REPORT NO. 684

Creation of a temporary rebate facility for the importation of white chocolate, in immediate packaging of a content of 25 kg or more, classifiable under tariff subheading 1704.90, for use in the manufacture of chocolate containing cocoa, in blocks, slabs or bars, classifiable under tariff subheading 1806.3, and other chocolate classified in tariff subheading 1806.90

The International Trade Administration Commission of South Africa herewith presents **Report No. 684: Creation of a temporary rebate facility for the importation of white chocolate, in immediate packaging of a content of 25 kg or more, classifiable under tariff subheading 1704.90, for use in the manufacture of chocolate containing cocoa, in blocks, slabs or bars, classifiable under tariff subheading 1806.3, and other chocolate classified in tariff subheading 1806.90**

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CHIEF COMMISSIONER

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..26.. /...04./ **2022**

REPUBLIC OF SOUTH AFRICA

INTERNATIONAL TRADE ADMINISTRATION COMMISSION OF SOUTH AFRICA

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Creation of a temporary rebate facility for the importation of white chocolate, in immediate packaging of a content of 25 kg or more, classifiable under tariff subheading 1704.90, for use in the manufacture of chocolate containing cocoa, in blocks, slabs or bars, classifiable under tariff subheading 1806.3, and other chocolate classified in tariff subheading 1806.90

Synopsis

The Commission considered an application by Kees Beyers Chocolates CC (the "Applicant" or "Beyers Chocolate"), for the creation of a temporary rebate facility under Schedule 4 of the Customs and Excise Act, No.91 of 1964, for the importation of bulk white chocolate, classifiable under tariff subheading 1704.90 for use in the manufacture of chocolate classifiable under tariff subheadings 1806.31, 1806.32 and 1806.90.

During its deliberations and in arriving at its recommendation, the Commission considered the information at its disposal, including comments received during the investigation period.

The Commission found that:

- The Southern African Customs Union ("SACU") market for sugar confectionery comprises of major confectionery manufacturers such as Tiger Brands Ltd (Beacon brand), Premier Foods (Manhattan brand), Lodestone Brands (Rascals, Mister Sweet and Candy Tops) and Trade Kings. Information submitted indicated that, for the sugar confectionary sector as a whole, Tiger Brands Ltd had a leading market share followed by Premier Food, Candy Tops and Mister Sweet.
- Information submitted showed that the subject product is currently only being manufactured by Nestlé SA (Pty) Ltd and Tiger Brands Ltd, both vertically integrated entities using domestic sugar as an input product, mostly for their own use in the manufacture of chocolate varieties that they sell.

- Information submitted further indicated that Tiger Brands Ltd competes with the Applicant in the final product market and Nestlé SA (Pty) Ltd does not supply third parties with the product concerned as it uses all the bulk white chocolate that it manufacturers for its own application. The Applicant may therefore experience price undercutting from its suppliers who are, at the same time, its competitors.
- According to the Applicant, it needs to import bulk white chocolate from the EU as a raw material in the production of retail-ready chocolate products at a rate of 25 per cent *ad valorem*, which makes it challenging to compete even in international markets. Compounding the situation is the fact that the final retail-ready chocolate products, originating from the European Union ("EU"), enter the SACU market duty free as a result of the Economic Partnership Agreement between the EU and its Member States on the one hand, and SACU and Mozambique on the other hand, which came into force on 16 October 2016 ("EPA").
- Import data obtained from the South African Revenue Service ("SARS") indicated that imports of chocolate originating from the EU, recorded a 58%, 55% and 60% share of total imports in 2017/18, 2018/19 and 2019/20 financial years, respectively.
- In terms of information supplied in its price cost build up, it was found that the Applicant has experienced negative profit margins until 2019/20, when a marginal profit was realised.
- The Applicant experienced price disadvantages against imported chocolates originating from the EU. Higher levels of price disadvantages were experienced against imports from other economic regions that are relatively lower priced when compared to EU prices.
- The Applicant's information relating to its employment levels indicated a general upward trend, during the period under investigation.
- In terms of reciprocal commitments, the Applicant committed to increase investment, production and employment during year 1, year 2 and year 3 should the application for the creation of a rebate provision be successful.
- In terms of pricing commitments, the Applicant submitted that prices will increase in year 1 subsequent to which it will reduce and stabilise in years 2 and 3.
- In line with the NGP, together with the Re-imagined Industrial Strategy, Master plans and SA Trade Policy, appropriate customs tariff policy under the new landscape must

reflect a strategic approach, which advances an industrialisation agenda based on, *inter alia*, creating and retaining employment, increasing production and investment, building dynamic firms and economic inclusion, building local capacity ("localisation") for both local and global markets, greening the economy and enhancing international competitiveness.

