

**Report No. 436**

**Investigation into remedial action in the form of a safeguard against the increased imports of frozen potato chips: Preliminary determination**

The International Trade Administration Commission of South Africa herewith presents its  
**Report No. 436: INVESTIGATION INTO REMEDIAL ACTION IN THE FORM OF A  
SAFEGUARD AGAINST THE INCREASED IMPORTS OF FROZEN POTATO CHIPS:  
PRELIMINARY DETERMINATION**

  
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# **INTERNATIONAL TRADE ADMINISTRATION COMMISSION OF SOUTH AFRICA**

## **REPORT NO. 436**

### **INVESTIGATION INTO REMEDIAL ACTION IN THE FORM OF A SAFEGUARD AGAINST THE INCREASED IMPORTS OF FROZEN POTATO CHIPS: PRELIMINARY DETERMINATION**

#### **SYNOPSIS**

On 08 March 2013, the Commission initiated an investigation for remedial action in the form of a safeguard against the increased imports of frozen potato chips through *Notice No. 175 of Government Gazette No. 36207* dated 08 March 2013.

The Application was lodged on behalf of the Southern African Customs Union (SACU) by McCain Foods (SA) (Pty) Ltd (the Applicant). The Application is supported by Nature's Choice Products (Pty) Ltd and Lamberts Bay Foods, the other producers of frozen potato chips in the SACU.

The investigation was initiated after the Commission considered that there was sufficient evidence to show that there was a surge in imports of the subject product, causing serious injury to the SACU industry.

On initiation of the investigation, the embassies of the countries with a significant interest in the exports of the subject product, were notified of the initiation of the investigation.

The Commission made a preliminary determination that there were unforeseen developments which resulted in the increased imports. The Commission further made a preliminary determination that there was a surge in imports of the subject product, causing serious injury to the SACU industry.

The Commission decided that critical circumstances exist that justify the imposition of provisional measures. The Commission therefore decided to request the Commissioner for South African Revenue Service to impose provisional measures for a period of 200 days.

## **1. APPLICATION AND PROCEDURE**

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### **1.1 LEGAL FRAMEWORK**

This investigation is conducted in accordance with the International Trade Administration Act, 2002 (ITA Act) and the International Trade Administration Commission Safeguard Regulations (SGR), read with the World Trade Organization Agreement on Safeguards (the Safeguard Agreement).

### **1.2 APPLICANT**

The application was lodged on behalf of the SACU industry by McCain Foods (SA) (Pty) Ltd (the Applicant), a major producer of frozen potato chips (subject product) in the SACU supported by Nature's Choice Products (Pty) Ltd and Lamberts Bay Foods.

### **1.3 ALLEGATIONS BY THE APPLICANT**

The Applicant alleged that the subject product is being imported into the SACU market in such increasing quantities relative to SACU production and under such conditions, to be causing serious injury to the SACU industry.

The Applicant indicated that the expansion of the capacity by the producers of frozen potato chips in the European Union and the absence of sufficient duty protection as a result of the Agreement on Trade, Development and Co-operation between the European Community and its member states and the Republic of South Africa (the TDCA), were unforeseen developments which resulted in the increased imports of frozen potato chips.

### **1.4 INVESTIGATION PROCESS**

1.4.1 The information submitted by the applicant was verified on the 27<sup>th</sup> and the 28<sup>th</sup> of September 2012.

1.4.2 The following countries were identified as having a substantial interest as exporters of the subject products to SACU:

- Egypt

- Belgium
- Netherlands
- France
- The United States of America (USA)
- Argentina
- Germany

1.4.3 Four importers established a non-incorporated body called Affected Potato Importers (API) to represent their interests in this investigation. The importers are K&M International Trading (Pty) Ltd, Lamb Weston/ Meijer Vof, Merlog foods (Pty) Ltd and Agristo NV.

1.4.4 Comments in response to the initiation of the investigation were received from API, the European Commission, the European Potato Processors Association (EUPPA), Yum Restaurants International, Embassy of Arab republic of Egypt and the Embassy of Argentina.

## **1.5 INVESTIGATION PERIOD**

The Commission considered information with regard to increased quantities of imports and serious injury information for the period 1 July 2008 to 30 June 2012.

1.6 The Commission considered comments received from interested parties with regard to the application and procedure. Non-confidential versions of these comments are available on the public file.

## **1.7 PRELIMINARY DETERMINATION**

The Commission made a preliminary determination that there were unforeseen developments which resulted in the increased imports. The Commission further made a preliminary determination that there was a surge in imports of the subject product, causing serious injury to the SACU industry.

The Commission decided that critical circumstances exist that justify the imposition of provisional measures. The Commission therefore decided to request the Commissioner for South African Revenue Service to impose provisional measures for a period of 200 days.

## **2. PRODUCTS, TARIFF CLASSIFICATION AND DUTIES**

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### **2.1 IMPORTED PRODUCT**

#### **2.1.1 Description**

The subject product is described as “frozen potato chips” or commonly known (in South Africa) as slap chips or French fries/pommes frites/chips.

#### **2.1.2 Tariff classification**

The subject product is classified as follows:

Tariff subheading	Description	Statistical Unit	General	EU	EFTA	SADC	Rebate provision item number
2004.10.90	Other	Kg	20%	FREE	20%	FREE	N/A

#### **2.1.3 Production process**

Raw potatoes are washed, steam peeled, cut , blanched in cold water, dried, partly cooked in vegetable oil, cooled, frozen, weighed, poli-bag packaging, cased corrugated board packaging, palletized and cold storage at minus 18 degrees Celsius.

### **2.2 SACU PRODUCT**

#### **2.2.1 Description**

The SACU product is described as Frozen potato chips or commonly known (in South Africa) as slap chips or French fries/Pommes frites/Chips.

