anybody, not simply the traditional full-time refiners; these could be part-time refiners as well. The reform, which took out a large amount of production in Spain, Italy and Southern Europe—the higher-cost Mediterranean countries—also opened up an opportunity, which some people went into, to invest in new refinery capacity.

We now have a problem in that there is excessive refinery capacity for the amount of raw sugar coming in, which is causing a problem. It is not a problem at the moment for any of the ACP suppliers, because prices are high because of that shortage of supply relative to capacity. How that can be sustained is of concern in that, if any of the larger refineries go out of production, it does introduce a problem for a number of us, in that we may be forced to supply to a refining capacity that is well away from the port. It adds another dimension to it. We do not have a natural size individually to be of importance to anybody. Belize supplying 100,000 tonnes and hoping to go up to 150,000 is not going to make or break any of these refineries.

Too much was made about it before. There was a very clear agreement before reform that we supplied a volume to Tate & Lyle that was jointly and severally guaranteed, in order to get a slightly better price. There was no compulsion there. It was always possible to sell refined sugar. There never was any impediment to selling refined sugar before the reform. This is another mythology that seems to have crept into things. It was a very old-standing relationship, and nobody was denied a price because the Commission price was, by law, paid at a certain level. There is nothing magic about it. A number of people have found it more advantageous to make their own decisions about when to do it. Some of them are doing very well at the moment because they are simply sitting back and not entering into long-term agreements. Some of us have been forced to retain long-term agreements by our bankers. They want to see where you are going to sell in three, four and five years' time, and if you have somebody who will buy it. If you have not, then maybe they are not going to lend to you. We are back again in this cycle of the small supplier and the big banker. It is not an easy thing, but some of us have gone into long-term agreements where these wonderful prices we are seeing do not touch us. We have taken a view and we will stand by the view that we want long-term stability in these prices and long-term stability in our relationships with our buyers, who also have a chain that they supply. The refiners are a relatively small part of the total EU output.

The Chairman: It seems a perfect point to stop at actually. It is a very clear message and we are very grateful for that. Thank you very much. It has been most helpful.

Barry Newton: Thank you very much for listening.

LMC International and Overseas Development Institute (ODI)—Oral evidence (QQ 1-51)

Evidence Session No. 1. *Heard in Public.* *Questions 1 - 51*

WEDNESDAY 13 JUNE 2012

Members present

The Earl of Caithness
Lord Cameron of Dillington
Lord Carter of Coles (Chairman)
The Earl of Courtown
Lord Giddens
Baroness Howarth of Breckland
Lord Lewis of Newnham
Lord Maclennan of Rogart
Baroness Parminter
Lord Renton of Mount Harry

Examination of Witnesses

Sheila Page, Senior Research Associate, Overseas Development Institute, **Anna Locke**, Head of Programme, Agricultural Development and Policy, Overseas Development Institute; and **John Adams**, Senior Research Economist, LMC International

Q1 The Chairman: I welcome Sheila Page, Anna Locke and John Adams. Thank you for coming to talk to us today and thank you for the paper that you sent us in advance. If I may, I will just deal with the formalities. In front of you is a list of interests that have been declared by Committee members, who are also required to declare those interests orally before they ask a question—I hope that you will bear with us on that. This is a formal evidence-taking session and full short-hand notes are being taken, which will go on the public record in printed form as well as, these days, on the parliamentary website. We will send you a copy of the transcript, which you may revise if there are any minor errors. This session is live and is being webcast on the parliamentary website. Would you like to make any sort of general positioning statement, or would you like us to go straight into questions?

Anna Locke: I have a brief opening statement, which I would like to read out as it provides some background.

Lord Renton of Mount Harry: Before you start, can I just ask you to speak a bit louder? I am quite deaf.

Anna Locke: Is this okay? An important consequence of the first round of reform of the EU sugar regime in 2006 was that it linked EU sugar prices to movements in world prices.

Previously, they had operated quite independently of each other, with EU sugar prices trading well above world prices almost all of the time. Further reform of the EU sugar regime, through the abolishing of internal production quotas or the full liberalisation of EU sugar production and trade, would strengthen that link. Most importantly, this would allow EU sugar prices to follow substantial declines in the world price, removing the support to African, Caribbean and Pacific States' and Least Developed Countries' (ACP/LDC) sugar suppliers provided so far by the EU sugar regime. Thus, under further reform, ACP/LDC suppliers would no longer be protected from low world prices. This is particularly important given that world sugar prices are extremely volatile and have often languished at low levels for extended periods. This creates greater uncertainty for ACP/LDC sugar suppliers: uncertainty over what levels of revenue the sugar suppliers will face and uncertainty over what the sugar industry in each country needs to do in order to adapt to a new situation.

In terms of measures to support affected countries in adapting to the new situation, there have been lessons learnt from the first round of accompanying measures for sugar protocol countries about the type of measures that could be applied, the mechanisms for applying them and the criteria for allocating funds between countries. The experience so far has been mixed and many countries have not yet achieved what was envisaged under the accompanying measures. The experience demonstrates the need for a strategic, rather than piecemeal, approach with adequate country-level funds and sufficient lead-in time to design appropriate plans and build the capacity to implement them. Such measures need to be targeted at issues that allow sugar producers to tackle constraints on competitiveness and develop new products or, crucially, move away from sugar production where there is no prospect of competing under the new situation. Above all, there is a need to be realistic about the time it takes to get things done in target countries. Thank you.

Q2 The Chairman: That is most helpful. Let me start with the first question, which is on the impact of future reform. Can you expand on your argument that the level of the world price will be a greater determinant of industry viability in the ACP/LDC countries than further reform of the EU regime?

Anna Locke: In fact, reform of the EU sugar regime will be a determinant because it will strengthen the link between EU prices and world prices—there is an impact of reform but it is through strengthening that link. Under high world sugar prices, some ACP countries may be fine if they have alternative markets into which they can sell their sugar, because under high world prices the EU will reduce its import needs as domestic producers expand production to meet domestic needs. However, low world prices could have a detrimental effect on ACP/LDC sugar suppliers. So it is a two-stage process. It is not that the reform will have no impact whatever, because there is a link with world sugar prices.

Q3 The Chairman: Looking forward, you see volatility of sugar prices. Do you discern any long-term trends in demand for sugar? Surely the trend is upwards.

Anna Locke: I will pass that to John Adams, who works specifically on world sugar markets.

John Adams: There is evidence to suggest that there will be structurally higher sugar prices over the next decade compared to the last decade, when sugar prices ranged between 10 to 20 cents per pound. That was primarily due to Brazil, which has expanded rapidly over the past 10 years and has become the price setter in the market. Over the past five years in particular, production costs in Brazil have expanded markedly as a result of higher wage costs, higher energy costs and an appreciating currency, with current production costs now around 20 to 21 cents per pound. Brazil will be a main influence on the world market price for sugar, as Brazil currently exports 50 per cent of the world's trade.

Q4 The Chairman: So there will be volatility but with demand at a higher level possibly?

John Adams: Quite possibly, yes. Having said that, prices are plummeting at the moment and could fall towards 17 cents per pound. However, although prices could fall to low levels, I would suggest that they will not stay at low levels for a lengthy period of time.

Q5 The Chairman: Finally, in terms of cents per pound, where does the pain really start?

Sheila Page: It is terribly variable among countries. Some countries have production costs that are over 20 cents per pound, but some do not. In all of this, one needs to look at the individual country. Some of them really have no chance of being competitive in sugar at any reasonable expected price; some of them, given their domestic market and their local regional markets, will probably be all right no matter what happens. So you have to ask country by country.

Q6 Lord Renton of Mount Harry: Sorry, you are talking in cents per pound. I find myself very much confused, because diagram 1 in the document that you provided[3] appears to say that the price has gone up from €200 per tonne to €500 or €600 per tonne.

Anna Locke: Perhaps John Adams can convert those prices for us.

John Adams: The world market price for raw sugar as traded in New York is quoted in cents per pound—

Lord Renton of Mount Harry: I was just trying to say that it seems to me that the figure in the document is much higher than the one that you have quoted today.

John Adams: The diagram gives the figure in euros per tonne. To convert from cents per pound to dollars per tonne, you multiply by 22.046 and the exchange rate—

Q7 The Chairman: I think that our question is more about the very large increase in price, which the diagram suggests has gone from €200 per tonne to a peak price that is north of €500 per tonne. That is the pattern, which I take it is also reflected in cents per pound.

Sheila Page: We were discussing this before we came into the room. To those of us who worked on this at the time of the Committee's previous report, the price for sugar was 4 cents per pound, but now that is quite clearly not the case and is unlikely to be the case again. There has been a fairly dramatic shift upwards. As John Adams said, the price may fall from 20 cents per pound to 17 cents per pound, but I do not think that we are expecting it to fall back to 4 to 5 cents per pound. The price is now much higher.

Anna Locke: Two things might be relevant to this. First, the benchmark has shifted up because production costs have risen not only in Brazil but everywhere because fertiliser prices and energy prices have increased. We now need to look not just at the behaviour of the price but, as Sheila Page said, the behaviour of individual countries' production costs. Diagram 1 in the study reflects partly the upward movement in world sugar prices, but it also reflects the fact that the EU has had to compete for sugar imports in the world market in a way that it did not do so before because the expected volume of imports from

[3] www.dfid.gov.uk/r4d/pdf/outputs/TradePolicy/LMC-ODI_SugarReportPublicVersion(Final).pdf

ACP/LDC sugar suppliers has not materialised. Those countries have not been able to supply as much as the EU needed.

Q8 Lord Cameron of Dillington: Presumably, some of the countries that cannot produce sugar at less than 20 cents per pound should consider moving out of sugar production altogether unless they can massively invest in their industry to improve the infrastructure and to lower their costs, which seems unlikely given the fact that they have had since 2006 to do so. How do we deal with those countries, which seem to have a serious problem?

Lord Giddens: That was my question.

The Chairman: Thank you for leading us into that, Lord Cameron.

Lord Giddens: I also thought that we were required to state our interests.

The Chairman: Yes, I should have said that I am a farmer.

Lord Cameron of Dillington: So am I.

Lord Giddens: My interest is zero, so I can be completely objective.

Lord Renton of Mount Harry: I have a vineyard.

Lord Giddens: Essentially, Lord Cameron has asked the question that I was delegated to ask. If there is further EU reform, should there be mitigating measures to help the less developed countries? If so, what form should those measures take? It is obvious from your paper that different sugar regimes have all sorts of discrepant consequences for less developed countries. It seems quite a tangle and a puzzle.

Anna Locke: The countries can be grouped according to different characteristics. Some countries such as Barbados and St Kitts—and until recently Jamaica, although Chinese investors have recently expressed an interest in improving Jamaica's sugar industry—are really struggling and probably need to move out of sugar altogether. As it currently stands, most of the Guyanese sugar sector is also uncompetitive. Some of these sugar companies and sugar suppliers are running just on a cash cost basis, which means that they are managing to stay afloat but they cannot invest to maintain the competitiveness of their industries.

Before answering the question about what would be the most appropriate measures, let me take you through what the results have been from what has happened so far. After the 2006 reform, a €1.2 billion compensation package was put together for the sugar protocol countries. A lot of that went to a small handful of countries, and the results have been very mixed. The rates of disbursement have been very variable and there have not been very tangible results in many countries, with the exception of Mauritius, which has done quite a lot of restructuring and diversification and has moved quite a long way towards becoming competitive. From that experience, we need to highlight the fact that things just take time and that this is not unusual compared to many projects in these countries, in particular those funded by EU funds. Therefore, as we were just discussing beforehand, the targets that one might have hoped to have hit in year 1 would probably start to be reached only in year 3 or year 4. Given the experience of the measures that have been taken so far, we need to be realistic and say that we need to allow more time to see what will happen.

Those measures were grouped into three categories: first, competitiveness, or how to improve competitiveness within those countries where there is a possibility of becoming competitive—

Q9 Lord Giddens: Do you mean with further EU help?

Anna Locke: At the moment, some of these countries have not yet spent the funds that they were allocated under the first round, so there are still funds available for them to implement their current plans. I suggest that it would be good to revisit those plans to see whether they are still valid and to see whether lessons have been learnt from other countries, given that there was no time to do that when the measures were originally designed. Mauritius could provide a useful example: it has taken quite drastic measures to restructure its industry. There is still work that can be done to make some of these industries more competitive.

The second set of measures was directed at diversifying production within the sugar sector. For example, rather than just produce raw sugar, sugar producers were asked to look at adding value by installing refining capacity and diversifying into electricity generation or ethanol production. However, that is not purely under the control of the sugar industry in each country, as it would depend on Government policy to make electricity generation and ethanol production viable. Again, Mauritius has some quite nice examples of this: it has set up a deal with Südzucker to export up to 400,000 tonnes of refined sugar per year to the EU. Thus, Mauritius is adding value within its own sugar sector.

The third set of measures were about diversifying sales into different markets. Again, that might mean having different types of sugar, or it might mean looking more regionally instead of concentrating purely on the EU sugar market. However, for those countries that have no real future in sugar, there is a need to look at retraining, financing for diversification into other agricultural activities or providing social buffers for all the people who would become unemployed so that we support them in their transition.

Q10 Lord Giddens: Do you think that the EU should have a role in that, given that the EU is often blamed for having set up a skewed market that has adversely affected less developed countries?

Anna Locke: I would separate the two issues. If the EU can apply funds in addition to those that it is already providing through the European Development Fund, I would say that it has a good structure for doing that. Whether morally the EU should do that, I am not sure that we should mix the two issues.

Sheila Page: At the time of the first sugar programme, the EC explicitly made a link in its documents between helping European farmers to adjust to the new regime and helping non-European ACP farmers to do the same. The ACP farmers tend to believe that, if that was done for the European farmers, the commitment should also apply to them.

Another point to remember is that the three stages that Anna Locke mentioned are, in a sense, the way that these countries tend to think about it as well. By this time, probably more are coming round to thinking about the third stage, which is about how to move out of sugar altogether. That really does take time because, by definition, there is not yet an alternative private sector available that people can move into. It is going to take time, but a higher proportion of countries will probably do that in this round.

Q11 Baroness Howarth of Breckland: I am aware that we are straying into Lord Renton's question, but I think that we have got there, if he does not mind—

Lord Renton of Mount Harry: I forgive you.

Q12 Baroness Howarth of Breckland: I know that you say that it takes time, but it sounds to me as though nothing is happening in some places. The money is available, but it is not being used for capital investment in order to change the infrastructure. That may relate to the culture of the few countries that are in that box where nothing at all seems to have happened. Is it reasonable that everyone should just wait? I suppose that we are looking for some recommendations about what kind of intervention would actually make a difference.

Sheila Page: Deciding what to do and how to do it is not something that an external Government can do; the Government of each country—or the private sector in each country as the case may be—has to decide what it will do. And yes, it will take time.