- The rebate facility concerned would be subject to an International Trade Administration Commission permit with specific Guidelines, Rules and Conditions.

In light of the foregoing, the Commission decided to recommend that a temporary rebate facility be created for white chocolate, in immediate packaging of a content of 25 kg or more, classifiable under tariff subheading 1704.90, for use in the manufacture of chocolate containing cocoa, in blocks, slabs or bars, classifiable under tariff subheading 1806.3, and other chocolate classified in tariff subheading 1806.90, in such quantities, at such times and subject to such conditions as the International Trade Administration Commission may allow by specific permit, provided the product is not available in the SACU market.

1. APPLICATION AND TARIFF POSITION

1.1. Kees Beyers Chocolates CC (the "Applicant" or "Beyers Chocolate"), applied for the creation of a temporary rebate facility under Schedule 4 of the Customs and Excise Act, No.91 of 1964 for the importation of bulk white chocolate, classifiable under tariff subheading 1704.90 for use in the manufacture of chocolate classifiable under tariff subheadings 1806.31, 1806.32 and 1806.90.

1.2. Beyers Chocolates considers itself as one of the largest independent manufacturers of boxed chocolate products in South Africa, supplying both the domestic and international markets. The company owns a range of confectionery, including local brands such as Sweetie Pie, Amarula and Dream Bear. According to the Applicant, the company also has a wide range of sub-brands and private label products that are supplied to airlines and the hospitality industry.

1.3 As reasons for the application, Kees Beyers stated, *inter alia*, that:

- *"Bulk white chocolate production in the SACU is mainly produced for own use by* *large chocolate producers who are predominantly multinational companies. Production of industrial bulk white chocolate for resell is minimal to non-existent locally;*

- *Beyers Chocolates does not manufacture bulk white chocolate; however, it imports bulk white chocolate which is used as a raw material in producing numerous retail-ready chocolate products;*

- *In the past, Beyers Chocolates exported chocolates to different countries including the EU. However, the locally produced products find it challenging to compete partly because of the significant duty on bulk white chocolate. The company intends to not only grow in the domestic market but also grow exports. It is therefore important to eliminate unnecessary customs duty costs on raw materials;*

- *Bulk white chocolate required by Beyers Chocolates is imported from Europe and attracts a 25% customs duty. The company intends on penetrating the EU market with innovative chocolate products. However, the EU has various customs duties on chocolates including those exported from SACU. The 25% duty on a vital raw material (bulk white chocolate) as well as the customs duties levied on the final manufactured products when entering the EU makes it challenging to compete in the EU market.*

- *Compounding the situation is that final retail-ready chocolate products originating from the EU enter the SACU market duty free because of the Economic Partnership Agreement (EPA). This is a significant challenge because in addition to having large economies of scale, EU manufacturers do not pay import duties on raw materials and their final retail ready chocolate products also do not pay any duty when entering the SACU market.*

- *SACU chocolate manufacturing has been under pressure for years and a number of companies have closed down over the years. Many jobs have been lost as a result. Furthermore, some well-known multinational chocolate manufacturers have shifted some of their manufacturing from SACU to Europe. They now import some of their chocolate product lines in addition to local manufacturing. This puts pressure on Beyers Chocolate which manufactures all of its products locally.*

- *Retail ready chocolate products originating from the EU have been a significant challenge for years and have in fact contributed to the closure of some local companies. Attempts have been made over the years to apply for protection against EU imports using the appropriate remedies, however, these efforts have not produced the desired outcome. These efforts are known to ITAC"*

1.4 The application was published in Government Gazette Number 45352, Notice 625 of 2021 on 22 October 2021, for interested parties to comment.

