# Sugar Update: April 2020

## COVID – 19 likely to impact liquidity of sugar millers.

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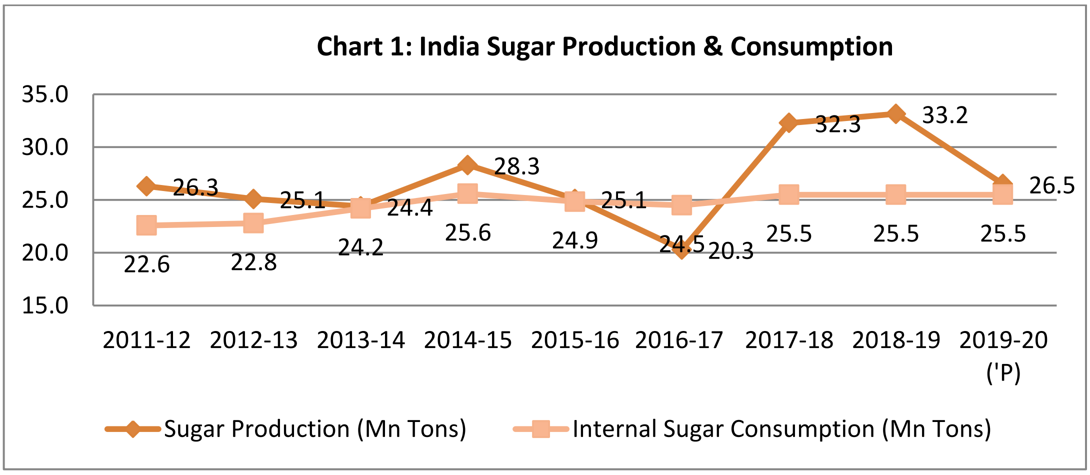
The ongoing pandemic is likely to put pressure on the sugar consumption patterns as there are curbs on social gatherings & outings, the industry is also facing reduced offtake from beverage & other FMCG companies amid the lockdown. This has even led to fall in domestic & international sugar prices recently. The export of sugar is also likely to get affected due to fall in international prices & also on account of supply chain disruptions at various ports. Though the Minimum selling price (MSP) for sugar & the moratorium allowed by RBI for the debt repayments is certainly giving cushion to the mill owners, however the increased stock at their ends and delay in receipt of power sales (for integrated sugar mills) from respective state discoms are likely to intensify their working capital requirements & will also result in mounting cane arrears which shall put pressure on their liquidity in the near term.

### Disruption in domestic demand supply scenario

According to ISMA's expectation sugar production in SS19-20 is expected to fall to 26.5 million tonnes (20% down as compared to production in SS18-19) due to lack of availability of water in Maharashtra and Karnataka. As against the expected production, in the first six months of SS which is Oct'19 - Mar'20, there is a de-growth in the production by almost 22% to 23.27 million tonnes (as against 29.68 million tonnes in the similar period of the last sugar season). The lower production is primarily due to lower contribution by Maharashtra owing to lower sugar output on account of damaged crops due to floods. After the breakup of COVID 19 most of the sugar mills still remained operational as sugar is considered as an essential commodity excepting few who have suspended operations. The crushing operations could however be affected in April till early May on account of labour shortages amid the COVID breakout and some other inputs like lime, sulphur, bags & other packing material which remain affected due to disruptions in transportation. Distillery units of certain sugar mills have started producing hand sanitizers as well. ISMA has assured production of Ethanol/ENA shall continue by the sugar millers for manufacturing of hand sanitizers.