Q13 Baroness Howarth of Breckland: If they are receiving subsidy or not using the subsidy that has been given, a decision has to be taken. You said very clearly that the current plans need to be revisited. I am still looking for that mechanism whereby the plans are revisited and the intervention happens alongside the Government of that country—I am not suggesting that the intervention should override the country's democracy or whatever might be in place—because otherwise the EU might as well withdraw.

Sheila Page: You have to remember that these countries could come back and say that the EU has taken 50 years to reform its own agriculture, so five years may not be all that long. However, given the fact that there are negative effects on all the other developing countries—we are not talking about those today, but the non-ACP countries have experienced negative effects from the EU's sugar policy since it began—postponing is not a zero-cost option. Postponing would be costly to the rest of the world, costly to the ACP countries because they are being held into an inefficient type of production and costly to the EU because it is paying for it. So while it is always tempting to make the adjustment slowly, I am afraid that I would take a different approach.

Q14 The Earl of Caithness: I have no interests to declare. Can I press you a bit more on Baroness Howarth's question? All of you have said that the reform is going to take more time. How long? Should there be a deadline? It is now six years. The €1.2 billion seems not to have been managed effectively, if at all. How much longer?

Sheila Page: In effect, the quotas system is being ended. Since 2001, there has been a commitment to remove import barriers for all ACP/LDC countries. That makes the original system unworkable. The Free Trade Agreements that have been signed or are in negotiation with some Latin American countries will make the system even less workable. The world price has changed. I am not sure what you mean by "How long?". It is happening. The EU price is now linked to the world price. Countries are now finding alternative markets or they are getting out of sugar. EU aid to those countries that receive EU aid will continue, because there is a commitment to provide that. Whether that aid is spent on sugar or on something else becomes a question of aid allocation.

Anna Locke: I would not want to be understood as saying that we should wait because it has taken time—that is not my point. I am saying that we should not expect that, just because it has not worked really effectively up till now, it will not work. We also need to look at the reasons why it has not worked: partly, it is to do with capacity within the Governments; partly, it is to do with capacity in the EU delegations. Having been in Mozambique when it was going through this process, I know that Mozambique never got its funds on time. Mozambique got a tiny volume (compared to other countries) of funds on time, and the administrative procedures associated with those actually cost more than the amount of money received. Furthermore, the funds did not target the issues that

Mozambique wanted to be targeted. I think that the EU delegations also need to get their act together.

The Chairman: We would like to know more about that. I am conscious of time today, but we would be very grateful for a note from you in some depth about that.

Does Lord Renton have a follow-up question?

Lord Renton of Mount Harry: Is it my turn?

The Chairman: Perhaps I should let Baroness Howarth ask first.

Baroness Howarth of Breckland: I will defer to Lord Renton, as this was supposed to be his question.

Q15 Lord Renton of Mount Harry: I am still a little confused by diagram 1 on page 1 of your document "The Impact of EU Sugar Policy Reform on Developing Countries". The diagram clearly shows that, over the past four years from September 2007 to September 2011, the price has gone up. I take it that the world price is represented by the line at the bottom of the graph and the EU price is represented by the line at the top. The world price has gone up from €200 per tonne to €500 per tonne, which apparently is 22 cents per pound according to your figures. Surely that must have made a tremendous difference to the ACP/LDC countries. Has it not?

Sheila Page: Yes. For those whose production costs are more than 20 cents per pound, the increased price may reduce their losses but it still leaves them at a loss. For those whose production costs are somewhere in the interval between those two prices, yes the increased price makes them profitable. However, the other thing that has happened is that the structure of sugar demand has changed—Anna Locke will be able to say more about this—because many of these countries are supplying their domestic and regional markets and the biofuel market. It is not just that the price has changed.

Anna Locke: I ask John Adams to provide some background information on how production costs have changed over those past years, particularly for ACP sugar producers. That may give a sense of whether they have been able to benefit from that.

John Adams: Certainly, some industries are more efficient and better able to benefit from the high level of world prices. For example, countries in southern Africa such as Zambia and Zimbabwe have traditionally been quite low-cost industries, but their costs have also risen markedly because, as Anna Locke has suggested, energy and fertiliser prices have increased over the same period. I am talking slightly from memory here, but I think that production costs in Brazil would have been perhaps 12 or 13 cents per pound in September 2007 whereas they are now more like 20 cents per pound. Moreover, Brazil is now moving production into land where the cost of production is 25 cents per pound.[4] Therefore, we need to take into account the fact that production costs have also risen.

Even though there are high prices, some of the ACP countries are located where there are no alternative regional markets that would allow them to benefit from those high prices. Finally, a lot of these industries are also in long-term contracts with the EU, which require them to provide a certain amount of sugar each year.

Q16 Lord Renton of Mount Harry: Is it your view, with the changes in the world and more and more African countries developing, that much more sugar will be required in the

[4] This land is less productive and located further away from the ports.

years ahead, and that that is one reason for looking for reform for the ACP/LDC countries? Is the picture in your mind one of a continuing growth in the demand for sugar?

John Adams: Absolutely yes. Global consumption and growth is approximately 3 million tonnes a year. In countries such as China and India, populations are expanding rapidly, incomes are increasing and tastes are growing more sophisticated. People are moving to cities and eating more and more sugar. So we certainly see fairly constant growth of some 2% in global consumption. In places such as Africa and India, the growth is at higher levels—3%. So there will certainly be continued demand in the years ahead. Other world industries are beginning to step up to the plate and to supply this additional demand.

Q17 Lord Renton of Mount Harry: Which will in turn help the ACP countries, will it not?

John Adams: It will help.

Q18 The Chairman: We have established that volume is increasing, but presumably, with the cost of inputs increasing, the margins are not going to increase enough to support domestic investment to keep participating in that. Do you see massive shifts, therefore, from certain high-cost producers to much more efficient scale producers? It is really a different question.

Sheila Page: Yes. Of course it is not only ACP producers. Certainly, sugar production within the EU increases as well as production in other areas. The structure is changing and it is very difficult, given how much intervention there has been in the past, to predict what will happen in a less intervened-in market.

Q19 Lord Lewis of Newnham: Are there any other parts of the world where sugar production is likely to occur where it is not happening at the moment. It strikes me that we seem to be talking about a static market, whereas, in fact, I can well anticipate that if you are considering expansion in Asia as a whole, it may be more appropriate to produce the sugar on a wider basis.

John Adams: There are already 120 countries in the world that produce sugar, so there are not too many other countries that could begin to produce sugar.

Q20 Lord Lewis of Newnham: But we are concerned here with only a relatively small group of those countries. You have only to have one of these other countries taking this into a much more economic range, and it can actually destroy completely the entire baseload that we are arguing about.

John Adams: That certainly could happen, but I would suggest that there are constraints, particularly in Asia, in there being suitable land for growing sugar cane.

Anna Locke: Also, there is competition from other commodities. Cereal prices have increased substantially, particularly in 2007-08 and 2010-11. Prices are projected to continue to rise, so we would need to look at sugar in the context of all the other options—even the competition between sugar production and ethanol production, depending on how the different biofuel polices progress, and how the oil price also develops.

Q21 The Earl of Courtown: I have just a very quick question on the practicalities of sugar production in different countries. How long does it take to start producing sugar cane, for example? I do not know the practicalities. How long after you sow, or whatever, can you start producing sugar?

John Adams: For sugar beet producers?

The Earl of Courtown: No, for sugar cane.

Lord Cameron of Dillington: Nine months?

Anna Locke: No, the first crop can be harvested in about 18 months.

John Adams: It varies between different countries.

Q22 Baroness Howarth of Breckland: The only interest that I have to declare is that I live in Breckland, which is full of sugar beet producers, but I do not have any interest in it, other than living in it—if you see what I mean. I want to come back to the issue of Europe, because we have already had some lobbying, if you like, from the British producers. It is clear that regardless of how the reform is managed, there will be some impact, even on our own and the European markets. How can this be managed to help the industry to move gradually from its present position into what the free-market position might well be?

We should remember that at one point we were net exporters, and the fact is that many people in the industry would say that they could produce a great deal more from sugar beet, given the opportunity in a free market. Yet, there seem to be real anxieties among refiners about the transition in relation to those world prices. How can that best be managed?

John Adams: It is a very difficult exercise. As you suggested, there are numerous stakeholders at the moment, including the beet producers, the refiners, and the ACP suppliers. It is very difficult to keep each one happy, in all honesty.

Q23 Baroness Howarth of Breckland: What do you think is the best way forward?

Sheila Page: A report was published yesterday as part of a G20 exercise by a group of all the major international institutions—from the International Monetary Fund through to the World Trade Organisation. There is a list of eight that I can give you. The report pointed out that the best way to raise agricultural productivity overall was to free the markets. If the sugar beet producers can produce competitively in a free market, that will be best for them also. If they cannot, we will find out. Just as one does not want to give the ACP countries an infinite amount of time to adjust—because if you have too much time to adjust you do not do so—the same argument holds at home. Yes, the market becomes more unpredictable than when there is the fixed flat price that the chart shows, but most other industries in Europe put up with unpredictable and changing markets.

Q24 Baroness Howarth of Breckland: Thinking about your previous evidence following Lord Renton's questions about the movement of sugar, if there is an increasing demand for sugar, as you say, and increasing costs that might have a difficulty as regards margins, why should a free market cause these sorts of problems?

Sheila Page: It should not.

The Chairman: Lord Renton, do you want to ask your question?

Q25 Lord Renton of Mount Harry: I was going to come to this later. I wanted to get down to the question of the current structure in this country. Perhaps I will do that now. Is it right to say that British Sugar has a monopoly on the making of sugar in this country? Is that a bad thing? Would it be better if it was not a monopoly?

John Adams: Possibly.

Q26 Lord Renton of Mount Harry: Be frank.

John Adams: It does not have a monopoly on all sugar consumed in this country. It owns all the sugar production sites, which account for approximately one-half of our demand for sugar each year. The remainder comes through the Thames Refinery. In that regard, it does not have the monopoly on our sugar supply. Yes, competition can always exist. The fact that all the EU beet producers are lobbying at the moment for retention of the status quo, to keep quotas in place, implies that they do not feel comfortable yet to compete on the world market. Production costs for sugar beet producers are typically higher than for sugar cane producers. They have to pay for their energy supply, which at the moment means high fuel prices. Cane producers do not have to do that. In the factories, they burn the gas that they get from the cane to fire their mills. At the moment, typically, cane sugar production costs are cheaper.

Q27 Lord Lewis of Newnham: That is including the other uses for it? You can use it in composting and various other things.

John Adams: Yes, taking into account the by-products that are produced.

Q28 Baroness Howarth of Breckland: Is that because of low wages? What are they?

John Adams: Yes, it is also in part because of slightly lower wages in the southern hemisphere countries, although those are now increasing quite rapidly. Beet producers are catching up in terms of production costs but primarily cane producers do not have to pay for the fuel to run their factories whereas beet producers do. At times such as now, fuel costs are quite a substantial outlay.

Q29 The Earl of Caithness: What is the differential?

Anna Locke: Between beet sugar and cane sugar production costs?

John Adams: I have some numbers here. In Brazil, you are looking at 20 or 21 cents per pound currently as a full production cost.

Q30 Baroness Howarth of Breckland: Chairman, perhaps since the witnesses have that written information, it would be very useful if they could send it to us.

The Chairman: Since you are on this, what is the UK cost per pound?

John Adams: The UK is the most cost-efficient producer in the EU. It has large factories which run for longer than other countries. It is about 22 cents or something like that. I have an average EU cost of 30 cents per pound.

Q31 The Chairman: Who has the highest cost in the EU?

John Adams: The majority of the Mediterranean countries in southern Europe.

Q32 The Chairman: Would you write to us with those costs? We would like to see that information. Rationally, are you saying that, if you were not worried about security of supply, apart from the UK a lot of this production would just move to more efficient providers and there is therefore a great distortion?

John Adams: Yes.

Q33 Lord Lewis of Newnham: Is beet production going down or up?

John Adams: At the moment, it is remaining relatively flat because the regulation dictates that they can produce only a certain amount.

Q34 The Chairman: Lord Renton, we have come round your question a number of ways.

Q35 Lord Renton of Mount Harry: This is a question about future reform with regard to the ACP/LDC countries. Do you feel that they are being well and properly treated at the moment? Is the impact of future reform something that worries them and should it be mitigated?

Sheila Page: It worries them. Any change worries countries. It does not worry some of them very much because they have alternative markets, such as the domestic market for some of them. Barbados has been trying to move out of sugar for years. It is moving out of sugar and is not the sort of country that you would expect to concentrate on sugar now. Some are worried even without reform. Guyana is producing at costs above anything that it can get even now. It will create the chance of volatility for all of them because the quota system for those who are within it—the EU and the ACP—provides security, in the past of price but still of quantity. For the rest of the world, it increases insecurity because, if you cut off one part of the market and protect that from fluctuations, whatever fluctuations are happening in the world will be concentrated elsewhere. It has been a guarded area of low fluctuations which makes life not necessarily profitable but a bit easier. Most of them will survive and can see how they will survive either by changing their sugar, their markets or what they are producing.

Q36 Lord Renton of Mount Harry: You mentioned Brazil, but of course one now thinks of Brazil in a totally different context as one of the five very large expanding countries, particularly in South America. One would get the feeling that sugar is less important to Brazil now than it would have been before. Is that fair?

Sheila Page: I do not have the numbers for Brazil's trade. Yes, it is less important, in the sense that sugar becomes less important in any country that diversifies. We saw the same thing with bananas in the Caribbean before sugar. The countries that moved from bananas to tourism have done quite well. They still produce some bananas but they are not totally dependent on them any more. The same is happening with sugar. The first thing that you tell any developing country when you work in development is, "Diversify, diversify, diversify".

Q37 Lord Giddens: I think that Brazil was a special case because of the use of sugar for ethanol that goes back such a long time. After all, that is a defining feature of Brazil's energy system.

John Adams: They have a massive increase in their flex-fuel car fleet which runs on ethanol, so sugar cane is very important for Brazil.

Anna Locke: Also, I think that when you look at Brazil you have to look locally because the vast majority of sugar cane production is concentrated in São Paulo state. Although at a country level it might not look like changes have a huge impact, at a provincial level they can have a quite substantial impact. We talk about Brazil but for the ACP/LDC suppliers that is also very important. Sheila made the point at the beginning that production costs can be quite different within countries. Something that might be okay at a country level for the average cost of production can have a marked impact at a more localised level where often sugar production is the major source of employment. We have to be quite careful to be context specific.

Q38 Baroness Howarth of Breckland: On the impact on the population that you indicated, one of the things that you say in your paper is that some producers provide social care of one form or another. You say that 200,000 people may be affected. That may be a small proportion, but a lot of people may be driven into a different level of poverty. Can you see any way in which the EU money that has not been used could help with that part of the transition, because that is something that you have not covered?

