

# India Sugar

## Not so sweet

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*(Prices as on February 16, 2010)*

# Summary

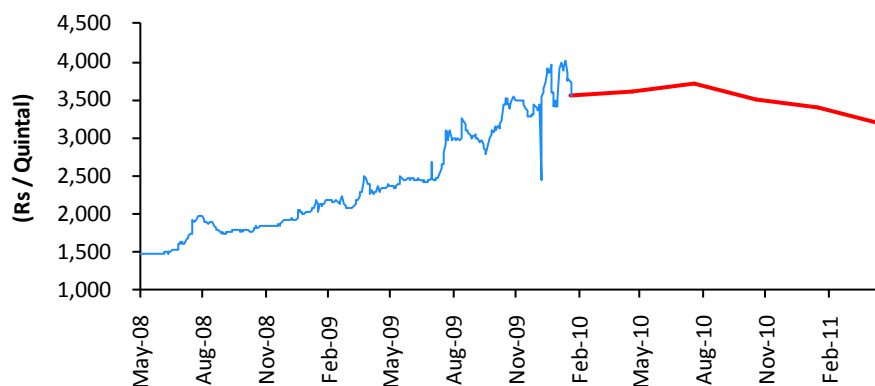
- **Domestic Sugar cycle to peak off in SS2010:** There has been lower sugar production in SS2009 and SS2010. The shortage in domestic sugar supply was compensated to some extent by healthy reserves in SS2009. However, the current year started with low opening inventory. Also, the production is expected to be at similar levels as that of SS2009. This has resulted in steep increase in sugar prices from Rs23.5/kg in SS2009 to the current level of Rs39/kg. However, with expectation of healthy increase in supply next year, we expect sugar prices to tide down from the current level of Rs39/kg to Rs33/kg.
- **Increased sugar supply in SS2011 due to higher cane availability:** We expect cultivation area for sugarcane to increase by 23% in SS2011. This would result in incremental supply by 3.5mT, where incremental demand is expected to rise by 1mT next year.
- **Sugar supply to increase due to higher cane price:** Cane cost rose only by 13.6% YoY in 2008-09 but by 77% YoY in 2009-10. This has given a good incentive to farmers to cultivate more cane.
- **Also, Cane more profitable than alternate crops:** With 77% increase in cane price YoY, cane has become more profitable than alternate crops.
- **Supply in international market to increase materially:** Sugar supply in international market is likely to increase due to increase in production in India, Brazil, Thailand as well as Australia.
- **Increased sugar supply to impact operating profit from sugar:** Operating profit/kg is expected to reduce next year due to increased sugar supply. Even with increase in volume of sugar sale by mill owners, we expect operating profit of sugar to remain firm or marginally decline next year.
- **Shree Renuka Sugars (SHRS)** was the biggest beneficiary of this cycle due to its ability to process sugar from cane as well as imported raw sugar. However, going ahead, we expect negativity of the cycle to impact the company too.
- **Bajaj Hindusthan (BJH)** was able to improve its financial position during the upcycle. However, as the cycle turns downwards, we expect profit of BJH to reduce significantly.
- **Balrampur Chini (BRCM)** is also expected to get affected due to reduction in sugar prices.
- On the basis of the above, we are **'Negative'** on the sugar sector. Hence, we change the rating of SHRS and BRCM from **'BUY'** to **'Reduce on Strength'** and BJH from **'Accumulate'** to **'Reduce on Strength'**.

## Key risk to our assumptions

- Delay in non-normal monsoon for 2010 in India and/or Brazil could impact the recovery of sugar from cane.
- Lower-than-expected amount of sugar production during SS2011 may increase sugar prices and improve profitability of mill owners.
- Lower-than-expected amount of sugar production in Brazil can increase international sugar prices.

# Operating profit/kg of sugar to peak in SS2010

## Domestic sugar prices to fall with increase in supply in SS2011



Source: Bloomberg, PL Research

## Total operating profit to remain same or marginally decline in SS2011

Particulars	2007-08	2008-09	2009-10	2010-11	
				Likely scenario in FY11	
Total production (m tonnes)	26	14.6	16	20	24
Average Recovery	9.5	9.5	9.5	9.5	9.5
Sugar price (Rs/ kg)	15.3	23.5	39	33	31
Cane Cost (Rs/ Quintal)	110	125	230	200	190
Raw Material Cost (Rs/kg)	11.6	13.2	24.2	21.1	20.0
Conversion Cost (Rs/kg)	3.5	3.5	3.5	3.5	3.5
Operating Profit/kg	0.2	6.8	11.3	8.4	7.5
Sugar production (m tonne)	1	1	1	1.3	1.5
Total Operating Profit (m Rs)	0.22	6.84	11.29	10.98	11.25

Source: Bloomberg, PL Research

- Due to drastic reduction in supply over the last couple of years, sugar prices rose significantly by 53.5% - from Rs15.3/kg to Rs23.5/kg YoY and 155.2% to the current price of Rs39/kg. However, with expectation of healthy increase in supply next year, we expect sugar prices to tide down from the current level of Rs39/kg to Rs33/kg.
- Cane cost rose only by 13.6% YoY in 2008-09 and 109.9% in 2009-10. As a result, operating profit/kg increased from 0.2 to 6.8 in 2008-09 and we expect the same to further rise to Rs11.3/kg in SS2010. However, going ahead in SS2011, we believe that operating profit/kg is likely to decrease. This is on account of higher decrease in sugar prices as compared to decrease in the cane cost.
- Even with an increase in volume, operating profit from sugar segment is expected to remain same or marginally decline.

### Key Assumptions:

- Increase in domestic sugar production by at least 25% - from 16mT to 20mT YoY. Material increase in supply of sugar in international market.
- Sugar price to reduce from the current price of Rs39/kg to Rs33/kg in SS2011. Accordingly, cane price is likely to reduce to Rs200/quintal from Rs230/quintal YoY.