#### **2.2.2 Production process**

Raw potatoes are washed, steam peeled, cut , blanched in cold water, dried, partly cooked in vegetable oil, cooled, frozen, weighed, Poli-bag packaging, cased corrugated board packaging, palletized and cold storage at minus 18 degrees Celsius.

### 2.2.3 Application or end use

The product is a frozen food product fit for human consumption.

### 2.2.4 Categories of users

The subject product, frozen chips, is distributed to quick service restaurants and food service outlets (including Retail Hot Deli's) which prepare the subject product for "out of home" consumer consumption. The subject product is also distributed to retail stores, to be bought by consumers for "in the home" consumption.

## 2.3 LIKE OR DIRECTLY COMPETITIVE PRODUCTS ANALYSIS

In determining the likeness or direct competitiveness of the product, the Commission uses the following criteria:

	Imported product	SACU product
<b>Tariff Heading</b>	2004.10.90	2004.10.90
<b>Raw materials</b>	i. Potatoes ii. Vegetable Oil	i. Potatoes ii. Vegetable Oil
<b>Production process</b>	Raw potatoes are: <ul style="list-style-type: none"><li>• washed</li><li>• steam peeled</li><li>• cut</li><li>• blanched in cold water</li><li>• dried</li><li>• partly cooked in vegetable oil</li><li>• cooled</li><li>• frozen</li><li>• weighed</li><li>• Poli-bag packaging</li><li>• Cased corrugated board packaging</li><li>• Palletized</li><li>• Cold storage minus 18 degrees Celsius</li></ul>	Raw potatoes are: <ul style="list-style-type: none"><li>• washed</li><li>• steam peeled</li><li>• cut</li><li>• blanched in cold water</li><li>• dried</li><li>• partly cooked in vegetable oil</li><li>• cooled</li><li>• frozen</li><li>• weighed</li><li>• Poli-bag packaging</li><li>• Cased corrugated board packaging</li><li>• Palletized</li><li>• Cold storage minus 18 degrees Celsius</li></ul>
<b>Application or end use</b>	For human consumption	For human consumption

The Commission decided that the SACU product and the imported product are like products for purposes of comparison, and therefore also directly competitive products in terms of Section 2 of the Safeguard Regulations.

### **3. INDUSTRY STANDING**

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#### **3.1 SACU INDUSTRY**

The application was lodged on behalf of the SACU industry by McCain Foods (SA) (Pty) Ltd (the Applicant), a major producer of frozen potato chips (subject product) in the SACU supported by Nature's Choice Products (Pty) Ltd and Lamberts Bay Foods.

The Commission considered comments received from interested parties with regard to the industry standing. Non-confidential versions are available on the public file.

The Commission decided that the application can be regarded as being made "by or on behalf of the domestic industry" in terms of Section 7.2 of the Safeguard Regulations.

## **4. UNFORESEEN DEVELOPMENTS**

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### **4.1 Requirements of Article XIX of GATT**

Article XIX of the GATT provides as follows:

"If, as a result of unforeseen developments and of the effect of obligations incurred by a contracting party under this Agreement, including tariff concessions, any product is being imported into the territory of that contracting party in such increased quantities and under such conditions as to cause or threaten serious injury to domestic producers in that territory of like or directly competitive products, the contracting party shall be free, in respect of such product, and to the extent and for such time as may be necessary to prevent or remedy such injury, to suspend the obligation in whole or in part or to withdraw or modify the concession."

In terms of the WTO this is interpreted to mean that the developments in the market should have been unforeseen at the time of negotiation of the relevant tariff concessions.

### **4.2 Information submitted by the Applicant**

The Applicant stated that in 1994 when South Africa became a signatory to the WTO Agreement and made tariff commitments with respect to frozen potato chips, the following developments were not foreseen:

#### **4.2.1 Proliferation of Quick Service Restaurants**

The Applicant stated that the SACU market for frozen potato chips at that time was in its infancy and imports of frozen potato chips were negligible. South Africa was just coming out of isolation under the Apartheid Era Sanctions with little exposure to global supply chains. In the period between 1994 and the present, household purchasing patterns have developed into a more convenience food (ready prepared) market. In addition, since 1994 there has been a proliferation of Quick Service Restaurants (colloquially called "take-aways") in the SACU market. The Applicant gave McDonalds as an example and stated that McDonalds entered the market in November

1995. These developments led to opportunities for investment and job creation in an industry barely existing in 1994.

#### **4.2.2 Excess production capacity of the frozen potato chips in the European Union**

The Applicant stated that in the period following 1994 excessive investment in the frozen potato chip industry in the European Union (EU) took place. The financial crisis that dampened demand for frozen potato chips in the EU since 2008 created surplus capacity. This encouraged EU producers to follow an aggressive export strategy to dispose of their surplus capacity into the world market thereby depressing the world price and forcing local manufacturers to compete with imports at that price level.

To substantiate its allegation of excess production capacity of the frozen potato chips in the European Union, the Applicant obtained the following extract from a report dated 4 November 2011 by PotatoPro.com on a presentation made by the Chair of the Dutch Potato Association Mr. Kees van Arendonk speaking about the Dutch and Belgian French fry industry at the opening of the trading year of the Dutch Potato markets. The Applicant stated that Mr. Kees van Arendonk highlighted the increasing market share of the French fry manufacturers in The Netherlands and Belgium in the global market of frozen French fries and also that Belgium keeps increasing their production rapidly and passed the 3 million tons of potatoes processed last year, while french fries production in the Netherlands also set another record the previous season of almost 3.5 million tons.

The Applicant stated that Kees van Arendonk mentioned the following striking statistics: "if you would draw a circle with a radius of 500 km around Utrecht (Let's say the center of the Netherlands for those not from the area) you get an area that processes 10 million tons of potatoes each year. To put that figure into perspective: The total amount of potatoes processed into French fries in the entire United States is also about 10 million tons"!

