

# Measures to Prevent Risks for Sugar Industry

by TRINH MINH CHÂU

## 1. The problem

Vietnam has natural conditions for development of sugarcane farming and mobilization of both foreign and domestic investment needed for sugar industry in order to meet the domestic market demand and reduce import of sugar. The 8<sup>th</sup> VCP Congress wants the sugar industry to "make intensive investment to expand existing factories, build new ones of medium and small sizes in provinces with small sugarcane areas, and build large-scale ones in provinces with bigger sugarcane areas with a view to producing some one million tonnes a year."

In 1994, the industry included 12 sugar refineries with a total capacity of 10,300 tonnes per day along with numerous small-scale ones that helped increase the total output to 270,000 tonnes. The Sugar Program in 2000-03 helped increase the number of industrial refineries to 44 with a total capacity of 82,950 tonnes per day and the output to 1,056,188 tonnes. The total output rose to 1,206,188 tonnes when small-scale refineries were included. However, up to June 2005, three refineries went out of business. In the 2004-05 crop, the industry produced 1,082,000 tonnes of sugar from 5,407,694 tonnes of sugarcane.

Besides achievements, the sugar industry also faces dangers to its sustainable development that caused many sugarcane planters to suffer losses over years. One of factors that produced negative ef-



fects on the industry and went unnoticed is the risk originated from changes in the market price.

The sugar industry will keep playing an important role in the economy and it will face greater dangers in the coming years when the trade barriers are lifted. That is why the industry should take measures to prevent risks.

## 2. Negative effects from changes in the market price

The sugar output, like other farm products, depends on natural conditions and the most visible risk is falls in prices when the harvest is good, and vice versa.

Sugarcane is usually grown on small areas so

it's hard to standardize its quality and gather enough quantity for big contracts.

Prices of farm products could change every crop or year, and before and after harvest time.

These factors make it hard for sugar refineries to fix their production cost (because the sugarcane accounts for 50% of the sugar production cost) and determine their selling price.

Sugar is usually sold under a spot delivery term, which implies many shortcomings: (1) temporary imbalance between the supply and demand leads to changes in prices at time of delivery; (2) the balance of market forces exists only at local level and this leads to differences in prices between different provinces; and (3) both sellers and buyers are affected by changes in relations between the supply and demand at time of delivery.





Keen competition between industrial refineries, and between them with manual ones usually leads to unnecessary price wars with the result that the margin profit is reduced.

### 3. Trade in sugar in Vietnam

In Vietnam, production and distribution of farm products are underdeveloped. In the sugar industry there is no top-down coordination or cooperation with the result that all transactions involve high degrees of risk. Most transactions are conducted on the cash market or on a spot-delivery basis. Even in exporting their goods, most refineries prefer cash-and-carry approach and they usually miss remarkable profits.

In the past few years, only shotgun measures have been taken to prevent price risks with the result that they were not effective and even produced more bad effects:

- In 2000, the decision to increase sugar storage produced no effect and the sugar price fell to a record low level, about VND3,000 per kilo.

- The Government decided to give grace periods, and exemption of interest payments, to sugarcane planters and sugar refineries, and imposed higher import duties on imported sugar. These measures are considered as non-market ones and tend to cause losses to the public funds and make producers more dependent on the governmental support.

- As for diversification of crops and products as a measure to distribute risks, it causes a lot of trouble for sugar refineries because they couldn't secure sources of raw materials when peasants grew other crops instead of sugarcane. Moreover, this measure goes against the common trend in which farming land is specialized

in certain crops in order to reduce the production cost.

- The PM made Decision 80/2002/QĐ-TTg in 2002 to encourage contracts to sell between sugarcane planters and refineries. This was a right policy that aimed at linking planters with sugar refineries but it failed to produce intended results because of lack of regulations against failure to carry out the contract.

- Decision 110/2002/QĐ-TTg to establish a fund for insurance of exports was issued in 2002 but the sugar authorities didn't carry it out.

- An Association of Sugar Refineries has been established but it failed to take measures to prevent risks or encourage production of sugarcane and sugar.

### 4. Some suggested measures

The market economy has just been in its first stages of development and many processes of producing and distributing goods and services didn't grow evenly. As for the agriculture, distribution of farm products and development of a market for them are the two weakest stages.

Peasants still produce goods at small scale and too many middlepersons exist between them and end users, and as a result, there is no concentrated source of supply that could regulate fluctuations in prices and compete against foreign ones. This situation is also found in the sugar industry. From foreign experience and surveys of local production, I suggest the following measures.

- a. On the spot market:

- Supplying information about market prices and demand to both planters and refineries in order to help them work out effective business plans.

- Establishing a sugarcane exchange that could supply information, trade sugarcane in large quantity, hold auctions and bidding for orders placed by the Government, keep a close watch on product quality, and help planters and refineries get accustomed with e-commerce.

- Developing B2B transactions by legalizing contracts exchanged by planters and refineries and standards of product quality.

- b. On the futures market:

Most refineries have not been ready for this market because they lack knowledge and investment but this market is a good measure to stabilize the market price and ensure sources of raw materials for refineries and stable income for planters. For the time being, the government could encourage refineries to buy options, forwards and futures on foreign sugar exchanges if necessary.

- c. Role of the Association of Sugar Refineries:

This Association must act as a center and forum for sugar refineries and sugarcane planters as well. Its main tasks are to secure sources of raw materials, make investment plans, and suggest an overall plan for production, distribution and pricing. In addition, it could supply information, technical assistance, and credit; and introduce derivatives to its members. By organizing and uniting all refineries, it could control the product quality and quantity, thereby stabilizing the market prices and helping prevent unnecessary risks. ■



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