Sheila Page: One of the original accepted spending aspects of the first EU plan was social safety nets, precisely for the reason that for some people when production ends there is no immediate alternative. Again, that is something that most of these countries are trying to build up anyway, so using some of the money for sugar that they may get to improve their position is certainly an acceptable way, and probably one of the better ways, of doing it because it does not distort the market, as choosing a particular industry might do.

Anna Locke: Also, perhaps one needs to think about retraining. It is a difficult question, because you do not necessarily know what kind of training you need, and often a lot of the people who work in sugar states, particularly the seasonal workers, have very low levels of skills. It is hard for them to switch from one activity to another. There is an interesting experience in Brazil, which operates at a different level. It is mechanising sugar cane harvesting there and is retraining the sugar cane cutters to service and maintain the machines. It looks from the outside to be a wonderful scheme, but I have not looked at it closely enough to see whether it is achieving everything that is claimed for it. However, it is an interesting model to look at.

The Chairman: I am conscious that we still have three more questions and a limited amount of time.

Q39 The Earl of Courtown: I will be brief. We have been looking at diversification, retraining and the social safety nets you were mentioning. This must involve some sort of institutional co-operation in Europe and member states. Are you aware of this co-operation between the European Commission’s agriculture and development directorates-general on this subject? How much is there and should there be more?

Sheila Page: Yes, there should be more, if I can perhaps start with your final question. From outside, it looks limited. When we first started working on what the effects of the reforms would be, we found it difficult to find out from any one of the DGs whom we should talk to in any of the other DGs—so there is a practical question. There was no attempt when the reforms were proposed to test them against the development DGs or to ask them to do assessments. At the policy level, there is relatively little co-ordination. On the ground, there are EC offices in these countries, which are supposed to co-ordinate everything.

Q40 The Earl of Courtown: Is that one of the reasons why the disbursements are not getting around? I did not mention this, but I should add that I have no interests to declare.

Sheila Page: The general problem of all EU aid, as Anna Locke said, is that it tends to be slower to disburse than UK aid, for example. Is it therefore done better or not? You would have to—

Q41 The Earl of Courtown: What about individual member states?

Sheila Page: Individual member states have generally taken the view that there is an EU programme of adjustment assistance and they therefore do not need to do it, so they carry on with their own aid programmes regardless. It is normally considered to be the responsibility of each developing country to try to co-ordinate the aid that it is given. Some of them do it extremely effectively, and some do not. As Anna Locke said, it is actually a difficult exercise because, as she said, administering the EU aid takes a lot of time, but the EU is only one of many actors.

Anna Locke: The evaluation report that was one of the main sources of my evaluation of the impact of the accompanying measures was quite critical of the EC delegations and there was a discussion of problems of capacity at the EC-delegation level. But, to be fair to the delegations, because of the extremely pressured timeframe that they were facing, they did not have the capacity to deal with the issue. It is usually the case that one person in the EC delegation, who is dealing with lots of other things, may have no knowledge of the sugar industry, and suddenly they have to deal with it. In the same way that some of the recipient countries need time to plan and implement, the EC delegations need to do so also, to ensure sufficient co-ordination. However, I would be concerned about a proposal that different member states should then do it, because the recipient countries already have to deal with many donors, and there are people who spend all their time just trying to co-ordinate. That might make it worse.

Q42 Baroness Parminter: There have been several years of reform of the EU beet sugar and cane refining industry. Have those changes made a positive or any impact on the ACP/LDC countries? In the past there have been complaints that countries were locked into refinery deals. Has it made any improvement because that has been reformed?

Anna Locke: In some sense, yes. More refining capacity has been established so there have been more alternatives as a result. Again, that may not be the sugar regime reform in itself. Sorry, let me back-track. Reducing EU sugar production and increasing the EU's need for sugar imports has created greater competition for imports of raw sugar. That has enabled the sugar suppliers to negotiate better deals with refiners. Although they have in general had long-term contracts with Tate and Lyle, they have renegotiated those deals. So it has made that better as it has given them the opportunity to have a better deal.

John Adams: Perhaps unintentionally so. As a result of the first round of reforms, the EU became a net importer of some 3.5 million tonnes. It was expected that ACP/LDC countries would provide around 2.1 million tonnes of that but that has not materialised, for various reasons from weather affecting their respective crops to the primary reason that world prices have been high and that has attracted their sugar to other destinations. As a result, EU prices for sugar have increased to historically high levels. As you can see from diagram 1 in our paper, the latest price was €700 per tonne. As a result of that, ACP industries have been able to benefit by selling their sugar at a higher price.

Q43 Lord Renton of Mount Harry: Did you say €700?

John Adams: Yes, that is the current average EU price quoted by the Commission. Prices for spot sugar tonnages are even higher than that. So they have benefited in the short-term through that, but that was not the intention of the reform.

Q44 Lord Cameron of Dillington: First, just so that I am absolutely clear, are you in favour of the proposed EU reforms? If you are and there is probably going to be a lead-in time, how long should it be? You are in favour of the proposed EU reforms and abolition of quotas?

Sheila Page: Yes.

Anna Locke: We may have slightly different views on it, which is very normal in the research community. I have some concern about the variability.

Lord Cameron of Dillington: The volatility of the price?

Anna Locke: Yes and about the possibility of going to low sugar prices. I would like to be able to see what the evolution of the production costs in supplying countries has been in relation to the world prices, to see whether they really have managed to get higher margins and greater profits from that. However, I think that the original EU sugar reform has worked to the benefit of the ACP countries. As John Adams said, that may have been unintentional. If you look at that diagram, the reference price is way below what actual prices have been. If it had worked as intended, they would have been quite hard hit. I am concerned about the level of uncertainty, but there have definitely been benefits from increased competition and flexibility.

Q45 Lord Cameron of Dillington: Dr Page, you remarked that if a country or industry is given too much time to adjust, it does not.

Sheila Page: Yes. That is true.

Q46 Lord Cameron of Dillington: Presumably you are in favour of a very short lead-in time.

Sheila Page: Yes, because it is not all that short. It was announced some time ago, we are talking about 2015 and that is not short in terms of the production cycle of sugar. It is not as if you are talking about growing hardwood trees where three or four years might seem short. The other point to make is that I do not really think that the price is likely to be under pressure in the next few years, for all the reasons that John Adams has given. Unless we are talking about postponing the scheme for 20 years to avoid all possible uncertainties, I do not think the sugar price should constrain us.

Q47 Lord Cameron of Dillington: Coming back to my official question about the influence of DG Development over DG Agriculture and the reform of the CAP, are they co-operating enough? Should they co-operate more? How does DG Development develop a policy that is complementary and coherent with the CAP reform?

Sheila Page: It is definitely that way around. There is no way that DG Agriculture consults Development in advance. Development effectively has to work with it. It treated the documents as we did, simply as something that came out for it to deal with. There should be coherence on this because the Lisbon Treaty requires that all measures of the EC should take account of the effects on development, but this is done at the moment in biennial *ex post* reviews. It is not done through impact assessments in advance. Therefore, you may be able to find out in two or four years' time whether the policy was coherent but there is no mechanism at the moment to prevent it from being incoherent.

Q48 Lord Cameron of Dillington: Should DG Development and Cooperation focus more on diversifying the agriculture of the least developed countries into other forms of production and food? The World Bank is saying that the African urban food market will increase by three or four times by 2030. There must be huge potential there to diversify and cash in on that growth.

Sheila Page: Yes, in some countries and areas, completely. I mentioned tourism in the Caribbean and there is manufacturing processing between India and East Africa. Yes, there are all sorts of interesting possible ways for different countries to act, diversifying out of the traditional CAP-controlled products.

Q49 Lord Lewis of Newnham: Can I just refer to a point that Lord Giddens made about Brazil? The motivation in Brazil for its production of cane sugar, if I understand it correctly, was primarily motivated towards ethanol production for motor cars and so on. We are now going into a stage where 10% of fuel in this country for car driving and so on will be ethanol. Is this likely to influence the price and production? I am not quite clear how much is actually used, but if one looks at the situation of fuel for vehicles, that is quite a significant factor. Will this make much difference to the production line?

Sheila Page: It depends on what happens to the import duty and whether we have to produce it within the EU, which would be more inefficient, or import it from outside.

Anna Locke: We discussed this with Brazil about a month ago in a round-table discussion. Brazil made the point that Sheila Page made, which was that at the current tariff it is not interesting for Brazil to supply the EU. It would much prefer to supply the US, which has not only removed the tariff on imports but gives Brazil a premium because the US classifies ethanol as an advanced biofuel. In addition, Brazil is much more concerned with its own domestic market: it has moved from a situation where it had an excess supply of ethanol to one where it is going to be struggling to meet domestic demand. We looked at the demand for ethanol in the EU initially as a great opportunity for bringing in cheaper ethanol from developing countries. The reality is that until 2020 almost all the EU supply will be met by domestic production, which, aside from being less competitive than it could be in tropical countries, is less efficient than sugar cane in terms of life-cycle analysis and greenhouse gas emission reduction.

Lord Lewis of Newnham: Oh yes.

Anna Locke: Up to 2020, the possibility of developing countries stepping up to meet the EU's domestic needs is very small. We have discussed the question of how much time it takes to get things going. Although the production cycle of sugar cane is that you plant it and that more or less 18 months later you can harvest it, in reality it takes a very long time to get it going. In Mozambique, which is where I have the most detailed knowledge, with an existing structure for the sugar industry, it probably took about 10 years to really get it going—and that involved very well established sugar producers. Ethanol production has not got going and I would therefore anticipate that it would take quite a while to get ethanol production going at any reasonable scale in the countries that could most competitively supply it.

Q50 Lord Lewis of Newnham: There is a big difference because the Brazilian use of ethanol is 80%, which of course involves a completely different design of motor car and engine structure than the method that we are talking about, for which the figure is 10%. Any figure up to 10% can be added with a certain degree of ease. I am interested to know whether that is going to make an immediate impact. I should have thought that that would make a much greater immediate impact than in the Brazilian situation.

Anna Locke: Correct me if I have not understood your question properly, but I think that because of the domestic production capacity within the EU, domestic ethanol needs will be met mainly through production of ethanol from wheat at a figure of 9.5% or 10% of fuel consumption.

Q51 The Earl of Caithness: Can I just ask for your opinion on two countries—China and India? Do you think that the change of diet in those countries will have an impact on sugar, and will the economic activities of China change the background to the picture, such as in Barbados?

John Adams: I certainly think that there is a change in the economics, with rural communities moving to the cities, where tastes are more sophisticated and people eat products such as more easily-prepared and ready meals, in which there are more sugar. Yes, the rate of growth in China is potentially high, looking ahead. There is also a huge growth in alternative sweeteners in China that will cut some of that increase in sugar demand. There has also been significant growth there in High Fructose Corn Syrup (HFCS) corn sweeteners, and it is a similar story in India.[5] We expect demand to increase to above the world average, but, at the same time, demand in areas such as the EU and the US is relatively flat. Per capita consumption reaches a certain level and then, perhaps with higher incomes, you realise that eating lots and lots of sugar is not quite so good for you. That offsets some of the growth we see in other economies.

The Chairman: Well, thank you very much. That has been very thought provoking and we are very grateful for your time.

[5] Demand is projected to be strong in India but as the world's second largest producer, it should be able to supply that growth in the near term.

National Farmers' Union (NFU)—(QQ 72-87)

Evidence Session No. 3 *Heard in Public.* *Questions 72 - 87*

WEDNESDAY 20 JUNE 2012

Members present

The Earl of Caithness
Lord Cameron of Dillington
Lord Carter of Coles (Chairman)
Baroness Howarth of Breckland
Lord Lewis of Newnham
Lord Maclennan of Rogart
Baroness Parminter
Lord Renton of Mount Harry
Lord Whitty

Examination of Witnesses

William Martin, Chairman, National Farmers' Union Sugar Board, and **Gail Soutar**, Senior CAP and International Affairs Adviser, National Farmers' Union

Q72 The Chairman: Mr Martin, welcome. Thank you very much. Gail Soutar, welcome to you as well. We are very grateful to you for coming here today. I have to re-do the formalities so, if you could bear with us, that would be helpful. I hope you have before you a list of interests that have been declared by Committee Members. This is a formal evidence-taking session of the Committee. We are having full shorthand notes taken, and they of course go on the public record in printed form and on the parliamentary website. We will send you a copy of the transcript, and you will be able to revise it in terms of minor errors. This session is on the record; it is being webcast live and will be subsequently available on the parliamentary website.

If I could start with the first question, a good place to start would be the impact of the last reform. Turning to the 2006 reform, how has that affected the beet-growing industry in the UK, in terms of three things: jobs, profitability and the issue of price and risk management? If you could break down the effects, what do you attribute the changes to and what are the strengths and weaknesses of the 2006 reform? I would be very keen on the emphasis on the latter: what are the weaknesses of it?

William Martin: Thank you very much, my Lord Chairman, and good morning. I have a brief comment, if I may, before I start to clarify the position that I occupy and why it is me who is here, as it were. I am a sugar beet farmer. I represent the 3,500 farmers in the UK who grow sugar beet and who sell sugar beet to British Sugar, the single processor of sugar beet in the UK. I am elected on an annual basis by those farmers to represent their interests. I know we are going to talk more about the details of the arrangement between us and British Sugar, but I thought it would be helpful to clarify that before I start.

In answer to your question, there are a number of things that have happened since 2006 in our industry. Before I enumerate one or two of them, it is worth saying that not all the things that have happened since 2006 can be directly attributed to the 2006 reform. There are some things that would have happened anyway. We need to be quite careful in not attributing things that are not a result of that reform and pretending they were. Certainly in the UK we now produce less sugar beet than we did before the reform; we have fewer growers producing it and we therefore produce less sugar. Some of that was the natural process of the less efficient growers leaving the industry. The reform process in 2006 certainly accelerated that but, in the UK, we went further than that, and we were also effectively obliged to close, as well as one inefficient factory in the west of the country, a relatively efficient factory in York. It was not a decision taken by the growers; all the decision-making power at that time was vested in the processor. They will have to speak for themselves as to what they would think, with hindsight, but certainly as a grower and representative of growers in that area, with the way things have developed since then, it is a shame that the York factory has closed and that we do not now have that extra potential to produce sugar beet and sugar in the UK, particularly with the way the market has changed and the way it perhaps looks as though it is going to be in the future.

We are overall now more efficient than we were. We are growing higher yields of sugar beet on farm than we were, but how much of that is directly attributable to 2006 and how much of that is part of normal progress? One of the things that we will talk about later, I am sure, is the way in which our industry has succeeded in continuing to invest in productivity and continues to do so, and why I think there is room for optimism about our sector in the long term.