The Applicant stated that Mr. Kees van Arendonk said "although the Dutch and the Belgians like their fries, there is no way they can eat all these French fries themselves: about 90% is exported".

The Applicant stated that this raises the question: where do they go? Not all French fries produced in that area travel far, but increasingly they go to all corners of the world.

The Applicant further stated that as Kees van Arendonk said: "I find it amazing achievement that the [Dutch and Belgium] French fry industry can export to places such as Australia and South America and be able to compete there with local suppliers".

The Applicant stated that the report concluded with the following warning to producers of frozen potato chips in countries to which Dutch and Belgium exports find their way: "... if you are in one of those far-away countries competing against the Dutch and Belgian French fry producers: Beware: ... they might have some extra fries to sell! Their market share in the global French fry market is unlikely to go down this season ..."

The Applicant further stated that all these unforeseen developments in the EU took place while duties on imports of frozen potato chips from the EU into the SACU were being phased out under the TDCA, which entered into force in 2000, leaving the local industry exposed to the surge in the volume of imports from the EU which consequently resulted in serious injury being inflicted on the local producers of frozen potato chips.

Lastly the Applicant stated that it is very clear that in accordance with Article XIX of the GATT 1994 the "developments" being the expansion of capacity in the EU, the financial crisis which resulted in the oversupply of frozen potato chips in the world market, an aggressive export strategy by the EU producers of frozen chips augmented by the absence of sufficient duty protection as a result of the TDCA culminated in circumstances that

occurred after the negotiation of the relevant tariff concessions that "could not have been foreseen at the time the concessions were negotiated".

#### **4.3 Other factors considered by the Commission**

In 1995 during the Uruguay round under the category "fruit, vegetables processed" the European Union committed to reduce export subsidies which enabled the developing countries to make commitments to tariff liberalization.

In terms of schedule LXXX submitted to WTO under the "fruit, vegetables processed" category EU committed to reduce export subsidies from 14.5 million Euros to 9.9 million euros in the year 2000. It should be noted that in terms of notification G/AG/N/EU/6 of subsidised exports, the EU made budgetary commitments under "fruit, vegetables processed" of 114.3 million Euros. It can be concluded that the EU did not keep up with its commitment to reduce export subsidies in this sector as it had committed in 1995 and thus this development could not be foreseen by the negotiators of developing countries when commitments were made to liberalise tariffs in 1995.

#### **4.4 CONCLUSION: UNFORESEEN DEVELOPMENTS**

The Commission considered comments received from interested parties with regard to unforeseen developments. Non-confidential versions of these comments are available on the public file

The Commission made a preliminary determination that the expansion of capacity in the EU, proliferation of Quick Service Restaurants, the failure by EU to keep up with its commitment to reduce export subsidies in this sector as it had committed in 1995 and the excess production capacity of the frozen potato chips in the European union represents unforeseen developments in accordance with Article XIX of the General Agreement on Tariffs and Trade (GATT).

## 5. RECENT, SUDDEN, SHARP AND SIGNIFICANT INCREASE IN IMPORTS

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The Applicant submitted the following information:

### IMPORT VOLUMES

	July 08- June 09	July 09- June10	July 10- June 11	July 11- June 12
<b>Total imports (tons)</b>	<b>14 892</b>	<b>33 039</b>	<b>47 706</b>	<b>28 555</b>
SACU market's own imports (tons)	(13 221)	(17 811)	(18 051)	(3 517)
Imports (after deducting own imports) (tons)	1 671	15 228	29 655	25 038
10% Adjustment	(167)	( 1 523)	(2 965)	(2 504)
<b>Net imports (tons)</b>	<b>1 504</b>	<b>13 705</b>	<b>26 689</b>	<b>22 534</b>
<b>*Total Production (tons)</b>	<b>100</b>	<b>103</b>	<b>86</b>	<b>115</b>
<b>*Imports as a % of the Applicant's output</b>	<b>100</b>	<b>889</b>	<b>2 056</b>	<b>1 300</b>

\*These figures were indexed due to confidentiality using the year ending 2009 as the base year

In comparing the 2009 and 2010 financial periods, the rate of increase in net imports in absolute terms was 811.23 per cent. The net imports increased by 94.74 per cent for the 2011 financial period compared to the 2010 financial period and decreased by 15.57 per cent in 2012 compared to 2011. The rate of increase in net imports relative to the production for the financial years 2009 to 2010 was 789 index points and for the financial years 2010 to 2011 the rate of the increase of 1167 index points. There was a decrease in net imports relative to production between the 2011 and 2012 financial periods of 756 index points.

In conclusion, the recent, sudden, sharp and significant increase in imports of the subject product occurred in the period 2009 to 2010 and the subject product continued to be imported in increased quantities both in absolute terms and relative to production. The imports in 2010 compared to 2009 increased in absolute terms by 811.23 per cent and in 2012 compared to 2009 the imports remained at high levels and were 1 398 per cent more in 2012 compared to 2009. The imports relative to production increased by 789 index points in 2010 compared to 2009 and remained at a high level in 2012 at 1 300 index points compared to 100 index points in 2009.

In making its determination, the Commission took note of the panel decision involving the US steel safeguard case. The panel made the following decision regarding instances where imports decline after increasing sharply and suddenly.

*"In U.S. – Steel Products, the Panel noted that the increase must indicate a degree of recentness, suddenness and sharpness, the increase need not continue up to the period immediately preceding the investigating authority's determination nor up to the very end of the investigation period, although the increase still had to be recent. (p. 10.162) The Panel noted that whether a decrease in imports at the end of the POI prevented a finding of increased imports would depend on the duration and the degree of the decrease at the end of the POI, as well as the nature of the increase that intervened beforehand. (p. 10.163). But also note that the Panel, reviewing the US's decision, product by product, found that for certain products the decreasing import trend towards the end of the POI, particularly a significant drop in the interim period did not consider the increase in imports to be recent enough."*

The Commission was therefore of the opinion that, although imports decreased in the financial period 2012, the imports in the said period remained at levels significantly higher than in the 2010 financial period.

