Survival Strategies for the Fiji Sugar Industry

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Abstract

This paper looks at the problems facing the Fiji sugar industry and the options and prospects for restructuring the industry. In recent years the sugar industry has been confronted with a number of problems, both internal and external, such as declining productivity both in the field and the factory, declining sugar quality, poor industrial relations, rising production costs, shortage of skilled manpower, ineffective management, fluctuations in world free market prices and phasing out of the long term market in the European Union. The sugar industry is too crucial to Fiji's economy to be ignored. The industry structure and stakeholder relationship is somewhat outdated and needs to be revisited. The study will explore some of the options for restructuring the industry to facilitate it survival.

Introduction

Sugar has been the backbone of Fiji's economy for most of the past century. Since its introduction in 1880, the sugar industry has dominated Fiji's commercial agricultural sector. While dependence on the sugar industry has declined substantially during the past 2 decades (Prasad and Narayan, 2003), currently it still accounts for 7 percent of the GDP, 25 percent of employment and approximately 22 percent of the annual export revenue (Sugar Commission of Fiji , 2002: 7). About ninety percent of Fiji's raw sugar is exported to international markets, mostly at premium prices under the ACP/EU Sugar Protocol and other preferential arrangements. Few sugar-producing countries are dependent to this extent on the export market. The industry also plays a significant role in generating internal food supply as cane farmers produce agricultural crops and livestock for their own consumption as well as for cash sale. Sugar consumption in the country itself, averaging 50 kilograms per year, is about twice the world average consumption.

In and before the mid 1980s, Fiji was regarded internationally as an efficient producer and reliable supplier of high quality sugar. It now has none of those rankings. A 1991 report by Landell Mills Commodities Studies found that Fiji is now ranked among the lowest in terms of key performance indicators such as cane yield per hectare, sugar yield per hectare, tonnes of cane to tonnes of sugar ratio, and sugar produced per tonne of milling capacity. However, its sugar mills are of average size by world standards. The question that needs to be asked, is what went wrong during the past 15 or so years that the industry has declined so rapidly as the LMC states. This paper identifies some of the major problems currently facing the industry, and how they could be addressed. It also provides an assessment of what some of the options are in terms of restructuring the industry.

Background of the Industry

The sugar industry initially started on a plantation and estate system but changed to tenant and small farm system because of labour shortage. Cane farming in Fiji is extended-family based. Farmer behaviour is not strictly what one would find in a business enterprise. This feature has remained intact over the past three quarters of a century. It distinguishes the Fiji sugar industry from those of many other sugar producing countries, where production is plantation based. In most other countries, sugar cane is grown on plantations owned by the millers and to a lesser extent by independent growers but on relatively large farms. In Fiji, on the other hand, over 21,000 independent growers, grow nearly all sugar cane on farms averaging four hectares. Most of the cane is planted on land leased either from the government or the Native Land Trust Broad. Land lease uncertainty is one of the major problems confronting the sugar industry currently (see Lal, et al, 2001: 106-119).

The structure of the sugar industry is complex. It is made up of many individuals and institutions. The two main partners are the sugar cane growers and the Fiji Sugar Corporation (FSC), the only miller, which owns and operates the country's four raw sugar processing mills, the rail transport system, the sugar cane research centre and other associated infrastructure. For much of the history of the industry, the relationship between these two parties has been adversarial rather than that of a partnership. A contract between the growers and the miller, called the 'Master Award', after an award made by an independent judge appointed by the Government, governs the commercial and legal relationship between the growers and the miller. The strict managerial control, which the Colonial Sugar Refining Company, the mill owner prior to the Fiji government buying it out, exercised on the growers, no longer exists. While the miller is the single buyer of sugar cane, thereby maintaining its monopsony status, the growers are strongly organised and carry significant clout; at certain occasions, they have demonstrated that they can also act as a single seller, thereby displaying the power of a monopoly.