Regarding specific strengths and weaknesses of the reform in 2006, I think a weakness was that it was based on a very particular view of the future. It was based on a view that said, effectively: sugar beet production is always likely to be less effective than cane production and we have provided a protected market for European beet sugar in the past; we have taken some steps through the "Everything But Arms" agreement to allow cane producers greater access to our market; that is inevitably going to lead to oversupply in the future if we do not do something; and the "something" was to produce less ourselves. I think that the idea of encouraging inefficient non-cost-effective producers to stop was a good one. Where it went wrong was in going too far, and effectively obliging those of us who were relatively efficient also to reduce our production, on the basis that we could never hope to compete and that we were going to be swamped by cane imports before too long. I think that the long-term picture for our industry is more optimistic than that. In the long term, we have an industry that will be able to compete, albeit not in 2015. However, if we continue the rate of progress we are making and continue to have the kind of stable market that Mr Newton has been talking about for a longer period—and we suggest 2020, as you know—by that time there is a very good prospect of our having an industry that actually can compete with a wide range of people, including cane production. That to me is the goal we should not be losing sight of.

Q73 The Chairman: Are you going to explain to us why you can do that?

William Martin: Certainly.

The Chairman: How are you going to get from now to then?

William Martin: Effectively there are two aspects to overall cost of production. There is the farm aspect and the processing aspect. On farm, the main thing is about increasing field yields of sugar beet and, therefore, of sugar. We have seen ongoing annual compound increases in yield of sugar beet of 2 per cent plus for many years now. Our yields are now at a level where they are better than or, at the very least, equal to the best cane-producing countries in the world, in terms of our sugar output per hectare. We and the processor are continuing to invest through our jointly funded research organisation, and we have set ourselves a challenge of actually increasing that rate of increase. We are aiming to increase our yields by 4 per cent annually over the period to come. I do not know if we shall necessarily achieve that but, if you do not set yourself a target, you have no prospect of reaching it. On farm, we believe that there is a considerable further increase that we can achieve in yields and field productivity. The other side of it is the processing efficiency. That is really more British Sugar's area than mine, obviously, but that is why I have considerable optimism that, certainly on the farm side, we can deliver that productivity if we are given the time to invest to do so.

Q74 Lord Lewis of Newnham: I think you have partly answered my question, but I will pose it to you. It is quite clear that the Commission's proposal for sugar in the CAP reform package is a factor that is of concern to you but, returning to this point about the beet industry's need for more time to adapt to the proposals by the Commission, if a longer transition period is negotiated, how would you like to see it managed and why do you propose a five-year period? I think you are improving your yields. Is this because of technique, sampling or research coming in? What is the causation of this particular increase?

William Martin: It is because of research and the application of that research. The biggest single factor has been plant breeding and the improvement in genetic performance of the varieties of sugar beet that we are growing. The other thing that we have been very successful at, as a sector in agriculture, is the rapid uptake by our growers of improved techniques in the findings of research. We have annual open days on farm for sugar beet growers. We get a very high percentage of sugar beet growers attending these events, so we have a very good record of taking up new techniques and improved techniques as they are delivered, but the main bit is probably around genetics and plant breeding in the past.

There is nothing magic about 2020 itself. It is trying to be realistic about how long it can take us to get where we are going, if we keep going at the same sort of rate. It might be worth and it might be helpful, Lord Chairman, if I set out where I see the longer term in this. What I do not want is to give the impression that I am hoping I can persuade everybody that, actually, phew, we have seen off this reform for another five years and so we can prepare for another round of these kinds of conversations in a further five years' time, so let us see how long we can keep this circus going. I am very optimistic that, by 2020, we can stand on our own two feet. Frankly, I would go further and say that, by 2020, if we cannot, well it is probably time to think about something different.

Why do I think that we need longer than elements in the Commission imagined was going to be the case in 2006? That is really about the changed world situation and the changes in production ability and costs around the world. We have talked about Brazil already, and there is no doubt that Brazil remains today a lower-cost producer than we are, but their costs are increasing for well-documented reasons to do with labour costs, currency, yields and so on. It might not have seemed realistic 10 years ago, or even five or six years ago, to hope that we could get there. It now is realistic. If you have, as I believe the European Union has, a long-term aspiration to use the policy that we have to deliver competitive industries, both within the EU and within some of the traditional supplying nations that Mr Newton has been talking about, we can effectively stop having to nanny them in quite the same way, because they can then stand on their own two feet. It does seem to be a legitimate use of the EU market management tools to provide an industry within the EU with the time to provide the growth, jobs and general prosperity that could come from having a globally competitive industry.

Q75 Baroness Howarth of Breckland: You realise from where I come that, although I do not have a direct interest to declare, I know an awful lot of people who work in the sugar beet industry in one form or another, so I thought I should just say that. I know the factories quite well, as distant and sweet smelling. I just feel I should have declared that.

I am very interested in the interprofessional agreement (IPA), which is a very interesting model, as far as I am concerned. From the documentation you sent us, it is clear that you put a great deal of value on this agreement. I wonder if you could just explain the benefits of it in the UK and whether there are any similar models elsewhere, particularly in the EU but anywhere else, particularly in relation to the work that the Commission is dealing with. How would you like to see the proposal from the Commission amended and how would the IPA be affected by that?

William Martin: There are two parts to that question. Perhaps I will take the second part first, it being relatively simple. The Commission's proposal removes our current legislative protection for these kinds of negotiating arrangements. I will talk in more detail in a moment about how that works and what it represents. They remove the legislative protection for those agreements, and they place the responsibility for allowing them to continue under a delegated act. To me, that signals that they regard this as being of secondary importance and that, at some stage in the future, if they think it is no longer important, they can just strike it out. I regard that as a very severe threat to our long-term ability to continue to have these agreements. That is the second bit; that is what I would like to see changed. I would like to see that legislative protection reinforced in the long term, rather than being undermined.

Why? What do these agreements represent? What is the importance? The starting point is where I began with my opening remarks: I represent 3,500 relatively small businesses selling sugar beet to the only customer that exists in the UK—a single processor. That is an obvious imbalance of power in the supply chain. We have seen the impacts of that in other agricultural sectors over the years and we are still seeing them. We are explicitly protected from the impact of competition policy, and we are allowed to negotiate collectively as a single body. The NFU carries out that function. Defra formally appoints us to do so, but we carry out that function on behalf of those growers, so effectively there is a single selling voice balancing that single buying voice in the supply chain. That is the starting point.

That is the bit that gives us that collective strength, but it is worth developing that a little further, because this is not just about legalising a cosy cartel, which allows us and British Sugar to disappear off into a darkened room and put up the price of sugar. The first thing is this does not affect the price of sugar at all. The price of sugar, as I am sure British Sugar will tell you, is a function of the European marketplace. Whatever price they do or do not have to pay me for beet, they are not necessarily able to translate straight through into the sugar price. What it does do is allow those farmers to negotiate a fair price for their sugar beet, rather than having what might otherwise be an unfair price imposed. More importantly than that, it allows us to work together with the processor to propel the industry forward more rapidly than might otherwise be the case.

If I can just take one example, some of you will perhaps be aware that, 18 months ago in very severe cold weather, we lost quite a lot of sugar beet in the UK. We lost in the region of 1 million tonnes of sugar beet to frost. Growers had no protection against that and growers received no compensation, although they felt very strongly that it arose as a result of decisions taken by the processor to prolong our campaigns, our processing seasons. Since then, by working together with British Sugar, we were able to announce last week to growers that, in future, not only have we improved the premium payments for sugar beet that are delivered late, we have also begun and almost concluded work to put in place a frost insurance package so that, if beet is lost, there will be some kind of comeback. That is the kind of thing that we can do by working collectively. If we were not allowed to do that, it would not just be about our prices; it would be about that kind of progress as well.

How far into Europe does this operate? There are several other member states where there are also farmers selling to a single privately owned processor. Quite a lot of European sugar protection is in the hands of co-operatives, and obviously the situation there is different but, in countries like Sweden and Denmark, and in parts of Germany and Austria, those farmers have no choice but to sell to a single privately owned processor, and so the same kind of arrangement exists. I would venture to suggest that ours is as forward looking as any of them, but I suppose I would say that. The kind of pricing mechanism we have in place has guaranteed, both to us and our processor, stability and transparency of price and, therefore, of supply, in a way that enables us to work for the future.

Q76 Baroness Howarth of Breckland: If you did not have this partnership and the market was more open across Europe, if this changes in the next review, will that leave your market open to much more competition with other European markets?

William Martin: Realistically, the market for beet is not susceptible to much competition, because it is such a bulky product that the transport of it across borders is, frankly, likely to be uneconomic. It is about how much sugar beet and, therefore, sugar we can produce in the UK, which is where we come back to where we started about the frustrations about the 2006 reform curtailing our production capacity, on the basis that we were going to be swamped by imports. If we now seem to be moving to an era where the world sugar market is going to be tighter, where there is increased demand and not so much production, and the EU is going to be looking to be more self-sufficient than it thought it would have to be, we in the UK are currently less able to take our full share of that than we would have been. If we are given time, then we can hope to work with our processor to perhaps increase again the capacity for producing sugar in the UK. The York factory will not reopen, but they might be able to make investments in the throughput of the existing factories. Last season, for example, we had to slow down a couple of the factories because they ran out of storage space for sugar. There are things that could be done to allow us, in the longer term, to take a greater share of our market.

Q77 Lord Renton of Mount Harry: Could I just declare an interest, in that I also have a lot of insurance with the NFU? I wanted to just mention that. Talking as a farmer, if I may, we hear very much from you about how you are going to increase the tonnage you can produce per acre and so forth, but what about the demand for the product? Do you see continuing growth throughout the world in the demand for chocolate, for example? That side of things somehow seems very rarely to come up in these discussions.

William Martin: Everything that I see leads me to believe that, overall, the demand for sugar in the world will continue to increase. There is a range of figures between 2 million and 3 million tonnes annually.

Q78 Lord Renton of Mount Harry: Are more people eating chocolate?

William Martin: It is not so much chocolate, with respect to you, Lord Chairman. It is more about developing countries, where actually sugar is a very efficient way of getting calories into an underfed population. As those countries start to become a little bit wealthier, sugar is one of the first things that they start to buy more. In a way, all of us probably ought to be eating less and all that sort of stuff, but, collectively in some of those poorer countries, sugar is a very valuable calorie-rich part of the diet. That is seen as increasing.

What is the implication of that for us? It is likely, if we move beyond 2020 to a situation where the European market is freer and more open, we are going to be operating more at world market levels. We can have a debate about whether that is or is not a desirable thing in terms of the volatility to which it subjects the European consumer in the longer term, but that is not the subject of today's discussion, I know. I think it is therefore almost inevitable that some of the cane suppliers, which might have been eyeing up the European market in times gone by, will see equally valuable markets closer to home. Therefore, the opportunity for European beet sugar production to supply a greater proportion of the European demand will emerge, and that is where our short and medium-term growth comes from: an increased ability to supply our own market, rather than exports.

Q79 Lord Renton of Mount Harry: I rather hoped that is what you would say, because obviously one thinks that, as some African countries, for example, grow, GDP gets bigger and so forth, use of sugar, in one way or another in those countries, would get larger. This is really what you are saying too, and one of the reasons why you expect that, if you do go on increasing your own yield by 4 per cent per annum, you are not going to have difficulty in selling.

William Martin: That is right—exactly. The outlook is reasonably bullish.

Q80 The Earl of Caithness: The first question is: you are fairly bullish about UK sugar; how does the UK position relate to the rest of Europe and how does the rest of Europe view this proposal from the Commission, in particular the French?

William Martin: The reaction that I am giving to you is pretty typical of the reaction of my colleagues across Europe. The French, for example, have just set off on a very ambitious plant-breeding activity to try to decode the sugar beet genome, again with the aim of increasing the rate of genetic progress there. We all see ourselves on a path to global competitiveness, but that it is going to take us until 2020 to get there. There are some parts of Europe that, frankly, will struggle to catch up. The majority of those where the sugar beet is now grown, northern and western Europe—us, the French, the Danes, the Dutch, the Germans and so on—would have a very similar view on it.

Q81 The Earl of Caithness: Are their costs the same as ours or is it more expensive for them?

William Martin: It varies from country to country. To take one example of the French, their farm yields are higher than ours, so their beet cost of production is probably a bit lower than ours, but their processing is less efficient than ours. They have more factories producing a smaller amount of sugar, so their processing costs are probably greater than ours, so it probably evens out roughly. We, the French and one or two others are in the front rank. There are one or two other countries that are in the second rank but stand a good chance of making it. There are some others that are lower down the scale, which are going to struggle.

Q82 The Earl of Caithness: If you could have your wish of three things that you wanted in the proposed reforms, what would they be?

William Martin: The first would be a guarantee that our collective negotiation rights would remain unthreatened for as long as there is a single buyer. I want to be sure that we can also be represented by a single seller to keep that balance in the supply chain. The second would be that we are given the stability until 2020 to complete our path to global competitiveness. The third would be that, in the mean time, and this is perhaps where we have talked about transition, the Commission in Brussels exercises the tools that they currently have available to them rather better than they have done over the last two years. We have talked about a market that is short; I do not actually believe the European market is short. If you look at the statistics, at the end of the year there is more sugar in stock than there was at the beginning of the year. The problem is the timing of when that sugar is released on to the market by the Commission; because of the delay, some of the people in the market think it might be going to be short and react accordingly. I would ask for the Commission to play their part and keep the thing more stable until we get there.

Q83 Lord Whitty: There are just a couple of other aspects of demand, with which you were dealing with Lord Renton. We are talking largely about sugar for food, but there was an expectation that there would be a significant growth in sugar for bioethanol. Are you yet seeing that in any significant degree? If not, is that a delayed start or would you see it playing a larger part beyond 2015-2020?

William Martin: There is an increased amount of sugar going into bioethanol. There is one plant in the UK, as I am sure you are aware. There are discussions, from time to time, about whether another one would be appropriate or not. Part of the problem is the same difficulty that you have with biofuel projects across most of the world, which is that they tend to rely upon government support and regulation, in one way or another. There continues to be uncertainty about the regulatory framework within which anybody investing in biofuel production would have to operate. I think that is why you are probably seeing more caution than we might have expected from some of those required to make those big investments, because they are less certain than they were about the ongoing direction of travel and the ongoing support for biofuels. The bottom line is that, at the moment, there is virtually nowhere in the world where biofuel production actually stands on its own two feet economically without some kind of regulatory support, be it price support or inclusion mandates.

Q84 Lord Whitty: The other part was: have you seen any significant effects from growing health concerns about sugar in the European market, and the British market in particular?

William Martin: It is a continuing backdrop. As you would expect, my position is that there is nothing wrong with sugar as such. It is inappropriate inclusion rates of sugar in a diet that is the problem. As I mentioned earlier on, there are parts of the world where that is clearly not a problem, and I do not think that we should allow ourselves to be sidetracked unduly by those concerns.

Q85 Lord Cameron of Dillington: I just have a slight problem here, because you are saying that you want to keep quota for five years, so that you can get your house in order and become more competitive with cane sugar producers, while Mr Newton was saying he wanted five more years so that he could get his business in order, so he could become more competitive on the world marketplace. Discuss. Surely if you did away with the five years, both of you would be in the same position.