#### **CONCLUSION: RECENT, SUDDEN, SHARP AND SIGNIFICANT INCREASE IN VOLUME OF IMPORTS**

The Commission considered comments received from interested parties with regard to recent, sudden, sharp and significant increase in imports. Non-confidential versions of these comments are available on the public file.

The Commission made a preliminary determination that there was a recent, sudden, sharp and significant increase in the volume of imports both in absolute terms and relative to production from the 2009 financial period and that the imports continued to be imported in increased levels both absolute and relative to production in 2011 and 2012.

## 6. SERIOUS INJURY

The Commission considered comments received from interested parties with regard to serious injury. Non-confidential versions of these comments are available on the public file.

### 6.1 DOMESTIC INDUSTRY – MAJOR PROPORTION OF PRODUCTION

The following injury analysis relates to McCain (SA) (Pty) Ltd, the Applicant, which constitutes 70,45 per cent of the total domestic production of the subject product.

The Commission decided that this constitutes “a major proportion” of the total domestic production, in accordance with Article 4.1 of the Safeguard Agreement.

### 6.2 THE RATE AND VOLUME OF THE INCREASE IN IMPORT VOLUMES

The following table shows the volume of the imports from 01 July 2008 to 30 June 2012.

Table 6.2.1

Country (tons)	2009	2010	2011	2012	Total imp	% of total imports
Egypt	792	1036	4374	3009	9221	7.42
Ghana	0	0	0	0	0	
	0	0	0	0	0	
Denmark	0	0	49	0	49	0.04
UK	915	0	357	0	1273	1.02
Belgium	1390	14660	22317	4816	43226	34.77
Netherlands	1228	5464	11246	1660	19617	15.78
Germany	0	0	267	12279	12559	10.10
France	1501	9824	2427	5034	18805	15.13
Italy	0	0	0	0	0	
Canada	175	144	0	1240	1561	1.26
USA	4962	99	3701	56	8827	7.10
Brazil	0	0	0	0	0	
Argentina	3463	1146	2409	131	7156	5.76
Cyprus	0	0	0	0	0	

India	248	597	556	135	1539	1.24
Bangladesh	0	0	1	0	1	
Philippines	0	0	0	186	186	0.15
Hong Kong	0	0	0	0	0	
Taiwan	0	0	0	8	8	0.01
China	0	0	0	0	0	
Japan	0	0	0	0	0	
Australia	168	0	0	0	168	0.14
New Zealand	50	69	0	0	118	0.10
<b>Total</b>	<b>14892</b>	<b>33039</b>	<b>47706</b>	<b>28555</b>	<b>124</b>	<b>100</b>
SACU own imports	13221	17811	18051	3517	53	
Imports excluding own	1671	15228	29655	25038		
10%adjustment	167	1523	2965	2504		
<b>Total Net imports</b>	<b>1504</b>	<b>13705</b>	<b>26689</b>	<b>22534</b>		

The Commission calculated the net imports by subtracting the Applicant's own imports from the total imports. An amount of 10 % was deducted from the total imports under tariff subheading 2004.10.90 as per the estimate provided by the Applicant, indicating that the subject product constitutes 90% of the imports made under the relevant tariff subheading which includes frozen potatoes, other than frozen potato chips.

The Applicant stated that the small demand for formed specially manufactured potato products in the local market, which directly reflects in the small volume imported by the applicant, it is of the view (supported by both of the two other manufacturers) that it would be a fair estimate to state that in excess of 90% of total imports of frozen potato products under tariff heading 2004.10.90 constitutes frozen potato chips, which forms the subject product of this application.

The imports in 2010 compared to 2009 increased by 811.23 per cent and in 2012 compared to 2009 from 1504 tons to 13 705 tons. The imports remained in 2012 at high levels and were 1 398 per cent more in 2012 compared to 2009, increasing from 1504 tons in 2009 to 22 534 tons in 2012.

The information in the table above indicates that the countries with a substantial interest as exporters of frozen potato chips to the SACU are Egypt, Belgium, the Netherlands, France, the USA, Germany and Argentina.

In comparing the 2009 and 2010 financial periods, the increase in net imports in absolute terms amounts 811 index points. The net imports increased by 864 index points for the 2011 financial period compared to the 2010 financial period and decreased by 27 index points in 2012 compared to 2011.

### 6.3 Effects on domestic prices

#### 6.3.1 Price undercutting

The following table compares the Applicant's ex-factory prices with the landed cost of the subject product.

**Table 6.3.1**

	<b>July 08- June 09</b>	<b>July 09- June10</b>	<b>July 10- June 11</b>	<b>July 11- June 12</b>
Applicant's average gross selling price / kg	100	108	118	112
FOB Rand/kg (Imports)	100	80	88	99
Duty (Rands/kg)	100	60	35	13
Insurance, Freight +Handling Charges/kg	100	100	103	75
Total Average Landed Cost/kg	100	84	88	88
Undercutting	100	238	275	239

This table was indexed due to confidentiality using the year ending 2009 as the base year

The Applicant experienced an increase in price undercutting in the financial periods 2009 to 2012 of 139 index points.

The Applicant also stated that this level of undercutting has serious competitiveness implications for the local industry. This trend has been further exacerbated by the advantages brought by the relatively stronger Rand against international currencies over this period.

The Applicant further stated that these advantages of price and forex has persuaded the end user to continue sourcing imported potato chips, thereby

negatively impacting on the applicant's potato chip sales volumes and profitability.

