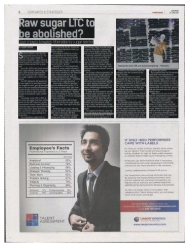
Raw sugar LTC to be abolished?

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Raw sugar LTC to be abolished?

Govt moves towards liberalising sugar sector

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SPECULATION is rife that the long term contract (LTC) for the raw sugar supply for Malaysia's domestic sugar refining industry may be abolished upon the expiry of the current LTC by year-end.

Since the 1970s, the Government, local sugar refiners and foreign suppliers have jointly negotiated for the LTC to procure the country's raw sugar supply over a three-year period.

The LTC stipulates the quantum of raw sugar to be purchased over the length of cover, pre-determined prices that are usually influenced by market prices at the time of negotiation as well as other purchases bought at the global sugar market prices.

Previously, some 70% to 80% of the total raw sugar purchase will be made via the LTC. However, as the Government moved toward liberalising the sugar sector, the quota has been reduced to about 30% under the current LTC especially with the removal of the sugar subsidy last November.

The remaining supply will be sourced directly by the respective sugar refinery operators from the global market.

According to industry sources, the negotiation for the new LTC with the involved parties should normally start in June but "so far there are still no talks on the LTC for the 2015-2017 period".

Should the LTC mechanism be abolished, some market observers are concerned that this might introduce more volatility to the domestic sugar refinery operators' gross margin going forward. Malaysia generally imports about 1.7 million tonnes of raw sugar per year.

Some sugar refiners, however, say the abolishment of the LTC is the least on their mind right now as "there is a large global surplus of raw sugar amounting to 7 million tonnes, resulting in a sharp drop in prices, trading at 17-18 US cents per pound currently.

Many have been able to take advantage of the low sugar prices to lock in their raw sugar costs this year.

In Malaysia, the sugar refining players are MSM Malaysia Holdings Bhd and Tradewinds (M) Bhd.

MSM's sugar refineries include Kilang Gula Felda Perlis Sdn Bhd and Malayan Sugar Manufacturing Company Bhd while Tradewinds owns Central Sugars Refinery Sdn Bhd and Gula Padang Terap Sdn Bhd.

Currently, domestic sugar refiners are most concerned with the four-decade old well regulated sugar industry being disrupted with the influx of cheaper refined sugar imports that has made their domestic business deemed "uncompetitive."

Local sugar refinery operators are also experiencing margin squeeze particularly with the removal of sugar subsidies last November which saw the Government giving out more approved permits (APs) for other manufacturing outfits to import refined sugar directly from suppliers overseas.

In 2009, the Government has also provided sugar subsidies to keep the retail sugar prices below the global prices. The domestic prices of coarse and fine white sugar are fixed by the Government while brown, caster and molasses prices are determined at prevailing market prices.

The imports of refined sugar are also controlled by the Government. Malaysia imported about 1.7 million tonnes of raw sugar per year.

However, the situation now has changed with the removal of the sugar subsidy.

The Government has even increased the APs for refined sugar imports to 16 this year from 13 beverage companies in 2013 which saw the refined sugar imports rising to 150,000 tonnes in the first five months of this year from 75,000 tonnes a year earlier.

MSM which controls over 57% of the total sugar market in Malaysia is feeling the brunt from the increasing imports.

Its president and group CEO Datuk Sheikh Awab Sheikh Abod says the competition from imported refined sugar is putting pressure on the company's domestic sales and profit margin despite the advantage it has in terms of lower raw material (sugar) costs given the big drop in global sugar prices.

He is hopeful that the Goverment could limit the importation of refined sugar into Malaysia to protect the local sugar refiners' business. Another alternative would to allow local sugar refiners to import refined sugar to compete on a level playing field with the other players that are allocated with the APs for refined sugar.

CIMB Research says in its report that the competition from higher refined sugar imports appears to be stiffer than its expectation.

"This is likely to negate the impact of lower sugar costs that we expect MSM to enjoy this year," it says, adding that the group has indicated that it will aggressively look at growing through mergers and acquisitiions to expand its earnings base over time.

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Tradewinds owns CSR and Gula Padang Terap. – Bernama