Other than the two immediate stakeholders, there are other partners in the industry. These are: the Sugar Commission of Fiji, which is the apex co-ordinating institution in the industry, the Sugar Industry Tribunal, Fiji Sugar Marketing Company, Sugar Cane Growers Fund Authority, Native Land Trust Board, Sugarcane Lorry Transport Association, and the Government of Fiji in the role as an arbiter rather than the owner of the mills. The government has a dual, and potentially conflicting, role in the industry; it is the majority shareholder in the milling company while it is also entrusted with the role of enacting and implementing the laws of the country which, inter alia, govern the industry. The Sugar Industry Act 1984 provides the legislative framework which defines the role and relationships among the various parties in the industry, whereas the Master Award governs the relationship between the growers and the miller.

The most contentious issue in all the contracts between the cane growers and the miller, including that in the current Master Award, has been the formula regarding the division of proceeds from the sale of sugar and molasses. Growers produce sugar cane, which is the raw material for the production of the saleable commodity raw sugar (and to a smaller extent molasses). Hence emerges the need to apportion the proceeds of sugar and molasses equitably between the two main stakeholders. Up till 1960, it was the miller who solely determined the price of cane that was to be paid to the farmers. After intense farmer agitation, the colonial government appointed a Commission, headed by Sir Malcolm Trustum Eve, who devised a proceeds sharing formula. The Eve Commission formula, which was operational in the 1960s, was a rather complex one where the farmers had great difficulty in understanding the approximate division of proceeds. The division turned out to be 57.75% for growers and 42.25% for millers (Moynagh, 1981:187-221). It was a complicated formula where the proceeds were split twice: in the first split the miller took out all its (miller's) costs while in the second split it divided the remainder of the proceeds between itself and the growers. The details of the formula are given in Appendix 1.

The pricing formula was such that it assured the operations of the miller and maintained the prior status where the growers shouldered most of the risks of the industry. When the sugar markets were depressed, it meant lower profits, but under the formula, it was the cane growers who bore the risks and received relatively low prices for their sugar cane.

After another series of agitation, another commission was appointed to look into the proceeds formula. Headed by Lord Denning, the Award divided the sugar proceeds 65% and 35% between growers and the miller respectively, with a guaranteed minimum price of cane at $7.75 per tonne. The miller no longer had the security of meeting all its costs as a first charge from the total sugar earnings. Its share of proceeds was also reduced. The miller protested; the government informed it that if it was not satisfied with the Award it would buy the miller out. The Denning Award led to the departure of the CSR in 1973. The new independent government of Fiji purchased the CSR interests and began operating the mills. Sugar cane price paid to growers increased from $9.76 tonne in 1973 to $20.90 in 1974. Growers regarded the Denning Award as much fairer than the Eve Award. The Denning Award, however, was to last only for a decade. In 1975, the share of proceeds to the growers was increased from 65% to 70%. From 1980 to 1989, a different contract, called the Sugar Advisory Council (SAC) contract, ruled the grower-miller relations. The SAC contract was similar to the Denning contract but with the growers' share being 70%. A new look into the formula took place in the late

1980's and early 1990's. The outcome, after an award by Justice Kermode, is known as the Master Award, which continues to provide the legal and commercial framework guiding the relationship between the growers and the miller.

The division of proceeds under the Master Award is based on sugar cane output. Table 1 shows the proceed sharing ratios.

Table 1: Sugar Proceed Sharing Ratios

Total sugar produced	**Growers' share**	**Miller's share**
Up to 325,000 tonnes	70 percent	30 percent
325,000 - 350,000 tonnes	72.5 percent	27.5 percent
Tonnes in excess of 350,000	75 percent	25 percent

* These percentages are based on net proceeds on sugar and molasses sales after industry cost have been deducted. Industry costs are defined as those relating to sugar marketing, and other industry institutions such as the Sugar Commission of Fiji, and the Sugar Cane Research Centre.
(Source: Sugar Industry Tribunal).