# Increased domestic cane availability to increase sugar supply in SS2011

## Increase in production of sugarcane may result in lower import and comfortable closing stock in SS2011

Particulars	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10P	2010-11P
Area under acreage (m Hectares)	4.3	4.4	4.5	3.9	3.7	4.2	4.9	5.2	4.3	4.2	5.2
Yield per hectare (Tonnes per Hectare)	68.6	67.4	64.6	59.4	64.8	66.9	71.1	65.0	65.0	62.0	62.0
Total sugarcane production (m tonnes)	295.7	297.2	292.0	233.4	237.2	281.0	344.8	338.0	280.5	262.2	322.4
Conversion factor for sugarcane to sugar	6.3	6.2	6.9	5.8	5.4	6.9	8.2	7.7	5.2	7.5	6.2
<b>Production</b>	<b>18.5</b>	<b>18.5</b>	<b>20.1</b>	<b>13.5</b>	<b>12.7</b>	<b>19.3</b>	<b>28.3</b>	<b>26.0</b>	<b>14.6</b>	<b>16.0</b>	<b>20.0</b>
Opening Stock	9.3	10.6	11.2	12.3	8.1	4.4	3.6	9.2	8.4	2.5	4.0
<b>(A) Total available for sale</b>	<b>27.8</b>	<b>29.1</b>	<b>31.3</b>	<b>26.2</b>	<b>22.9</b>	<b>23.7</b>	<b>31.9</b>	<b>35.2</b>	<b>25.0</b>	<b>27.5</b>	<b>28.0</b>
<b>(B) Domestic Consumption</b>	<b>16.2</b>	<b>16.8</b>	<b>17.5</b>	<b>17.9</b>	<b>18.5</b>	<b>19.0</b>	<b>21.0</b>	<b>22.0</b>	<b>22.5</b>	<b>23.5</b>	<b>24.5</b>
A-B	11.6	12.3	13.8	8.3	4.4	4.7	10.9	13.2	2.5	4.0	3.5
Exports	1.0	1.1	1.5	0.2	-	1.1	1.7	4.8	-	-	-
Import	-	-	-	0.4	2.1	-	-	-	2.0	9.0	4.0
Closing Stock	10.6	11.2	12.3	8.1	4.4	3.6	9.2	8.4	2.5	4.0	3.5

Source: Crisil, PL Research, Year ending - September

- We expect cultivation area for sugarcane to increase by 23% in SS2011.
  - This would result in incremental supply by 3.5mT, where incremental demand is expected to rise by 1mT next year.
- Cane production in Maharashtra is expected to increase by 20% to 60mT, while in UP, it is expected to increase by 33% to 6.2mT (Maharashtra contributes 32% and UP contributes 30% of the total domestic cane production).
- Currently, total import contracted is about 6mT. Total amount actually arrived in the country is about 3.5-4mT. There is a requirement of another 3mT to be contracted for import to maintain the closing stock at the comfort level of 4mT. This could result in increase in sugar prices over the medium term. However, total import is expected to reduce due to increase in domestic production by about 4mT next year.
- Natural factors like delay in monsoon and/or non-normal monsoon would impact yield of sugar from sugarcane.

# Sugarcane more profitable to alternate crops

In Maharashtra, sugarcane to be more profitable in absolute terms even though the margins could be below third option

Crop	1 Jowar+1 Wheat	1 Jowar+1 Sweetcorn	1 Moong+1 Sweetcorn+1 Bajra	Sugarcane						
				2008-09	2009-10	2010-11E	2011-12E	2012-13E	2013-14E	
Yield (Qtl /Acre)	28	30	32	425	425	425	425	425	425	425
SP (Rs/Qtl)	1,061	900	1,160	140	190	200	210	215	230	250
Total Earnings / Annum	29,700	27,000	36,550	29,750	40,375	42,500	44,625	45,688	48,875	53,125
Cultivation Cost (Rs / Acre)/ Annum	12,029	10,000	11,000	16,800	16,800	16,800	16,800	16,800	16,800	16,800
Net Earnings/ Annum	17,671	17,000	25,550	12,950	23,575	25,700	27,825	28,888	32,075	36,325
Earnings (As % of Cost)	146.9	170.0	232.3	77.1	140.3	153.0	165.6	171.9	190.9	216.2

Source: PL Research

Jowar: Jun-Jul, Wheat: Nov-Apr, Sweetcorn: Nov-Jan, Bajra: Apr-May, Sugarcane: Oct-Jan (Next year)

In UP, sugarcane to be more profitable in absolute terms as well as on margin basis

Crop	Wheat	Paddy	1 Wheat + 1 Paddy	Sugarcane
Yield (Qtl / Acre)	15	20	35	425
SP (Rs/ Qtl)	1,200	800	2,000	210
Total Earnings	18,000	16,000	34,000	44,625
Cultivation Cost (Rs / Acre)	7,029	8,500	15,529	16,800
Net Earnings	10,971	7,500	18,471	27,825
Earnings (As % of Cost)	156.1	88.2	118.9	165.6

Source: PL Research

Wheat : Nov - Apr, Paddy: July - Sep

- In the previous year, earnings (as % of cost) was higher for alternate crops due to lower cane price and favourable price for Jowar, Wheat, Moong and Paddy. However, with 77% increase in cane price YoY, cane has become more profitable than alternate crops. We expect this condition to increase sugar supply next year.