### 6.3.2 Price depression

Price depression occurs when the domestic industry experiences a decrease in its selling prices over time. The table below shows the domestic industry's selling prices:

**Table 6.3.2**

Rand	July 08- June 09	July 09- June10	July 10- June 11	July 11- June 12
Average gross selling prices per kg	100	108	118	112

This table was indexed due to confidentiality using the year ending 2009 as the base year

The above table shows that the Applicant's average selling prices increased for the financial period 2009 compared to the financial period 2012 by 12 index points. This therefore indicates that the Applicant did not experience price depression.

### 6.3.3 Price suppression

Price suppression is the extent to which increases in the cost of production of the subject product, cannot be recovered in selling prices.

The following table shows the Applicant's costs of production and its actual selling prices for the subject product:

**Table 6.3.3**

Rand per kg	July 08- June 09	July 09- June10	July 10- June 11	July 11- June 12
Selling prices R/kg	100	108	118	112
Total Product cost (COG + Variable)	100	109	106	88
Total Cost	100	109	109	92
Total COS (Total Spend + Dist) Ex. Factory	100	108	123	108
Total cost % of Selling Price	100	100	104	97

This table was indexed due to confidentiality using the year ending 2009 as the base year

The table above indicates that the Applicant was suffering price suppression.

The Applicant stated that there has been a significant change to cost and price structures during the last 18 months, taking into consideration the impact of imports, the market recessionary conditions, and inflation. Selling prices have been reduced to retain market share. The Applicant indicated that it had to focus more on tighter controls, input costs, as well as the contractual conditions pertaining to raw potato supply. The Applicant indicated that this was necessary as raw material contracts are fixed in advance for the season and that the factory needs to be kept operational 'at volume' in order to retain overhead cost recovery rates. It indicated that it also has a policy of avoiding retrenchments, and labour cost forms part of costs to be recovered. Moreover, the applicant calculates a Bill of Materials/Cost price for each year. Any variance in raw material, oil costs etc are accounted for in variances for the month.

#### **6.4 SIGNIFICANT CHANGES IN THE PERFORMANCE OF THE SACU INDUSTRY**

##### **6.4.1 Sales volume**

The following table shows the Applicant's sales volume for their total potato business:

**Table 6.4.1**

	<b>July 08- June 09</b>	<b>July 09- June10</b>	<b>July 10- June 11</b>	<b>July 11- June 12</b>
Applicant's sales volume (Tons)	100	98	87	97

This table was indexed due to confidentiality using the year ending 2009 as the base year

The information in the table indicates that the Applicant's sales volumes decreased by 13 index points in the financial period ending 2011 compared to the financial period ending 2009 and it increased by 10 index points for the financial period ending 2012 compared to the financial period ending 2011.

The Applicant stated that the advantages of price and foreign exchange persuaded the end user to continue sourcing imported potato chips, thereby

negatively impacting on the applicant's potato chip sales volumes and profitability.

#### 6.4.2 Profit and Loss

The following table shows the Applicant's profit and loss situation for the total potato business:

**Table 6.4.2**

	July 08- June 09	July 09- June10	July 10- June 11	July 11- June 12
Tons	100	98	87	97
KG's Sold	100	98	87	97
Total Rand Net Sales	100	106	95	63
Net Loss (000's)	100	111	154	64

This table was indexed due to confidentiality using the year ending 2009 as the base year

The table above indicates that the Applicant's net loss increased by 54 index points from the 2009 financial period compared to the 2011 financial period. Due to a cost reducing strategy which is in the Applicant's adjustment plan the following were put into place:

- Access to sufficient raw material for local production
- Diversification of raw material input
- Efforts to reduce administrated costs (water and energy)
- Increasing productivity; and
- Increasing production capacity

After the implementation of the above the Applicant's net loss decreased by 90 index points from 2011 to 2012 financial periods.

The Applicant stated that the prime contributor to the decline in profits previously experienced stemmed from the continued "cheap" pricing of imported chips in the local market. The Applicant further stated that also impacting the decline in profits where the negative impact of recessionary conditions in the market place affecting consumer buying behaviour, the unusual local weather conditions negatively impacting on supply and demand

leading to rising market prices of raw potatoes, and supported by currency advantage of 'a strong Rand'.

#### 6.4.3 Output

The following table shows the Applicant's output:

**Table 6.4.3**

	<b>July 08- June 09</b>	<b>July 09- June10</b>	<b>July 10- June 11</b>	<b>July 11- June 12</b>
Applicant's total production of frozen potato chips (Tons)	100	103	86	115

This table was indexed due to confidentiality using the year ending 2009 as the base year

The table above indicates that production declined by 14 index points in the period 2009 to 2011. Output increased by 29 index points in the 2011 to 2012 financial periods.

The Applicant stated that the prime contributor to the decline in output stemmed from the continued "cheap" pricing of imported chips in the local market. The Applicant further stated that also impacting the decline in output where the negative impact of recessionary conditions in the market place affecting consumer buying behaviour, the unusual local weather conditions negatively impacting on supply and demand leading to rising market prices of raw potatoes, and supported by currency advantage of 'a strong Rand'.

#### 6.4.4 Market share

The following table shows the market share for frozen chips:

**Table 6.4.4**

<b>Percentage held by:</b>	<b>July 08- June 09</b>	<b>July 09- June10</b>	<b>July 10- June 11</b>	<b>July 11- June 12</b>
Applicant's market share	100	86	73	78
Net imports	100	930	2 036	1 554

This table was indexed due to confidentiality using the year ending 2009 as the base year

The table above indicates a decrease in the Applicant's market share of 14 index points for the financial year ending 2010 compared to the financial year ending 2009 and in 2011 financial period the market share decreased by 13 index points compared to 2010. The market share of the applicant increased in 2012 by 5 index points compared to 2011, however the market share in 2012 is lower than that in 2009 by a significant 22 index points.