The millers share of the proceeds is now regarded by the FSC as among the lowest in the world. According to the Landell Mills Commodities Studies 'the proportion going to growers must now be approaching the limit beyond which the miller's capacity to finance adequate renewal of factory and transport installations would probably be jeopardised' (1991: 13). It ought to, however, be noted that the structure of the sugar industry varies from country to country and there is a need for caution when comparing the division of proceeds.

Some observers believe that it was political expediency rather than commercial astuteness that allowed the government, which is the majority shareholder in the milling company, to accede to the Kermode formula. Though the Award was made by a judge (Justice Kermode), the miller did not have to accept the Award; it could have appealed. But it was a time of political uncertainty and government could not be fighting on too many fronts.

Industry Problems

The sugar industry is currently inundated with numerous problems. It is at a critical crossroad now. The problems have been highlighted publicly as well as within the industry circles. A newspaper editorial predicted doom for the industry:

> Fiji's sugar industry has no God-given right to survive. Like any other commercial enterprise, it stands or falls by its ability to supply its market with a product of the quality and price those markets demand. Fiji's sugar industry cannot do those things and is doomed to fall unless it learns to do them. Many, including this newspaper, have reminded the industry stakeholders of this simple rule of business. Politics has not only stifled the growth of this vital export earner but now threatens to kill it completely. Without radical and rapid reforms, this industry will die " (Fiji Times, 26/11/2001 p 5).

There are problems on the side of both, the growers and the miller.

On the *growers* side, the major problems include declining production and farm productivity, rising cost of inputs, serious shortage of farm workers and cane cutters, an apparent unwillingness to accept best production practice, harvesting and delivery methods, cane weight based payment system, the supply of a high proportion of burnt and stale cane to the mills (which slows the milling process and produces poor quality sugar), and the expiry of native land leases with consequent demands for large 'goodwill' payments and high land rentals which further erode the commercial viability of cane cultivation.

For *FSC*, the problems include low production and productivity (which means lower level of revenue), inadequate factory capacity, rising cost of production, high fixed cost, lack of skilled personnel, a deteriorating rail transport system (which is not able to efficiently haul the crop to the mills), declining sugar quality, and poor financial and business management which has seen a lack of investment to maintain factory and rail capacity

Then there are problems which are applicable to all the stakeholders. The major problem on this account is the possible loss of the preferential European Union market, which was established under the Lome Convention/Sugar Protocol. This loss would see a substantial decline in the gross sugar proceeds flowing into Fiji. Additional domestic problems include a lack of consensus on the proposed restructuring of the industry, poor industrial relations among the various parties in the industry, possible politicisation of the sugar industry, and the general state of politics and uncertainty in the country following the events of 2000. Furthermore the industry alleges that it has lost about $100 million over the last decade as a result of boycotts and strikes. The FSC, however, has not provided any figures to back this claim.

Another problem is that there is widespread belief throughout the industry that the sugar industry will not be allowed to fail because the stakes are too high. The stakeholders believe that the government will eventually step in to keep it going. This has bred complacency in the industry. During the last two years the government has provided special financial assistance to the miller (FSC) to facilitate its continued operation, thereby making the stakeholders more complacent.

What, however, has been accepted by all stakeholders is that there is an urgent need to bail out the industry. There, however, is no agreement on what the process ought to be and what outcomes are expected.

Industry Restructuring

From 1995, sugar industry leaders have been considering options for reforming the industry. But stakeholders have been unable to agree on the fundamentals like the nature of the problems and the likely solutions. In 1997, the stakeholder statutory representatives were able to agree on a Sugar Industry Strategic Plan. This document set out a 20-year plan to make the industry internationally competitive.

Some of the strategies proposed are slowly being implemented by the FSC and the government. But the institutional environment was substantially changed with the 2000 political instability. The FSC's financial position continued to deteriorate; in 2003, it could only keep its machines running on the basis of a government write-off of a major loan, and a government guarantee of a further multi-million dollar loan. On the other hand, the government has so far not found a satisfactory solution to the land lease crisis. So far approximately seventy percent of the expired native leases have not been renewed.