1.5 The current tariff structure for bulk white chocolate is shown in Table 1 below:

Table 1: Tariff structure of subject product – input material

Tariff heading	Tariff subheading	Description	Statistical unit	Rate of Duty					
				General	EU/UK	EFTA	SADC	MERCOSUR	AfCFTA
17.04		**Sugar confectionery (including white chocolate), not containing cocoa:**							
	1704.90	Other	Kg	37%	25%	37%	Free	37%	37%

Source: SARS

1.6 Table 1 above shows that bulk white chocolate is currently classifiable with other products under tariff subheading 1704.90. The subject product currently attracts a 37 per cent *ad valorem* duty from countries under the General, European Free Trade Association ("EFTA"), the African Continental Free Trade Area ("AfCFTA) and MERCOSUR regions and 25 per cent *ad valorem* duty under the European Union/United Kingdom ("EU/UK") region, and free of duty under the Southern African Development Community ("SADC") region.

1.7 Table 2 below shows the tariff structure of the final product/s manufactured by the Applicant. The final products are classifiable under tariff subheadings 1806.31, 1806.32 and 1806.90. Currently, chocolate products classifiable under tariff subheading 1806.3 attract a 20 per cent *ad valorem* duty under the General, EFTA and MERCOSUR regions and 16 per cent *ad valorem* duty under the AfCFTA region. Chocolate products classifiable under tariff subheading 1806.90 attract a 10 per cent *ad valorem* duty under general, 17 per cent under EFTA and Mercosur and 13.4 per cent from AfCFTA. Chocolate products originating from the EU and SADC are currently imported at free of duty.

Table 2: Tariff structure of final manufactured products

Tariff heading	Tariff subheading	Description	Statistical unit	Rate of Duty					
				General	EU/UK	EFTA	SADC	MERCOSUR	AfCFTA
18.06		**Chocolate and other food preparations containing cocoa:**							
	1806.3	**Other, in blocks, slabs or bars:**							
	1806.31	Filled	Kg	20%	Free	20%	Free	20%	16%
	1806.32	Not filled	Kg	20%	Free	20%	Free	20%	16%
	1806.90	Other	Kg	10%	Free	17%	Free	17%	13.4%

Source: Applicant

1.8 The Applicant requested a 4th Schedule rebate, which makes provision for rebate of the full customs duty on bulk white chocolate, with the following rebate description provided by the South African Revenue Service ("SARS") as shown in Table 3 below:

Table 3: Rebate description

Rebate Item	Tariff sub heading	Description	Extent of Rebate
xxx.xx	1704.90	White chocolate, in immediate packaging of a content of 25 kg or more, classifiable in tariff subheading 1704.90, for use in the manufacture of chocolate containing cocoa, in blocks, slabs or bars, classifiable in tariff heading 1806.3, and other chocolates classified in tariff subheading 1806.90, in such quantities, at such times and subject to such conditions as the International Trade Administration Commission may allow by specific permit, provided the product is not available in the SACU market	Full duty

Source: SARS

2. DISCUSSION

2.1. Information at the Commission's disposal indicates that bulk white chocolate is a chocolate confection, pale ivory in colour, made from cocoa butter, sugar, milk solids and sometimes vanilla.

2.2. The subject product is used to manufacture different types of chocolate for retail sale. The two basic ingredients used in the confectionery industry are sugar and cocoa. White chocolate does not contain cocoa solids, which are found in other types of chocolate such as milk chocolate and dark chocolate.

2.3. According to information at the Commission's disposal, chocolates manufactured by the Applicant are molded into a variety of different shapes and sizes. They may also contain a variety of fillings, which includes but is not limited to peanuts, raisins, almonds, hazelnuts, coconuts, fudge, toffee coated in chocolate, among others. However, some chocolates do not contain any sort of fillings.

2.4. Figure 1 below shows the position of the subject product in the value chain:

Figure 1: Chocolate value chain

Source: Adapted from Applicant

2.5. Information submitted showed that the subject product is currently only being manufactured by Nestlé SA (Pty) Ltd and Tiger Brands Ltd, both vertically integrated entities using domestic sugar as an input product, mostly for their own use in the manufacture of chocolate varieties that they sell.

