

# MANAGEMENT DISCUSSION

## & ANALYSIS



### GLOBAL SUGAR INDUSTRY

The global sugar production is dominated by Brazil, India and China, accounting for around 40% of the total produce. During 2010-11, sugar production stood at 166.958 million tons as against 157.994 million tons in 2009-10, an increase of 5.67% over the previous year. The sugar consumption for 2010-11, on the other hand, stood at 166.179 million tons as against 162.619 million tons in 2009-10, an increase of 2.19% over the previous year. After a considerable time gap, the industry has witnessed

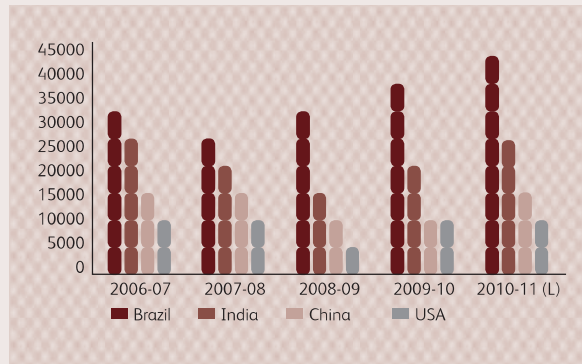
surplus production, though very marginal. Even the stocks/consumption ratio has reduced to a 20-year low, indicating the rebound. The global sugar prices peaked to a 30-year high during the year, owing to limited supply and overall surge in commodity prices. However, there has been significant volatility as prices first started to soften since January 2011 following the news of surplus productions across various sugar producing regions and then rebounded again during June 2011.

#### World sugar balance (million tons)

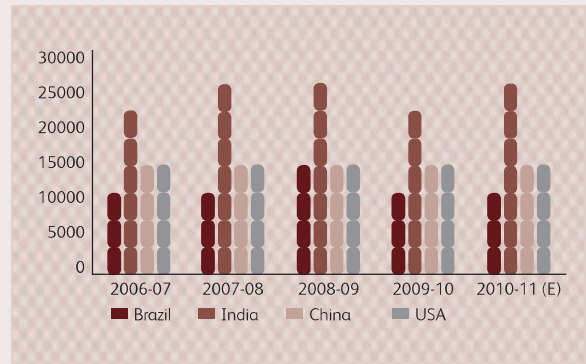
Particulars	2010-11	2009-10	% change
Production	166.958	157.994	5.67
Consumption	166.179	162.619	2.19
Surplus/deficit	0.779	-4.625	
Import demand	50.422	53.776	-6.24
Export availability	51.287	54.236	-5.44
End stocks	56.159	56.199	-0.07
Stock/consumption ratio in %	33.79	34.56	

(Source: ISO quarterly market outlook, May 2011)

Production by major countries ('000 metric tons)

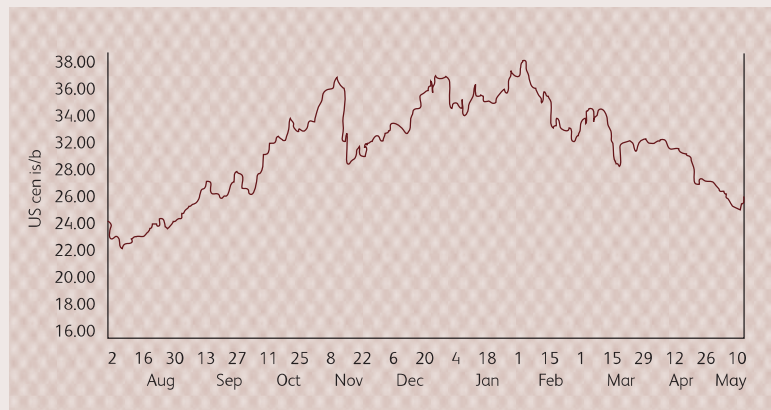


Consumption by major countries ('000 metric tons)



(Source: US Department of Agriculture)

International sugar prices



(Source: ISO quarterly market outlook, May 2011)

## INDIAN SUGAR INDUSTRY

### A QUICK VIEW

**600+**

Sugar factories widely dispersed across Uttar Pradesh, Maharashtra, Karnataka and Tamil Nadu among others