#### 6.4.5 Productivity

The following table shows the productivity of the Applicant:

**Table 6.4.5**

	<b>July 08- June 09</b>	<b>July 09- June10</b>	<b>July 10- June 11</b>	<b>July 11- June 12</b>
Total production volume (tons) for all frozen potato chips	100	103	86	115
Number of employees (manufacturing only)	100	101	101	112
Units per employee	100	102	86	103
Total employment	100	106	105	92
Total investment (Rands)	100	108	110	111
Output ratio	100	105	128	96

This table was indexed due to confidentiality using the year ending 2009 as the base year

From the table above, productivity increased by 2 index points in 2010 compared to 2009 and decreased by 16 index points in 2011 compared to 2010. In the 2012 financial period the applicant's productivity increased by 17 index points compared to 2011.

#### 6.4.6 Utilization of production capacity

The following table provides the Applicant's capacity and production:

**Table 6.4.6**

<b>Tons</b>	<b>July 08- June 09</b>	<b>July 09- June10</b>	<b>July 10- June 11</b>	<b>July 11- June 12</b>
Capacity	100	100	100	100
Applicant's output	100	103	86	115
Utilisation of capacity	100	102	86	114

This table was indexed due to confidentiality using the year ending 2009 as the base year

The table above indicates that utilization of production capacity increased by 2 index points in 2010 compared to 2009 and decreased by 16 points in the financial period ending 2011 compared to the financial year ending 2010. However, productivity increased by 28 index points in the financial period ending 2012 compared to the financial period ending 2011.

#### 6.4.7 Employment

The following table provides the Applicant's employment figures for frozen chips production:

**Table 6.4.7**

	July 08- June 09	July 09- June10	July 10- June 11	July 11- June 12
Number of employees (manufacturing only)	100	101	101	112

This table was indexed due to confidentiality using the year ending 2009 as the base year

The table above indicates that direct employment for the 2009 to 2012 period increased by 12 index points.

#### 6.5 Any other relevant factors

The Applicant stated that the European products have been marketed by a cross section of importers: traditional frozen importers, as well as importers who have taken advantage of the low pricing from Europe and good exchange rates. It stated that these types of importers have targeted the larger areas of the food-service business and initially had success with the smaller food-service wholesalers. As the consistency of supply and pricing was noticed by the trade, these imports then moved into the larger wholesalers which distributed to restaurants, coffee shops etc. as well as into the retail delis (such as Shoprite, Pick 'n Pay and Spar).

The Applicant further stated that imports have been basically of the European retail packs (not food-service packs), and as such, these products found their

way into the retail trade and sold to end consumers. All of the imports achieved their current sales volumes based on pricing levels that are substantially below that at which the applicant is able to market and sell locally produced product. In some cases, the pricing being offered to the food-service wholesalers by importers has been below that at which the Applicant is able to produce and distribute the product. The Applicant stated that it is also notable that imports are not complying with the requirements of the Consumer Protection Act or South African food labelling requirements.

In 2011, upgrading of the applicant's packaging plant to meet with domestic legislation cost approximately R7 million. The Applicant stated that importers are seemingly not making this investment in meeting regulatory requirements.

Lastly, the Applicant stated that the clients which it has lost and those putting its pricing under pressure confirmed that this was due to substantially cheaper imports. Those clients made no mention of competition from other SACU manufacturers as a reason for not buying the applicant's product.

## **6.6 CONCLUSION: SERIOUS INJURY**

The Commission made a preliminary determination that the SACU industry is experiencing serious injury in that:

- the volume of imports increased significantly;
- the loss situation increased further;
- the sales volume declined; and
- the market share declined.

## 7. CAUSAL LINK

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### 7.1 VOLUME OF IMPORTS AND MARKET SHARE

An indication of causality is the extent of the increase in volume of imports and the extent to which the market share of the domestic industry has decreased since the commencement of injury, with a corresponding increase in the market share of the imported subject product.

The following table compares the market share of the SACU industry with that of the alleged increased imports:

**Table 7.1.1**

<b>Percentage held by:</b>	<b>July 08- June 09</b>	<b>July 09- June10</b>	<b>July 10- June 11</b>	<b>July 11- June 12</b>
Applicant's market share	1.00	86	73	78
Net imports	100	930	2 036	1 554

This table was indexed due to confidentiality using the year ending 2009 as the base year

The table above indicates a decrease in the Applicant's market share of 14 index points for the financial year ending 2010 compared to the financial year ending 2009. In the 2011 financial period the market share decreased by 13 index points compared to 2010. The market share of the applicant increased in 2012 by 5 index points compared to 2011. However, the market share in 2012 is lower than that in 2009 by a significant 22 index points.

The market share held by net imports increased from 100 index points in 2009 to 930 index points in 2010 and increased to 2 036 index points in 2011 compared to the 100 index points in 2009. In 2012 the market share of net imports decreased to 1 554 index points compared to the 2 036 index points in 2011. However, the net imports market share was still significantly higher than in 2009.

**Table 7.1.2**

<b>Import volumes (Tons)</b>	<b>July 08- June 09</b>	<b>July 09- June10</b>	<b>July 10- June 11</b>	<b>July 11- June 12</b>
<b>Net imports</b>	1 504	13 705	26 689	22 534

This table was indexed due to confidentiality using the year ending 2009 as the base year

In comparing the 2009 and 2010 financial periods, the increase in net imports in absolute terms is 811 index points. The net imports increased by 864 index points for the 2011 financial period compared to the 2010 financial period and decreased by 27 index points in 2012 compared to 2011. The rate of increase in net imports relative to the domestic production for the financial years 2009 to 2010 was 789 index points and for the financial years 2010 to 2011 the rate of the increase of 1167 index points. There was a decrease in net imports relative to production between the 2011 and 2012 financial periods of 756 index points.

The Applicant stated that the European products have been marketed by a cross section of importers: traditional frozen importers, as well as importers who have taken advantage of the low pricing from Europe as well as favourable exchange rates.