Overall, there are six broad options involved in restructuring the sugar industry. These are:

1. Privatisation of the Fiji Sugar Corporation
2. Continuing with the status quo
3. Implementing the Sugar Industry Strategic Plan (internal industry restructuring)

4 Implementing the ‘Way Forward Proposal’
5 Entering into a management contract with an experienced international sugar milling organisation
6 Entering into a joint venture or strategic alliance with an international sugar milling organisation.

These options are considered below.

Option 1: Privatisation of the Fiji Sugar Corporation

The government is currently engaged in implementing a public sector reform programme in the country. This programme started over ten years ago (see Appana, 2003). A number of organisations have been identified for privatisation. The government's focus so far has been on commercialising and corporatising state owned enterprises. Privatisation is seen as the last stage of the process. Since its inception, the FSC has operated as a commercial company rather than as a department of the government with normal civil service type management. Its operations are guided by the Companies Act, and decisions are made by shareholders. In 1973, the government, holding 98.4% of the shares, was in almost total control of the company. But it gradually began selling its shares to the private sector. Currently it retains only 68% of the shares in the company. Table 2 gives the shareholding structure of the FSC.

Table 2: Shareholding Structure of FSC, 2002

Shareholder	Shares Held	% of all shares
Govt of Fiji	30,239,160	68.11%
Fiji National Provident Fund	7,544,219	16.99%
Fijian Holdings Ltd	3,933,900	9.00%
Unit Trust of Fiji (Trustee) Co Ltd	374,539	0.84%
Fijian Holdings Securities Ltd	300000	0.68%
Colonial Mutual Life Assurance Society Ltd	250,080	0.56%
Sugar Cane Growers Council	119,401	0.27%
Ba Provincial Holdings Ltd	101,951	0.23%
Robert Lee	98,720	0.22%
Reddy's Enterprises Ltd	74,050	0.17%
Top Ten Shareholders	43,096,020	97.1%
Other Small Shareholders	1,303,978	2.94%
Total shares	44,399,998	

(Source: FSC Annual Report)

The FSC has the necessary organisational and operational structure necessary for privatisation. During its nearly thirty years of existence, it has nearly always operated on a commercial basis, as well as without financial support from government. However, it incurred losses during the financial years ending 1986, 1997, 1998, 2001, 2002 and 2003, with projections for greater losses in the future.

There have been occasional interests shown by private investors in purchasing the majority interests in the industry. But the privatisation option is not likely to be successful for numerous reasons. First, the FSC's current financial position is precarious. The company is not able to operate without further support and loan guarantee from the government. The government loaned FSC $25.5 million in 2002; it continually asks for, and gets, further loan guarantees from the government. In 2002 the FSC informed the Sugar Industry Tribunal, as required under the Sugar Industry Act 1984, that it was not in a financial position to operate the mills for the 2003 crushing season. Under contractual obligations, the miller is required to give the cane growers a one-year notice of how much sugar cane it would accept for crushing. The government reluctantly gave an assurance of financial support to FSC to allow it to operate the mills during the 2003 season.

Second, trading in FSC shares was suspended by the South Pacific Stock Exchange for about two months in 2001 when FSC started discussion on the restructuring of the organisation. This was done at the request of the FSC to avoid any insider trading as some individuals could be privy to confidential information and others not. Fiji is a small country, where there is a close association between large entrepreneurs, policy makers and policy implementers. In such an environment, the possibility of insider trading is significant. Possibilities of insider trading could erode the value of the company.

Third, given the state of the company now, its value would be pretty low. Investors would more likely offer a very low price for the assets. Table 3 shows the trends in the share prices of the FSC.

Table 3: Share Price Trends

year	Share price	Dividend
1998	$0.55	$0.0375
1999	$0.75	$0.025
2000	$0.55	$0.025
2001	$0.35	$0.00
2002	$0.35	$0.00
2003	$0.25	$0.00

(Source: South Pacific Stock Exchange)

In the context of a continuously declining share prices, and the insolvent nature of the company now, it would not be commercially prudent, from an owner's point of view, to sell the company now. From the seller's point of view, it is better to sell an organisation when it is doing well rather than to sell it when it has been run to the ground, unless there was no hope of resurrecting the business at all.

