

**Sugarcane FRP increased to Rs.275 per quintal for 2018-19 sugar season**

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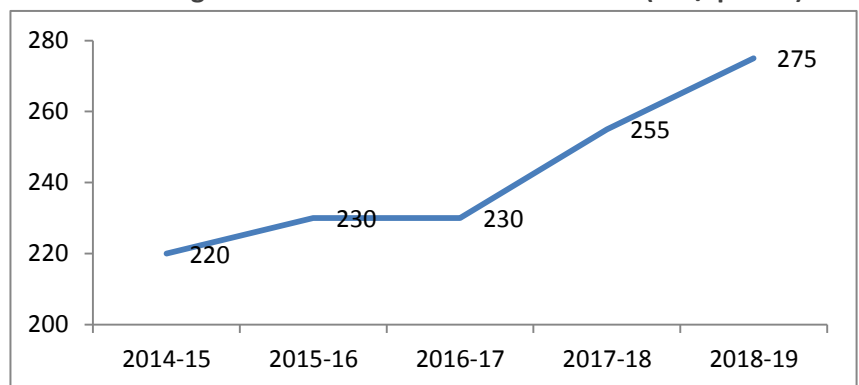
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**Increase in sugarcane FRP for 2018-19 season**

On 18<sup>th</sup> July 2018, the government increased the Fair and Remunerative Price (FRP) of sugarcane to Rs.275 per quintal for a basic recovery rate of 10% based on the recommendations of Commission for Agricultural Costs and Prices (CACAP) for the sugar season 2018-19. This is a rise of 7.8% y-o-y compared with the FRP of sugarcane last year.

**Chart1: Sugarcane Fair and Remunerative Price (Rs. /quintal)**



Source: CMIE

The cost of sugarcane production for the season 2018-19 is at Rs.155 per quintal. Thus, the price fixed by the government is 77.4% higher than its cost of production which the government says will provide a return of more than 50% to the farmers over their cost.

**Hike in FRP compared to increase in MSP of other crops**

In the initial week of July 2018, the government had announced a hike in Minimum Support prices of kharif crops for the year 2018-19. While the MSP for some of the crops was increased in the range of 1%-10% on a y-o-y basis, the MSP for some of the crops had been raised as high as 40%-50% on a yearly basis.

It can be seen from the below table that the 7.8% y-o-y hike in sugarcane price for the season 2018-19 falls in the range of 1%-10% like that of tur, urad and groundnut. Excluding these crops, the y-o-y rise in MSP for other crops like maize, moong, bajra, nigerseed, ragi etc. is more than 10% as shown below.

**Table 1: Range-wise classification of y-o-y % change in MSP of crops for 2018-19**

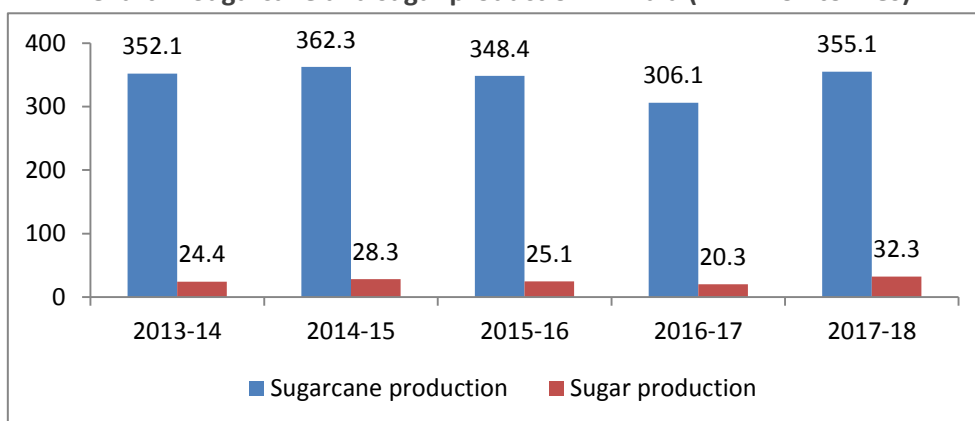
1%-10%	10%-20%	20%-30%	30%-40%	40%-50%	50%-60%
Tur, Urad, Groundnut, Sugarcane	Paddy common, Paddy (F) grade 'A', Maize, Soyabean, Sesamum	Moong, Medium staple cotton, Long staple cotton	Bajra, Sunflower seed	Jowar-Hybrid, Jowar-Maldandi, Nigerseed	Ragi

Source: PIB

While the government by increasing cane cost is considering providing returns of 77.4% over the cost of production to the farmers, this decision is unlikely to augur well for the sugar mills given the current sugar supply glut situation in India which is likely to keep the prices under pressure in the new sugar season 2018-19.

