Fresh import duty on refined palm oil
the solution for survival of refiners

CARE Ratings
Professional Risk Opinion

Indian Edible oil industry:

India is one of the largest producers of oilseeds in the world with an area of 26.54 million hectares under cultivation producing 23-28 million tonnes of oil seeds every year depending on the monsoons. The per capita consumption, though grew by 8.1 per cent over the last five years up to FY12 is considerably low as compared to the global average. As consumption exceeds domestic production, India has to largely depend on imports for bridging the demand-supply gap.

The overall oilseed production (Kharif & Rabi) for the current year (2012-13) is estimated to be similar to that of the previous year (2011-12) at 256.16 lakh tonnes. Accordingly, the vegetable oil availability for the year 2012-13 (November-October) is pegged at 8.2 million tones as against the total demand of 18.3 million tonnes. The balance requirement of 10.1 million tonne will be met through imports, of which palm oil contributes about 75% of the total imports.

Palm oil, being the cheapest, constitutes the largest proportion (around 44%) of the oil consumed. Palm oil and soybean oil are among the most commonly consumed oils in India.

International Scenario:

Out of the global oilseed production of 469.4 million tonnes for 2012-13, the soya oil seed production was about 57.3%, followed by rapeseed, sunflower palm kernel & others.

In 2012-13, Palm Oil production increased by 6.5% to 54,322 million tonne primarily on account higher Indonesian production which rose by 8.7% y-o-y. Indonesia & Malaysia together contribute about 87.4% of global palm oil production. The increased production with stagnant demand led to sharp rise in inventory level (as a proportion of consumption), resulting in southward movement in prices. However, with only marginal increase in production of soybean oil in 2012-13 the closing stocks declined substantially.

Key concerns:

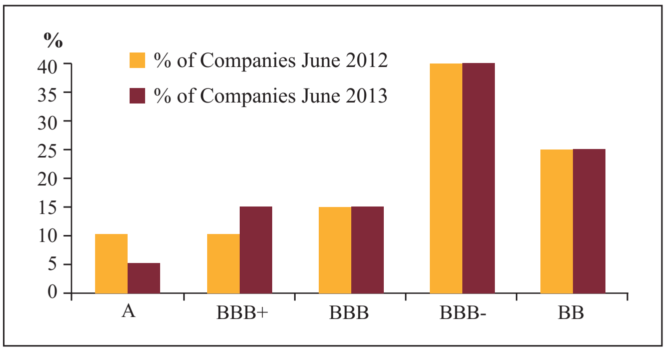
Surging Palm Oil Inventory: With expected strong production in Malaysia and Indonesia, surging palm oil inventory, the global prices are expected to remain soft. The global palm oil inventory as on April 30, 2013 stood high at 8 million tonnes.
Preference for Trading over Refining of palm oil: Domestic refiners are turning to packers as they are focusing more on low margin trading operations at the expense of refining operations due to the regulatory changes favouring direct import of refined oil over crude palm oil. Thus the same will have an impact on profitability margins of the companies, especially for the refiners.
Weakening of Rupee: As India imports about 60% of its domestic consumption of edible oil, free fall of Rupee against USD in recent times will make imports costlier by about 10%. Since the edible oil prices are already subdued and present palm oil prices are ruling at about 70% of the last year level, the ultimate impact on revision of final domestic price will be marginal.

Credit perspective

While assessing credit profiles, CARE assesses the industry scenario followed by assessment of management and business model. Besides, analysis is carried out to examine the impact of changes in duty structure, forex fluctuation, substitution effect and capex on the company's financials to ascertain the expected cash flow and the ability to meet the debt service obligation.

CARE has observed that the low profitability, forex fluctuation risk, frequent regulatory changes both in exporting and importing countries have limited the earning potential and cash flows of companies in the edible oil sector. As a result, the credit ratings of CARE rated edible oil companies are skewed towards 'BBB- (Triple B Minus)' category.

Rating dispersion of CARE rated edible oil companies as on June 30, 2013 reveals a fairly stable portfolio.



Outlook

With the persisting high inventory of palm oil, the global prices are expected to remain subdued at the current level with minor variation in the domestic prices due to fluctuation in exchange rate.

Though the integrated players are expected to be in a better position as compared to refiners, CARE believes that with the current duty structure the profitability margins and liquidity of the domestic edible oil companies in general, will continue to be under pressure. The situation may improve with the Government accepting industry demand of hiking import duty on refined palm oil to restrict cheaper imports and strengthen prices.

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