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Government announces package of about Rs.7,000 crore for sugar industry

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On 6th June 2018, the government approved interventions to deal with the current crisis in the sugar industry and to provide some relief to the sugar millers that are pressurized with sugarcane arrears of more than Rs.22,000 crore to be paid to the sugarcane farmers. The government announced the following measures that involve a total amount of about Rs.7,000 crore:

Measure 1: The announcement involves creation of buffer stock of 3 million tonnes of sugar for one year that would result in estimated expenditure of Rs.1,175 crore. The reimbursement under this scheme would be directly credited to farmers' account for the arrears that are to be paid to the farmers.

Measure 2: The Cabinet decided to fix the minimum selling price of white/refined sugar at the mill gate below which no white/refined sugar can be sold and delivered by a sugar mill in the domestic market. Initially, the minimum selling price of white/refined sugar has been fixed at Rs.29per kg.

The first two measures would be reviewed by the Department of Food & Public Distribution (DFPD) any time based on the actual situation in the market and industry.

Measure 3: The government will bear interest subvention of maximum Rs.1,332 crore over a period of 5 years including moratorium period of one year on estimated bank loan amounting to Rs.4,440 crore to be sanctioned to the sugar mills by the banks over a period of 3 years. This amount would be used to increase the capacity of existing distilleries and to install new distilleries.

Expected impact of the above measures

Sugar stock situation

As per Indian Sugar Mills Association (ISMA), India produced around 31 million tonnes of sugar during October 2017-April 2018 and the association estimates sugar output to be at 31.5-32 million tonnes for the ongoing sugar season October 2017-September 2018. This implies a growth of about 55%-57% compared with 20.3 million tonnes of sugar produced during sugar season 2016-17.

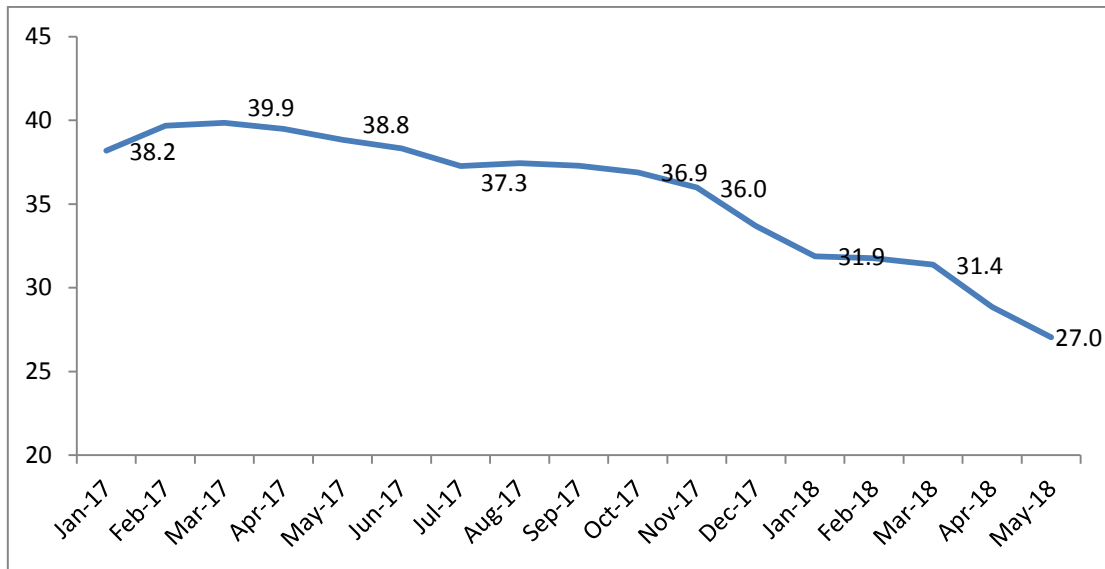
Along with production, the country has an opening stock of 3.9 million tonnes of sugar which brings the domestic availability of sugar to 35.4 million tonnes to fulfil the domestic consumption needs of around 25.2 million tonnes (assuming a growth of 2.5% y-o-y). Thus, India will be left with 10.2 million tonnes of sugar as opening stock for the next year.