2.6. According to information at the Commission's disposal, in the domestic market, the major sugar confectionery manufacturers are Tiger Brands Ltd (Beacon brand), Premier Foods (Manhattan brand), Lodestone Brands (Rascals, Mister Sweet and Candy Tops), Trade Kings and Aldor. Tiger Brands Ltd has a leading market share in the sugar confectionary sector as a whole, followed by Premier Foods, Candy Tops and Mister Sweet.

2.7. The other local manufacturers of chocolates include Nestlé SA (Pty) Ltd, Mondelēz International, Sally Williams Fine Foods, Dicks Sweets, and Cadbury. It is important to note that some of these local manufacturers are also importers of retail-ready chocolate products.

2.8. Information at the Commission's disposal also indicated that the domestic market share of domestic manufacturers continues to be challenged by imported premium brands and niche chocolatiers, which are imported duty-free from the EU as Europe continues to dominate the global confectionery market especially with regard to chocolate. The imported premium brands include brands such as Ferrero Rocher and Lindt, and niche chocolatiers, like Hamlet and Butlers, amongst others.

2.9. Information submitted confirmed that over the period of investigation, the Applicant's capacity utilisation increased in line with its increased production volume.

2.10. According to information at the Commission's disposal, Tiger Brands Ltd competes with the Applicant in the final product market and Nestlé SA (Pty) Ltd does not supply third parties with the product concerned as it uses all the bulk white chocolate that it manufacturers for its own application. The Applicant may therefore experience price undercutting from its suppliers which are, at the same time, its competitors.

2.11. Information submitted indicated that the Applicant is experiencing a price disadvantage against imported products originating from the EU. Information at the Commission's disposal indicated that imports from other economic regions are relatively low priced when compared to EU imports, and would therefore likely confirm higher levels of price disadvantages when compared to EU imports.

2.12. Reciprocal commitments made by the Applicant for the proposed tariff amendment were provided, particularly with respect to increased production, investment and employment creation, which is consistent with the New Growth Path ("NGP").

2.13. Comments with regards to this application were received from, *inter alia,* the South African Sugar Association ("SASA"), Eurochoc, Tiger Brands Ltd, and Nestlé SA (Pty) Ltd.

2.14. The South African Sugar Association ("SASA") objected to the application stating, among others, that although the subject product is being manufactured locally by other local companies, the reason why the subject product cannot be purchased locally remains unclear.

According to SASA, the concerns raised by the Applicant have largely been one of the subject matters of the Sugarcane Value Chain Master Plan 2030, specifically Task Team 10 (which comprises of sugar convertors). This task team's approach has been to seek means of resolving Sugar Convertors' challenges in favour of increasing the manufacturing of local sweets and chocolate production, local job creation, and sugar usage.

SASA concluded that there are various initiatives seeking to assist the downstream players and increase the utilisation of locally based products to grow the economy and create jobs.

2.15. Tiger Brands Ltd submitted its comments objecting to the application. Tiger Brands Ltd is one of the largest manufacturers in the confectionery market and regards itself as the market leader in the South African sugar confectionary segment. In its objection to the application, Tiger Brands Ltd stated that the statement by the Applicant that: "*...production of industrial bulk white chocolate for resale is minimal to non-existent*" is not backed by any evidence as the Snack, Treats and Beverages department of Tiger Brands Ltd currently produce bulk white chocolate both for the company's own use as well as for resale. Tiger Brands Ltd stated that it can supply the subject product to the Applicant and other market players.

Tiger Brands Ltd argued that the alleged challenge facing the Applicant is the importation of retail-ready chocolates (final products), and such challenge can therefore, not be solved by a rebate on the raw material. According to Tiger Brands Ltd, the Applicant should rather consider an application for a duty increase on the final product through the imposition of an agricultural safeguard.

Applicant's counter comments:

2.16. The response of the Applicant to the objections submitted by Tiger Brands Ltd and Nestlé SA (Pty) Ltd follows below.

2.17. The Applicant stated that the fact that Tiger Brands Ltd and Nestlé SA (Pty) Ltd compete in the same market with regard to the final product is major issue. According to the Applicant, if it procures all its bulk white chocolate requirements from its competitors, its final costs and pricing might be materially constrained. The Applicant indicated however, that should the domestic pricing be reasonable and the recipe be correctly formulated, it is committed to sourcing bulk white chocolate locally.