# Supply in international market to increase materially

- Supply in 2009 dropped due to variety of reasons:** Total supply in international market reduced in 2009-10 mainly due to reduced production in India and Brazil. In India, it reduced due to lower cane prices, delay in payment to farmers as well as more profitable alternate crops, while in Brazil, it reduced due to unseasonal rains that brought negative effects through most of 2009.
- Production in India and Brazil to increase:** With the change in situation in both India as well as Brazil, we expect increased sugar production in both countries. Brazil has most of the facility to convert cane to ethanol. However, it intends to start crushing 15 days in advance (on 15th March 2010) to overcome facility constraint. Thus, it would crush approximately 56mT of last year's cane as well as increased cane amount of this year.
- Export from Thailand also to increase:** Thailand, world's second biggest sugar exporter, is expected to produce up to 80mT of cane in 2010/11 at an average recovery of sugar of 10%. Sugarcane production is expected to increase due to higher profitability as compared to that from cassava and rice.
- Australia's sugar production to increase by 10%:** Given the good rains in December 2009 that helped in yield improvement as well as rally in sugar prices to 29-year highs, Australia's raw sugar production is expected to rise by 10% to 4.7mT next year. Domestic consumption would be approximately about 1.2mT. Thus, export from Australia would rise from 2.3mT to 3.1mT.

## Increase in exports due to increase in production in India, Brazil...

Particular	2007-08	2008-09	2009-10	2010-11E
North America	0.9	1.0	0.4	0.4
Caribbean	1.4	1.3	1.3	1.3
Central America	2.2	2.3	2.4	2.4
South America	21.2	21.9	25.2	28.8
- Brazil	19.8	20.3	23.5	27.0
- Others	1.5	1.7	1.7	1.8
Western Europe	1.5	1.8	1.6	1.6
Eastern Europe	1.2	1.4	1.3	1.3
Africa	3.7	3.8	3.8	3.8
Middle East	3.7	3.7	3.6	3.6
Asia	16.3	11.1	1.3	7.5
- India	5.8	0.2	-8.0	-3.0
- Thailand	4.9	5.5	5.7	6.1
- Australia	3.7	3.5	2.3	3.1
- Others	1.9	1.9	1.3	1.3
<b>TOTAL</b>	<b>52.0</b>	<b>48.2</b>	<b>40.8</b>	<b>50.7</b>

Source: USDA, PL Research

## Total cane production in Brazil reduced by 3.6% in 2009-10

Particular'	MY2007-08	MY2008-09	MY2009-10
Total Cane Production	491	555	530
Utilization for sugar (% of total cane)	45.5	40.5	40.9
Utilization for Alcohol (% of total cane)	54.5	59.5	59.1

Source: USDA, PL Research

# Government measures helps to keep prices in check to some extent

- **Government to weigh option of asking bulk consumers to use only imported refined sugar:** In order to control domestic sugar prices, Government recently asked bulk consumers like makers of sweets, soft drinks, fruit juice, chocolate, ice cream, biscuits to use only imported refined sugar instead of buying domestic supplies. These bulk consumers, who account for 65% of total domestic consumption, will be given a three-month period until April 2010 to make arrangements to import sugar. Post that, if they continue to buy domestic supplies, government can initiate action against them under the Essential Commodities Act.
- **To set a weekly sub-quota within free sale quota (FSQ) allocated to mills for selling in open market instead of fortnightly sub-quota for February 2010:** Till now, mills were obliged to sell and dispatch their monthly FSQ on a fortnightly basis in two equal installments. But in a new measure aimed at ensuring uniform supplies to the market, the Centre has asked mills to liquidate the FSQ according to a weekly schedule. Moreover, mills have been directed to report actual sale and dispatch sugar to the Directorate of Sugar within seven days of the end of that particular week. As of now, Centre has taken this measure only for the month of February 2010. With this measure, the sugar prices fell from Rs43-44/kg to Rs37-38/kg. Given the positive impact of the measures taken by the Centre, we expect this to continue beyond February 2010.
- **Extension of duty-free import of white sugar till December 2010:** Till the previous year, mill owners were allowed to import raw sugar with not only 60% import duty but also obligation to re-export one tonne of white sugar against import of 1.5 tonne of raw sugar. Since March 2009, centre has step-by-step reduced the import duty to zero and also extended the re-export obligation till December 2010. Also, there is no levy obligation on white sugar produced from raw sugar if sold in the domestic market.
- **Increase in levy sugar requirement - from 10% of output to 20%:** Sugar mills to deliver 20% of their output as 'levy' for the Public Distribution System (PDS). This measure, which came into effect from October 2009, was to maintain level of sugar by Centre to cater to the need of the masses who depend solely on PDS.
- **Reduction of validity period of release orders for white sugar processed from raw sugar from three months to one months:** Mills were originally given three months (from the date of issue of release order) within which they had to sell the white/refined sugar processed from imported raw materials. But now this validity period has been reduced to one month. This measure was to prevent mill owners from holding sugar which was also one of the reasons for the spurt in sugar prices over the last few months.



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# Companies

- Negative sugar cycle to impact business unfavourably:** With the sugar cycle expected to turn downwards, operating profit/tonne of sugar is expected to reduce to Rs7.4/kg from Rs12.4/kg YoY. Operating profit is expected to marginally increase from Rs5bn to Rs5.3bn YoY due to significant increase in volume of sugar from cane. Operating profit from alcohol is expected to reduce from Rs24.5/litre to Rs22.5/litre. With increased amount of bagasse, we expect SHRS to sell 599m units of power in FY11 as compared to 400m units in FY10. However, with improving power scenario in the country, we expect power price per unit to reduce from the current Rs5.5/unit to Rs5/unit.
- Valuation:** Sale has grown by 72% CAGR and profit has grown by 63.7% over the last couple years. Going forward, even though there would be 57.6% CAGR in sales and 123.4% CAGR in profit over FY09-11, we expect the domestic sugar cycle to peak in FY10 and FY11 is likely to enjoy increased supply with stable demand, keeping downward pressure on sugar prices. Also, refining margins are expected to reduce because of healthy increase of sugar supply in the international market. This would affect the profitability of sugar (from cane as well as raw) as well as alcohol segment. At CMP of Rs185, the stock trades at P/BV of 3.9x FY09, 1.8x FY10E and 1.4x FY11E. We change the rating of the stock from 'BUY' to 'Reduce on strength'.

