Fertilizer Industry - March 2021 update

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Production, Imports and Sales during April-January 2021 i.e. 10M-FY21

Table 1: Production, Imports and Sales of Key Fertilizers (Unit: Lakh Metric Tonnes- LMT)

			Change (y-o-y)	
	2019-20	2020-21	2019-20	2020-21
Overall Fertilizers Production	359	370	4.2%	3.0%
Overall Fertilizers Imports	204	230	21.8%	12.6%
Overall Fertilizers Sales	486	581	0.4%	19.4%
Urea Production	204	210	2.3%	2.7%
Urea Imports	84	98	26.0%	16.6%
Urea Sales	325	308	20.8%	-5.3%
DAP Production	38	34	26.5%	-12.2%
DAP Imports	46	47	-21.1%	4.2%
DAP Sales	87	97	11.1%	11.4%
MOP Imports	34	38	-2.4%	14.4%
MOP Sales	24	30	-1.3%	23.6%
SSP Production	37	41	6.5%	13.0%

Source: Department of Fertilizers, CMIE, Office of the Economic Adviser
Note: Fertilizer sales are considered as a proxy for demand.

- **Overall fertilizers** production has increased by 3% during 10M-FY21 after registering a growth of 4.2% during 10M-FY20. The country witnessed an on-time arrival of Southwest monsoon, followed by a quick spread across the region which has resulted in higher sowing thus augmenting the sales of fertilizers which has led to an increase in production. Increase in production can also be ascribed to restocking activities undertaken by the manufacturers in order to keep up with the sharp increase fertilizer sales witnessed during the year. On a monthly basis, production increased by 2.7% during January '21 due to build-up of stocks by companies and increase in production of Complex fertilizers and DAP. The demand for these fertilizers is usually high during the rabi season. Imports have increased sharply by 12.6% due to by the sharp increase in urea and MOP imports. Import dependence (imports as a proportion of production plus imports) has increased from 36% during 10M-FY20 to 38% during 10M-FY21.

- Production of **urea** increased by 2.3% during 10M-FY21 due to favourable weather and market conditions. Urea is largely sourced domestically however, high demand necessitates imports which have risen sharply by 16.6% to supplement the increase in demand. Import dependence of urea (imports as a proportion of production plus imports) has increased to 32% during 10M-FY21 compared with 29% during 10M-FY20.

- **DAP** production fell by 12.2% during 10M-FY21. Decline in production can be attributed to the shortage in raw material availability and increase in prices of inputs. Imports on the other hand have risen by 4.2% in the same period and import dependence of DAP (imports as a proportion of production plus imports) has increased to 59% during 10M-FY21 compared with 54% during 10M-FY20

- **MOP** imports have increased sharply by 14.4% during 10M-FY21. India meets its Potassium chloride (commonly referred to as Muriate of Potash or MOP) requirements completely through imports from Canada, Russia, CIS+ Belarus, Israel, Jordan and Lithuania.

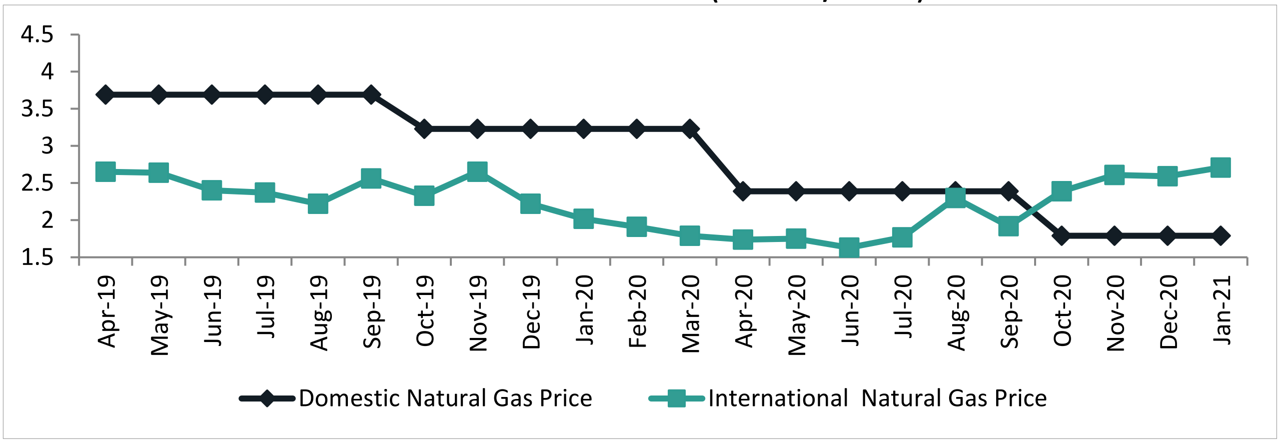
- The production of **SSP** which is an indigenous phosphatic multi-nutrient fertilizer increased sharply by 13% during 10M-FY21. SSP is a cheaper alternative to DAP.