William Martin: I can understand that being the perception of what we are saying. I think what we are both trying to say is that the European Union has an opportunity to allow both our industry and the industries that he represents to ready themselves for competition on a global market by allowing us some stability and protection until then. At the end of that time, we are not going to be fighting with each other for a European market. Actually, some of these other people may be going out into the big wide world. The European Union, almost as an aid activity as well as a trade activity, will have allowed them the time, through the accompanying measures and access to a stable market, to make the investments necessary to stand on their own two feet thereafter. There is some coherence behind it.

Q86 Baroness Howarth of Breckland: I am still struggling to see where you see there should be controls and where there should be greater freedom. You have just described common market behaviour that is seriously interfering with the market in terms of storage, release and the quotas. Surely if there were a freer market in Europe, the market would take care of that and you would not find yourself criticising the Union for not getting its bureaucratic programme right. What would you see as the answer to that?

William Martin: The answer is that, if we were immediately subjected to the vagaries of the world market and were no longer relying upon the European Commission to manage the market for us, we would be subjected to much greater volatility than is currently the case, and the opportunity that exists for us, as an industry, to make the investments for the longer term to provide for domestic growth, jobs and longer-term competitiveness would risk being lost. It is that stability and protection that gives us the opportunity to invest for the longer term. If we were forced to deal with volatility now, we would be more likely to retrench. I certainly cannot see capacity expanding, because I cannot see investments being made to expand that capacity. You are much more likely to see retrenchment and, as I say, the possibility that the European Union could grow its sugar production in the long term.

Q87 Baroness Howarth of Breckland: I have heard you make that argument very clearly, but what about the short-term problem? What do you say to the European Union about the short-term problem?

William Martin: What I say to the European Union about the short-term problem is, "You have the tools available to you. Please use them in a timely way." For reasons I do not fully understand, they have been reluctant to use them in a timely way, whether it is because they are trying to demonstrate that the current system is broken because they want everybody to sign up to their vision of a new system, I do not quite know; perhaps that is too cynical of me.

Baroness Howarth of Breckland: It is worth saying.

William Martin: That is what I would ask them to do. Just do their job better while we are doing our job better. In a certain period of time, we can all move on.

The Chairman: Mr Martin, Gail Soutar, thank you very much. We appreciate your evidence.

Overseas Development Institute (ODI) and LMC International—Oral evidence (QQ 1-51)

Transcript to be found under LMC International and Overseas Development Institute (ODI)

Tate & Lyle Sugars—Oral evidence (QQ 156-201)

Evidence Session No. 6. *Heard in Public.* *Questions 156 - 201*

WEDNESDAY 27 JUNE 2012

Members present

The Earl of Caithness
Lord Carter of Coles (Chairman)
Lord Giddens
Baroness Howarth of Breckland
Lord Lewis of Newnham
Baroness Parminter
Lord Renton of Mount Harry
Lord Whitty

Examination of Witnesses

Ian Bacon, President, Tate & Lyle Sugars, and **Gerald Mason**, Vice President, EU Affairs and Strategy, Tate & Lyle Sugars

Q156 The Chairman: Mr Bacon, Mr Mason, good morning and thank you for joining us today. You heard me do this before, but I have to do it again, which is the formalities. You should have before you a list of interests that have been declared by Committee members. This is a formal evidence-taking session of this Committee. A full shorthand note will be taken. Obviously, this will go on the public record in printed form and on the parliamentary website. We will send a copy of the transcript to you and you will be able to revise it in terms of minor errors. The session is on the record. It is being webcast live and will subsequently be available on the parliamentary website. Would you like to make a few comments to set the scene or go straight to questions?

Ian Bacon: I would like to make a few comments, if I may. My Lord Chairman, first let me start by thanking the Committee for inviting us to give evidence. We welcome this open and transparent debate as a vital part of the policy-making process, particularly when it gives minorities, such as cane refiners, an opportunity to make their voice heard in the debate.

You may have noticed that our written submission was maybe a little more candid than usual. This is no accident. We have a fight on our hands, probably more so than we did in the last reform debate in 2005. Our goal is to get a fair deal, despite being in the minority in the European sugar market. As someone said, if the regulator decides to fix the market, it should at least fix it in a way that is fair or, to be more precise, parallel for all.

Our contention—as you will have quickly gathered from our written submission—is that protectionism is strongly back on the agenda. In the short term until 2015, in our view that means that the European Commission is attempting to roll back the quota cuts and the direction of the 2006 reform under the auspices of emergency actions to solve the European sugar market crisis. This crisis has been brought about solely by the Commission's forecasts for cane imports not being met. In the long term, post-2015, our concern is that a parallel policy for cane refiners is not on the table. In other words, if national quotas remain, traditional cane refiners should also have a national quota. If quotas are abolished, our access to raw material should be unrestricted.

A parallel policy for cane refiners in Europe is important for some key policy reasons. Not only are we competitive in a market sense without legislation, we also bring consumers choice and competition. We contribute to food security. We provide a stable and long-term market for the developing world. Last but not least, 4,500 high-quality manufacturing jobs around Europe are at stake if we do not get a fair, parallel deal.

Q157 The Chairman: Thank you very much. That is very helpful. If we may we will go to the questions. I think basically you would hold the view that the 2005 reform has really failed. In your view, is the market any better for you now than it was pre-2005? If that is the case, why? Why did 2005 really fail as a reform? How did you respond as a business, being the leader in that area?

Ian Bacon: It is clearly much worse for us now than pre-2005. As far as cane refining was concerned, the 2005 reforms were based on the forecasts that imports would rise to 3.5 million tonnes by this point in time. On that basis, the effective quota system for cane refiners' access to raw material was abolished and the cane supply was made available to all. At the same time—perhaps because the beet industry felt it did not have the confidence in its own competitiveness—there was a significant investment by the beet industry into cane refining. In fact, 1.85 million tonnes of new cane refining capacity was put in by the beet industry, which is getting close to double. As the supply has not materialised, the result is that cane refiners are running at around 60 per cent capacity.

How that has further failed is that, in the original intention of the reform, the shortfall in the imports would have been made up by more imports, but the first measure that the Commission took was effectively to reintroduce quotas or to increase quotas under the emergency measures. That has helped to push up the prices, as cane refiners and the beet processors are competing for a smaller supply than they need for running their factories. That pushes up the price of the available supply dramatically and also has the impact of pushing up the market price.

Among that there is quite a paradox in that the price that we have to pay for our raw material is escalating. Our profits are squeezed dramatically, and it is a paradox that it is actually in the interests of the beet industry to keep pushing up those cane prices. Its costs are covered by their beet quota, but if the price is much higher, the profits that it will make overall are much higher, whereas the cane refiners are predominantly making losses.

Q158 The Chairman: If you compare your profitability with that of British Sugar, its profitability will have risen in this period and yours will have declined. Would that be fair?

Ian Bacon: Absolutely.

Q159 The Chairman: And dramatically so?

Ian Bacon: Dramatically so.

The Chairman: Thank you.

Q160 Lord Renton of Mount Harry: I must say that it is a very puzzling industry, is it not?

Ian Bacon: It is a very strange industry to work through, I can assure you.

Q161 Lord Renton of Mount Harry: It is a strange industry. If I got it right, you have just said that 1.85 million tonnes were put into cane by the beet industry. Yet in your submission you also say that there has been a cross-subsidy effect that has benefited beet refiners over cane refiners. I confess that I just do not understand it. Perhaps you could explain the cross-subsidy effect in more detail and how you consider it should be avoided in the future. Clearly, you are experts in this field. Do you find it very puzzling yourselves?

Ian Bacon: Let me give you an overview. The beet industry has a quota for its raw material supply, so it will structure its factory around that supply base. In fact, that is predominantly what it is making the money on.

Q162 Lord Renton of Mount Harry: Are we talking about the beet industry anywhere, not just in the UK?

Ian Bacon: Anywhere. A number of countries and companies have gone more into cane refining than others, but if you have covered all your costs on your beet processing, cane refining is on top of that. It is icing on the cake. It is basically a margin or a cash cost, whereas for the cane refiners it is their absolute lifeblood. If you have a business that has all its costs covered already by the beet business, and is then able to start processing cane, we see that as a somewhat unfair advantage because you have made your profit on your beet business. We have not actually started and the whole business is based on cane. As the competition for that supply rises, our start cost rises with it, which pushes the market price up. You can see that the price is just going up, so the whole market is going up. Even the business that has already been done on the beet will eventually benefit from a higher price.

Gerald Mason: If I may I will add that there are four types of cross-subsidy that we talk about.

Q163 Lord Renton of Mount Harry: Four types of cross-subsidy?

Gerald Mason: Four types. The first one is that the beet sector was given around €5 billion to reduce its quotas in 2006. Some of that has been used to reinvest in cane refining, which is quite legitimate. Some €5 billion of money was given to the beet sector to restructure out of the 2006 reform to reduce its quotas, and quite naturally some of those businesses have decided to reinvest into cane refining. The second one is that some of the machinery from the beet factories that were closed down was reused to build the cane refineries with. The third one is the cash cost competition, which Ian described. When we compete for raw material with the beet sector, we have our full costs to cover. It only has cash costs and, as with any sophisticated manufacturing business, fixed costs are the main element of your total costs. Then the final one—and probably the most dangerous one that has become more apparent more recently—is that now that we are all buying from the same pool of sugar, it is clearly in the interests of the beet sector to pay higher and higher prices for the cane sugar, because that forces up the marginal cost of supplying Europe. It forces up the white sugar price, which it clearly benefits from on the majority of the sugar that it sells, which is beet sugar. It clearly does not face the same costs on that. That is really why at the moment you see record profitability from some of the major quota producers in Europe. In Germany, which has the largest and the second largest quota holder, the profits announced for the last year are up 70 per cent and 60 per cent respectively. The companies talk about record profits, not just for this regime but for the whole companies' lifetimes.

Q164 Lord Renton of Mount Harry: If you were running it all, what would you do now?

Ian Bacon: We are very simply asking for a fair deal. If quotas are to stay—

Q165 Lord Renton of Mount Harry: You would rather they did not?

Ian Bacon: We are ambivalent in that sense. If quotas stay, from what has happened in the market today I think it is very clear that the national quotas for cane refiners need to be reintroduced. If the quotas are abolished, and the beet industry can produce as much as it wants, why is it unreasonable for cane refiners to have the same access? The profitability of the beet industry in Europe is very good. We marvel at the competitiveness. It is very good, and I congratulate the beet growers and the processors. The UK's are among the best. They are competitive on the world stage, so why do they demand protection on that basis?

Q166 Baroness Howarth of Breckland: I do not know whether I have understood this, which is not surprising, I suspect. Could I just ask a very simple question? Does this mean that the people who are making substantial profits—to use that word—are actually being subsidised by the taxpayer across Europe by these subsidies? Where is the funding coming from?

Gerald Mason: It is not a direct transfer of public money, but it is the structure. There are two structures. In the internal market, you have the quota system, which protects it from new entrants, so there is a barrier to entry to competition. Around the market, overall, you have this import duty structure that we discussed in the last session, which effectively doubles the cost of our raw material. If we wanted to buy sugar outside the preferential sugars that we are able to buy, from countries such as Brazil and Thailand, we would have to pay an import duty, which effectively doubles the raw material cost. There is no explicit transfer of value, but the structure that the legislator sets creates an environment that makes those profits.

I know you have heard in previous sessions that there is less protection. Our argument is that today there is more protection because the quota system has not changed. It presents barriers to entry to new entrants. That duty structure—the €419 that we discussed earlier—has not changed, despite the reference prices.

Q167 Baroness Howarth of Breckland: How does the cross-subsidy play into all that?

Gerald Mason: Very much so eventually, because by benefiting from the cross-subsidy, they will be able to kill our industry, the cane-refining sector. We cannot compete because of the legislator. That will add to the concentration in the sugar market. The competition authorities are very concerned about competition in the sugar market. There are four ongoing investigations around Europe. A large merger investigation has recently completed and it is clear that they are concerned. There are now six companies, which account for 80 per cent of the beet quota in Europe compared with eight pre-reform. The cross-subsidy does not necessarily contribute to those profits today, but it will eventually mean that we cannot compete on fair terms. We will have to close, and that will continue to concentrate the market.

Q168 The Chairman: Just building on that, if the quotas and the tariff were removed, what would the effect be upon the price that consumers pay for sugar?

Ian Bacon: The price that consumers pay would then be much more of a market price.

Q169 The Chairman: Do you have any sense of how much it would come down by?

Ian Bacon: In today's world it would come down significantly. I think the question earlier was: what is the world price equivalent of sugar today? It is about €350. We would probably pay something more than that, but it would be significantly lower than the recent price that we have paid, which has been over €700 for raw sugar.

Q170 The Chairman: Just from a consumer point of view, when I buy a packet of sugar, how much will it come down by? Could you send us a note on that?

Ian Bacon: I cannot tell you how much the price of sugar in the retail world would come down by because it is illegal for me to tell the retailer what price he needs to sell the sugar at.

Q171 The Chairman: But you could give us some guidance so that we could work it out for ourselves?

Ian Bacon: Yes.

Gerald Mason: To give you some guidance, the legislative cost of our sales price—the duties we have to pay, and the way our raw material price has been forced up above the market price—is probably about 30 per cent to 40 per cent of our total cost. If you took out the legislative interference, that would be the order of change. Of course, our contention is that removal of the quotas and the duties is not what is on the table. What the Commission has tabled for life after 2015 is just the removal of the quotas. That can be a difficult one because you might think that that will create a more liberal market, a more market-orientated market, but it is only part of the jigsaw. Without removing the duty structure as well, clearly it may do the opposite and produce a more concentrated market.

Q172 Lord Renton of Mount Harry: What about this tax that is put on, which we were told about just recently?

Gerald Mason: It comes from before I was born, actually. Way back in the past, someone somewhere would have said, "We need to fix a duty under the GATT (General Agreement on Tariffs and Trade) round because we are members of this international trade agreement". Someone would have looked, over an historic period of time, at the duties that were charged and amalgamated that into a fixed duty. Each time there is a global multilateral trade deal, such as the GATT round in the 1990s and the WTO round that is being talked about today, a percentage reduction is eventually reached on that. The €419, which you discussed today, would have been the result of some complicated formula in the 1990s that was applied to a fixed duty, which was there as a result of some agreement that we made in the past about what level of import duty we are legally allowed to charge under the multilateral trading system. I hope that makes it a little clearer.

Q173 Lord Renton of Mount Harry: Basically, who does it go to?

Gerald Mason: It is a European Union duty. I believe that what happens is that the British Government get to keep a small share of that as part of the collection process, but the majority of that goes back to the European Union.

Ian Bacon: We can send you a little more information on specifics.

Q174 The Chairman: Yes, we must press on. But before we do, on the beet growers, just to be clear about this, if someone grows beet, first they get the single farm payment—a straight subsidy—for owning the land. Then they get protected by a quota and people cannot come in and compete with them, so it is a highly protected market that is subsidised on two levels. There is a tariff to protect them as well as a single farm payment. Is that correct?