## Key Financials (Rs m)

Y/e September	FY07	FY08	FY09	FY10E	FY11E
Revenue (Rs m)	9,506	21,143	28,165	69,887	70,371
<i>Growth (%)</i>	-	122.4	33.2	148.1	0.7
EBITDA (Rs m)	1,320	2,526	4,632	22,485	16,657
PAT (Rs m)	830	1,332	2,199	15,779	11,392
EPS (Rs)	2.5	4.1	6.7	47.3	34.2
<i>Growth (%)</i>	-	63.5	63.9	610.5	(27.8)
Net DPS (Rs)	-	0.2	0.4	0.6	0.6

Source: Company Data, PL Research

## Profitability & Valuation

Y/e September	FY07	FY08	FY09	FY10E	FY11E
EBITDA Margin (%)	13.9	11.9	16.4	32.2	23.7
RoE (%)	22.3	20.4	17.9	64.1	29.4
RoCE(%)	10.3	12.2	12.8	43.7	23.6
EV/ Sales (x)	5.5	3.3	2.6	1.0	1.0
EV / EBITDA (x)	39.6	27.8	15.9	3.3	4.2
PER (x)	55.1	40.4	27.7	3.9	5.4
P / BV (x)	10.3	6.2	3.9	1.8	1.4
Net Dividend yield (%)	-	0.2	0.3	0.5	0.5

Source: Company Data, PL Research

## Major Shareholders

Promoters	34.5%
Foreign	29.8%
Domestic Inst.	15.16%
Public & Others	20.6%

# Operating Metrics

Particulars	Units	FY09E	FY10E	FY11E
<b>Cane Sugar</b>				
Amount of cane to be crushed	Mn Tonnes	3.5	4.0	5.6
Avg. Yield	(%)	10.7	10.9	10.9
Amount of sugar produced	Mn Tonnes	0.37	0.44	0.61
Sold	Mn Tonnes	0.34	0.44	0.75
Avg. Realisation	Rs / Tonne	23950	34000	30600
Cane Cost	Rs / quintal	178	225.7	228.8
R. M Cost	Rs / Tonne	16636	20703	20991
Operating Profit	Rs / Tonne	3614	9797	6109
Net Sales from Cane Sugar	Rs m	8143	14960	22950
<b>Total Operating Profit</b>	<b>Rs m</b>	<b>1229</b>	<b>4311</b>	<b>4582</b>

<b>Raw Sugar</b>				
Amount of Raw Sugar imported	Mn Tonnes	0.46	1.1	1.1
Average Realisation	Rs / Tonne	23950	38000	32000
R. M Cost	Rs / Tonne	21000	22400	21467
Operating profit	Rs / Tonne	750	13400	8333
Net Sales from Raw Sugar	Rs m	11017	41800	35200
<b>Total Operating Profit</b>	<b>Rs m</b>	<b>345</b>	<b>14740</b>	<b>9167</b>

Particulars	Units	FY09E	FY10E	FY11E
<b>Distillery</b>				
Amount of Alcohol due to Int. Molasses	Mn Litres	65	72.2	70.2
Amount of Alcohol due to Ext. Molasses	Mn Litres		50	50
Average Realisation	Rs / Litre	25.9	28	26
Cost of Molasses	Rs /litre		15.2	14
Cost of processing	Rs / Litre	3.5	3.5	3.5
Operating profit due to int. Molasses	Rs / Litre	22.4	24.5	22.5
Operating Profit due to Ext. Molasses	Rs / Litre		9.3	8.5
Net Sales from Distillery	Rs m	1684	3420	3126
<b>Total Operating Profit</b>	<b>Rs m</b>	<b>1456</b>	<b>2233</b>	<b>2005</b>

<b>Power</b>				
Amount of Saleable Power	Mn units	232	401	599
Selling price	Rs /unit	6.48	5.5	5
Operating Profit	Rs /unit	2.48	1.5	1
Sales from Power	Rs m	1503.36	2207	2995
<b>Operating Profit from Power</b>	<b>Rs m</b>	<b>575.36</b>	<b>602</b>	<b>599</b>
Sales due to trading of sugar	Rs m	5818	7500	6100
Operating Margin	(%)	17.65	8	5
Operating Profit	Rs m	1027	600	305
<b>TOTAL SALES</b>	<b>Rs m</b>	<b>28165</b>	<b>69887</b>	<b>70371</b>
<b>TOTAL OPERATING PROFIT</b>	<b>Rs m</b>	<b>4632</b>	<b>22485</b>	<b>16657</b>

# Financials

## Income Statement (Rs m)

Y/e September	FY07	FY08	FY09	FY10E	FY11E
<b>Net Revenues</b>	<b>9,506</b>	<b>21,143</b>	<b>28,165</b>	<b>69,887</b>	<b>70,371</b>
<b>Expenditure</b>					
Raw Materials	6,749	15,767	15,316	34,509	40,057
<i>% of Net Revenues</i>	<i>71.0</i>	<i>74.6</i>	<i>54.4</i>	<i>49.4</i>	<i>56.9</i>
Personnel	239	419	704	909	1,759
<i>% of Net Revenues</i>	<i>2.5</i>	<i>2.0</i>	<i>2.5</i>	<i>1.3</i>	<i>2.5</i>
Mfg. & Other Expenses	1,067	2,431	7,512	11,984	11,898
<i>% of Net Revenues</i>	<i>11.2</i>	<i>11.5</i>	<i>26.7</i>	<i>17.1</i>	<i>16.9</i>
<b>EBITDA</b>	<b>1,320</b>	<b>2,526</b>	<b>4,632</b>	<b>22,485</b>	<b>16,657</b>
Net Interest	134	701	1,077	890	560
Dep & Amortization	249	193	676	1,000	1,175
<b>EBIT</b>	<b>1,070</b>	<b>2,333</b>	<b>3,956</b>	<b>21,485</b>	<b>15,482</b>
<i>EBIT margin (%)</i>	<i>13.9</i>	<i>11.9</i>	<i>16.4</i>	<i>32.2</i>	<i>23.7</i>
<b>PBT</b>	<b>1,066</b>	<b>1,784</b>	<b>2,944</b>	<b>20,795</b>	<b>15,122</b>
Total Tax	236	427	720	4,991	3,705
<i>Effective Tax rate (%)</i>	<i>14.0</i>	<i>23.9</i>	<i>24.5</i>	<i>24.0</i>	<i>24.5</i>
<b>PAT</b>	<b>830</b>	<b>1,332</b>	<b>2,199</b>	<b>15,779</b>	<b>11,392</b>