- Overall **sales** of fertilizers have increased by 19.4% during 10M-FY21. Sales of DAP and MOP have increased by 11.4% and 23.6% during 10M-FY21 while that of urea has declined by 5.3%. Initially in the start of FY21, panic buying by farmers and dealers coupled with the low prices of the commodity had led to an increase in the sales of fertilizers. Farmers were stocking up fertilizers for the on-going kharif season and were building up stocks in order to avoid any logistical issues which could have been faced due to the coronavirus pandemic. However, the momentum in sales has been sustained due to a favourable monsoon season, which has led to a good crop sowing for the country.

Trend in prices of key input raw materials

Natural gas is used as a feedstock for the manufacturing of urea and accounts for 50%-80% of the raw material cost. The fertilizer industry is the leading consumer of domestic natural gas. Additional requirement of natural gas is supplied through imports in the form of RLNG. Out of 31 urea plants in India, 28 are gas based and 3 are naphtha based. Natural gas is preferred as; it is intrinsically hydrogen rich as compared to other feedstock on a unit weight basis and is easier to process.

Chart 1: Trend in Domestic and International Natural Gas Prices (unit: USD/mmBtu)



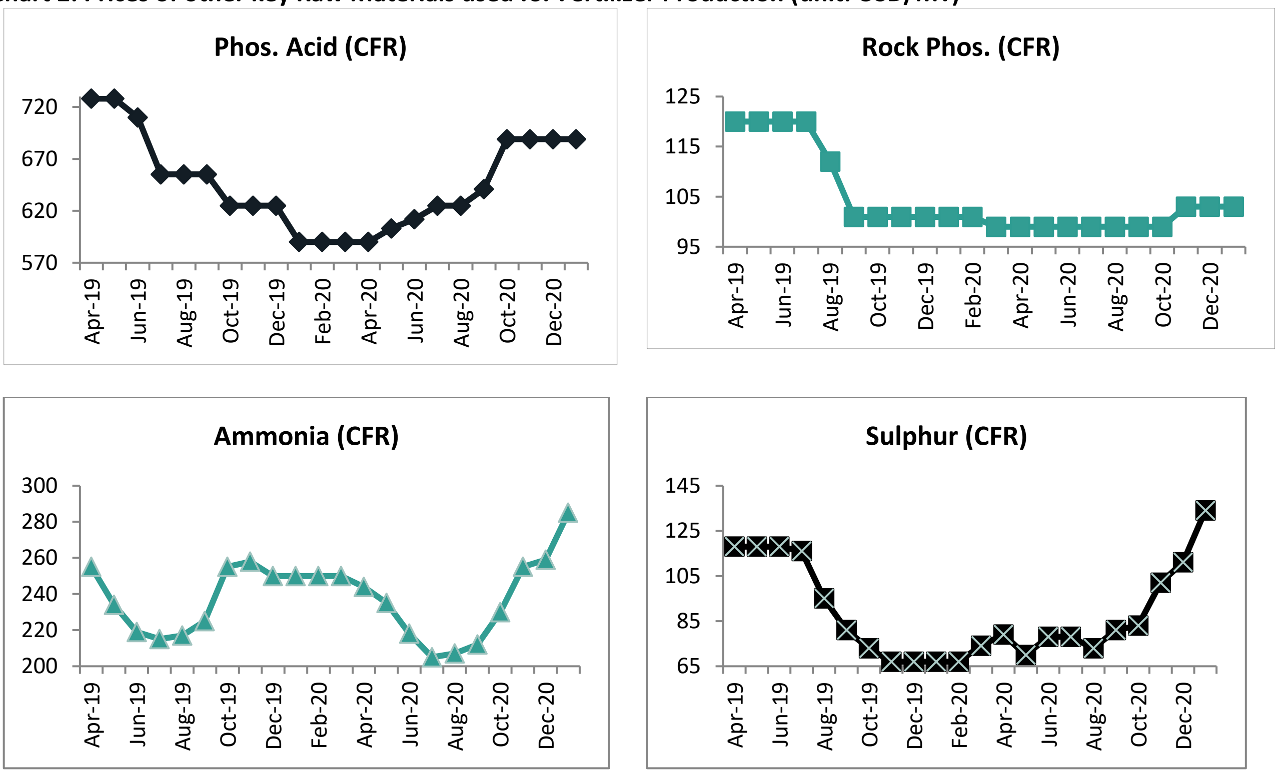
Source: PPAC and EIA

As per the New Domestic Gas Policy, the government revises the domestic natural gas price every six months i.e. April-September and October-March. Currently (H2-FY21) the price for gas produced from local fields has been revised to USD 1.79/mmBtu which is the lowest price ever set as per the New Domestic Gas Policy.

As per our estimates, a 25.1% fall in natural gas prices could potentially lead to a 12% decrease in cost of production of urea, thus decreasing the working capital intensity of the fertilizer manufacturers and it will also act as a relief for the fiscal spending of the government while disbursing the urea subsidy, which is already constrained at the moment. This also comes at a good time as the finances of the centre are already strained with the COVID-19 pandemic on the loose.

Prices of R-LNG are usually governed by market dynamics based on contracts and are linked with the global crude oil prices. However, soon fertilizer plants could be taking delivery on India's first gas exchange (prices are based on market demand-supply) — the Indian Gas Exchange (IGX) which has been launched in the start of FY21. Currently the exchange is only dealing with delivery of imported natural gas (LNG).

Chart 2: Prices of other key Raw Materials used for Fertilizer Production (unit: USD/MT)