**5 million hectares+**

Area under sugar cane cultivation

**3,500 tons per day**

Average capacity of sugar mills

**0.7%**

Contribution to India's gross domestic product (GDP)

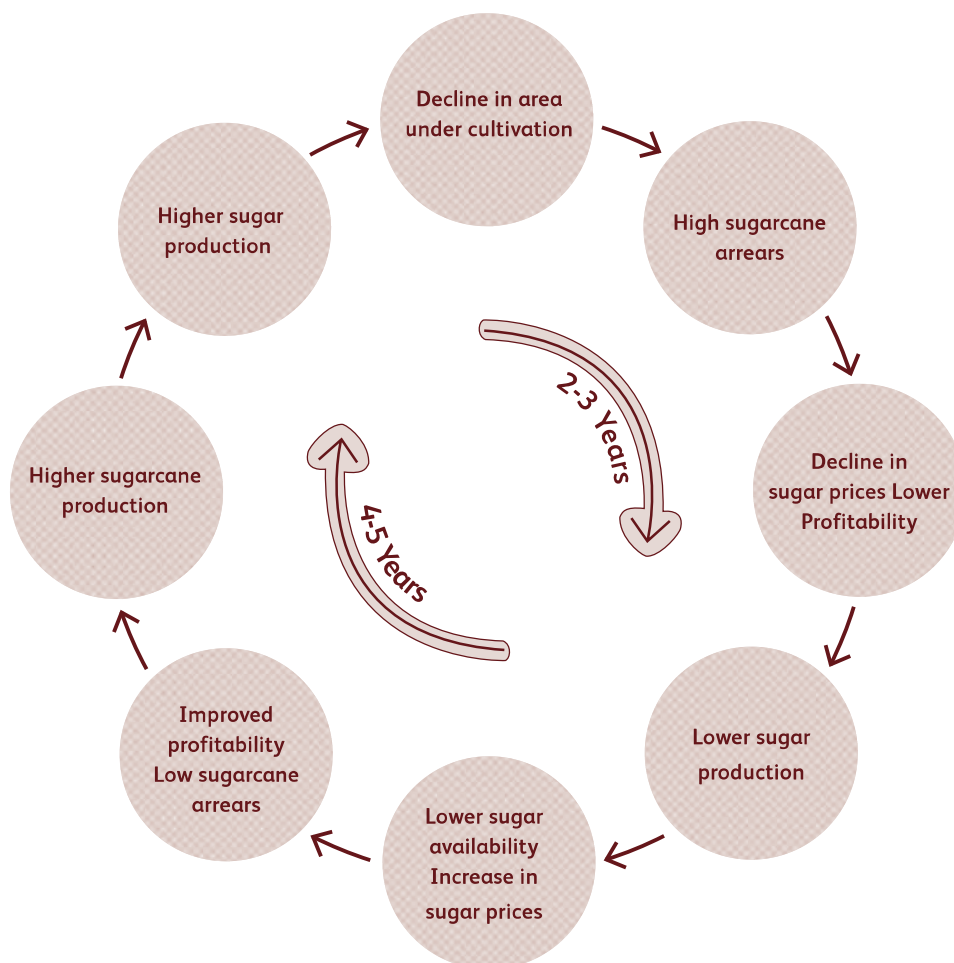
**12%+**

Contribution to global sugar production

**Rs. 2,700 crores**

The sugar industry's contribution to national exchequer and various state governments in terms of cane purchase tax and excise duty

## The cyclical nature of the sugar industry



The Indian sugar industry follows a particular cycle (5-8 years) wherein 2-3 years of high sugar production gives way to 2-3 years of lower production.

In the high production phase, sugarcane acreage increases resulting in higher cane output and sugar production accompanied with declining realisations (as a result of oversupply). The resulting low prices for sugar impacts the ability of mills to pay the farmers thus leading to creation of arrears. High arrear provokes the farmers to shift to other crops, resulting in a decline in sugarcane acreage. From here-on, the sugar cycle enters the low production phase, where sugarcane acreage decreases resulting in lower cane output and sugar production accompanied with higher realisations (as a result of short supply) and decline in arrears to the farmers, thus inducing the farmers to shift back to sugarcane plantation.