(Note: We believe minimum exports to take place during 2017-18 even though the government had announced export of 2 million tonnes of sugar by end of September 2018 under Minimum Indicative Export Quota (MIEQ) on 29 March 2018. This is because the international prices are weaker compared with the domestic sugar price which is likely to act as a barrier for sugar mills with respect to exports. Thus, exports are not considered for calculating opening stock.)

Impact of measure 1: Now with the government announcing a buffer stock of 3 million tonnes of sugar, this quantity will be out of the system for some time now. Despite this, the country will end the year with a closing stock of 7.2 million tonnes which is around 1.2-2 million tonnes more than the normative requirement of 3 months stock for the next sugar year.

Sugar prices

Chart 1: Movement in wholesale small grade sugar prices in Mumbai (in Rs./kg)



Source: CMIE

The small grade sugar prices in Mumbai though declined on m-o-m basis in most of the months during January –November 2017, they had remained in the range of Rs.36-Rs.40 per kg during this period. However, the prices then declined to Rs.33.7 per kg in December 2017 which then reached at a low of Rs.27 per kg in May 2018. The sharp fall in prices is on account of bumper production in the ongoing sugar season 2017-18 and an estimated increase in sugar production in the next year.

Impact of measure 2: Considering the sharp decline in prices, the government decided to fix the minimum selling price of white/refined sugar at the mill gate at Rs.29 per kg. This will act as a support to domestic prices and will help the wholesale prices to accelerate to Rs.32 per kg-Rs.34 per kg in the coming months which stood at Rs.27 per kg in May 2018.

Despite this, the industry will not be much benefitted as the cost of sugar production remains high compared with the mill gate price of Rs.29 per kg. If the FRP is considered, the cost of sugar production stands at Rs.31.6 per kg while considering SAP (for Uttar Pradesh), the cost of production stands at Rs.37 per kg. Table 1 highlights the same.

As per a sample of 46 sugar companies for 2016-17, the raw materials cost accounted for around 85% of the total expenses, primary raw material here being sugarcane. Considering this, Table 1 is prepared which provides an idea on sugar production cost.

Table 1: Cost of sugar production considering FRP and Uttar Pradesh SAP

	(in Rs./tonne)	Total cost of cane for producing one tonne of sugar (in Rs.)	Sugar price (in Rs./tonne) considering raw material cost at 85% of total expenses	Cost of producing sugar (in Rs./kg)
FRP	2,550	26,840	31,576.5	31.58
SAP	3,150	31,500	37,058.8	37.06

Thus, it can be seen that the fixing of sugar mill gate price at Rs.29 per kg will not be sufficient for the clearing of sugarcane dues given that it does not cover the cost of sugar production.

Ethanol supply

Under Ethanol Blended Programme (EBP), the blending target with petrol which was earlier set at 5% has been increased over the years to 10% to promote blending of ethanol with petrol and its use as alternative fuel. The ethanol supply however has remained below the target. During 2016-17, the blending was at 4.3%.

Impact of measure 3: The announcement will encourage more diversion of sugarcane towards ethanol and will motivate sugar millers to opt for ethanol production. This, in turn, will help the sugar industry to move towards the target of EBP. Also, more diversion of sugarcane towards ethanol will augur well for the industry when there is a surge in sugar production. As per CACP, the distilleries manufacturing ethanol had a capacity of 6,655 klpd (kilo litres per day) during 2015-16.

Concluding remarks

The announcement comes as a relief to the sugar industry as it will help the sugar prices to increase in the coming months but does not provide major benefits to the industry. This is because the sugar mill gate price of Rs.29 per kg will not be sufficient for the clearing of sugarcane dues given that it does not cover the cost of sugar production.

The industry however cannot rely on these interventions constantly and therefore the problems of the sugar industry needs to be addressed with some determined solutions.