

Operating profit for sugar companies to decline: UP based mills to register a loss on sugar business ...

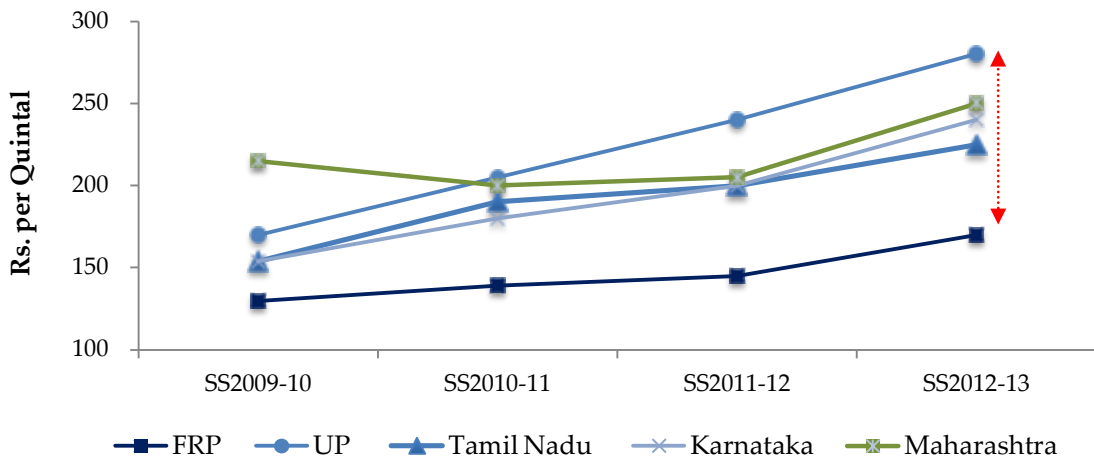
In Sugar Season (SS) 2012-13, sugar companies are expected to witness a drop in operating profit led by the higher cost of production coupled with lower sugar prices. The rise in cost of production is mainly attributable to the substantial rise in the sugarcane procurement cost which accounts for almost 80 to 85 per cent of the total operating cost of the industry.

For every Sugar Season, the central government determines the minimum price payable to the sugarcane farmers known as Fair and Remunerative Price (FRP). However, in some states, like UP, Tamil Nadu, Haryana and Punjab, the state government fixes minimum price at which the sugar mills have to procure sugarcane from the farmers, known as State Advised Price (SAP). Even in the other states like Maharashtra and Karnataka, which do not declare the SAP prices, sugar mills have to pay sugarcane farmers higher prices than the FRP fixed by the central government. This is done to support farmers and boost the area under sugarcane cultivation. Thus, the per tonne sugarcane cost differs from company to company based on the location of the plants.

Widening gap between sugarcane procurement cost of North based sugar mills over South & West based sugar mills...

In past few years, the SAP declared by the UP government has been the highest among other sugar producing states. The gap between the sugarcane prices of UP and other states has widened in the last two sugar seasons. The difference between the SAP of sugarcane by UP was as high as Rs. 40 per quintal in past couple of years. For the sugar season 2012-13, this difference has increased to a level of Rs. 55 per quintal. So, the sugar mills in the UP region have to bear comparatively higher sugarcane cost due to high SAP prices as against the sugar mills based in other states.

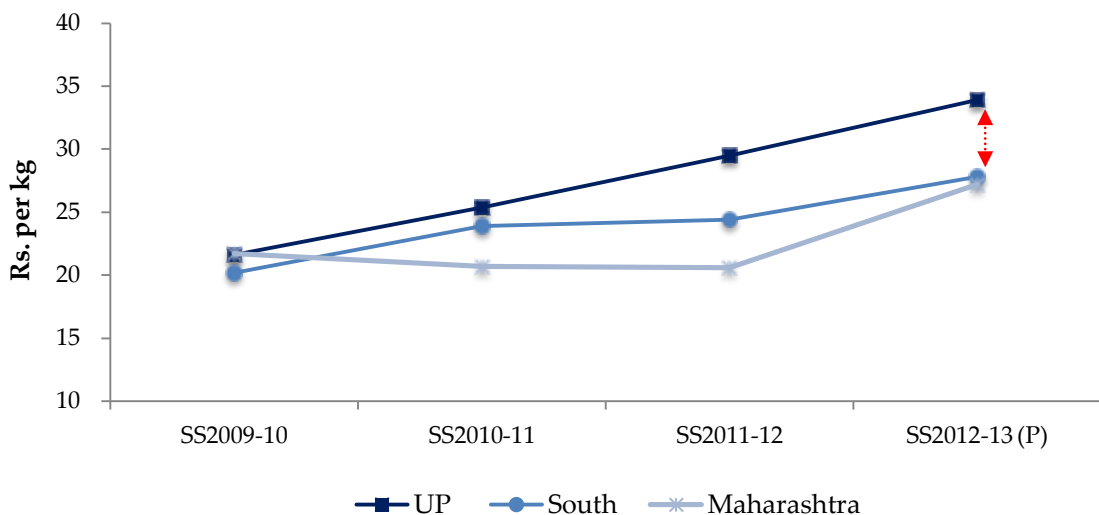
Trend of sugarcane procurement prices



Source: ISMA and CARE Research

On account of the incremental SAP charged by the UP state, the cost of sugar production of UP based sugar mills had remained higher compared to the west and south based sugar mills. During the period SS2009-10 to 2011-12, the cost of production of sugar for the sugar mills in UP region has increased by Rs. 7.8 per kg while the same for sugar mills in the south region has increased by about Rs.4.1 per kg. However, it decreased by Re.1 per kg for sugar mills in Maharashtra mainly on account of some softening in sugarcane prices during the same period.

Trend of sugar production cost



Source: CARE Research

The rise in cost of sugar production has adversely affected the profitability of the sugar mills across the country but the magnitude of impact was higher for the north based

sugar mills. During the period of SS2009-10 to SS2011-12, the operating profit on each kg of sugar sold for the UP based sugar mills and south based sugar mills has decreased by Rs. 5.5 per kg and Rs.1.8 per kg, respectively while for Maharashtra based sugar mills it has increased by Rs.3.5 per kg.

UP based sugar mills to incur an operating loss of Rs. 2 per kg on sugar for SS 2012-13...

For the SS2012-13, UP government has increased the SAP of sugarcane by 17 per cent on a YoY basis to Rs.280 per quintal. Tamil Nadu and Karnataka have increased sugarcane prices for SS 2012-13 by about 15 per cent on a YoY basis. Maharashtra state government has increased sugarcane prices by 22% to Rs. 250 per quintal for SS 2012-13. CARE Research has estimated that in SS 2012-13, the sugar production cost of UP based sugar mills will increase by about Rs.4.4 per kg to about Rs.34 per kg on account of the higher sugarcane procurement cost. The sugar production cost of south and Maharashtra based sugar mills is expected to be at about Rs.28 per kg and Rs.27 per kg, respectively. CARE Research expects average sugar prices to remain range bound in Rs.33-34 per kg in SS2012-13.

So, in SS2012-13, the sugar mills based in west and south regions will be relatively better placed compared to the sugar mills based in UP region. CARE Research estimates that, due to rise in the sugarcane procurement cost, the UP based sugar mills will incur an operating loss of about Rs. 2 on each kg of sugar sold in SS2012-13. On the contrary, the south and Maharashtra based sugar mills are expected to earn an operating profit of about Rs.4 on each kg of sugar sold albeit lower than the previous sugar season.

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