Sugarcane Market Secret Scenario

The Sugar Industry of Pakistan – Understanding Structural and Regulatory Underpinnings of the Current Sugar Crisis of Pakistan

Keywords: Sugarcane, Competing Crops, Water Use Efficiency, Sugar Crisis, Export Subsidy

1. Background

Pakistan is ranked 7th both in terms of production and export of sugar and is ranked 8th in consumption. Since 2010-11, Pakistan consistently has a surplus in sugar production and has earned $2.3 billion through exports. However, the recent sugar crisis has brought to the focus the important issue of export subsidy for sugar. Prior to Government permission of sugar export in December 2018, the retail prices of sugar were Rs.55 but then continuously start to increase with the increase of export. The export subsidy was granted at the rate of Rs.5.35 per kg amounting to Rs.2.47 billon which boost up the export and created deficit between demand and supply. This lead to increase prices in the local market.

2. Protection through Regulatory Distortions

It has been argued that the perennial nature of the sugarcane crop, non-storability, and non-transportability create demand for the protection both at the farm and sugar mills level to get the industry to flourish and survive. In this context, several regulatory distortions at the farm and industry level have been introduced to protect the interests of both farmers and millers (Box 1). However, in fact, the majority of distortions are introduced to protect the interest of sugar mills only and in some cases even at the cost of farmers' welfare.

3. Dissecting the Recent Sugar Crisis

It is observed that support prices had not been

BOX 1:
Details of different Distortions to protect Sugar mills and farmers

- Mills get benefits by not paying minimum support price to the farmers.
- Domestic Industry is protected through 40% customs duty on sugar imports. This creates economic distortions in favour of sugar mills.
- Crop zone changes with changing climate patterns but geographical barriers to the shifting of milling plants discourage competition and create inefficiencies in the sugar industry. Removing such barriers could lead to developing a cluster of sugarcane production in specialized areas of sugar production.
- License Raj: The new entry has been restricted in the sugar industry by introducing license Raj as a barrier because each new entrant requires a NOC from the province.
- However, mandatory crushing law provides protection to farmers, which cannot be ignored.

increased since 2015-16. In 2019, the support prices announced very late when the crushing season had already started. Resultantly, there was a slight decrease in sugarcane cultivated area. This leads to competition between sugar mills to purchase sugarcane during the 2019-20 crushing season. This forced the sugar mills against the usual practice to offer about 15% higher prices than the announced support prices to meet their demands, indicating the gap between supply and demand.

However, Economic Coordination Committee (ECC) at the recommendation of Sugar Advisory Board (SAB) approved the export of 1.00 and 0.10 million tons of sugar on October 2, 2018, and December 4, 2018, respectively. During the same meeting, secretary Ministry of National Food Security and Research raised the concern over low production of sugarcane due to water shortages and reduction in the area allocated to the crop.

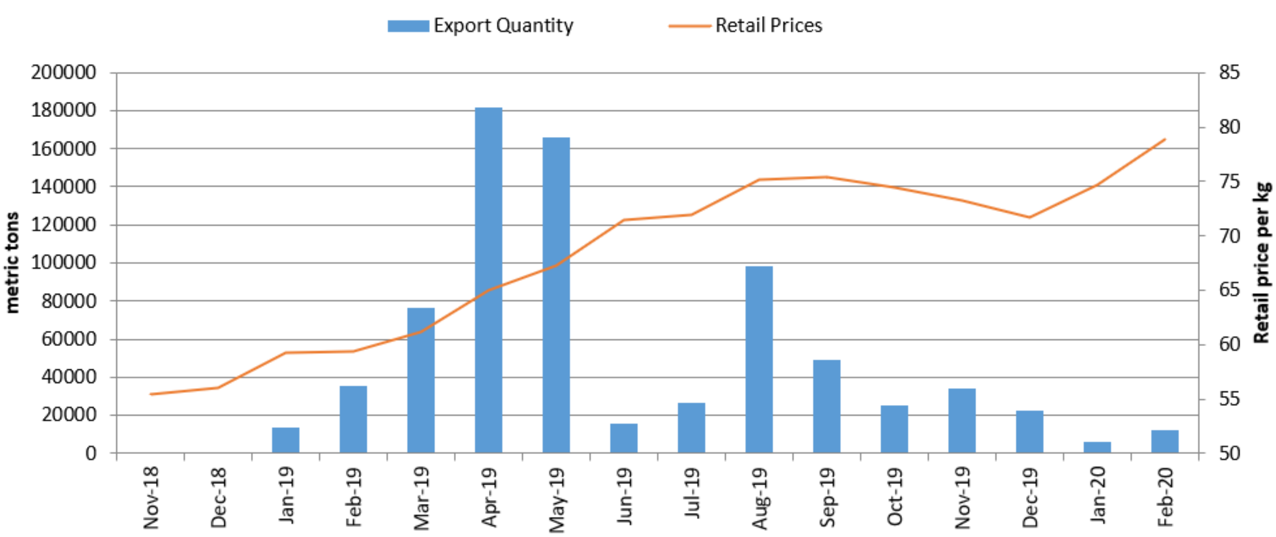

Figure 2: Sugar Exports and Retail Prices
Source: Pakistan Bureau of Statistics and State Pakistan

The retail price of sugar started to increase in December 2018 when the export of sugar was allowed (Figure 1). The retail price was the lowest at Rs.55.99 per kg on November 18 but by June 2019 it had reached to Rs.71.44 per kg and the retail prices further increased from Rs.71.44 to Rs.74.64 from July 2019 to January 2020.

In the subsequent meeting of SAB, Punjab raised the concern about the increasing prices of sugar in the local market but ban on export was not recommended by SAB. Even though estimates clearly demonstrate that net stocks is at negative 0.191 million tons and facts was also presented in the meeting. However, SAB was continuously believing that increasing prices of sugar is mainly the result of hoarding but not of export. It is important to note that there was no increase in GST or other taxes and prices of other inputs remained stable during this period.

4. Key Takeaways

The support price for sugarcane is only national because the government does not procure sugar and, hence, there is no mechanism in place to enforce it. Sugarcane is sold above the support price whenever there is a shortage and below the support price when there is a surplus.

The License Raj limits new entrants into the sugar industry. It creates cartelization and leads to an increase in the profitability of sugar mills only. Similarly, trade barriers like import tariffs need to be removed or rationalized. Both these measures may lead to an efficient allocation of resources in this sector and an improvement in the welfare of local consumers.

Price quota and subsidies have been used as a tool for offloading the surplus supply of sugar and to fill the gap between supply and demand. However, the government failed to take a timely decision in light of available information, which led to the recent sugar crisis.

Deregulation of the sugar market is extremely important to promote free trade mechanism where price signals can be effectively conveyed to all stakeholders to attract investment and increase competitiveness.