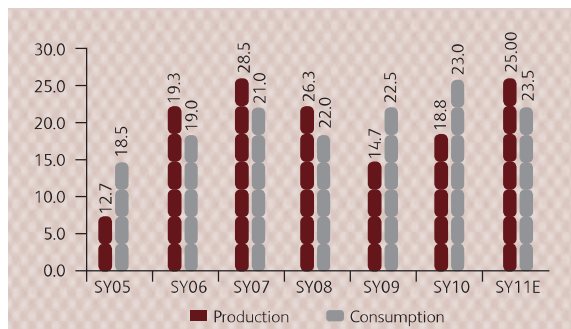
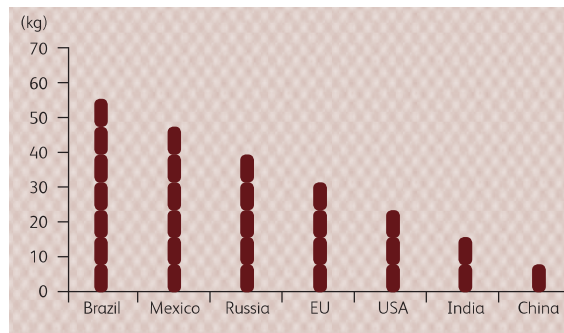
### Production

The sugar production in India has averaged 21.3 million tons between 2000-01 and 2010-11 with highest and lowest

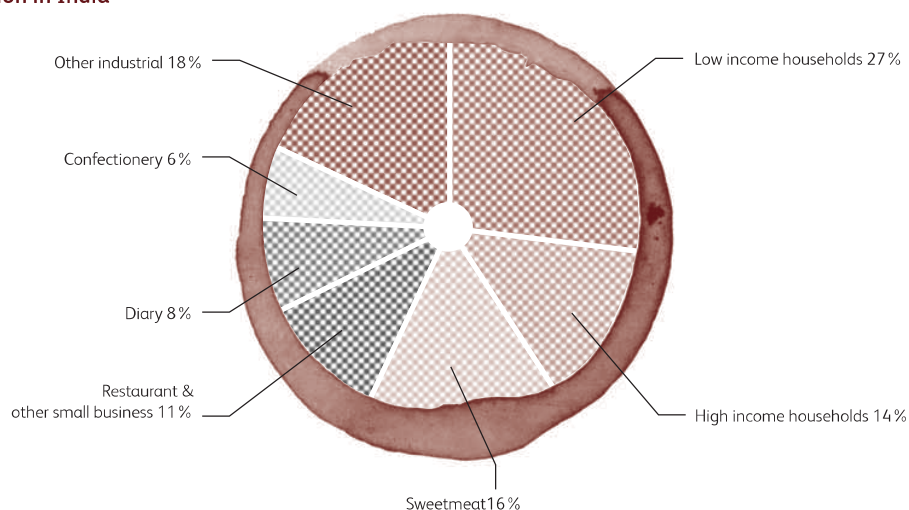
production of 30.7 million tons (2005-06) and 13.8 million tons (2008-09) respectively. Currently, the sugar cycle is witnessing an upswing with an estimated output of around 25 million tons for 2010-11, an increase of 33% over the previous year.

### Consumption

India is considered to be the largest consumers of sugar in the world. Its sugar consumption has been increasing at an average of 3.5% annually over the last decade fuelled by rising incomes, population growth, substitution of by-products and food sector (ice creams, confectionaries, sweets and other household products who account for about 60% of mill sugar demand). Despite this growth, India's per capita sugar consumption of 20 kg is still lower than most developed countries. The consumption for 2010-11 has been estimated around 22 million tones, an increase of 2% over the previous year.

**Domestic sugar production and consumption (million tons)****Per capita sugar consumption (kg)****Break-up of sugar consumption in India**

Only 41% is household consumption while 59% sugar consumption includes restaurant, confectionery, soft drink dairies and others. Low income households consume 27% which is taken care of by the levy quota (10%) that is distributed through public distribution system.