Fourth, the government may not yet be ready to relinquish ownership and control of an industry, which is of high strategic significance to the economy. Government ownership of the milling organisation also gives it political control of the industry. The government has, over the years, used the sugar industry, via its ownership of the FSC, as a vehicle for promoting and implementing its national development plans. The history of the nation over the last 120 years, race relations, politics, and Fiji's growth and development, all have a symbiotic relationship with the sugar industry. Hence, it would be difficult, if not imprudent, for any national government to relinquish ownership of Fiji Sugar Corporation to a private investor under the current circumstances.

Option 2: Continue with the status quo

Another option is to continue with the current structure, especially if the stakeholders are not able to agree to reform the industry. This option is already a problem as FSC is now technically insolvent. As such, this option would only remain possible if the government continued to pump in money into the business. But this is unlikely to be the case. The government could help in the short term but certainly not forever. In the past, it has financially assisted numerous statutory organisations (such as Housing Authority, Pacific Fishing Company, Air Pacific, Fiji Electricity Authority, Radio Fiji, Fiji Pine Commission) as well as other private companies (like Emperor Gold Mining Company, Fijian Holdings Ltd, and Native Land Development Corporation). But the government's financial position itself is such that even if it wanted to, it could not provide unlimited funding to the FSC.

Another important factor is that for many years, it was believed in Fiji that if there were one government owned enterprise which would continue to operate with financial prudence and not rely on government aid, it would be FSC. This is no longer the case. Giving FSC untrammelled access to government coffers would send wrong signals to business institutions in general and statutory organisations in particular.

Continuing with the status quo will, thus, bring an early demise of the industry. The closure of the sugar industry will bring massive dislocation in the sugar belt and directly affect about forty thousand workers and approximately one-quarter of the nation's population. This will affect the entire fabric of the society. Without any viable alternative, it will lead to widespread poverty and deteriorating law and order conditions.

Option 3: Implement Sugar Industry Strategic Plan

In 1997, the Sugar Commission of Fiji published a report called *'Sugar Industry Strategic Plan: Changing Attitudes – Implementing "Best Practice" for a new World in trade'*. The plan sought to increase productivity and reduce costs, both for the growers and the miller over a twenty-year period. The main objectives of this plan are to:

(i) introduce a quality cane payment system, improve cultivation and harvesting practices;
(ii) reduce crushing season to 26 weeks, from the current 34–week period, thereby increasing sugar content by 13.4% by 2010;
(iii) modernise the railway system and the mills by appropriate new investment to help increase sugar recovery to 90%; and
(iv) achieve a tonne cane : tonne sugar ratio of 7.7 by 2010.

Table 4 provides the strategies for achieving the main objectives under the plan.

Although the strategic plan was developed in 1997 and some of the circumstances have substantially changed, it is proposed in this paper that this plan is the most realistic one vis-a-vis the other five options listed above. Implementing this plan would be easier for the FSC if government were the sole owner of the FSC, for this would enable it to make the painful decisions regarding restructuring.

Some of the positive features of the strategic plan are:

- This plan was approved and accepted by all the statutory sugar industry institutions in 1997. This is a significant feature because there is currently no agreement on any of the other options

Table 4: Strategies under Sugar Industry Strategic Plan

Stage	Period	Focus	Main Strategies
1	1997-2001	Investing in Efficiency	* Introduce Productivity Payment * Re-organise Industry Institutions * Revitalise Rail Transport * Invest in Mill Efficiency * Improve Public/Grower Awareness * Phase in Mechanical Loading * Start Land Utilisation Board * User-Pay Charges on Rail
2	2002-2006	Quality Cane Benefits	* Introduce Quality Cane Pay * Set Sector Based Targets * Improve Rail/Farm Interface * Selective Mechanical Harvesting * Optimum Mill Efficiency/Capacity
3	2007-2020	Best Practice Culture	* Maximise Sugar Content/Acre * Expand in Vanua Levu * Automate Mills appropriately * Increase Mill Capacity to 4.6 MT