Gerald Mason: That is true. To be fair, the quotas are not allocated to the farmers.

Q175 The Chairman: No, what is the effect of that?

Gerald Mason: The third element that you might not be aware of is that under the Commission's proposals for post-2015, not in the single CMO (Common Market Organisation) part but in the direct aid part, there is also a provision for coupled aid payments to come back in for sugar and a number of other crops.

Q176 The Chairman: What are those?

Gerald Mason: At the moment, the area aid payment is decoupled from production. The farmer gets that whether he grows a crop or not, but, under the Commission's proposal, as well as that there is a provision for Member States to allow for coupled aid payments. A farmer gets it for growing sugar or other crops. It is quite clear that it has to be for specific reasons, but you should be aware that that is now on the table again for post-2015.

Q177 Lord Lewis of Newnham: But this is aid for sugar beet? It does not apply to cane?

Ian Bacon: It does not apply to cane at all, no.

Q178 The Earl of Caithness: You have touched on it quite a lot in reply to Lord Renton's supplementary question, but clearly you do not think that the Commission's market management measures in the past have been fit for purpose. What should the future measures be, and how fit is the Commission to operate such a system?

Ian Bacon: Our experience is that we do not think that it should be left with the Commission to operate, so we would like it enshrined in whatever legislation comes forward. The reason why it went wrong is, despite the fact that we were flagging that there was a problem two years before the crisis or emergency powers were invoked, that our warnings were ignored. The Commission should have acted earlier, and consistently with the intention and the legislation as it was originally framed, which was to allow more imports of tariff-free, duty-free sugar to make up the gap for 3.5 million tonnes. I think the changes would be an automatic correction of the lack of imports at zero duty, and that should not be left to the Commission. If we had a similar situation today, that is what we would be advocating.

Q179 The Earl of Caithness: When the Commission imposed these measures, why was there no flood of cane sugar coming in?

Ian Bacon: Very simply, because the preferential suppliers, or the supplying countries who have tariff-free access, physically do not produce the volumes of cane sugar that were forecast in the pre-2005 workings. In fact, the work that we have done has looked at their total exports now compared with pre-2005, and they are actually either the same or less than they were in 2005. That is partly because some of the industries in these countries are in significant decline, and there is population growth and development in some of these countries. As you have a developing economy, the consumption of sugar tends to increase. There was never going to be 3.5 million tonnes. That is the problem that we live with now: that the cane sector was supposedly liberalised—in other words, everyone was allowed to buy the supply—but the supply never increased. The capacity has increased by nearly double, but the supply did not change.

Q180 The Earl of Caithness: In your research, did you find any evidence that the EU was not fulfilling its obligations in giving the preferred countries investment money that it was promised—the €1.2 billion?

Ian Bacon: That is quite a big question, and it is something that I suppose we have got more involved in recently. The messages that we got back from a number of the supplying countries is that they have found it quite difficult to access the funds. It is not something that is our strength or part of our business, but because of the situation that we have found ourselves in—the limited supply and the long-term relationships we have had with most of these countries—a few of the countries have asked us to assist where we can with getting access to those funds. The answer would be they have found it quite difficult, and we are now providing expertise and carrying out studies. In fact, we have a paper that we could let you have that talks about how difficult and complicated it is actually to get access to all these different funds. That was part of the work that we did to start off with: to see what we were up against. So I think it has been mixed. Some countries have had more success than others, and I think some countries have definitely found it very complicated.

The Chairman: Thank you. I think we have about 25 minutes and five more questions.

Q181 Baroness Howarth of Breckland: That was my question, but may I ask a different one? The evidence we have received has been quite confusing in that we have got a different picture from different witnesses, particularly of the needs of developing countries where the worry is that, if production is impeded, disadvantaged groups—women who work in factories, for example—will find it even more difficult to manage. The other bit of evidence is that there are plenty of outlets for the sugar market. They are using it in their own countries. There is demand elsewhere, and therefore there is no problem. The third factor is the one that we have just been discussing which I would like us to elaborate on a bit more. They have not been able to develop their own industry, because the money from the Commission that might have helped them to do so has not arrived. Taking as our point where we are now, what would be the best way to help those developing countries to become as self-sustaining as possible in their own industry and to use the funds that do exist to develop them? For example, Mauritius has clearly managed to do it, so if there is one model, what could we learn from that model to help the rest of these developing countries?

Ian Bacon: There are a lot of pieces to that question. I would agree that Mauritius has done a very good job. I would say it is a very sophisticated tariff-free access supplier to the EU. It also has a fairly unique location that makes the supply of the kind of sugars that it has fairly viable for it. Some of the other countries would struggle to copy the Mauritius model, so it is definitely not a one-size-fits-all solution. With a number of our suppliers we have now invested in endeavouring to bring down their costs of production, making them more efficient and bringing up their volumes, both from a commercial self-interest, because that is the only place we can buy the sugar from, and in the recognition that if they are going to survive—as you rightly observe—they need to become far more competitive in the world.

That will not be an overnight fix. Some of the industries in particular really do need to do an awful lot of work, effort and investment to bring them up to a competitive standard.

How would changes in the legislation now play out for them? If the quotas stay, it is easy to imagine a mechanism whereby they still have their preferential access. That has to be exhausted, or forecast to be exhausted, before the excess or the extra is allowed in. In a completely deregulated market, that would be more difficult to imagine. I think we would be keen to see them survive. We are also a European business and we have to survive, so we also need to have a competitive source of supply. I do not know whether that answered your question.

Gerald Mason: There are three key challenges. From our limited and most recent experience, the first is the capacity of the industries—the farmers and the millers—to join together and to plan coherently. You have to put a plan forward to get the money in. Farmers and processors do not necessarily agree in Europe, and they certainly do not necessarily agree in the developing countries.

The second one is often that the views of the local EU officials are very important. The power basically to spend the money is delegated to the local officials. The views of those local officials and what they feel is the right solution for their country can be quite central to the process.

The third one is that, once the money is there, often in the supplying countries there is not necessarily the capacity to spend it. We are talking about large amounts of money quite quickly, and the capacity to spend it and spend it well—not necessarily just in the sugar mills but among the thousands and tens of thousands of growers in these countries—is a real constraint as well. Those are the areas that Ian described that as a business we are trying to help with.

Q182 Lord Whitty: Going back to the supply and the trade dimension, the tariff is there to protect not just EU beet producers but the preferential countries. In the past five years, we have had some other agreements for free trade for other producers, or are moving towards that. Has that eased the situation when the tariff comes down as a result of those bilateral agreements, which broadens the number of tariff-free or near-tariff-free countries?

Ian Bacon: The only arrival in the near future is the Central American and Andean community.

Lord Renton of Mount Harry: I did not hear that.

Ian Bacon: The only one that is in the immediate prospect of actually bringing any new sugar to the market is the Central American free trade agreement and Columbia/Peru. That has still not been enacted yet. In a situation with a probable 1.5 million tonne deficit, the maximum that they will bring with them is 250,000 tonnes. While we welcome it, in the short term I do not see that making a big difference to the overall supply and the overall impact on the market.

Q183 Lord Whitty: Is the longer-term implication, though, that you might see more refining capacity at the point of production?

Ian Bacon: Only if the current state of play existed. Around the globe, the common model for sugar production—and the most efficient model of sugar production—is cane sugar, grown in the tropical countries or in places where it is most suited to be grown, shipped as a bulk non-food grade product to the point of consumption, and refined into the more sophisticated products that are required by the more developed markets. As Tim Innocent eloquently put it, the biggest issue that the major food manufacturers and most of our customers face is security of supply and the window of delivery that the local refinery, in our case, can provide for them.

Gerald Mason: If I can add to that, we are not scared of white sugar imports, whether they are from the preferential countries or any supplying country. If we had the raw material, we could compete with that. The problem is that we are being asked to compete with white sugar imports with in effect one hand tied behind our back. The worst situation would be if a European manufacturing industry such as ours died, not because we were not competitive in the market sense but because the legislator did not give us the raw material to compete with white sugar from places such as the new free-trade agreements and, increasingly, full duty-paid white-sugar imports as the market becomes stressed, as we heard earlier.

Q184 Lord Whitty: As a matter of fact, you used to be dominant in European cane refining capacity. You are now saying that there is more, both here and elsewhere. What proportion of cane is still refined in Europe?

Ian Bacon: Thirty five per cent.

Q185 Lord Giddens: What I find interesting about what are essentially sugar wars—that could be the title of our inquiry—is that I am still not fully sure in my own mind where that leaves us. In your view, what would be the optimum strategy that the Commission could follow that would effectively represent your interests? The Commission cannot control what the WTO does. Therefore, we are talking about elements strictly within the framework of what the Commission does. Could you summarise what you would see as an optimum position?

Ian Bacon: All the way through the debate we have said that we want fair and parallel treatment.

Q186 Lord Giddens: What does that mean?

Ian Bacon: It simply means that if the Commission decides to keep quotas, we should have similar protection, which is what it is. If the Commission decides to abolish quotas but does not abolish tariffs, the volume of beet already produced—and more is being encouraged by reclassifying out of quota to quota—would swamp the cane refiners in a very short time.

Q187 Lord Giddens: That is why you say it would see the end of cane refining in Europe?

Ian Bacon: Yes.

Gerald Mason: To add to that, your point about the duties not being under the auspices of the Common Agricultural Policy is correct. The common agricultural policy also has the ability to set specific measures for specific operators and specific purposes. Our argument is that if the quotas go, cane refiners, as a group of European manufacturing businesses, should have specific access to raw sugar at zero duty. In our view, that is a legal requirement. The Common Agricultural Policy (CAP) also has an overriding legal requirement to treat operators, which produce the same product but in different ways, in a fair way. You are right; it is not under the auspices of the CAP to wipe away all the duties, but it is under the auspices of the CAP to perform specific actions for specific sectors.

Q188 Lord Giddens: I am not quite clear whether you are asking for a level playing field or for internal protectionism as against a more successful industry?

Gerald Mason: That is a really good question. At the moment, it works like a ratchet. No one can enter the beet market; the quotas stop anyone from entering. But anyone can enter cane refining, including beet processors. It is a one-way street. The only people who are protected today are the beet sector. If that protection is going to continue, we need some protection back to allow us to be able to buy at least a minimum level of supply, as they are able to do without any interference. If the quotas go, and they can produce and sell as much as they want, the only way we will be able to compete fairly is to have the same terms. We know that we can do that in a market sense. The cost of producing refined sugar from beet or cane in Europe, since the reform began in 2006, is broadly similar: about €400 to €450 per tonne. We know we cannot compete if the legislator adds extra costs or constraints to our model and not to the other. I apologise if this seems a bit complex, but what we are arguing is that if the beet sector continues to have its protectionism, we should have something back that gives us the same terms. If the protectionism is swept away and the constraints are swept away from the beet sector, we should have the same. That is not just because of our little refinery in London; it is because some of the big policy themes, consumer choice, competition in the sugar market, food security—all the things that we try to argue to the stakeholders in Brussels—should be on their radar as well as just the cane refineries in Europe.

Q189 Lord Giddens: The reason why I am pushing this question is that I think we have to decide what a fair playing field is and what pleading for special interests is. It is not so easy when hearing you use these terminologies to decide which is which. You would claim that your argument is simply for a fair playing field?

Ian Bacon: Absolutely. We have some numbers and charts that we can add to what we have submitted already, if that would help?

Q190 Lord Giddens: Can I ask you briefly about an issue you mentioned, which is that there is an oligopoly issue in the European sugar industry, not just in the UK?

Gerald Mason: Yes. The competition authorities in Europe are concerned about the concentration in the sugar market. It is one of the areas they spent a lot of time focusing on. There are four ongoing anti-trust investigations at national level around Europe. Also, the largest quota holder in Europe, Südzucker, has recently announced the purchase of 25 per cent, I think, of shares in one of the world's biggest sugar traders, ED & F Man. As part of that, there was a long investigation and there were some very interesting conclusions about the Commission's concerns about competition in the European sugar market. There was also a report by the European Competition Network a few weeks ago, DG Competition and the Member State competition authorities, highlighting their concerns. It is a highly concentrated area. As I said, there are only six quota holders, which account for nearly 80 per cent of the quota. That is one of the reasons why we think that cane refiners deserve a fair deal, because if cane refiners disappear, that market will only become even more concentrated.

Q191 Lord Giddens: You have access to those reports?

Ian Bacon: Yes, we can send you details. They are publicly available on the web.

The Chairman: Yes, if you can send us the links. Thank you.

Q192 Lord Renton of Mount Harry: A quick question about market prospects. How significant a driver of future demand do you think diet is likely to be? Is it going to become more of a driver, both in the EU and elsewhere, or not?

Ian Bacon: In global terms, the consumption or the demand for sugar goes up by something like 3 million tonnes a year.

Q193 Lord Renton of Mount Harry: Which is what sort of percentage?

Ian Bacon: It is about 2 per cent.

Q194 Lord Renton of Mount Harry: Three million tonnes a year?

Ian Bacon: Yes. In the EU, I think it is probably more static, even to the point of declining as people are more exposed to stories about diet and health. From where we sit, that does not seem to be a problem, since our business is shrinking by considerably more than 3 per cent through supply issues. Our shrinking is dramatic. Prior to 2005, we were refining 1.1 million tonnes of preferential sugar. This year that will probably be around the 600,000 tonne mark. The rest of that capacity is by and large lying idle. That is the 60 per cent I mentioned earlier. That is because of the issue that we are debating today: the supply issue.

However, coming back to the diet issue, our view is that it will remain fairly static. In the more developed countries, consumption is becoming more sophisticated. It moves away from just basic bulk sugar and becomes either manufactured products or, interestingly, goes back into more sophisticated brown sugars—special sugars, what have you—which are now used in baking.

While we are on the subject, I would like to pick up on a point that was made earlier about the obesity and health debate, simply because that is one point of view. I would like to state firmly —and I think the sugar industry would state the same—that the balance of scientific evidence does not bear out that sugar is the primary cause of all those items that were mentioned. In addition, the actual consumption of sugar according to the Government's own figures has not increased. I am happy to send you peer-reviewed evidence for that and the Government's statistics. That is not a good story to put on the TV, which is why you only see the story that it is causing all major illnesses and is bad for you.

Q195 Baroness Parminter: A statement that one would expect from your industry. Perhaps I could ask whether you would agree that, in effect, you have a monopoly in that you are the only cane supplier in the UK? You have made a very convincing case for a fair playing field today. I accept that. Can you talk us through why you think it is acceptable that you should be the only supplier, and whether that guarantees the industrial users of sugar in the UK a fair price?

