

Ugar Sugar Works

STOCK INFO. **BLOOMBERG**
BSE SENSEX: 9,311 UGSW IN
REUTERS CODE
S&P CNX: 2,833 UGSW.BO

16 January 2006

Not Rated

Rs45

Equity Shares (m)	90.1
52-Week H/L (Rs)	45/10
1,6,12 Rel. Perf. (%)	109/88/295
M.Cap. (Rs b)	4.1
Avg. Daily Vol. ('000)	127.1

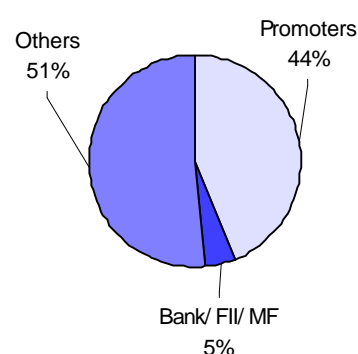
YEAR END	NET SALES (Rs M)	PAT (Rs M)	EPS (RS)	EPS GROWTH (%)	P/E (X)	P/BV (X)	ROE (%)	ROCE (%)	EV/ SALES (X)	EV/ EBITDA (X)
09/04A	2,305	90	1.6	-	28.2	5.3	19.0	13.0	1.6	8.9
09/05E	3,330	120	1.3	-17.1	34.0	7.2	21.0	9.8	1.5	15.5
09/06E	4,730	438	4.9	265.2	9.3	4.2	45.2	23.5	1.0	6.8
09/07E	5,420	630	7.0	44.0	6.5	2.6	40.7	26.2	0.9	5.2



We met the management of Ugar Sugar Works. Key takeaways of the meet are:

- Ugar is likely to record a 53% increase in sugar production at its 10,000 tcd plant at Ugarkhand, aided by increased cane availability and higher recovery.
- It has taken two plants on lease. This will help it to augment capacity without incurring any major capex and saving on the gestation period required for setting up a plant.
- It is also undertaking a greenfield capacity expansion of 2,500 tcd at Jewergee (Karnataka). The plant would also have cogeneration facilities.
- Another greenfield expansion of 2,500 tcd in joint venture with Sadashiv Sugars (Patil family) is also being contemplated at an investment of Rs100m in the equity of the joint venture company by Ugar.
- Ugar is also setting up a sugar fragies (sugar ship) project, which entails making sugar cubes in the shape of ships. It has entered into a contract with Fragies Verwaltung GMBH, Germany, for sale of products for a period of five years.
- The company is likely to report net sales of Rs4.73b and Rs5.42b in FY06 and FY07, respectively. Net profit is estimated at Rs438m and Rs630m. The stock currently trades at 9.3x FY06E EPS of Rs4.9 and 6.5x FY07E EPS of Rs7. We do not have a rating on the stock.

SHAREHOLDING PATTERN



With the global sugar cycle turning up, sugar companies are expected to perform well going forward. Ugar, which had been suffering in the past due to low sugar prices and inadequate availability of cane, is well poised to reap the benefit of the excellent cane crop in the current season.

Sugar production up 53%, due to good crop

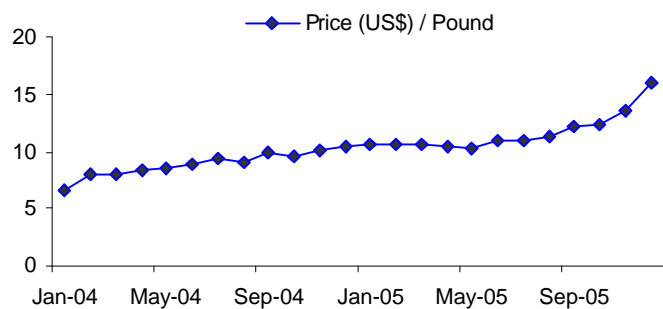
The company is situated on the Maharashtra-Karnataka border, where the crop was not good last year, which led to a short crushing season in sugar year (SY)2004-05. An excellent crop in the current year has helped Ugar crush 1m ton of cane so far, as against 1.05m ton of cane in SY2004-05. We believe the company should end the current crushing season (SY2005-06) with over 1.5m ton of cane.

Average recovery from cane is also higher this year and is expected to be ~11.25% this year compared to 10.85% in FY05 and 10.15% in FY04. This will lead to sugar production of ~178,500 ton (116,000 ton in FY05).

International sugar prices on an upswing

International sugar prices have risen sharply over the last few weeks and are expected to remain strong going forward. This is mainly due to the diversion of more cane for ethanol production by Brazil and expected lowering of the EU price of sugar by 36% over four years as per WTO regulations.

INTERNATIONAL SUGAR PRICES

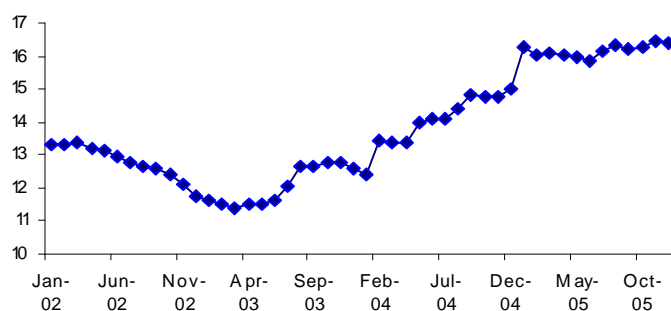


Source: Motilal Oswal Securities

Low inventory to result in higher domestic prices

Sugar output plummeted from over 20m ton to 14m ton in 2003-04 and to 12.5m ton in 2004-05. This led to a decline in sugar inventory from 11.6m ton at the end of SY2002-03 to 8.5m ton at the end of SY2003-04. It is estimated to be 4.5m ton at the end of SY2004-05. The significant drop in inventory has resulted in a critical balance between sugar production and consumption. Also, the tight inventory position, along with global hardening of sugar prices, led to an uptrend in domestic sugar prices.