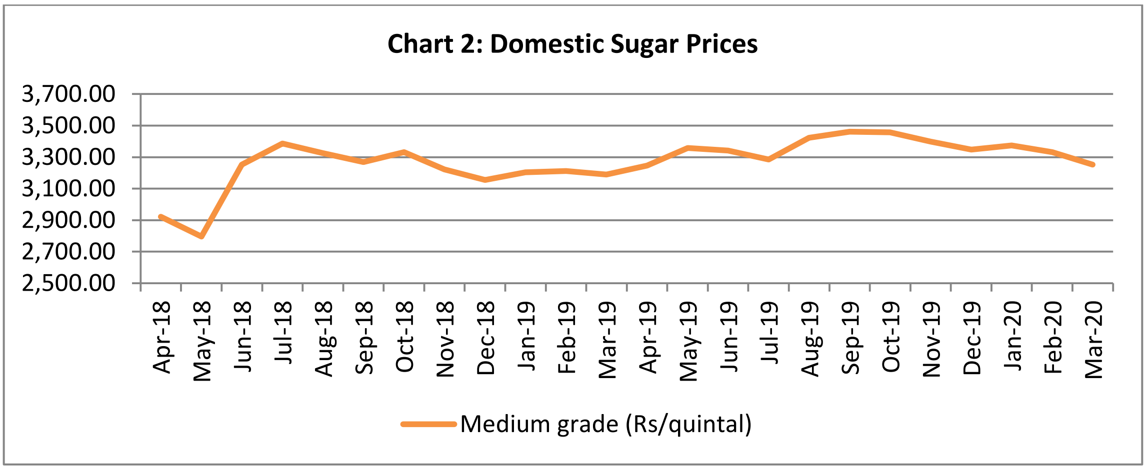
Further, due to COVID-19, there are concerns that the sugar industry might also experience a fall in sugar consumption. Temporary disruptions in the supply chain have been experienced by the millers in the past few weeks; and a drop in the consumption levels from the usual of ~26 million tonnes is expected as there are curbs on social gatherings, celebrations, weddings, etc. People are also avoiding cold drinks & ice-creams to avoid falling sick. The FMCG & beverage companies are either working on reduced capacities or have suspended operations. All this is likely to have an impact on the annual sugar consumption. In the current scenario, CARE Ratings expect domestic sugar consumption could fall to ~25 - 25.5 million tonnes (as against 26 million tonnes expected previously) with the possibility that the consumption could be further lower given the extension in the nationwide lockdown.