(Source: Sugar Commission of Fiji, 1997: 7)

- Some of the strategies are already being implemented, for example trial mechanical harvesting and loading.
- This plan appears most feasible in terms of financial requirements. Had the plan been implemented from 1998, it would not have required substantial sum of money as its funding was spread over a longer time period. But still, it is not too late, though the financial costs would be higher now. The plan requires all stakeholders to implement their part of the strategy, with the government assisting with funding.
- All stakeholders have incentives to support and implement the strategies. The plan requires the stakeholders to change their attitudes and act like partners in an effort to make the sugar cake bigger rather than demanding a bigger slice of a decreasing pie. It is estimated that, with sound investment and increased efficiency in all areas of the industry's operation, an extra 107,000 tonnes of sugar, valued at $35 million annually (Sugar Commission of Fiji, 1997: 19) could be gained.

Some of the negative features of this option are:

- The success of the plan depends on the commitment of the stakeholders to put the interests of the industry ahead of sectional interests, petty politics, historical mistrust and rivalry. There appears to be much change in the attitudes of some of the stakeholders since 1997 when the plan was brought into effect. There are indications that the growers, the FSC and the workers have hardened their positions regarding what they are going to give and take. Some stakeholders who had originally agreed with the plan are now attempting to stall its implementation.
- The individual mills will not compete for profitability and efficiency, as would be expected in the 'Way Forward' proposal. The poor performance of any one of them would affect the overall performance of the miller as well as the industry. It would be difficult to incorporate accountability on an individual mill basis, when they are in fact, part of a bigger corporate entity.
- The circumstances have changed so much since 1997. Substantial funding is now required to improve mill efficiency, rail transportation and related infrastructure. Without this immediate help, there is not much of this plan left to implement and concomitant with it, any immediate or significant benefit to the stakeholders.
- There is no sign yet that the world's best practices are being implemented. For example, the delivery of burnt and delayed cane is on the rise; it now averages about fifty percent of the annual crop for the past five seasons.
- Without some solution to the land lease problem, there cannot be any meaningful industry restructuring. The plan assumes that there will be sufficient sugar cane available for crushing. The longer the land lease issue remains unresolved, the less likely would it be a sound assumption to proceed with.
- There will be redundancies in all sectors of the industry. There is no social security or welfare net to cater for those adversely affected. Financial packages will have to be arranged to reduce the pain of dislocation to those affected by this restructure.

Option 4: The 'Way Forward Proposal'

The 'Way Forward' proposal was made in 2002 by the FSC and the Sugar Cane Growers Council. It suggests fundamental reforms to the industry, including sweeping restructure of the industry. The key features of this proposal are:

(i) Bring in a commercial approach to the entire sugar industry. The major stakeholders also become shareholders in the milling company, which would act to bring in the much-needed 'unity of purpose'.

(ii) Reorganise the agriculture side of the industry as a business on a commercial basis. Cane growers with annual output less than 200 tonnes will have the option of exiting the industry by selling their farm harvest quotas, as well as encouraged to amalgamate to achieve economies of scale.

(iii) The four current mills will become separate commercial businesses, each responsible for its own performance and survival. Each will compete against the other mills. This will force them to reduce costs and increase efficiency in all areas of their operations. This will help prepare them to compete in the global market under a freer world trade in sugar.

(iv) After buying out the minority shareholders, the government will need to transfer the ownership of the mills to the four separate companies, which will be owned by the stakeholders.

(v) Repeal the Sugar Industry Act 1984, which currently regulates the industry.

Some of the positive features of this option are:

- The whole industry will operate on a commercial basis and market forces will determine its operation.
- It will provide lessons to other government-owned organisations on how to manage businesses commercially, and eventually bring in a business and commercial culture to a wider cross section of the community.
- If truly accepted and implemented on a partnership basis, it will bring peace to an industry plagued with stakeholder bickering and mistrust.