Source: Department of Fertilizer

Prices of phosphoric acid, rock phosphates, ammonia and sulphur have fallen by 2.2%, 8.7%, 1.2% and 3.4% respectively on a y-o-y during 10M-FY21.Manufacturers have passed on the benefit of soft raw material prices by lowering the MRP of decontrolled fertilizers which has greatly supported the increase in sales as well.

However with the opening up and pickup in the economy, the prices of raw materials have been seeing a gradual uptrend and going forward, with the increase in key input costs such as that of phosphoric acid, ammonia and sulphur there could be a consequent increase in the retail price of fertilizers as well.

Status on the Progress of the Revival of 5 fertilizer plants

The government is reviving 5 closed fertilizer plants - 4 of Fertilizer Corporation of India Limited (FCIL) in Talcher, Ramagundam, Gorakhpur and Sindri and 1 of Hindustan Fertilizer Corporation Ltd. (HFCL) in Barauni. This is being done by setting up new ammonia-urea plants with a capacity of 12.7 LMT (Lakh Metric Tonne) per annum. The Government expects that with the commissioning/ start of the above plants, it can increase indigenous urea production significantly leading to a substantial reduction in imports and make India self-sufficient in the years to come.

- Ramagundam Fertilizers and Chemicals Limited (RFCL) has already achieved 99.92% (upto January 2021) of physical progress. Presently the project is in pre-commissioning/commissioning stage.
- Gorakhpur, Sindri and Barauni fertilizer plants have achieved 88%, 84.6% and 83.7% of progress respectively (upto January 2021).
- Overall project progress for the Talcher Fertilizer Plant in Odisha is around 9.26%.

Post the commissioning of all the above plants the domestic indigenous urea production is slated to increase by at least 63.5 LMT/year which will bring down the imports of urea by 70% (assuming FY20 level of imports).

Subsidies offered to the Fertilizer Sector

The fertilizer industry is highly regulated and monitored by the government. The difference between the cost of production which is higher than the price at which the fertilizer is sold to the beneficiary, is reimbursed by the Government in the form of subsidies. Whenever there is shortage of funds, the Government either announces an additional subsidy amount or liquidates the pending subsidy by arranging loans under a Special Banking Agreement (SBA).

While the MRP of urea is fixed and controlled by the Central Government that is not the case with decontrolled fertilizers where in the manufacturers have the liberty to price the product freely according to the prevailing market conditions.