Source: ISMA, CARE

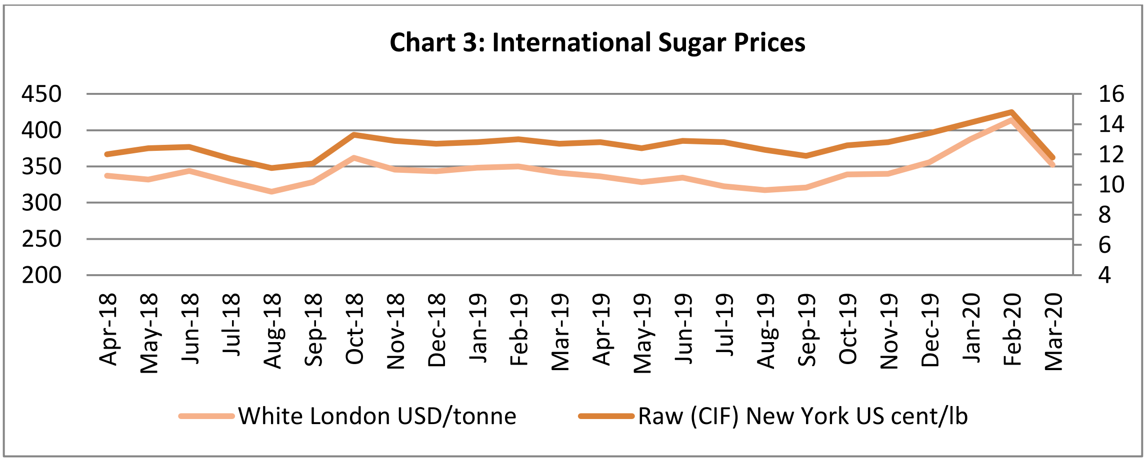
### Trend in sugar price movement

The excess supply of sugar in India restricted the growth in prices in the recent past. In a high supply & inventory scenario, sugar prices generally fall & even so below cost of production, resulting in losses to the sugar millers. What aided the sugar prices in SS19 to stay above cost of production was levy of minimum support prices by the government all throughout & further controlled supply by government. The prices so far from October 2019-February 2020 remained steady at average of Rs.34 per kg in the current season. The prime reasons that supported the stability in sugar prices so far were lower production in the on-going sugar season, government's MSP measures (slated to continue) and focus on higher export and diversion of sugarcane towards ethanol. The wholesale domestic prices however declined marginally in March 2020 to Rs 32.52 per kg after the COVID-19 breakout. The MSP by the government is however providing cushion to the domestic mill owners in the current environment.




Source: CMIE

The international sugar prices increased on a sequential basis in each of the months during October 2019 to February 2020. During February 2020, the average international prices were up by 17%-22% compared to the prices in October 2019. The white sugar prices in London and the raw (CIF) sugar prices in New York that had averaged at USD 339 per tonne and US cent 12.6 per lb, respectively, in October 2019 increased and averaged at USD 415 per tonne (white sugar price in London) and US cent 14.8 per lb (raw sugar price in New York) in February 2020. The global sugar prices were hovering around 14.5 cents per pound since mid-Jan 2020. However with the recent impact of fall in crude oil prices, expectation of Brazil to increase sugar production & due to COVID-19 pandemic there has been a decline in the global prices as well. Raw sugar prices in the international market were down by ~20% to 11.8 cent per pound in March 2020 from 14.8 cents per pound in Feb 2020. Owing to on-going pandemic & low crude price, CARE Ratings believe it is unlikely that the global sugar prices will bounce back to earlier levels of Jan or Feb 2020. This may put some pressure on the exports from India.




Source: CMIE

## Exports & Ethanol Offtake: Impacted after COVID-19

The government announced the Minimum indicative export quota (MIEQ) scheme to encourage export of sugar to reduce surplus in the country. Under MIEQ, the industry was allowed to export 6 million tonnes of duty-free sugar in SS19-20. Production and transportation subsidy for millers was declared by the Central government with the condition to export proportionate quantities of sugar for millers. Moreover, the government is supporting those sugar mills that have plans to export sugar above their original Maximum Admissible Export Quantity (MAEQ) by reallocating the quotas of those mills that have failed to export sugar under MAEQ.

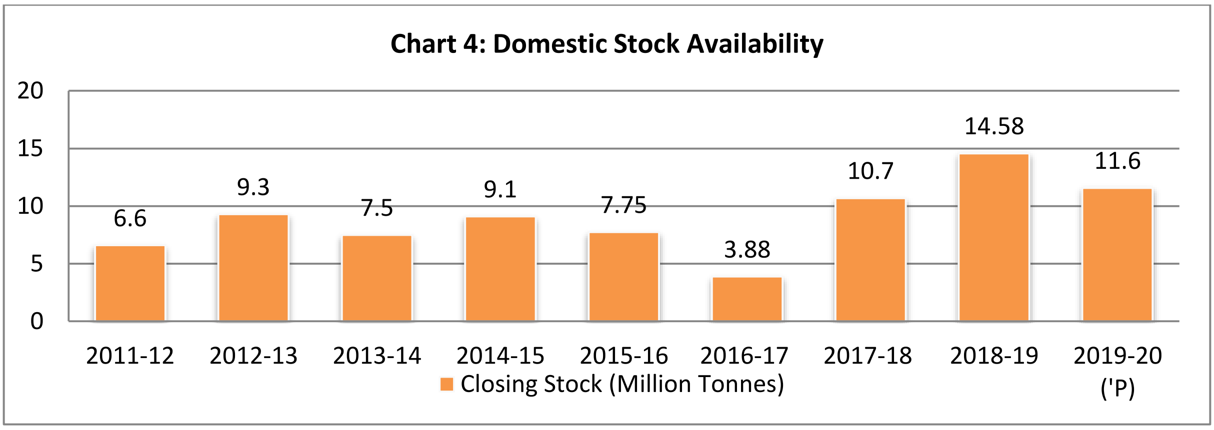
This subsidy was essentially introduced when the global prices were trading 20-30% below the cost of production for Indian millers & export seemed unviable without any support. In August 2019, the export subsidy of Rs.10.4 per kg to sugar mills for the sugar season 2019-20 was announced by the government. With the up-tick in global sugar prices and higher incentive by the government, sugar export looked promising for Indian sugar producers. The raw sugar prices in New York averaged at (Rs.21.3 per kg plus Rs.10.4 per kg) Rs.31.7 per kg in October 2019-February 2020 in rupee terms including the export incentive of Rs.10.4 per kg for sugar exports. During this period, the prices after considering export incentives averaged higher than the MSP of Rs.31. As per the industry data, of the allocated quota sugar mills had cumulatively contracted for around 3.5 million tonnes and transported around 2.8 million tonnes out of their factories for exports. Due to the lockdown, India's private ports have declared force majeure & government ports are also operating at lower capacities owing to shortages of labourers; all this has brought the current sugar exports to a standstill. Owing to COVID-19 lockdown, fall in crude price & expectation of Brazil increasing its sugar production in this season, global prices are likely to remain muted at the current levels & hence CARE Ratings expects the exports to remain at levels of ~4 million tonnes against the targeted 6 million tonnes.

