State subsidies to support sugar mills' liquidity, help clear cane dues

October 2018

- In the light of the high cane dues of close to Rs. 10,000-crore as on mid-September 2018, the state governments in the SAP-following states, including Uttar Pradesh (UP) and Haryana, announced a cash subsidy.

- The Uttar Pradesh (UP) state government has approved a cash subsidy of Rs. 4.50/quintal and soft loans to the tune of Rs. 4000 crore under the Scheme for Extending Financial Assistance to Sugar Undertakings-2018 (SEFASU-2018). The sugar mills availing the facility of loan under the SEFASU-2018 scheme will have to ensure 100% payment of outstanding cane price of the crushing season SY2017 and SY2018, including utilisation of this sanctioned loan, by November 30, 2018. The loan tenure is for five years and the repayment is to be done in monthly instalments, starting from July, 2019.

  The cash subsidy of Rs. 4.50/quintal by the UP Government is likely to improve the contribution margin from sugar by Rs. 400 – 450/MT, translating to about higher PBT margins by around 100 bps. Further, the soft loans of Rs. 4000-crore are at low interest rates of 5%, which would enable the mills to save the interest costs as against the working capital limits.

  The Government of Haryana has approved a subsidy/loan for the crushing season SY2018 only for those mills who repaid the outstanding amount against loans taken in SY2015 and SY2016. The amount of the loan and subsidy to be given is based on the formula of SAP – FRP (at an average recovery of 11.03%). The financial assistance (subsidy and soft loans) is to the tune of Rs. 16/quintal.

  These measures are likely to result in some improvement in the mills' liquidity and aid them in making cane payments to farmers.

- To improve the liquidity of the sugar mills and their ability to pay sugarcane farmers, the GoI has taken a number of measures over the last few months. Earlier, in September 2018, the Government of India (GoI) notified a cane production subsidy of Rs. 138.8/MT (as against Rs. 55/MT last year), which would be paid directly to farmers as part of the cane costs during SY2019. The total subsidy amount is expected to be around Rs. 4500 crore. The Government had also approved the export of 5 million MT sugar under the Minimum Indicative Export Quota (MIEQ) for SY2018, towards which the transport subsidy is provided. Sugar mills meeting 100% of the target notified under the Minimum Indicative Export Quota (MIEQ) are eligible for this subsidy.

  Given the prevailing international prices, the companies are likely to make losses on sugar exports. However, these losses are likely to be partly offset by the production subsidy of Rs. 138.8/MT of cane crushed, which translates to Rs. 8.5-9/kg of sugar exported. This apart, the transport subsidy (for the mills not located in coastal states) of Rs. 3/kg is also provided on sugar exported.

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- In September 2018, the CCEA increased the basic price of ethanol produced from B-grade molasses to Rs. 52.43/litre (by ~Rs. 5.0/ litre or 11%) for the procurement season 2018-19 (starting December 2018), while the procurement price of ethanol produced from C-grade molasses was Rs. 43.70/litre (increased from Rs. 40.85/litre in June 2018). Further, the Cabinet has also notified the price for ethanol produced directly from sugarcane juice at Rs. 59.10/litre, around 25% higher than the previous procurement price of ethanol from B-grade heavy molasses. In case of a sugar surplus scenario, the production of ethanol through B-grade molasses and sugarcane juice would support the sugar mills in producing ethanol from relatively higher sucrose content materials. This measure is likely to help reduce sugar surpluses in the overproduction scenarios, thus indirectly supporting sugar prices to an extent. According to ICRA estimates, while the increase in ethanol price from B-grade molasses will slightly improve the margins of integrated sugar mills, the higher price for ethanol directly from sugarcane juice will take time to yield results on the ground as at present no mills are completely diverting sugarcane for ethanol production. This apart, distillery capacities available with sugar mills are also a constraint to some extent.