The Applicant stated that these types of importers have targeted the larger areas of the food-service business and initially had success with the smaller food-service wholesalers. As the consistency of supply and pricing was noticed by the trade, these imports then moved into the larger wholesalers which distributed to restaurants, coffee shops etc. as well as into the retail delis (such as Shoprite, Pick 'n Pay and Spar).

## **7.2 CONSEQUENT IMPACT OF SURGE OF IMPORTS**

<b>Serious injury indicator</b>	<b>Analysis (July 2008 – June 2012)</b>
<b>Sales volume</b>	<b>Decrease</b>
<b>Loss</b>	<b>Decrease</b>
<b>Output</b>	<b>Increase</b>
<b>Market share</b>	<b>Decrease</b>
<b>Productivity</b>	<b>Increase</b>
<b>Utilisation of capacity</b>	<b>Increase</b>
<b>Employment</b>	<b>Increase</b>

The information in the table indicates that there was a negative impact on all the serious injury factors except employment. Employment remained unchanged while the Applicant's loss situation worsened from 2009 to 2011.

### **7.3 FACTORS OTHER THAN THE INCREASE IN IMPORTS CAUSING INJURY**

#### **7.3.1 Contraction in demand for the product**

The Applicant stated that there was an increase in demand for the subject product for the period 2009 to 2011. However, the Applicant's market share and sales volumes decreased over the same period as a consequence of the increase in imports.

The Applicant stated that it has experienced a contraction in demand and that this contraction in demand was caused by imports and also that it is further exacerbated by the current recessionary circumstances which are impacting the buying patterns in the local market place for foodstuffs generally.

The Applicant further stated that, despite the contraction in demand for its product, demand generally is growing and consumption has not declined. The logical conclusion is that local demand is being satisfied through imports which are substantially more aggressively priced to meet local demand under recessionary conditions.

#### **7.3.2 Developments in technology**

The Applicant stated that in 2007, it spent R700 million to upgrade its Delmas Plant. Delmas is an exclusive potato processing facility. This upgrade, through the installation of a second potato chip processing line, represents the latest technology.

The Applicant further stated that continuous improvement projects are undertaken by its Centre of Excellence (the McCain Center of Excellence) focusing on developing and implementing new technology which would further enhance productivity. On a regular basis, Kaizen & Six Sigma workshops are

conducted, led by on-site specialists, with a view to improve productivity, enhance Best Operating Practices (BOP's), and evaluate waste management practices. Extensive training and skills upgrading was done for staff operating the potato chip factory at the Delmas Plant.

### **7.3.3 Productivity of the domestic industry**

The Applicant stated that continuous improvement activities conducted in its local Processing Plants including the Delmas Plant contribute towards better productivity levels.

The Applicant stated that Comparative analysis against Global Best Operating Practices forms part of its Foods Global Manufacturing Strategy to identify areas of 'investigation and analysis' with the focus on improving processes.

The Applicant also stated that the European potato market is more readily supplied by raw material as a result of more favourable and conducive agricultural conditions for producing the primary product. The local processing industry does not have the accessibility to many processing potato varieties as have the European Processors, because in Europe there is a much larger pool of table potato varieties, with fewer processing varieties for the SACU processors.

### **7.3.4 View of the Applicant's clients regarding quality, delivery times, service and after sales service**

- **Quality**

The Applicant stated that it is perceived to be the Industry Standard "Benchmark";

- **Delivery times**

The Applicant stated that Customers are satisfied with the its delivery times as indicated by its customer service level reports, which are available upon request.

- **Service and after sales**

The Applicant stated that Customers are satisfied with its service as indicated by its customer service level reports, which are available upon request.

The Applicant further stated that it is the Industry Standard “Benchmark” and that its after-sales service is a ‘given’ supported with product demonstrations and technical training given to its Customers. The Applicant also stated that these value added services are neither provided for by importers nor reflected in the landed costs of imports. To the extent that customers switch partially to imported product from that of the applicant, imports “free-ride” on the technical training and support provided by the applicant.

#### **7.3.5 Attitude of the workforce towards the company**

McCain Foods as a company employs approximately 890 permanent employees and approximately 350 seasonal employees. Recent employee surveys indicated that locally staff satisfaction is amongst the best in the McCain Group as measured globally. The Company negotiates pay and conditions of employment with the Food and Allied Workers Union (FAWU) which represents bargaining unit staff at the company’s three manufacturing plants on an annual basis.

#### **7.4 CONCLUSION: CAUSAL LINK**

The Commission considered comments received from interested parties with regard to the causal link. Non-confidential versions of these comments are available on the public file.

After taking the above into consideration, the Commission made a preliminary determination that there was a causal link between the recent, sudden, sharp and significant surge in imports of the subject products and the serious injury experienced by the Applicant.

## **8. CRITICAL CIRCUMSTANCES AND RELIEF SOUGHT**

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### **8.1 Requirements of the Safeguard Agreement**

In accordance with Article 6 of the safeguard Agreement a member may impose a provisional safeguard measure pursuant to a preliminary determination in critical circumstances where delay would cause damage, which would be difficult to repair.

### **8.2 Information on critical circumstances**

- **The volume of imports**

Imports in 2010 compared to 2009 increased from 1504 tons to 13 705 tons which represent an increase of 811.23 per cent. The imports remained in 2012 at high levels and were 1 398 per cent more in 2012 compared to 2009 from 1 504 tons in 2009 to 22 534 tons in 2012.

- **Impact on the Applicant**

The SACU industry's market share declined from 98.09% in 2009 to 76.84% in 2012 and the SACU industry's sales volume decreased from 2009 to 2012 by 3.34%.

### **8.3 Relief Sought**

The Applicant requested the relief in the form of an increase in customs duty via a Safeguard Duty in terms of section 11 (f) and 21.5 (a) of the Amended Safeguard Regulations as published in Government Notice R662 of 8 July 2005.