Some of the negative features of this option are:

- This structure looks fine in theory but lacks practicality in local context. This is very much an imported and a modern commercial solution to an industry, which has intractable socio-economic and cultural ties with the entire fabric of the nation.
- The socio-economic cost of the proposal is too high. It will require the displacement of about 13,000 farming families without any alternative employment option. This will substantially increase unemployment in the country.
- This proposal requires about $160 million of funding, most of which would have to be upfront. The use of this level of funding would have significant opportunity costs. But some international financial institutions have shown a willingness to finance the restructure if it proved viable.
- The time frame is too ambitious. Some stakeholders wanted this restructure to commence from as early as the 2002/2003 season. While top leadership of two of the major partners (FSC and Sugar Cane Growers Council) are in support of this proposal, others, including the majority of the employees, and a large section of the cane growers, are opposed to it. Like other proposals, without the unanimous support of the key stakeholders, this proposal would also prove difficult to implement.
- The government, which is a key stakeholder, has not come out in support of this option, but is still seeking wider discussion and consultation.
- As with the privatisation option mentioned earlier, the government may not as yet be ready to part with, let alone ex-gratia, the sugar milling assets and activities to stakeholders.

Option 5: Management contract with an experienced international sugar-milling organisation

Another option to save the industry is to invite, via a management contract, an experienced international sugar-milling organisation to manage the milling side of the industry. The assumption behind this proposal is that the FSC would do fine if there were a management revamping. This assumption may not necessarily be with a strong foundation. The state of the industry shows that the entire industry now needs a total reform and a 'shock therapy', to enable it to operate in a globally competitive sugar industry. The industry is too politicised for any international sugar milling organisation, or any other international management organisation, to be able to adequately fix the problems without getting stakeholder support.

Some of the positive aspects of this option are:

- This option will help FSC by ready access to modern technical know-how and management skills.
- It will help improve the efficiency of the factories which have substantially deteriorated in the last few years.
- It will improve cane transport especially the rail system. Over the last ten years the average locomotive speed hauling cane has declined from seventeen to seven kilometres per hour.

Some of the negative aspects of this option are:

- It will be very expensive to get international organisations to get involved on a commercial basis. The industry's current financial position precludes them from engaging in this option.
- It is doubtful that many reputable international organisations would be interested in the option in view of the magnitude of the problems and the institutional environment within which the industry operates.
- It may be seen by some sections of the country as neo-colonialism, where the nation is not able to successfully manage its most important industry and commercial business organisation.

Option 6: Joint venture or strategic alliance with an international sugar milling organisation

The government may be able to get a joint venture partner or strategic alliance with an international sugar-milling organisation. However, under the current scenario, it may be difficult to get private investors of repute interested in the industry. Those with technical and appropriate management expertise may consider the economic and financial opportunities but will be reluctant to invest large amounts of their own funds. Private investors may be willing to enter into partnership with relatively low shareholding, with special provision of management contract. In such cases, their return would be immediate and loaded front-end.

If potential financial benefits are significant, then there is a greater likelihood of attracting private investors with milling trackrecords. But the prospect of the sugar industry does not appear to be too good. The premium price and preferential access to the European Union market will expire in 2008 and all indications are that any further agreement will be on less favourable terms to both Fiji and the other ACP countries. Furthermore, the sugar industry is much too regulated, and the institutional environment too volatile to attract reputable sugar milling companies.

Role of the Government

The two principal stakeholders, growers and the miller, have now taken a much more hardened position regarding how to restructure the industry. The growers and workers are highly organised. To get them to agree to any restructure proposal seems unlikely unless their interests were well catered for. The government also has a conflicting role – as a shareholder which wants a larger share of the revenue, and as an arbiter in the dispute. It is proposed that the government stress its role of an arbiter and take a more proactive and leadership role in getting the industry on a business-like and commercial footing. An inclusive decision making process is necessary for such a vital matter as sugar industry restructuring. Past trends show that policies or restructuring which are made without the endorsement of the stakeholders, do not succeed. For this reason, for any restructuring to succeed, there needs to be broad consensus on the ingredients of the restructuring.