Table 2: Allocation of the Subsidy within the Fertilizer Sector (figures in Rs/crore)

				Y-O-Y change	
	2019-2020 (A)	2020-2021 (RE)	2021-22 (BE)	2020-2021 (RE)	2021-22 (BE)
Urea Subsidy	54,755	94,957	58,768	73.4%	-38.1%
Nutrient based Subsidy	26,369	38,990	20,762	47.9%	-46.8%
Total	81,124	1,33,947	79,530	65.1%	-40.6%

Source: Budget.nic,

Note A-Actuals; RE- Revised Estimates; BE Budget Estimates

Technically the overall subsidy has increased by 11.5% from its FY21 BE amount. Though it seems like the amount has fallen by 40.6%, the FY21 RE figure also includes the additional Rs 65,000 crore announced by the FM in November 2020. The Finance Minister had announced a Rs. 65,000-crore fertilizer subsidy for farmers as part of her stimulus package (Atmanirbhar III). The allocated amount is being provided to ensure adequate availability of fertilisers to farmers and to enable timely accessibility of fertilisers in the upcoming crop season.

Under NBS, the subsidy given to the companies is fixed annually on the basis of its nutrients content (i.e. Nitrogen, Phosphate, Potash and Sulphur) on per kg basis which is converted into subsidy per tonne depending upon the nutrient content in each grade of the fertilizers. These rates are determined taking into account the international and domestic prices of P&K fertilizers, exchange rate, inventory level in the country.

Table 3: Rates of Nutrients under NBS (Unit: Rs/kg)

			Change y-o-y (+/-)	
Nutrient Type	2019-20	2020-21	2019-20	2020-21
Nitrogen (N)	18.9	18.8	0.0%	-0.6%
Phosphorus (P)	15.2	14.9	0.0%	-2.2%
Potash (K)	11.1	10.1	0.0%	-9.1%
Sulphur (S)	3.6	2.4	31.9%	-33.4%

Source: PIB

For FY21, there has been a downward revision for the nutrients covered the NBS. The government approved the inclusion of a complex fertilizer namely Ammonium Phosphate (NP 14:28:0:0) under the NBS Scheme. Per kg subsidy for FY22 will now be announced in April 2021.

Table 4: Fertilizer Subsidies paid upto January 2021 (Unit: Rs/crore)

	2020-21 (RE)	Actuals up to January 2021	% of Actuals to Revised Estimates
Urea Subsidy	94,957	72,210	76%
Nutrient Based Fertilizers Subsidy	38,990	26,462	68%
Total	1,33,947	98,671	74%

Source: Controller General of Accounts

In the current financial year, FY21 the government has already paid 74% of the revised budgeted subsidy amount upto January 2021. This is post the inclusion of the additional Rs 65,000 crore subsidy, disbursement for which was commenced January 2021 onwards. In the corresponding period of the previous financial year, the government had disbursed 100% of the urea subsidy and 100% of the NBS.

Conclusion/ Outlook for FY21

Rural demand and markets has been buoyed and very promising despite the coronavirus pandemic and macroeconomic uncertainty. This has translated in improving the underlying macros for the Indian fertilizer industry. Agricultural operations have been well placed and has grown backed by a bumper Rabi harvest and good monsoon during the Kharif season. With surplus reservoirs levels, record high kharif crop sowing and plentiful rainfall during the monsoon season, demand for the procurement of fertilizers has been promising till date.

Sales have increased sharply by 19.4% during 10M-FY21 and going forward with the increase in liquidity of farmers and good moisture level in the soil we expect a very good Rabi season. Keeping this in mind, the demand for fertilizers for the rest of FY21 seems sanguine.

- The rural economy continues to be a bright spot with two consecutive years of above normal rainfall. Further the government has announced an increase of MSP upfront on the Rabi crops with its objective to provide minimum 50% returns on the cost of production to farmers.
- Decontrolled fertilizer sales is also to increase on the back low prices of DAP and SSP and the government's thrust on improving balanced nutrition. Usually the demand for DAP and DAP blends increases during rabi sowing.

With the forecast of normal monsoons and the rollout of COVID vaccination program in the coming months, we expect the economic activities to normalize during FY22. Currently, IMD is forecasting a normal monsoon, which will commensurate in moisture levels being healthy and water levels too remain elevated as well. This will lead to the acreage being favourable as well. So from that standpoint, we should see the consumption and the growth in demand to continue.

The overall fertilizer production is to grow by 4-6% during FY21. Overall fertilizer production had increased by 2.7% during FY20 and has increased by 3% during 10M-FY21.

- We expect production to increase in the coming months on the back of restocking activities undertaken by fertilizer manufacturers.
- Currently the liquidity situation of manufacturers seems to have improved. Fall in input costs and disbursement of the additional subsidy has improved the working capital situation of manufacturers during the year.
    - Urea manufacturers are to immensely benefit with the current low gas prices. Domestic gas prices have fallen furthered during the second revision.

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