The quantum of relief required is such so as to equate the price of imported frozen potato chips to the unsuppressed local sales price of the Applicant.

### **8.4 CONCLUSION: CRITICAL CIRCUMSTANCES**

The Commission decided that there are critical circumstances, which justifies the immediate imposition of provisional measures.

## **9. SUMMARY OF FINDINGS**

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### **9.1 Unforeseen Developments**

The Commission decided that the unforeseen developments are the following:

- Proliferation of Quick Service Restaurants
- Excess production capacity of the frozen potato chips in the European union; and
- EU not keeping to its export subsidy commitments made in 1995.

### **9.2 Serious injury**

The Commission made a preliminary determination that there was sufficient evidence that the SACU industry was suffering serious injury in that:

- the volume of imports increased significantly;
- the loss situation increased further;
- the sales volume declined; and
- the market share declined.

### **9.3 Recent, sudden, sharp and significant increase in imports**

The Commission made a preliminary determination that there is sufficient information to indicate that there has been a recent, sudden, sharp and significant increase in imports.

Imports decreased in the financial period 2012, although the imports in the said period remain at a level significantly higher than in the 2010 financial period at 22 534 tons compared to 1 504 tons. Furthermore, although there was a decrease in net imports relative to production of 1 300 index points percentage points in 2012 compared to 2011 the net imports, relative to production are still higher than in 2010 at 2 056 index points compared to 889 index points.

#### **9.4 Causal link**

The Commission made a preliminary determination that there is sufficient information to indicate that there was a causal link between the serious injury experienced by the SACU industry and the recent, sudden, sharp and significant surge in the volume of imports.

#### **9.5 Critical circumstances**

The Commission decided that there are critical circumstances that justify the imposition of provisional measures.

## **10. PROVISIONAL MEASURES**

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### **10.1 Duration of provisional measures**

In accordance with section 17.2 of the Amended Safeguard Regulations, the duration of the provisional measures shall not exceed 200 days. The duration of such provisional measures shall be counted as part of the overall time frame of the safeguard measures.

### **10.2 Calculation of provisional measures**

The Commission decided to determine the provisional measures to be equal to the price undercutting experienced by the Applicant.

The price undercutting is the extent to which the price of the imported product (landed cost) is lower than the verified ex-factory selling price of the SACU product.

#### **10.2.2 Landed cost calculation**

The landed cost was calculated by using the weighted average fob import price for 2012, as obtained from the official SARS import statistics, after deducting own imports by the three local producers. The costs for freight, insurance and clearing charges were added to the fob export price to arrive at the landed cost.

The Commission decided to calculate the provisional measures based on the price undercutting which was then expressed as a percentage of the fob export price to arrive at the rate of provisional payment of 61.42 %.

## **11. PRELIMINARY DETERMINATION**

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The Commission made a preliminary determination that:

- there was a surge in the volume of imports of the subject product into the SACU market;
- the increase in the volume of imports was as a result of unforeseen circumstances;
- the SACU industry was experiencing serious injury; and
- there is a causal link between the increase in imports and the serious injury experienced by the SACU.

As the Commission considers that critical circumstances exist that justify the imposition of provisional measures, it decided to request the Commissioner for SARS to impose a provisional measure of 61.42 % on the imports of frozen potato chips, classifiable under tariff subheading 2004.10.90, for a period of 200 days pending the finalization of the investigation.

The provisional measures should be imposed against all countries, except the following developing countries that should be excluded from the provisional measure:

# **LIST OF DEVELOPING COUNTRIES EXCLUDED FROM THE MEASURES**

Country	Country
Afghanistan	Fiji
Albania	Gabon
Algeria	Gambia, The
American Samoa	Georgia
Angola	Ghana
Antigua and Barbuda	Grenada
Armenia	Guatemala
Azerbaijan	Guinea
Bangladesh	Guinea-Bissau
Belarus	Guyana
Belize	Haiti
Benin	Honduras
Bhutan	India
Bolivia	Indonesia
Bosnia and Herzegovina	Iran, Islamic Rep.
Botswana	Iraq
Brazil	Jamaica
Bulgaria	Jordan
Burkina Faso	Kazakhstan
Burundi	Kenya
Cambodia	Kiribati
Cameroon	Korea, Dem Rep.
Cape Verde	Kosovo
Central African Republic	Kyrgyz Republic
Chad	Lao PDR
Chile	Latvia
China	Lebanon
Colombia	Lesotho
Comoros	Liberia
Congo, Dem. Rep	Libya
Congo, Rep.	Lithuania
Costa Rica	Macedonia, FYR
Côte d'Ivoire	Madagascar
Cuba	Malawi
Djibouti	Malaysia
Dominica	Maldives
Dominican Republic	Mali
Ecuador	Marshall Islands
El Salvador	Mauritania
Eritrea	Mauritius
Ethiopia	Mexico
Nicaragua	Micronesia, Fed. Sts.
Niger	Moldova
Nigeria	Mongolia
	Montenegro
	Morocco

Country	Country
Pakistan	Mozambique
Palau	Myanmar
Panama	Namibia
Papua New Guinea	Nepal
Paraguay	South Sudan
Peru	Sri Lanka
Philippines	St. Lucia
Romania	St. Vincent and the
Russian Federation	Grenadines
Rwanda	Sudan
Samoa	Suriname
São Tomé and Príncipe	Swaziland
Senegal	Syrian Arab Republic
Serbia	Tajikistan
Seychelles	Tanzania
Sierra Leone	Thailand
Solomon Islands	Timor-Leste
Somalia	Togo
South Africa	Tonga
Uganda	Tunisia
Ukraine	Turkey
Uruguay	Turkmenistan
Uzbekistan	Tuvalu
Vanuatu	
Venezuela, RB	
Vietnam	
West Bank and Gaza	
Yemen, Rep.	
Zambia	
Zimbabwe	