Source: Company Data, PL Research

## Balance Sheet (Rs m)

Y/e September	FY07	FY08	FY09	FY10E	FY11E
<b>Sources of Fund</b>					
Share Capital	311	297	334	334	334
Resrves and Surplus	4,128	8,039	15,133	32,484	43,572
Total Shareholder's fund	4,439	8,867	15,998	33,349	44,437
Total Loan Fund	6,470	8,595	12,220	11,500	8,000
<b>Total</b>	<b>11,111</b>	<b>17,929</b>	<b>28,898</b>	<b>45,828</b>	<b>53,422</b>
<b>Application of Fund</b>					
Assets					
Gross Block	6,314	8,401	14,500	18,100	21,000
Less: Dep & Amortization	691	884	1,560	2,560	3,735
Net Block	5,623	7,517	12,940	15,540	17,265
CWIP	2,087	5,212	4,500	3,500	900
Total Current Assets	4,436	7,663	12,948	31,377	37,646
Total Current Liab. & Prov	1,218	2,789	1,800	4,900	2,700
Net Current Assets	3,218	4,874	11,148	26,477	34,946
<b>Total</b>	<b>11,111</b>	<b>17,929</b>	<b>28,898</b>	<b>45,827</b>	<b>53,422</b>

Source: Company Data, PL Research

- Power compensates for negative sugar cycle:** With the increase in sugar supply, operating profit/tonne of sugar is expected to reduce to Rs6.7/kg from Rs10.3/kg YoY. Operating profit from the sugar segment is expected to reduce marginally from Rs4.87bn to Rs4.69bn YoY, even if the volume of sugar is expected to increase from 0.5mT to 0.7mT. Operating profit from alcohol is expected to reduce from Rs24.5/litre to Rs22.5/litre on account of an increase in the supply of molasses. However, we expect sale of power units to increase from 450m units to 650m units YoY due to the modification of boilers. Thus, operating profit from sugar increased by 50% to Rs2.47bn YoY.
- Outlook & Valuation:** We expect 23.7% CAGR in sales and 69% CAGR in profit over FY09-11. However, we expect the sugar cycle to peak in SS2010 and SS2011 is expected to have increased supply with stable demand keeping downward pressure on sugar prices and thus, impacting profitability of sugar as well as alcohol segment. At CMP of Rs116, the stock trades at P/BV of 2.7x FY09, 2.0x FY10E and 1.5x FY11E. We change the rating on the stock from 'BUY' to 'Reduce on strength'.

## Key Financials (Rs m)

Y/e September	FY07	FY08	FY09	FY10E	FY11E
Revenue (Rs m)	13,948	14,909	17,532	24,140	26,845
<i>Growth (%)</i>	-	6.9	17.6	37.7	11.2
EBITDA (Rs m)	765	3,141	4,623	9,316	9,003
PAT (Rs m)	(470)	783	2,095	6,194	5,985
EPS (Rs)	(2.5)	3.1	8.6	24.2	23.4
<i>Growth (%)</i>	-	(220.2)	179.1	183.5	(3.4)
Net DPS (Rs)	-	1.0	1.0	2.0	2.0

Source: Company Data, PL Research

## Profitability & Valuation

Y/e September	FY07	FY08	FY09	FY10E	FY11E
EBITDA Margin (%)	5.5	21.1	26.4	38.6	33.5
RoE (%)	(7.4)	7.8	17.7	35.6	26.3
RoCE(%)	0.2	6.4	13.0	26.9	22.3
EV/ Sales (x)	3.0	2.9	2.2	1.6	1.3
EV / EBITDA (x)	54.5	13.8	8.5	4.1	4.0
PER (x)	(45.5)	37.8	13.6	4.8	4.9
P / BV (x)	3.3	3.2	2.7	2.0	1.5
Net Dividend yield (%)	-	0.8	0.8	1.7	1.7