### Sugar production

During 2017-18, sugar production increased by a sharp 59% to about 32.3 million tonnes on a y-o-y basis. This surge in production resulted in surplus supply of sugar in the country. To add to the glut, India's sugar output is estimated to increase to 35-35.5 million tonnes in 2018-19 as per the preliminary estimates released by Indian Sugar Mills Association (ISMA). This is a rise of 8.5%-10.1% on a y-o-y basis backed by a growth in acreage under sugarcane in the country. The country's cane area is estimated to be about 8% y-o-y higher at around 54.4 lakh hectares for 2018-19 sugar season.

**Chart 2: Sugarcane and sugar production in India (in million tonnes)**

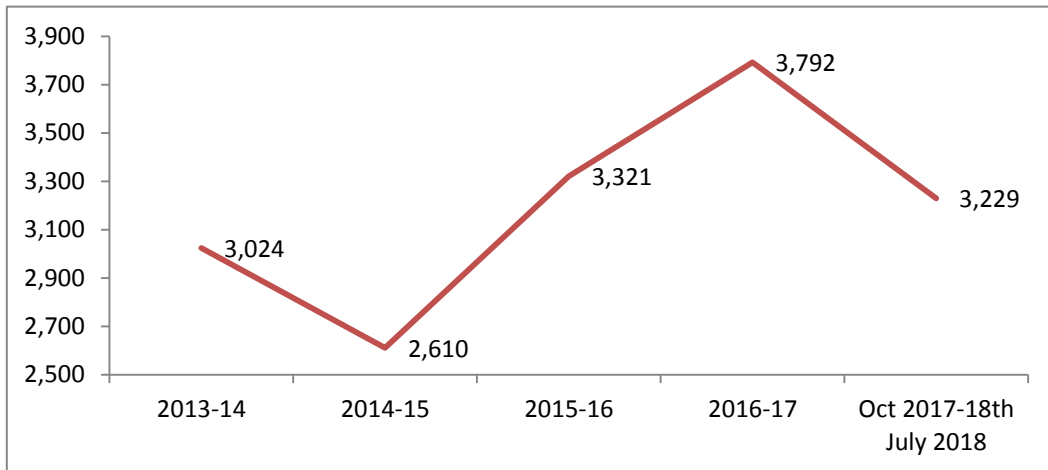
Source: Ministry of Agriculture and ISMA

While production is estimated to be around 35-35.5 million tonnes, consumption during the year is estimated to stand at 25.6 million tonnes. Considering production of 35 million tonnes, the country will be left with surplus stock of 9.4 million tonnes from the season 2018-19. Moreover, India would have an opening stock of 11.1 million tonnes of sugar for the new season 2018-19. This will bring the additional stock to a total of 20.5 million tonnes of sugar at the end of September 2019 considering no exports are made during the year. **Two years of surplus production is expected to keep the prices under pressure during the season 2018-19.**

### Sugar prices

During the sugar season 2016-17, the prices averaged at Rs.3,792 per tonne, a y-o-y growth of 14.2% on account of a fall in sugar production during the year to 20.3 million tonnes. However, with the production increasing to 32.3 million tonnes for 2017-18, the prices started falling and averaged at Rs.3,229 per tonne during 1 October 2017-18 July 2018.