**Sugar consumption in India****Imports and exports**

Restrictions have been imposed on free exports from India due to the controls exercised by the Government to control inflation. Despite surplus output, while India did not witness any sugar imports during the year, a glut of sugar was created in the domestic market by banning exports that resulted in plummeting of sugar prices. On a need basis, the Government of India has allowed the Indian sugar mills to export 500000 tons of sugar by March 2011 and 500000 tons by June, 2011.

**Cane production**

Sugarcane plantation is carried out all round the year, while harvesting happens only in September –October. As a result of improved payments to farmers, the total area under cane cultivation increased from 42.02 lac hectares in 2009-10 to 50.80 lac hectares in 2010-11. According to the first advance estimate of the government, the Indian sugarcane acreage in the next crushing season of 2011-12 is expected to be at 52 lac hectares which shall further increase the sugar production. The industry has made its first estimate of 265 lac tonnes during 2011-12.

**Prices**

In 2009-10, the Union Government introduced the Fair and Remunerative Price (FRP) system to replace the Statutory Minimum Price (SMP) system. FRP is the minimum price that sugarcane farmers are legally guaranteed. It is computed by factoring in the imputed value of family labour, rent, element of risk and profit for the farmer. However, a number of states especially in North India have their own legislation under which they announce a higher price known as the State Advised Price (SAP). The industry has been protesting against the SAP on the grounds that it is fixed arbitrarily without any economic justification but is based purely on political criteria. Nevertheless, the industry has been paying the SAP wherever applicable. For SY 2010-11, the Centre fixed the FRP at Rs 139 per quintal while SAP was fixed at Rs 205 per quintal in Uttar Pradesh. This affected the profitability of the sugar industry significantly.

## Government Regulations:

The sugar industry continued facing difficulties on account of the negative policies of the Government during the year under review. While on the one hand sugar prices remained under severe pressure during the year 2010-11 largely due to various measures taken by the Government of India in its overall policy to control inflation the release mechanism of the government for free sugar resulted in large releases of sugar at unremunerative prices.

### Some of other restrictions imposed by the Government were:

1. Restrictions on export of sugar. During the year 1 million tone sugar only was allowed to be exported and that too in two tranches. This denied the industry the benefit of spurt in international sugar prices which went as high as 32.57 cents per pound in February 2011.
2. Stock holding limit on sugar. While on the one hand the institutional customers were not allowed to hold stock of sugar beyond their ninety days' consumption they were allowed to import sugar without any restriction. This led to lesser off take of sugar and softening of the prices.
3. The Government continued its policy to impose 10% levy obligation for the Public Distribution System (PDS) on the domestic sugar mills which was procured at a price lower by Rs 1000/qtl as compared to the market price. The levy price fixed for 2010-11 was Rs 1863.47/qtl in UP and Rs 2052.01 in Bihar. The PDS price for SY 2010-11 was retained at Rs 13.50/kg.

### Levy and free sale quota

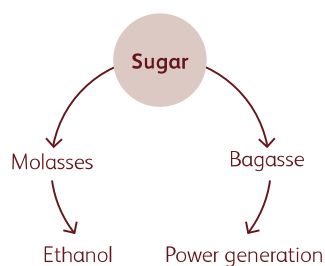
Sugar season	Levy (%)	Price per kg (Rs.)
2009-10	20	13.50
2010-11	10	18.00

(Source: CRISIL Research)

The retail prices of sugar on the other hand continued to hover between Rs. 30 – 32/kg during the year.

### Sugar and its by-products

The by-products of sugar (molasses and bagasse) provide an alternative source of revenues for sugar companies and are utilized towards producing industrial alcohol and power. As a result, the Companies can strengthen their bottomline as well as contribute towards cleaner environment through the production of green power.



## Ethanol

Molasses is primarily used in alcohol production and it accounts for 4.3-4.7% per ton of crushed sugarcane. Alcohol is used as a raw material for industrial manufacture of potable and fuel ethanol. The result is that 80% of the total potable alcohol production in India is derived from molasses.

In August 2010 the Cabinet Committee fixed an interim price of Rs. 27 per litre for ethanol under the Ethanol Blending Programme (EBP) for blending of 5% ethanol with petrol. India's 330 distilleries produce 4 billion litres of alcohol annually of which 115 distilleries have the capacity to distill 1.8 billion litres of ethanol that is sufficient to meet the 5% mandate. The blending levels shall be further increased to 20% by 2017.