Source: Company Data, PL Research

## Major Shareholders

Promoters	36.4%
Foreign	14.8%
Domestic Inst.	26.0%
Public & Others	22.8%

# Operating Metrics

Particulars	Units	FY09	FY10E	FY11E	Particulars	Units	FY09	FY10E	FY11E
<b>Cane Sugar</b>					<b>Distillery</b>				
Amount of cane to be crushed	Mn Tonnes	4.89	5.35	7.45	Sold	Mn Litres	55.0	58.8	81.9
Avg. Yield	(%)	9.20	9.35	9.40	Average Realisation	Rs/Litre	23.3	28.0	26.0
Amount of sugar produced	Mn Tonnes	0.45	0.50	0.70	Cost of processing	Rs/Litre	3.5	3.5	3.5
Sold	Mn Tonnes	0.66	0.50	0.70	Operating profit	Rs/Litre	19.8	24.5	22.5
Avg. Realisation	Rs/Tonne	22,570	34,800	31,500	Net Sales from Distillery	Rs Mn	1,282	1,647	2,130
Cane Cost	Rs/quintal	133	201	200	Total Operating Profit	Rs Mn	1,089	1,441	1,843
R. M Cost	Rs/Tonne	14,457	21,550	21,301	<b>Power</b>				
Operating Profit	Rs/Tonne	4,613	9,750	6,699	Amount of Saleable Power	Mn units	360	450	650
Net Sales from Cane Sugar	Rs Mn	14,783	17,400	22,050	Selling price	Rs/unit	3.1	4.0	4.1
Total Operating Profit	Rs Mn	3,022	4,875	4,690	Operating Profit	Rs/unit	2.8	3.7	3.8
<b>Raw Sugar</b>					Sales from Power	Rs Mn	1,116	1,778	2,665
Amount of Raw Sugar imported	Mn Tonnes		0.1		Operating Profit from Power	Rs Mn	1,008	1,643	2,470
Average Realisation	Rs/Tonne		39,000		TOTAL SALES	Rs Mn	17,181	24,140	26,845
R. M Cost	Rs/Tonne		20,527		TOTAL OPERATING PROFIT	Rs Mn	5,119	9,316	9,003
Operating profit	Rs/Tonne		15,973						
Net Sales from Raw Sugar	Rs Mn		3,315						
Total Operating Profit	Rs Mn		1,358						

# Financials

## Income Statement

Y/e September	FY07	FY08	FY09	FY10E	FY11E
<b>Net Revenues</b>	<b>13,948</b>	<b>14,909</b>	<b>17,532</b>	<b>24,140</b>	<b>26,845</b>
<b>Expenditure</b>					
Raw Materials	10,705	9,062	10,640	12,520	14,910
<i>% of Net Revenues</i>	<i>76.7</i>	<i>60.8</i>	<i>60.7</i>	<i>51.9</i>	<i>55.5</i>
Personnel	772	864	856	1,010	1,200
<i>% of Net Revenues</i>	<i>5.5</i>	<i>5.8</i>	<i>4.9</i>	<i>4.2</i>	<i>4.5</i>
Mfg. & Other Expenses	1,619	1,842	1,413	1,293	1,732
<i>% of Net Revenues</i>	<i>11.6</i>	<i>12.4</i>	<i>8.1</i>	<i>5.4</i>	<i>6.5</i>
<b>EBITDA</b>	<b>765</b>	<b>3,141</b>	<b>4,623</b>	<b>9,316</b>	<b>9,003</b>
Net Interest	600	1,000	1,068	720	595
Dep & Amortization	838	1,253	1,160	1,175	1,225
<b>EBIT</b>	<b>33</b>	<b>2,039</b>	<b>3,484</b>	<b>8,182</b>	<b>7,806</b>
<i>EBIT margin (%)</i>	<i>0.2</i>	<i>13.7</i>	<i>19.9</i>	<i>33.9</i>	<i>29.1</i>
<b>PBT</b>	<b>(568)</b>	<b>1,039</b>	<b>2,416</b>	<b>7,462</b>	<b>7,211</b>
Total Tax	65	256	231	1,269	1,226
<i>Effective Tax rate (%)</i>	<i>(11.4)</i>	<i>24.6</i>	<i>9.6</i>	<i>17.0</i>	<i>17.0</i>
<b>PAT</b>	<b>(470)</b>	<b>783</b>	<b>2,095</b>	<b>6,194</b>	<b>5,985</b>

Source: Company Data, PL Research

## Balance Sheet (Rs m)

Y/e September	FY07	FY08	FY09	FY10E	FY11E
<b>Sources of Fund</b>					
Share Capital	248	256	256	256	256
Resrves and Surplus	8,343	9,659	11,462	17,056	22,440
Total Shareholder's fund	8,591	9,915	11,718	17,311	22,696
Total Loan Fund	12,891	13,804	9,795	8,500	6,500
<b>Total</b>	<b>22,714</b>	<b>25,236</b>	<b>23,081</b>	<b>27,379</b>	<b>30,764</b>
<b>Application of Fund</b>					
Assets					
Gross Block	20,820	24,881	24,900	25,600	26,200
Less: Dep & Amortization	4,279	5,516	6,675	7,850	9,075
Net Block	16,542	19,365	18,225	17,750	17,125
CWIP	3,337	82	300	200	300
Total Current Assets	6,805	8,382	8,072	13,446	18,305
Total Current Liab. & Prov	4,007	2,626	3,550	4,050	5,000
Net Current Assets	2,797	5,756	4,522	9,396	13,305
<b>Total</b>	<b>22,714</b>	<b>25,236</b>	<b>23,081</b>	<b>27,379</b>	<b>30,764</b>

Source: Company Data, PL Research

- Higher sugar production to impact margins adversely:**  
 Operating profit/tonne is expected to reduce from Rs9.46/kg to Rs5.16/kg YoY. Amount of sugar sale is expected to increase significantly by 58% to 0.98mT YoY. However, increased sugar supply (on industry basis) and operating profit is expected to reduce from Rs5.3bn to Rs5.0bn due to reduction in sugar prices from the current Rs39/kg to Rs33/kg next year.
- Higher cane production to impact Alcohol and Power business:** Higher cane production would have an adverse impact on profitability of alcohol which is expected to reduce from Rs24.5/litre to Rs22.5/litre. Also, we expect the company to sell lower power (produced only through bagasse) as very low amount of sugar is expected to be refined next year.
- Valuation:** Even though there would be 23% CAGR in sales and 160% CAGR in profit over FY09-11, we expect the sugar cycle to peak in FY10 and FY11 is likely to enjoy increased supply with stable demand, keeping downward pressure on sugar prices; thus, impacting profitability of sugar as well as alcohol segment. We expect sales and profit to reduce by 34.5% and 58.1%, respectively in SS2011. At CMP of Rs175, the stock trades at P/BV of 1.6x FY09, 1.2x FY10E and 1.0FY11E. We change the rating on the stock from **'Accumulate'** to **'Reduce on strength'**.