### Ethanol Offtake

The outbreak of Covid & subsequent lockdown has reduced the demand for petrol & diesel drastically nationwide resulting in lower offtake from OMC's depot which in turn has resulted in reduced procurement by OMCs from sugar millers owing to problems of storages. Further slide in crude prices has also resulted in reduced off take of ethanol. The ethanol requisition was contracted for by the OMC targeting 10 per cent blending, the reduction in the demand for fuel has impacted the ethanol requirement as well. Now, the Indian Sugar Mills Association (ISMA) has asked the OMCs to reallocate ethanol to other depots, which have ready storage space and can take additional ethanol supplies beyond the contract.

## Sugar stock position

The season started with a balance of 14.58 million tonnes in October'19 and by clubbing the estimation of production which will be 26.5 million tonnes, the total availability of sugar is estimated to be around 40.58 million tonnes. Against the availability, the consumption is estimated to be around 25.5 million tonnes, after assuming 4 million tonnes of exports, India is likely to end with closing stock of ~11.58 million tonnes in Sep'20 (which is higher than the earlier estimate of ~10 million tonnes). This will be more than enough to meet the requirements of domestic consumption.




Source: ISMA, CARE

## Credit Perspective

CARE Ratings believes that the liquidity of the sugar companies could be impacted in the near term owing to disruptions in the dispatches on account of lockdown issues. Sugar companies have to resort to additional working capital borrowings in order to fund the high level of inventory which leads to increase in its working capital intensity which can be further accentuated by stretch in the receivables from the respective discoms for the power sale. Integrated sugar mills sell the surplus electricity generated (after their captive consumption) to the respective State discoms. Liquidity profile of the discoms is expected to be adversely impacted after the breakout of COVID-19 as the lockdown imposed by the government is impacting the demand for electricity which will have an impact on their revenue & cash accruals and may result in delay in payments by them. The moratorium extended by RBI amid the lockdown will bring in some relief for the sugar millers in the near term. However, the mills might be cash strapped owing to dip in the demand of sugar due to lockdown, fall in sugar prices and rising cane arrears. Large sugar companies who have sufficient liquidity cushion in the form of unused working capital lines, sufficient Cash or liquid investments or have a strong parent to meet both- their operational expenses and debt obligations will be in a favourable position. Liquidity pressures could mount on Companies which have high repayment obligations in the short to medium term & are holding excess inventory. Cane arrears are also likely to get accumulated in the current scenario & any further extension in lockdown may put more pressure on the liquidity of the millers.

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