DOMESTIC SUGAR PRICES (RS/KG)



Source: Motilal Oswal Securities

Indian sugar inventory (Million tones)	SY 2003-04	SY 2004-05E	SY 2005-06E
Opening inventory	11.6	8.5	4.5
Production	14	12.5	17.5
Imports	0.55	2	1.5
Usage	17.65	18.5	19
Closing Inventory	8.5	4.5	4.5

Source: Motilal Oswal Securities / ISMA

The Ugar Sugar Works

Ugar Sugar was incorporated in 1939 with 500 ton crushed/day (tcd) capacity. Currently, it has a 10,000 tcd sugar mill at Ugarkhurd, Belgaum, Karnataka. It has also set up a 45 MW co-generation unit (bagasse-based) and 45 kilo litre/day distillery along with sugar mill. The company is managed by Shirgaonkars since 1940.

Capacity expansion via leased plants

Co-operative sugar mills in Maharashtra have been facing innumerable problems and have been unable to make profits. Around 72 sugar mills have been declared sick despite repeated efforts by the government to bail them out. Hence, the alternative of leasing the mills was considered by the government of Maharashtra. Ugar has taken two such plants on lease, details of which are as follows:

Tasgaon plant

This plant is located at Tazgaon in Maharashtra and has a capacity of 2,000 tcd. The plant is taken on lease in the current year and hence crushing could be started only in the last week of November, thereby losing ~45 days of the current crushing season. Average recovery till date is about 10.8%, but is expected to stabilize at 11% in SY2005-06 and 11.25% in SY2006-07. We expect it to crush ~300,000 ton of cane in the current season and ~400,000 ton of cane next year. The plant is expected to break even in the current year. However, the lease agreement provides for retaining all the existing 850 workers, which may lead to high fixed costs.

Falton plant

This plant is located in Pune district and has a capacity of 1,250 tcd. The plant started crushing in mid-November and has crushed over 60,000 ton of cane to date. We expect it to crush ~175,000 ton of cane in the current season and ~250,000 ton of cane next year. The plant is expected to break even in the current year.

Greenfield expansions

Sugar Plant at Jewergee (Karnataka)

Ugar is setting up a sugar plant at Jewergee (Karnataka) with an average capacity of 2,500 tcd with an attached 15 MW co-generation plant. At present, there is no sugar factory in the vicinity of the proposed site. There is great potential of growing cane due to irrigation facilities of distributaries from Narayanpur Dam. The cogeneration project will facilitate availing of carbon credit on account of lowering carbon dioxide emission. The co-generation plant will attract tax benefits such as 100% depreciation, income tax holiday, sales tax exemption and excise duty exemption. The total cost of the project is estimated at ~Rs700m with the project expected to be commissioned in February 2007, thereby losing SY2006-07.

Sugar plant at Bagalkot

The company is also setting up another sugar plant at Bagalkot (Karnataka), in joint venture with Sadashiva Sugars. The plant has an average capacity of 2,500 tcd and a 15 MW co-generation unit. The company has joined hands with Patil family (Sadashiv Sugars) from Bagalkot who control a large tract of land in the catchment area of Almatti dam. This will ensure risk distribution, management sharing and location advantages. Investment by Ugar for a 50% stake in the company is estimated at ~Rs100m. The plant is likely to be commissioned in February 2007, thereby losing SY 2006-07.

Location	Capacity (tcd)	Ownership	Status
UgarKhand	10,000	Own	Operational
Tasgaon	2,000	Lease	Operational since end November 05
Falton	1,250	Lease	Operational since mid November 05
Jewergee	2,500	Own	Expected to be commissioned in February 07
Bagalkoat	2,500	Jt. venture	Expected to be commissioned in February 07
Fragies project	1.125m kg p.a.	Own	Expected to commissioned in June 06

Source: Motilal Oswal Securities

EOU plant for sugar fragies (sugar ship project)

Ugar is setting up a 100% EOU for manufacture of sugar fragies adjacent to its 10,000 tcd plant at Ugarkhand. (Fragies are a floating and exciting alternative to the rather dull sugar cube and have the shape of a boat. "Fragies" make the ideal media for any catering customer client, the showbiz or the convenience sector. It consists of approximately 75 flow-packed "Fragies". The installed capacity is 3,750 kg of sugar fragies per day (i.e. approximately 1.13m kg a year). The company has entered into a buy-back agreement with the Fragies Verwaltung GMBH, Germany. The German company has agreed to buy 22.5m boxes (i.e. approximately 56.25m kg) within a period of five years or up to achievement of net profit of 3.5m Euros (Rs189m) by the manufacturer (Ugar),

whichever is earlier. The project is expected to be commissioned in June 2006 and entails an investment of Rs200m.

Concerns

Sugar being an agro commodity is subject to the vagaries of nature. Production of sugar depends on cane production. Reduction in cane production can severely impact sugar production and industry profitability.

Sugar is a politically sensitive commodity and prices are regulated to a certain extent by the government.

The government fixes the minimum support price for sugarcane to be paid by the sugar mills to the farmers. But the actual payments made by Ugar to farmers are still higher, to ensure cane availability.



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Disclosure of Interest Statement	Ugar Sugar Works
1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	Yes
3. Broking relationship with company covered	No
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