## Key Financials (Rs m)

Y/e September	FY07	FY08	FY09	FY10E	FY11E
Revenue (Rs m)	17,805	20,701	22,993	48,185	36,655
<i>Growth (%)</i>	-	16.3	11.1	109.6	(23.9)
EBITDA (Rs m)	1,907	2,941	6,948	14,378	9,080
PAT (Rs m)	(103)	(447)	580	7,622	3,542
EPS (Rs)	0.1	(2.3)	3.0	39.9	18.5
<i>Growth (%)</i>	-	(3,863.6)	(229.6)	1,215.3	(53.5)
EPS (Rs) (incl. Forex los	-	(21.8)	3.0	39.9	-
Net DPS (Rs)	0.6	0.6	0.7	2.0	1.6

Source: Company Data, PL Research

## Profitability & Valuation

Y/e September	FY07	FY08	FY09	FY10E	FY11E
EBITDA Margin (%)	10.7	14.2	30.2	29.8	24.8
RoE (%)	0.1	(12.1)	3.5	30.4	11.6
RoCE(%)	1.5	1.2	6.4	18.2	10.2
EV/ Sales (x)	3.4	3.3	3.2	1.2	1.4
EV / EBITDA (x)	31.8	23.2	10.7	4.1	5.7
PER (x)	2,816.0	-	57.7	4.4	9.4
P / BV (x)	1.8	2.1	1.6	1.2	1.0
Net Dividend yield (%)	89.0	0.3	0.4	1.1	0.9

Source: Company Data, PL Research

## Major Shareholders

Promoters	37.1%
Foreign	23.3%
Domestic Inst.	14.8%
Public & Others	24.8%



# Operating Metrics

Particulars	Units	FY09	FY10E	FY11E
<b>Cane Sugar</b>				
Amount of cane to be crushed	Mn Tonnes	6.5	6.8	10.7
Avg. Yield	(%)	9.2	9.1	9.2
Amount of sugar produced	Mn Tonnes	0.6	0.6	1.0
Sold	Mn Tonnes	0.9	0.7	1.0
Blended Avg. Realisation	Rs/ Tonne	23,000	34,800	31,500
Cane Cost	Rs/ quintal	125	215	210
R. M Cost	Rs/ Tonne	13,587	23,642	22,838
Operating Profit	Rs/ Tonne	5,913	7,658	5,162
Net Sales from Cane Sugar	Rs Mn	20,700	24,360	30,870
Total Operating Profit	Rs Mn	5,322	5,361	5,059
<b>Raw Sugar</b>				
Amount of Raw Sugar imported	Mn Tonnes		0.5	
Average Realisation	Rs/ Tonne		39,000	
R. M Cost	Rs/ Tonne		24,810	
Operating profit	Rs/ Tonne		11,990	
Net Sales from Raw Sugar	Rs Mn		19,500	
Total Operating Profit	Rs Mn		5,995	

Particulars	Units	FY09	FY10E	FY11E
<b>Distillery</b>				
Sold	Mn Litres	71.5	74.9	117.2
Average Realisation	Rs/ Litre	23.3	28.0	26.0
Cost of processing	Rs/ Litre	3.5	3.5	3.5
Operating profit	Rs/ Litre	19.8	24.5	22.5
Net Sales from Distillery	Rs Mn	1,666	2,098	3,047
Total Operating Profit	Rs Mn	1,416	1,836	2,636
<b>Power</b>				
Amount of Saleable Power	Mn units	90	202	180
Selling price	Rs/unit	3.30	4.10	4.10
Cost of producing	Rs/unit	0.30	0.30	0.30
Operating Profit	Rs/unit	3.00	3.80	3.80
Sales from Power	Rs Mn	297	827	738
Operating Profit from Power	Rs Mn	270	766	684
TOTAL SALES	Rs Mn	22,963	48,185	36,655
TOTAL OPERATING PROFIT	Rs Mn	6,948	14,378	9,080

# Financials

## Income Statement

Y/e September	FY07	FY08	FY09	FY10E	FY11E
<b>Net Revenues</b>	<b>17,805</b>	<b>20,701</b>	<b>22,993</b>	<b>48,185</b>	<b>36,655</b>
<b>Expenditure</b>					
Raw Materials	13,441	13,693	12,208	28,954	22,381
<i>% of Net Revenues</i>	<i>75.5</i>	<i>66.1</i>	<i>53.1</i>	<i>60.1</i>	<i>61.1</i>
Personnel	1,423	1,483	1,653	1,819	2,000
<i>% of Net Revenues</i>	<i>8.0</i>	<i>7.2</i>	<i>7.2</i>	<i>3.8</i>	<i>5.5</i>
Mfg. & Other Expenses	2,425	2,584	2,184	3,034	3,194
<i>% of Net Revenues</i>	<i>13.6</i>	<i>12.5</i>	<i>9.5</i>	<i>6.3</i>	<i>8.7</i>
<b>EBITDA</b>					
Net Interest	915	2,071	2,781	1,300	1,050
Dep & Amortization	1,619	2,799	3,457	3,600	3,651
<b>EBIT</b>	<b>612</b>	<b>644</b>	<b>3,833</b>	<b>10,828</b>	<b>5,479</b>
<i>EBIT margin (%)</i>	<i>3.4</i>	<i>3.1</i>	<i>16.7</i>	<i>22.5</i>	<i>14.9</i>
<b>PBT</b>	<b>(303)</b>	<b>(1,427)</b>	<b>1,052</b>	<b>9,528</b>	<b>4,429</b>
Total Tax	(160)	(980)	472	1,906	887
<i>Effective Tax rate (%)</i>	<i>52.9</i>	<i>68.7</i>	<i>44.9</i>	<i>20.0</i>	<i>20.0</i>
<b>PAT</b>	<b>(103)</b>	<b>(447)</b>	<b>580</b>	<b>7,622</b>	<b>3,542</b>