Conclusion

The sugar industry has for some time been faced with fundamental problems. The government as well as the sugar industry stakeholders recognised the need for addressing the problems. This paper has looked at six options which have been proposed to address the sugar industry problems. These are: privatisation of the Fiji Sugar Corporation, continuing with the status quo, implementing the Sugar Industry Strategic Plan, implementing the 'Way Forward Proposal', entering into a management contract with an experienced international sugar milling organisation, and entering into a joint venture or strategic alliance with an international sugar milling organisation.

The paper proposes that the best solution out of the six is to implement the sugar industry strategic plan developed in 1997. This plan calls for grower and miller partnership in addressing the problems. The paper also proposes that the government ought to clearly distinguish its role as a shareholder of the FSC and its role as an independent arbiter in the disputes. The paper stresses the need for consensus on the sugar industry reforms. For any reform to succeed in the sugar industry, it is vital that stakeholders be involved in the reform process, and that the process and the ingredients of the reform get stakeholder endorsement.

Appendix 1: The Eve Formula

In this pricing formula the sugar proceeds were split twice as follows. First, the millers were allocated 30% of the net sugar proceeds to meet the basic sugar making cost. This was apportioned as 10% for all costs incurred by the miller on the agricultural side of the industry, called grower services, and 20% for manufacturing and administration costs.

Then, the balance of the 70 percent of the sugar proceeds were split between growers and millers as follows: 82½% (of 70%) to growers and 17½% (of 70%) to millers. The growers, therefore, got 57¾%, while the millers received 42¼% (comprising 30% cost + 12¼% profits). In this way, the miller was guaranteed a minimum profit of 12¼% on the industry proceeds.

Quite often the miller's cost of production was less than 30%. Any savings in costs, for example a reduction to 26%, was divided between growers and millers according to whether the savings were in 'growers' services' or in 'manufacturing services'. If, for example, there was a 4 percent point saving, of which if 1 percent was in growers' services and 3 percent in the manufacturing services, then the cost savings would be split as follows:

To the growers' share of proceeds, add 2/3rd of 1 percent from the reduction in growers' services, plus 1/3rd of the 3 percent due to savings in manufacturing costs, giving a total of 1 2/3 percent.

To the miller's share of profit, add 1/3rd of 1 percent, plus 2/3rd of 3 percent, giving a total of 2 1/3 percent.

In the above example, the final split of the sugar proceeds would be as follows:

* To the growers, 59 5/12 percent (57 ¾ plus 1 2/3).
* To the millers, 40 7/12 percent (26 percent for sugar making costs, plus 12 ¼ profits, plus 2 1/3 savings in costs).

However if the actual costs exceeded the 30 percent allocation of the sugar proceeds (within the 10 percent and 20 percent standard set in the formula), then half of the excess in cost was deducted from the growers' and miller's shares.

The above formula was based on the assumption that there was a fundamental difference between the agriculture and factory side of the operations represented by 'growers' services' and 'manufacturing costs' respectively. The Eve Commission reported that the 'cost of growers' services and cane transport could be influenced considerably by growers. The costs of manufacture, transport and storage of sugar can similarly be influenced by millers. In neither case however is the influence wholly by one party. It was on this particular assumption that the Eve Commission provided two-thirds of any savings to growers from 'growers' services.' The growers would receive only one-third of any savings from 'manufacturing costs.' The millers were to receive the other proportions of the savings from the respective costs. The reasoning behind this was that it would provide an incentive to each party to reduce costs in its area of relative influence, i.e. 'growers' services' for growers and 'manufacturing costs' for millers.

The Eve pricing formula, to say the least, was in favour of the millers. The millers were allowed to have 'two bites at the cake.' They were able to meet all their costs of production from the first bite and the second split was its net profit. Even if the price of sugar had fallen substantially there was sufficient revenue to meet the cost of production. In such circumstances the millers would have lower profits. The growers had no such protection. It was only after the millers had deducted their costs of production that the growers were able to receive their share of the proceeds.

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