Sugar may remain sour for long

MARKET MIND

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The Prime Minister's ambition of doubling farmer incomes was strengthened when the Uttar Pradesh (UP) government announced a ₹10 per quintal increase in the 2017-18 cane price that sugar manufacturers were required to pay farmers. What the country had not reckoned was the extent of increased production: against an initial sugar production estimate of 25 million quintals in 2017-18 (October to September), India is estimated to have produced over 32 million quintals—a complete failure of intelligence gathering sources.

The country produced 60 per cent more than in the previous sugar season; sugar consumption increased from 25 million quintals in 2016-17 to 25.1 million quintals in 2017-18 and the vast surplus (estimated at five months of annual consumption) affected realisations — from ₹36 per kg ex-factory at one point to ₹26 per kg. Most sugar companies reported sizable losses in the last quarter of 2017-18, reversing the momentum of the earlier years. The pronunciation of 'stable medium-term outlook' put out by analysts now needed to be pencilled out.

The UP government's enthusiasm to 'reward' cane growers and win opinions (before the 2019 votes) proved lose-lose for stakeholders. The Bharatiya Janata Party-led UP government lost a recent assembly seat ostensibly due to the vast farmer discontent (not being paid by millers). The fact that millers are losing money is likely to create the next mini-loan repayment crisis. Shareholders have seen their portfolio value erode. The possibilities of sugar companies mobilising net worth to invest in downstream non-sugar businesses are minimal. In this sector, the 'make in India' promise is at a standstill.

There are bigger questions for the central government.

Why does a pro-market government continue to tell sugar manufacturers what price they must pay vendors and not leave it to market dynamics?

What is the logic of raising cane prices following a 40 per cent cane yield increase in the last few years, creating a case for prices to be reduced?

What is the logic of getting mills to pay farmers a higher cane price and spending the following year frantically undoing the damage (buffer stock and export loss subsidy)?

What is the logic of a policy that makes a miller pay a higher price (which is anyway not completely paid) and suffering NPAs of PSU bank balance sheets?

Why not link cane prices with sugar prices (recommended by virtually instituted committee)?

Most sugar stocks have more than halved. The ones (Balrampur, Dhampur, Dalmia and Dwarikesh) that restructured their balance sheets in the last sectoral rebound could be the first off the blocks in the next revival.

So, when is the next rally expected? The UP government's cane price recommendation for 2018-19 holds clues. The mind says it will raise prices again to influence the 2019 elections; the heart says that after the 2017 debacle it may maintain status quo.

However, an even bigger question is whether, even after a sectoral rebound, investors and lenders will trust the sector again.

This trust deficit (which has less to do with the sector than the government) could, in turn, affect fund mobilisation, investments, growth and servicing national needs.

One bureaucrat's blunder may have put the sector back by years.

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