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The sugar situation could turn explosive

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The 2016-17 peak crushing season for sugar is coming to an end. Most mills in southern parts of the country have stopped crushing as cane availability has dwindled considerably. The situation is not markedly different in the western region of the country, especially Maharashtra, traditionally the country's largest producer.

A look at the sugar balance sheet for 2016-17 is scary and should shake up policymakers and consumers alike. Production is estimated at 200 lakh tonnes, a clear 50-lakh-tonne decline from the previous year.

Private estimates peg sugar production even lower at 195 lakh tonnes. So, there is an indisputable fall in production to the extent of 20 per cent.

On the demand side, the situation is near normal. This year's consumption is set to expand driven by rising rural incomes following improved farm output. For the year, consumption is estimated anywhere between 245 lakh and 250 lakh tonnes. This leaves a clear mismatch as production trails demand by a massive 50 lakh tonnes.

Prices up

The price implication of this mismatch is unmistakable. The market has already taken cognisance of the emerging shortage, and as a result, open market prices have moved up, notwithstanding the fact that the peak crushing season is just about coming to an end and stocks logically should be at the year's highest level.

Some industry representatives point to opening stock of 77 lakh tonnes and suggest that there is sufficient stock of the sweetener to meet demand until the next season. They could be either mistaken or misguiding.

Anecdotal evidence suggests that the specified quantum of opening stock is probably overstated to the extent of 20 to 30 per cent. In the event, the supply situation is even more precarious.

In commodity markets worldwide, it is axiomatic that prices move not on the basis of current demand-supply fundamentals, but on anticipated changes in the future. It is important to recognise this basic feature of the market.

Going forward, sugar availability is going to be tighter. The situation is potentially explosive when one considers that soon after summer demand for sugar (soft drinks, juices and so on) festival demand will kick in four to five months from now. Sugar consumption expands manifold from August to October .

Supply imperative

Prices will get completely out of hand if availability is not augmented in time.

For the policymakers there seems to be no alternative but to ensure that adequate supplies are organised in time as otherwise the country risks facing a "sugar shock" on the lines of dal shock of 2015-16 that consumers have still not forgoten.

The government can ill-afford a bull run in sugar prices and ignore early warnings.

While there is reason to believe the government is seized of the precarious demand-supply situation, it is likely that a decision to augment sugar supplies through imports is being delayed pending the result of elections in a few states.

That, of course, makes sense. It would be better take a call on imports soon instead of waiting for the market situation to deteriorate further, forcing a decision.

A genuinely worrisome feature is the market concentration. An analysis of region-wise sugar stocks clearly reveals that a dominant portion of the stocks is in northern India, while in the rest of the country stocks are rather tight. This is a case of 'market concentration', where a group of producers in a region will find themselves eminently placed to squeeze the national market. This is best avoided.

The writer is global agribusiness and commodities market specialist. Views are personal