- In June 2018, the Cabinet Committee on Economic Affairs (CCEA) approved the creation of 3 million MT of buffer stock to soak the excess supply from the market. This is likely to cost around Rs. 1200 crore and the move should improve the demand-supply situation in the domestic market and support the sugar prices in the near term. Further, the impact of the carrying cost alone would amount to a benefit of around Rs. 400-450/MT of sugar, translating into a higher PBT margin by 1%-1.5%. The Cabinet has also approved a minimum selling price of Rs. 29/kg, which is a positive for the mills in the western and southern regions as the prices here were around Rs. 26 – 27/kg. The Government has also approved soft loans to the tune of Rs. 4,500-crore for creating ethanol capacity. In addition to these, a Rs. 1,300-crore interest subvention would be provided on the loans for creating new ethanol capacity or expanding an existing one.

- *On sugar prices* - Supply pressures resulted in a decline in the sugar realisations from November 2017 onwards. An upward revision in the sugar production estimate along with most mills liquidating the sugar produce to repay cane payments, resulted in a further correction in sugar prices to Rs. 32,500-33,000/MT in January 2018 and to around Rs. 30,000/MT in March 2018 from Rs. 33,500 – 34,000/MT in December 2017. Despite the Government announcing an MIEQ of 2 million MT sugar exports, another upward revision in production estimates continued to exert pressure on sugar prices to Rs. 28,000 – 28,500/MT in April 2018. With exports yet to start in full swing, along with the prevailing surplus scenario, sugar prices declined to a low of Rs. 26,500/MT in mid-May 2018. In September 2018, prices declined to around Rs. 31,000/MT, after increasing to Rs. 33,500/MT in June 2018 following the Government support measures.

EXHIBIT 2: Monthly trends in domestic wholesale sugar prices (UP ex-mill)

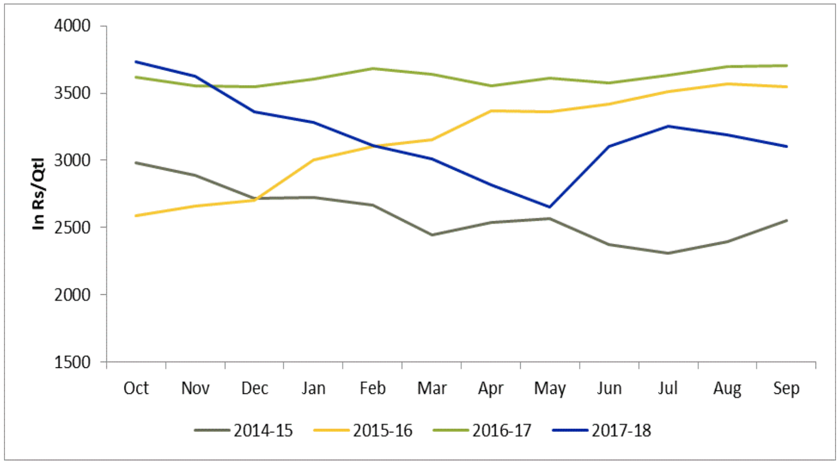
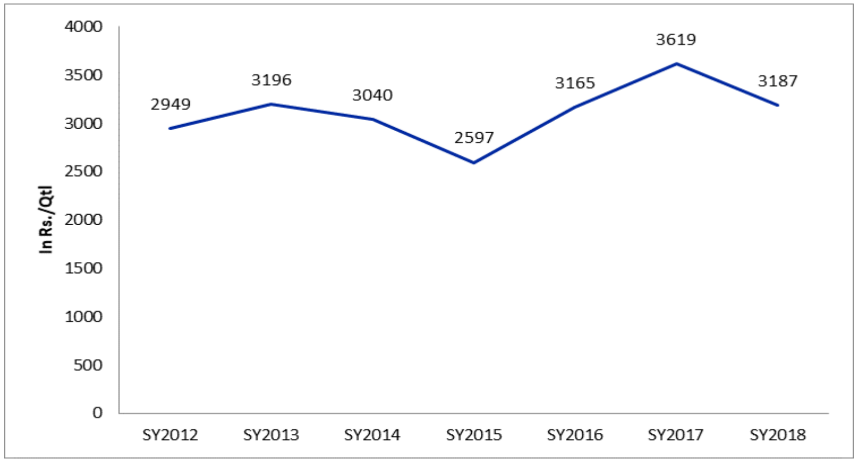


EXHIBIT 3: Yearly trends in domestic wholesale sugar prices (UP ex-mill)



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