2.18. The Applicant reiterated the fact that the challenges currently experienced could be reduced through enforcement of the Agricultural Safeguard in terms of Article 35 of the EPA on imports of retail ready chocolate. The Applicant anticipates that the granting of this rebate provision could alleviate the pressures experienced from the influx of retail ready chocolates originating from the EU.

2.19. The Applicant stated that not granting the requested rebate provision on the basis of its sugar content is misguided when considering the fact that retail ready chocolate products, which are currently being imported at free of duty, contain similar or even more sugar in terms of the active ingredients.

2.20. The Applicant submitted that it currently does not have sufficient volumes to justify manufacturing its own raw material product.

2.21. According to the Applicant, the majority of retailers such as Clicks, Checkers, Pick n Pay, and other domestic manufacturers such as Cadbury, currently import retail ready chocolate whilst the majority of employment opportunities lie in the conversion of consumer ready chocolate instead of importing the final product.

3. SUMMARY OF FINDINGS

3.1. The Commission found that:

- The SACU market for sugar confectionery comprises of major confectionery manufacturers such as Tiger Brands Ltd (Beacon brand), Premier Foods (Manhattan brand), Lodestone Brands (Rascals, Mister Sweet and Candy Tops) and Trade Kings. Information submitted indicated that, for the sugar confectionary sector as a whole, Tiger Brands Ltd had a leading market share followed by Premier Food, Candy Tops and Mister Sweet.

- Information submitted showed that the subject product is currently only being manufactured by Nestlé SA (Pty) Ltd and Tiger Brands Ltd, both vertically integrated entities using domestic sugar as an input product, mostly for their own use in the manufacture of chocolate varieties that they sell.
- Information submitted further indicated that Tiger Brands Ltd competes with the Applicant in the final product market and Nestlé SA (Pty) Ltd does not supply third parties with the product concerned as it uses all the bulk white chocolate that it manufacturers for its own application. The Applicant may therefore experience price undercutting from its suppliers who are, at the same time, its competitors.
- According to the Applicant, it therefore has to import bulk white chocolate from the EU as a raw material in the production of retail-ready chocolate products at a rate of 25 per cent *ad valorem*, which makes it challenging to compete even in international markets. Compounding the situation is the fact that the final retail-ready chocolate products, originating from the EU, enter the SACU market duty free as a result of the EPA.
- Import data obtained from SARS indicated that imports of chocolate originating from the EU, recorded a 58%, 55% and 60% share of total imports in 2017/18, 2018/19 and 2019/20 financial years, respectively.
- In terms of information supplied in its price cost build up, it was found that the Applicant has experienced negative profit margins until 2019/20, when a marginal profit was realised.
- The Applicant experienced price disadvantages against imported chocolates originating from the EU. Higher levels of price disadvantages were experienced against imports from other economic regions that are relatively lower priced when compared to EU prices.
- The Applicant's information relating to its employment levels indicated a general upward trend, during the period under investigation.
- In terms of reciprocal commitments, the Applicant committed to increase investment, production and employment during year 1, year 2 and year 3 should the application for the creation of a rebate provision be successful.

- In terms of pricing commitments, the Applicant submitted that prices will increase in year 1 subsequent to which it will reduce and stabilise in years 2 and 3.
- In line with the NGP, together with the Re-imagined Industrial Strategy, Master plans and SA Trade Policy, appropriate customs tariff policy under the new landscape must reflect a strategic approach, which advances an industrialisation agenda based on, *inter alia*, creating and retaining employment, increasing production and investment, building dynamic firms and economic inclusion, building local capacity ("localisation") for both local and global markets, greening the economy and enhancing international competitiveness.
- The rebate facility concerned would be subject to a permit issued by the International Trade Administration Commission with specific Guidelines, Rules and Conditions.

4. RECOMMENDATION

4.1. In the light of the foregoing, the Commission recommended the creation of a temporary rebate facility for the importation of white chocolate, in immediate packaging of a content of 25 kg or more, classifiable under tariff subheading 1704.90, for use in the manufacture of chocolate containing cocoa, in blocks, slabs or bars, classifiable under tariff subheadings 1806.3, and other chocolate classified in tariff subheading 1806.90, in such quantities, at such times and subject to such conditions as the International Trade Administration Commission may allow by specific permit, provided the product is not available in the SACU market.