Ian Bacon: Can I say that being accused of being a monopoly at the moment seems rather hard to take, since we are struggling to survive. We would very much argue that it is the other way around. The monopoly is much more in the competition's court here. Anyone can buy cane sugar. Most countries now around Europe that have sugar industries are buying raw cane sugar and refining it. There is no barrier to entry, so I cannot quite get my mind around the monopolistic accusation. I do not know whether I have missed something, Gerald, but it does seem a little hard to take.

Gerald Mason: If you stand back and reflect on the situation the sugar market is in, we find ourselves having much more in common with the view of the sugar users now. We are a European food manufacturing business that cannot access raw material at competitive prices.

You asked in the last session whether that was actually a physical problem or a price problem. For our industry, it is a physical problem. At the moment, we close the refinery in London two to three days a week. We have recently gone through the process of making job cuts. In other Member States, the refineries in Europe are actually closing for two to three months at a time because of physical lack of availability. In answer to the question about a monopoly position, in a strange way—as you have probably gathered from the evidence—we find ourselves much closer to the sugar users' position at the moment, which is that we cannot access, in the same way that they cannot, competitive supplies of raw material at a price that ensures that we are viable.

Q196 The Chairman: If the tariff and the quotas came off, and a wall of sugar then came, your monopoly position would be a tremendous spot to be in, would it not?

Ian Bacon: The issue there is the view that a wall of sugar would come. I think the market would find a balance, which is really what we should be looking for. What is the market price? What is the market able to stand?

Q197 The Chairman: Even so, you would easily go back up to 1.2 million tonnes a year?

Ian Bacon: Not necessarily. I think we would move the capacity to whatever made sense from a market point of view.

Q198 The Chairman: Is it likely that another refiner for cane sugar would come and build a plant down the Thames to compete with you?

Ian Bacon: I think you probably need to look at where other refineries might pop up around Europe at that point, because you have Greece, which has a sugar industry that is a beet industry, which is probably struggling. You would probably find refineries going to places where there was no sugar industry.

Q199 Baroness Howarth of Breckland: On a point of clarification again, you said a little while ago in answer to the diet question that you thought that the consumption of sugar was rather static, yet we heard from our previous witnesses that in fact they were sometimes struggling to get the right quantity of the right sugar that they needed at any point. The Chairman has just asked whether there would be a wall of sugar. Can you just clarify those rather conflicting positions?

Ian Bacon: There is a paradox.

Baroness Howarth of Breckland: We are finding it difficult to hear. Do not be deceived by the microphones; they do not help us, they just help—

Ian Bacon: There is no shortage of sugar, *per se*. It is a matter of price. We could go out and buy sugar on the world market and make any of the products, but the issue is whether we would then be able to sell it to our customers at the price we would need to achieve to cover the duty and the processing costs. I do not think there is a lack of sugar. The price is just something that people would rather not pay when enough tariff-free, duty-free sugar is coming into the market.

Gerald Mason: The arithmetic of the European Union sugar legislation does not work at the moment. That is why people say there is not enough sugar. If you add up the quotas and the amount of sugar that comes from the preferential suppliers in any one year, it is about 1.5 million to 2 million tonnes short of the demand. That is why the Commission has to take these emergency measures each year. Globally, there is no shortage of sugar. In fact, there is a surplus of sugar and prices are going down but, because of the duties and the quotas in Europe, the amount of sugar in our system is not enough to meet the demand. It is about how you make that correction to correct the shortage in our legislative system with sugar from the outside world where it is plentiful. That is where the debate is about how that should be corrected.

One final thing about the wall of sugar is that the arithmetic is very interesting. Already today, 4 million to 5 million tonnes of sugar are produced over the quotas in Europe. As we heard earlier from the sugar users—a figure we agree with—there could well be 3 million to 4 million tonnes of extra sugar equivalent from the isoglucose sector if the quotas are removed. When you add all these things up and you look at our industry, which at the moment produces about 2 million tonnes of sugar, you can see why we are concerned. We would argue the wall of sugar would come not from the cane refiners but overnight from the beet sector, which already has this physical sugar available, and possibly very quickly from an expanding isoglucose sector as well. It is a difficult question to answer because it depends on your long-term view on price, but today the advantage would be for a very quick expansion in market share from the sugar that is already produced over quota but that cannot be marketed in Europe.

The Chairman: That leads us to the final question.

Q200 Lord Lewis of Newnham: I am sorry; this is just a point of clarification. You were making the point earlier, I believe, that one of your problems is that the beet group of people are now producing cane sugar as a side effect. How do they compare with the quantities that you are producing? Is this a small factor or a significant factor, if you take the totality?

Ian Bacon: About half the cane refining capacity is now in the hands of people who are predominantly in the beet industry. That is probably a fair view of the amount of cane sugar that is being processed.

Q201 Lord Whitty: A fair view of capacity or production?

Ian Bacon: I think you would probably find the same.

The Chairman: It is 12.30 pm. Thank you very much. That is most informative.

UK Industrial Sugar Users Group (UKISUG)—Oral evidence (QQ 118-155)

Evidence Session No. 6. *Heard in Public* . *Questions 118 - 155*

WEDNESDAY 27 JUNE 2012

Members present

The Earl of Caithness
Lord Carter of Coles (Chairman)
Lord Giddens
Baroness Howarth of Breckland
Lord Lewis of Newnham
Baroness Parminter
Lord Renton of Mount Harry
Lord Whitty

Examination of Witnesses

Tim Innocent, Chair, UK Industrial Sugar Users Group (UKISUG) and Head of Purchasing -Direct Materials, Nestlé, and **Dominic Goudie**, Trade Policy Executive, UKISUG and Food and Drink Federation's Biscuit, Cake, Chocolate and Confectionery Group

Q118 The Chairman: Mr Innocent and Mr Goudie, welcome. Thank you very much for coming today to give us evidence. I will deal with the formalities and then how we might conduct ourselves. Before you is a list of the interests declared by Committee members. This is a formal evidence-taking session of the Committee. Full shorthand notes are being taken. These will go on the public record in printed form and on the parliamentary website. We will send you a copy of the transcript and you will be able to revise any minor errors. The session is on the record. It is being webcast live, and subsequently will be available on the parliamentary website.

Mr Innocent, it might be useful if you made a couple of opening remarks before we go to the questions, or we could go straight to the questions?

Tim Innocent: We will just say a few words, thank you, Lord Chairman.

My name is Tim Innocent. I am the chair of UKISUG, which is a snappily named organisation. It is the UK Industrial Sugar Users Group. We combine the interests of members in food and drink across the UK for small and large organisations. My day job is as head of procurement for Nestlé in the UK. I will let Dominic introduce himself, and then we will talk a little about where we are as an organisation.

Dominic Goudie: My name is Dominic Goudie. I work at the Food and Drink Federation and specifically represent the biscuit, cake, chocolate and confectionery manufacturers. I also work with UKISUG providing secretariat services. As it stands, the group currently covers a range of different products and sectors, including the ones I have mentioned, which I am responsible for. We also have manufacturers of soft drinks, breakfast cereals, ice cream, yoghurts, chilled desserts and some other assorted products, so there is a very wide range of interests within our membership.

The sectors we currently represent employ around 70,000 people and have a total turnover of around £12.3 billion, which also represents around £2 billion of exports in the last year.

Q119 Lord Renton of Mount Harry: £2 billion?

Dominic Goudie: Yes, for our sector alone. I do not know whether you want to say anything on the position?

Tim Innocent: No. We have issued our position paper to you. We are very much pro-reform as an organisation. We are very much pro a free market approach to all these things, but we can perhaps tease some of that out in the questions. I should make it clear that the comments I am making here—I am the chair of UKISUG; I am not in my day job at the moment—are not necessarily to be attributed to Nestlé.

Q120 The Chairman: We are very clear on that. Thank you very much. In your very helpful submission, you describe the sugar market since reform. You paint a very dark picture, observing that supply has been extremely tight since the last reform. I suppose the question is: did the last reform improve the market in any way, or was it a better market for industrial sugar users pre-2005?

Tim Innocent: That is an interesting question. I guess it was predictable before 2005 in that we had a lot of availability. We knew that we were not going to be facing short supply or that we would have contracts that were volume-specific, but were able to flex in some way, either up or down as business needs arose, so you were not having to land the exact number all the time. I think I could predict that every year I would have in my day job a small number of discussions—round about Christmas time—about what the price might be for the next year, which was to be expected. We did not really have any supply issues, and that was the key difference. I think that was driven through a market that had a lot of sugar available within it.

We know the reasons for the reform, and we know that not all that sugar landed within industrial users, but let me say there was enough sugar available. We were not in a constrained market. I think that reform has taken us to more of a constrained market position. So, yes, it is more predictable. Supply is not an issue. Price is always going to be a discussion point between a supplier and a buyer, and that was really to be expected in the normal transactions that occurred.

Q121 The Chairman: Price aside, what difference was there? Supply got tighter, but it did not impede your operations or those of your members, did it?

Tim Innocent: Pre-reform or post-reform?

The Chairman: Post-reform.

Tim Innocent: Post-reform, I guess, as a large user of sugar I have specific needs and I have a range of suppliers that I can talk to to fulfil those needs. My colleagues in UKISUG who are in smaller organisations may have a more limited choice. They may have fewer suppliers that they can go to. They may have more specific or tighter specifications. They may not have done some of the work that a large company can do to look at its specifications. In those circumstances, once a market begins to contract to where demand and supply are out of balance, pressures are felt. Because the sugar regime works in a particular way, which is about marketing—October to October—even large companies like us at times, in the August/September period, have had difficulties getting supply of all the materials that we need. That is particularly the case with specific grades of sugar at certain times. Some types of sugar, say fine sugars, might be in more limited supply. Also you might end up with sugar that is slightly outside your normal specification, as they come to the end of one and the start of the other. So certainly I would say that we have seen some supply issues at all levels of the industry.

Q122 Lord Lewis of Newnham: How far have the actual restrictions, in supply and things such as that, related to quota? I am not quite clear. If you have a quota on a specific area, can you actually buy that specific commodity elsewhere?

Tim Innocent: I can buy sugar from anywhere in the world, but I have to pay quite a heavy import duty on that sugar. As a manufacturer, I need sugar of a certain quality, so predominantly I use variants of a white, crystallised sugar. I might use some liquid sugar and I might use some fine sugar, but essentially I am into refined white sugar. On the open market, on the world market, refined white sugar is available, but it is probably not a great supply chain for bringing white into Europe. If I buy raw sugar, I need to get it refined and I do not run a refinery. So, yes, I can buy from outside the quota system but at a high price for the import duty, which I think is at €419 on white sugar.

Dominic Goudie: Yes, €419 per tonne.

Tim Innocent: So, whatever the world price of sugar is, plus setting up my logistics system, plus making sure that it arrives at my factories at the right time and all that kind of thing, I have to pay the world price plus €419.

Q123 Lord Renton of Mount Harry: At €419 per tonne?

Tim Innocent: At €419 per tonne, plus the world price.

Q124 The Chairman: What is the world price? You get the aggregate of that margin?

Tim Innocent: That varies, and it is denominated in cents a pound. Back in the day it has probably been as low as perhaps 12 or 15 cents and as high as 30 cents. I think it is in the 24-cents region at the moment. It is very difficult to talk about price. Clearly I can talk only about published prices and publically available information.

A person could do the calculation of converting raw sugar, plus bringing it in, plus some margin, plus the duty, and it would be easy to imagine that that equated to about what the market price might be. The market price has been variable, and we have seen lots of published information on that, but it has been much higher than the €404 a tonne reference price, which is what I am trying to say. So, yes, you can, but even if it would cost you nothing it would be €15 more than the reference price, so maybe that puts it into some context.

Q125 The Earl of Caithness: To whom do you pay the money?

Tim Innocent: To the supplier; to British Sugar or Tate & Lyle, or to any one of the other suppliers that are prevalent in the UK market, such as Napier Brown or Tereos.

Q126 The Earl of Caithness: When you are paying over and above the market price?

Tim Innocent: Yes. I am paying the price in the market for white sugar.

Q127 The Earl of Caithness: But then you said that you had to pay over and above that because you could import from anywhere?

Tim Innocent: Yes. I would pay that provider of sugar and then I would have to pay the €419 to the Revenue.

Q128 The Earl of Caithness: The €419 goes to—?

Tim Innocent: It goes to the Government, to the Revenue. It is a tax, an import duty.

Q129 Lord Lewis of Newnham: To the UK?

Tim Innocent: Yes. Actually, that is an interesting point. I do not know whether it is collected and kept in the UK or if it goes into the European Union.

The Earl of Caithness: That is what I was trying to get to.

Tim Innocent: Sorry, I apologise.

The Chairman: It goes to the EU, apparently.

Q130 Lord Renton of Mount Harry: €419 just sounds an extraordinary figure. €410 or €420 might have been sensible. How did it happen? How long has it been there?

Tim Innocent: I do not know the history. Maybe my colleagues who come later might know where that duty came from at that level.

Q131 Lord Renton of Mount Harry: That figure has been there a long time?

Tim Innocent: I think it has been there for a fair amount of time, yes, but it has certainly been there in this legislation. I think that even pre-reform a duty was brought in to be paid on sugar. I must admit that I do not know whether it was €419, but I am sure that the people who follow will be able to answer that question much better than I can.

Q132 The Earl of Caithness: Could you please tell us what the advantages and disadvantages are in having just two sugar producers in the UK?

Tim Innocent: I am happy for there to be two producers, five producers, 10 producers. I would be less happy if there was one producer. I am not really worried about how many sugar producers there are. My primary concern, and the concern of our industry, is to get a product that is within our specification and that can arrive at our factories when we use it. A large manufacturing organisation such as Nestlé, Coke or other organisations, will consume vast quantities of sugar on a daily basis, so we need a really good, strong infrastructure of available people bringing in two, three, four, five or six lorries' worth of sugar per day. There are other players in the market. There are traders and so on that we can look to use. There are suppliers that can come from continental Europe and provide that logistics solution. I am not wedded to having one or two in the UK. I am a free marketeer, so I am happy to have as many people as possible who want to play in the market playing in the market.

Q133 The Earl of Caithness: Does the EU produce the right quality of sugar that you want?

Tim Innocent: Yes.

Q134 Baroness Parminter: I am interested in your analysis of the future markets for sugar, both in Europe and globally. Do you see the market remaining static or going up?

Tim Innocent: Globally, there are constraints and changes within markets. The difference is that on a global level you can attempt to understand, whether or not a market is regulated, the natural supply/demand economics of population growth, whether people want to use or to eat more sugar or not, and uses in other areas. If there is a weather issue or crop failure, you can do research and you can have techniques and tools to try to find a way of containing or quantifying that risk.

In a market, even in the one that we will go to, there will still be a huge element of regulation and constraint that is outside all the normal factors. As a personal statement, if I am being absolutely honest, I am not confident about the future of the reform. We are still in the process of constraining the supply of the material, and just from a very basic food security sense this is the last of the materials in the CAP that has massive usage and that is constrained in the way it is. I think it is now time to say, "Enough is enough", really, and to allow the market to develop. If farmers want to grow more sugar in the UK, I am more than happy. If we want to bring more in and there is an industry there, I am more than happy, as long as the quality is there for us.