Source: Company Data, PL Research

## Balance Sheet (Rs m)

Y/e September	FY07	FY08	FY09	FY10E	FY11E
<b>Sources of Fund</b>					
Share Capital	141	141	177	191	191
Resrves and Surplus	13,696	11,711	20,796	28,711	31,894
Total Shareholder's fund	14,060	12,013	21,134	29,063	32,246
Total Loan Fund	35,934	43,350	40,562	25,856	18,056
<b>Total</b>	<b>51,266</b>	<b>56,076</b>	<b>62,833</b>	<b>55,970</b>	<b>51,353</b>
<b>Application of Fund</b>					
<b>Assets</b>					
Gross Block	29,218	47,452	52,951	53,000	53,500
Less: Dep & Amortization	4,671	7,191	10,598	14,198	17,849
Net Block	24,547	40,261	42,353	38,802	35,651
CWIP	16,299	1,587	1,548	1,800	1,900
Total Current Assets	20,549	25,920	30,369	33,207	21,623
Total Current Liab. & Prov	7,143	9,584	9,027	16,061	6,042
Net Current Assets	10,420	14,227	19,372	15,367	13,802
<b>Total</b>	<b>51,266</b>	<b>56,076</b>	<b>63,274</b>	<b>55,970</b>	<b>51,354</b>

Source: Company Data, PL Research

# Appendix

## Q&A with **Mr. Prakash Naiknavare**, *Managing Director – Maharashtra State Co-op Sugar Factories Federation*

### Q **What is your outlook on domestic sugar for SS2010 and SS2011?**

A This year, India had an opening stock of 2.5mT, production of approximately 16mT and as of now the country has contracted for import of about 6mT. With domestic consumption of 23.5mT, India is expected to import another 3mT to maintain a comfort level of closing stock of 4mT. Farmers are happy with the cane price and I expect next year's production to increase to 21.5mT.

### Q **What is your outlook for SS2010 and SS2011, specifically with respect to Maharashtra?**

A In Maharashtra, I expect increase in amount of cane to be crushed from 41mT to 50mT due to increase in weight of cane as well as extension of crushing period from March 15 to end of April. I expect cane production to improve to 58mT next year, with average recovery of 11.5%, assuming normal and timely rainfall. Two main reasons for increase in cane amount are a favourable cane price and higher profitability of cane over alternate crops.

### Q **How much did farmers in Maharashtra receive in terms of cane price this year?**

A In the beginning of this crushing season, farmers received cane price of Rs157.5/quintal. I expect cane price to reach level of Rs220/quintal.

### Q **Area wise, how is the scenario going to be in Maharashtra?**

A About 66% of cane production would take place in Western Maharashtra, while the rest in Marathwada, Khandesh and Vidarbha. Higher proportion of cane production would be in Western Maharashtra due to better water availability.

### Q **How does the payment system for farmers in Maharashtra work?**

A First advance payment (Statutory Minimum Payment) is made within 14 days of procuring cane by millers. Second advance payment of Rs100-200/T coincides with Diwali and the bullock festival 'Pola'. Third advance payment is in Feb-March 2010 and the final payment is done in Aug-Sept 2010.

### Q **How does profit-sharing mechanism work for Maharashtra Sugar Co-operative society ?**

A This Co-operative society has farmers as its members. Entire profit is shared by all farmers in proportion to cane supplied by them.

### Q **What is your outlook on cane production in Brazil?**

A I expect Brazil to start crushing almost 50mT of last year's cane 15 days in advance along with an increased amount of cane this year. As a result, I expect raw sugar available for export to increase from 17mT in MY2009-10 to 22mT in 2010-11 (assuming normal monsoon).

### Q **So, overall how do you see domestic sugar supply demand scenario next year?**

A I see increased sugar supply (assuming normal and timely rainfall) and demand remaining relatively stable. This increased sugar supply would help sugar prices to fall below the current levels.

# About Maharashtra State Co-op Sugar Factories Federation (MSCSFF)

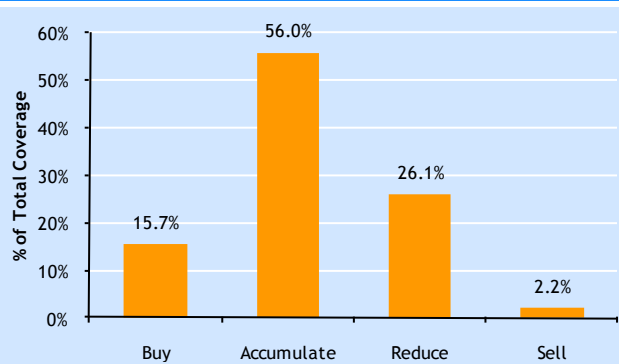
- At present MSCFF (Sangh) has 190 Co-operative sugar factories as its members and is the biggest State Federation of its kind in the country. Only the co-operative sugar factories registered under the Maharashtra State Co-operative Societies Act are eligible for Sangh membership.
- Sugarcane growers in the State were encouraged by the announcement in 1954 by the then Bombay State Government, of the 12 places in the State where sugar factories could be established with an offer of Government share capital contribution of Rs10 lacs each if Co-operative Societies are organized for the same. The announcement fetched rush of application from about 16 Co-operative Societies. A Central Committee under the Chairmanship of Prof. Dhananjayrao Gadgil was formed for guiding the Societies about important issues like share capital, sugarcane area, irrigation, site selection, land, transport facilities etc. State Government also appointed a Cabinet Sub-Committee for Co-operative sugar factories. With an increase in number of Co-operative sugar factories and the tremendous response received from co-operators, need of apex institutions to guide and advise the Societies was felt. Hence on 11/2/1956, Bombay State Sahakari Sakhar Karkhana Sangh was registered when 14 factories (inclusive of a Khedut Factory from Surat Dist.) were affiliated.

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