**Chart 3: Small grade sugar prices in Mumbai (Rs./ tonne)**



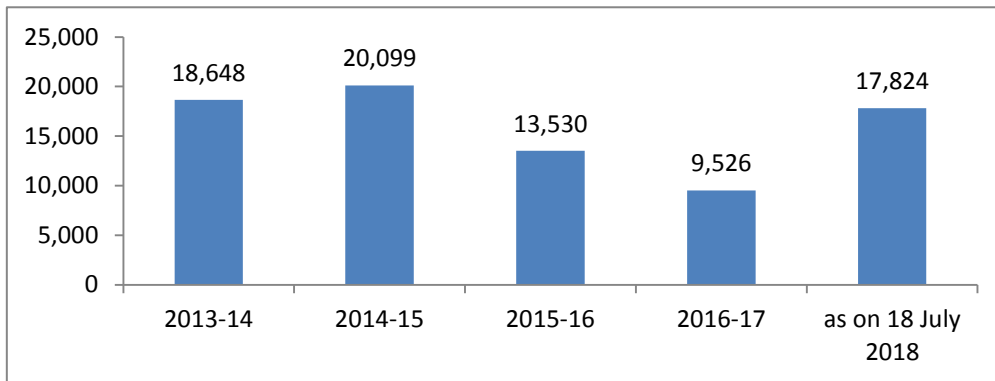
Source: CMIE

While the sugar prices fluctuate depending on the demand-supply situation in the country, the cane prices have seen an increase in most of the years. This, in turn, results in sugarcane arrears that are to be paid to the sugarcane farmers.

**Sugarcane arrears**

The sugarcane arrears increased in each of the years during 2013-15 when the sugar prices had declined on a y-o-y basis. This was coupled with a rise in sugarcane price. When the sugar prices were at low at Rs.26.1 per kg, sugarcane arrears touched a high of Rs.20,099 crore in 2014-15. In the next year, the arrears declined to Rs.13,530 crore backed by a rise in sugar prices to Rs.33.2 per kg during the year.

**Chart 4: All-India sugarcane price dues as on 31st March (Rs. in crores)**



Source: ISMA

As on 18 July 2018, the sugarcane arrears stood at Rs.17,824 crore. The arrears were at a high of Rs.23,232 crore as on 21 May 2018. The package of about Rs.7,000 crore announced by the government in June 2018 and fixing of minimum selling price of sugar at Rs.29 per kg are believed to have reduced the arrears.

**Financial performance of sugar companies**

The industry’s performance remained subdued in the financial year 2017-18 compared with the corresponding period a year ago due to the fall in sugar prices on account of supply glut situation in the country. During 2017-18 on a y-o-y basis,

the industry's sales fell by 5.4% and made losses amounting to 10.6% of the sales compared with profits made amounting to 5% of the sales in 2016-17. A mismatch in sugar and sugarcane prices is also believed to have impacted the industry's performance.

**Table 2: Sales growth rate and net profit margin**

	2013-14	2014-15	2015-16	2016-17	2017-18
Sales growth rate (y-o-y % change)	-6.7	-1.5	8.3	21.2	-5.4
Net profit margin (in %)	-4.1	-4.2	-1.2	5.0	-10.6

Source: Ace Equity

The financial performance is based on the performance of the 23 companies included in our sample.

### Cost of sugar production considering FRP

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 3 is prepared which provides an idea on sugar production cost.

**Table 3: Cost of sugar production considering FRP**

	(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)
2017-18	2,550	26,840	31,576.5	31.6
2018-19	2,750	27,500	32,352.9	32.4

The increase in FRP of sugarcane will increase the cost of production for manufacturing of sugar. The production cost is expected to increase by 2.5% on a y-o-y basis to Rs.32.4 per kg for the year 2018-19. On the other hand, the sugar prices are likely to remain subdued given the surplus situation and may hover around Rs.31 per kg considering that the minimum selling price for sugar will continue to be at Rs.29 per kg. Thus, the sugar prices are unlikely to cover the cost of sugar production.

### Concluding remarks

- While the government by increasing cane cost is considering providing returns of 77.4% over the cost of production to the farmers, this decision is unlikely to augur well for the sugar mills given the current sugar supply glut situation in India which is likely to keep the prices under pressure in the new sugar season 2018-19.
- With the increase in FRP, the cost of producing sugar is expected to increase by 2.5% on a y-o-y basis to Rs.32.4 per kg whereas the sugar prices are likely to hover around Rs.31 per kg. Thus, the sugar prices are unlikely to cover the

cost of sugar production. As a result, the sugar mills are expected to continue to face losses which may not result in sufficient reduction in cane arrears.

- Considering production of 35 million tonnes, the country will be left with surplus stock of 9.4 million tonnes from the season 2018-19. Moreover, India would have an opening stock of 11.1 million tonnes of sugar for the new season 2018-19. This will bring the additional stock to a total of 20.5 million tonnes of sugar at the end of September 2019 considering no exports are made during the year.

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