Q135 Baroness Parminter: You are a global FMCG (fast moving consumer goods company), and are you telling me that you cannot comment on whether you project your usage of sugar going up globally, what people are eating, or whether the market in Europe is going to remain fairly static, given that some of the regulatory drivers—such as the French taxation on sugary drinks and other initiatives—might be pushing the market in a particular direction?

Tim Innocent: As an FMCG company, we and the other members of UKISUG are all here really to make products that the consumer wants to eat. While there is a demand for those products, we will try to fulfil it. In this instance, if I speak for Nestlé, our driver is to make products that are healthy, are what consumers want to eat and are safe for them to eat. Quality is our primary driver.

As health and consuming trends change—as a manufacturing organisation responding to consumer need—clearly we will look to match that need. On the question of whether that will reduce sugar in Europe, it is possible that sugar usage will fall, but I do not know by how much. Contrary to that, on the world stage, as more countries move to a more developed economy their diets are changing to more westernised diets, and we have seen, not just in sugar but in many of the commodities that we buy, huge changes in price and in sources of demand. As China moves to a more industrialised society, not only does it develop different tastes but it needs food in different formats. For example, not everyone can grow their own food outside their flat if they work in the city. Big changes like that will change the balance. I have a team of people who can give me better advice on that. As a personal view, I would say that diets will change, world sugar is probably likely to increase, and Europe could well reduce or stay static, but I think that consumption has been fairly static for many years.

Q136 Lord Lewis of Newnham: In your paper you observe that isoglucose can be used by many manufacturers as an alternative sweetening ingredient, and in point of fact this could be more useful if the quota associated with it was actually removed. The quota for isoglucose in this country is very limited. I think it is about 5 per cent. That is only run by Tate & Lyle, if I understand it correctly. Do you find, then, that the processing is the limitation here, or is it the application of this isoglucose that is important?

Q137 The second factor that I would like to ask you about is this. Isoglucose of course is also a commodity that is used for the production of ethanol for renewables, and things of that nature. Does the quota include the use of it in this particular direction, or is it only used as a sweetener? After all, it is sugar in any other way. Really what we are saying, if I understand it correctly, is that it does not come from beet or cane sugar but from an alternative source such as wheat and maize.

Tim Innocent: There are all kinds of sweeteners that you might use to make a product. There will be certain times when you need sugar and there will be certain times when you need glucose, and certain products that need high fructose corn syrup. It seems strange that high fructose corn syrup is in the same legislation as sugar and is of quite limited quantity.

Q138 Lord Lewis of Newnham: But they are all sugars?

Tim Innocent: They are all sugars of different sorts. I am not a scientist at all, but my scientific colleagues tell me that you need the properties of crystallised sugar to make certain products, just as you need the properties of high fructose to make other types of product. We can have a range of recipes and it depends on the industry that you are in. It seems strange, in a constrained market, to have a further constraint on an alternative use. That would be my overriding comment. Why it is so low, I am not sure. Historically, I believe there was pressure from some to keep those quotas quite low. But that is a question for other people. I do not think that it includes the amount that is used in bioethanol, because bioethanol is produced out of sugar as well. I think that all that is outside the quota for food use.

Dominic Goudie: The quota is specifically for food use, as I understand it, and kept very low. As you have seen in the position paper, which was produced for a research project by our European organisation committee of European sugar users, there was potential in the market to move to around, I think, 20 per cent or so of sweetener consumption coming from isoglucose. There is that potential there, and I guess it is a case of whether the investment is available and whether it is economically viable to ramp up production. Obviously there are constraints on the storage of isoglucose. If we, as users in the UK, were to benefit from that, I think we would need isoglucose to be produced locally in the market, because transportation costs and storage could be a problem.

Q139 Lord Renton of Mount Harry: I must say I am no expert in this at all, but I do find what is going to happen to sugar a very puzzling business: quotas, no quotas and such like. Last week we had the NFU Sugar Board and British Sugar with us. They were very emphatic that quotas should continue and, if possible, continue as far as 2020. I also have a letter from Napier Brown, which supports the continuance of quotas. It does not support the outdated practice of importing raw sugar for refining into the EU. Your view is quite different from that of British Sugar, is it not? You think that quotas are unnecessary, and so on. How is it then that you feel that this product can survive without any market management?

Tim Innocent: Because many products do survive without market management. If you think about some of the other big things that we use, wheat is managed without market intervention. If you think about all the dairy products, they are still within the CAP, but there has been a gradual abolition of quota. A so-called soft landing has been described for the dairy industry, where quotas are extended year by year and thereby make quotas almost irrelevant to the production.

I am a great believer in farmers being able to grow crops that they want to grow, that we want to buy and that we can get into more partnerships. Some of the work that we are doing in other areas outside sugar is to get much closer to our farmers, and as an organisation Nestlé does that, too. I know that a lot of my competitors are doing the same thing. A lot of the cereals manufacturers are spending a lot of time getting much closer to the source. My view—we have had a discussion with the NFU as well and have expressed our differences of opinion—is that the market should be in a position where it can flex, grow or contract as the market demand requires, and not have an artificial constraint in place.

In some ways, what I find strange is the beet quota that we have in the UK, which does not allow the industry to have enough sugar to satisfy the entire needs of the UK. If farmers like growing it and it is a good crop, why would they not want to grow more? That is not an attack on Tate & Lyle; it is just to say that if Tate & Lyle has a great model, let it run that as well, but why not let the market decide rather than the politicians?

Q140 Lord Renton of Mount Harry: But the politicians do not decide, do they? I do not think that the Commission is politically driven in what it is doing, or is it driven by the needs of the French?

Tim Innocent: I perhaps should not comment, but—

Lord Renton of Mount Harry: No, I am asking you a question. You can comment freely on this.

Tim Innocent: I believe that there is a high degree of politics in the sugar-lobbying industry on the part of farmers and positions in other countries, but I do not know whether Dominic would want to comment on that.

Q141 Lord Renton of Mount Harry: Last question. Do you actually think that the Commission should continue and perhaps improve on what it is doing, even if everything becomes more and more deregulated? Is there really a purpose in the EU Commission being involved in this?

Tim Innocent: I guess for things such as ultimate food security, you might need someone looking at—

Q142 Lord Renton of Mount Harry: Food security?

Tim Innocent: The ability to supply. For example, if it was a completely free market and a particular product was no longer grown, you would want some understanding of what was going on there and maybe some form of safety net. I am afraid I do not know how that would work, but I think there will always be some requirement to make sure of that. From my brief knowledge of history, the foundation of the CAP was really to make sure that we had enough food to make sure that Europe never starved again. That was where it started from. It did not end up there, but it kind of started with that very good principle. I do not think that it is a bad principle to have, really—the ability to satisfy consumers' needs from agriculture, as close to source as possible, is always a good thing to have.

Q143 Lord Renton of Mount Harry: So to some extent do you agree with the Commission continuing to have powers relating to sugar?

Tim Innocent: To some extent but not to the extent that it has. There is a role to play in understanding the dynamics of the market and a more balanced approach. If we do not have enough beet sugar, why can we not look at imports, and why do we have to pay this ridiculous import duty? Why is there not a more level playing field? I am not assuming that tomorrow we will just say, "No quotas" and everything will be fine. The Commission will have a part to play in any managed transition away from quotas, but I am fundamentally of the opinion that we no longer need quotas and we should be away from them sooner rather than later. The year 2015 feels like a long time away, and 2020 seems a hell of a long way away.

Q144 Lord Giddens: My generous neighbour has already asked my question about precisely what kind of safety net there would be in a deregulated system, so can I ask you something different following on from the question asked by Baroness Parminter? It is the issue of the moment, really. What kind of responsibilities should the sugar industry, and more generally the food and drink industries, have for the health consequences of the foods that they produce, given the global nature of the obesity epidemic and something like 1 billion people in the world radically overweight? The health implications of that are stupendous. Is the industry doing enough to specify the responsibilities for that, or do you think that is a matter just for Government?

Tim Innocent: Dominic, do you want to make a comment?

Dominic Goudie: It is not my area of expertise by any stretch of the imagination, but the industry is doing an awful lot. We are working very closely with the Government. Companies have put pledges in place, as part of the responsibility deal, to make their products healthier for consumers. Ultimately, regulation on its own cannot achieve this. So many other factors come into play. Work is being done around education and working with consumers to establish how they consume these products to tackle the obesity epidemic. I do not think that focusing purely on individual products produced by the companies using sugar in their organisation will have the desired effect on its own.

Q145 Lord Giddens: I do not want to press you on something that is not your area of expertise, but you could argue that the companies advertise their products. Quite a lot of these adverts are aimed at children, who are pretty vulnerable. The health consequences are ginormous. They are picked up via the National Health Service, which is paid for by the taxpayer, and the industry is simply not contributing to the costs of the consequences of its efforts for health of the wider society, could one not argue? It is just some companies, such as Coca-Cola, that have been much more conscious of this issue in recent times.

Tim Innocent: Health and wellness is at the core of companies such as Nestlé. Nestlé as an organisation was founded as—

Q146 Lord Giddens: I know, I have looked on its website, but I think there is a difference between what is said and the actual consequences of what the companies do.

Tim Innocent: I think that we do everything that we can. We are in this business to produce products that consumers want to buy. To educate them, we do lots of work on reformulating our recipes to make them healthier and more permissible, but there is an element of choice in all this and in taste. It is not just going to end at products that contain sugar. You could equally look at products that contain fat and at products that contain excessive amounts of dairy. There are many reasons for obesity. Again, it is not my area, but across the piece we do a lot of work around health at the moment.

Lord Giddens: Except that, with respect, we know that sugar is one of the drivers. The consumption of sugar is one of the main changes that affects diet and produces such a range of health consequences that health systems are struggling to contain them.

Q147 Baroness Howarth of Breckland: We know from all the research that the products that make a difference worldwide to obesity are highly sweetened drinks. Why should there not be, as there is on tobacco and alcohol, a tax on highly sweetened drinks—this is a big sugar issue, and I am on your side in other things—in order to improve health, and is the industry looking at some of those wider issues?

Dominic Goudie: On the drinks side, I think we have seen an example of a tax brought in, and I do not think it is conclusive that it has the benefits for health that would be desired. Where it has been used it seems to be more of a tax-raising exercise.

Q148 Baroness Howarth of Breckland: You would not say that about tobacco. Look at the statistics.

Dominic Goudie: I am sorry, I do not know about that. As far as a tax on the sugar in soft drinks is concerned, I do not think the evidence has actually borne out that this has the desired consequences on public health—from what I have heard anyway.

Q149 Lord Whitty: There are multiple dimensions to this, but if you are going for a free-trade situation, the objective of a free-trade situation is that you get a cheaper price. If you get a cheaper price, you will have a higher consumption, particularly from low-income groups and children. There is a consequence for health of the trade and protectionist policy, so I do not think that we can ignore that. It is a fairly hefty one. There is also a development issue and a trade issue here. The quota system and the balance between cane and beet sugar in the distribution of quotas is partly to protect the EU beet producers, but it also protects industries in developing countries. We have seen some attempt to maintain that, but we have also seen a freeing up of that as a result of the last reform and the bilateral agreements with non-LOMA or non-ACP/LDC countries, which has freed up access to cane sugar. My question is really this: have you seen that as a significant benefit? If I can add to that, what do you think would happen if there were no quota for protecting beet? Would you then buy your sugar at something close to the global market price for cane sugar? If the quotas and the tariff went, to put it crudely would you be buying all your sugar from Brazil?

Tim Innocent: I do not think we would be buying all our sugar from Brazil, no. I think we would be looking to source from a number of places. The question maybe is whether, if it was that easy, we do not do some of that already? It is not that easy. The infrastructure is not in place. Aid through trade is a good thing to do, but it should not be the only driver. There are other ways to implement those mechanisms. I do not think we would buy all our sugar from Brazil. Brazil has enough domestic consumption of sugar for its own people and occasionally—or more than occasionally—for its ethanol production.

Q150 Lord Whitty: What I am really saying is that focusing on Brazil is probably not the right thing to do, but whatever the world price, whether we are talking about Brazil or Africa, whatever the lowest price is would appear to be at a lower price if you took the tariff off EU beet production. Therefore, would your demand not switch, if not to one country then to low-cost producers of cane sugar?

Tim Innocent: I do not think it would be lower than the reference price that the EU has set.

Q151 Lord Whitty: No. We are removing all those market interventions. If you removed quotas, reference prices and tariffs—you said you are a free marketeer—what would actually happen?

Tim Innocent: The market would adapt to the price level of the overall market. We would work within that, as would the suppliers.

Q152 The Chairman: Knowing what you know, would it drive down the domestic EU production of sugar beet, and would that be substituted for by imports, knowing what you know today?

Tim Innocent: Knowing what I know today, there are some very, very efficient producers of beet sugar in Europe that I think can compete with cane sugar. Their advantage is that they have an infrastructure in place that can deliver to users, which we cannot do. If you imagine that we take 20 or 30 tonnes in a lorry—and we have seven or eight of those every day—and wind that back into buying a 30,000-tonne container on the sea, how are you going to put the infrastructure and logistics in place? It is not impossible, but it would seem strange, when you already have that infrastructure, not to try to use it differently. I personally think that the market would compete at that point.

Q153 Lord Whitty: It would be useful to have a breakdown of costs as to how much you would pay for transportation and what effect that would have on the price. You have three: you have the production costs if you buy in Mozambique or wherever, you have the transportation and logistical costs, and you have the tariff. It would be interesting if we could see that breakdown, at least in broad terms.

Tim Innocent: Yes, we could look at doing something like that. We have some broad numbers around that.

The Chairman: That is very helpful, thank you.

Q154 Baroness Howarth of Breckland: I think you have addressed my general question, but I will just ask it in a different way. You talk about the tension between the production of sugar for food and sugar for alternatives—we have also talked about biofuels. You are a free marketeer, but you talk about these tensions and say that they would have to be managed for the sake of food security. Therefore, do you think there would be a different regulation regime to manage that tension even if the market was free?

Tim Innocent: There probably needs to be, and I do not think there is at the moment. Some of the issues that we have seen around the biofuel requests from Europe—that 5 per cent is to come from biofuels—have been completely delinked from anything to do with the CAP or the food industry. A joining mechanism at a European level might have been a good thing. I do not think that it has one, though, so maybe it could divert its attention into joining some dots rather than siloing.

Q155 Baroness Howarth of Breckland: That might be a better use of regulatory time than the present complex system.

Tim Innocent: Possibly, yes. As an organisation, we are trying to move from silo thinking to continuous excellence and thinking across the piece, so perhaps we could help Europe with that.

The Chairman: I think we are all done, Mr Innocent and Mr Goudie. Thank you very much. That has been most informative.

Tim Innocent: Thank you.