## Cogeneration sector

Bagasse has a very robust demand in the paper and bio-mass based power projects. The sugar industry uses bagasse as a fuel to produce electricity and steam by cogeneration. The potential to generate cogeneration power is approximately 5,000 MW. There are around 149 cogeneration projects with an installed capacity of 1,562 MW in the Indian sugar mills. Approximately 70 cogeneration projects are under implementation that surmount to 700 MW. (Source: MNRE). The government provides incentives like exemption from income tax for a period of ten years within the first 15 years of operation, waiver of capital goods import duties on mega power projects above 1,000 MW generation capacities.

As per the Eleventh Plan (2007-12) the government of India has aimed to add around 1,700 MW of power from biomass and bagasse. This is more than twice the actual addition of 750 MW as in Tenth Year Plan.

## Indian sugar industry on SCOT

### Strengths

- Second largest producer after Brazil and largest consumer globally
- Catalyzed socio-economic development in rural India as it provides direct employment to farmers (including ancillary activities)
- Supports the downstream industries by providing raw materials (by products in the form of alcohol, ethanol and cogeneration)
- Generates replenishable biomass without depending on fossil fuel

### Challenges

- Cyclical nature of the industry
- Sugarcane pricing
- High production costs due to under-utilised crushing capacities
- Outdated and obsolete technology

**Opportunities**

- Potential to enhance sugar production in the event of de-regulation of industry
- High value of by-products for downstream industries
- Advanced technology available for product distillation
- Increasing focus on cogeneration and ethanol utilisation by the government of India

**Threats**

- Political intervention in cane pricing, levy purchase, release mechanism and others
- Deterioration of the soil quality due to imbalanced use of fertilizers and pesticides
- Low groundwater availability

**Outlook**

The outlook for SY 2011-12 looks quite optimistic in terms of increased sugar production which would be fuelled by increasing sugarcane plantation. The realisations on the other hand are expected to remain under pressure due to sufficient supplies and would largely depend upon the export policy of the Government. India will be in a position to cater to the global demand by exporting its surplus production while ensuring remunerative prices to the farmers. The industry is eagerly waiting for any development towards the industry deregulation which shall

equally benefit all the stakeholders – farmers, millers and consumers. The mandating of ethanol will help in countering the increase in fuel prices. Combined with India's growing appetite for automobiles the demand for fuel will increase. The automobile makers in India are considering the dual fuel mode for the cars they will be manufacturing in the coming years and this in turn will further encourage ethanol consumption.

**COMPANY REVIEW****Operational performance**

The improvement in the sugar scenario in India was visible in our operational performance. This year we crushed 275.33 lac quintals of sugarcane, an increase of 28.45% over the previous year due to an increase in area under cultivation. The crushing would have been higher but was affected due to irregular monsoons resulting in lower yield and lower sucrose formation in the cane belt of U.P and Bihar. Nevertheless, due to the remunerative prices paid to the farmers, the area under sugarcane increased significantly resulting in greater availability of sugarcane for crushing. The Company paid Rs. 205 per quintal to the farmers towards cane purchase which encouraged them to produce more. Further, the Company took varied initiatives towards improving the productivity and yield of the sugarcane. The crushing days increased from 376 days in 2009-10 to 436 days in 2010-11 for your company.

**Production of Sugar**

	Year 2010-2011					Year 2009-2010				
	Hargaon	Rosa	Narkatiaganj	Hata	Total	Hargaon	Rosa	Narkatiaganj	Hata	Total
Sugarcane Crushed (lac quintals)	124.83	31.84	68.15	50.51	275.33	102.54	30.58	51.65	29.58	214.35
Recovery (%)	9.45	8.50	9.40	9.67	9.26	9.41	8.51	9.51	9.26	9.17
Sugar Produced (lac quintals)	11.80	2.71	6.41	4.88	25.80	9.65	2.60	5.10	2.74	20.09
Crushing days	136	103	101	96	436	119	91	82	84	376

With an improvement in sugarcane output, the availability of the by-products also improved:

- The industrial alcohol production increased 73.70% over the previous year; ethanol production was reported at 345.36 lac litres and the entire output was supplied to state run oil companies at Rs. 27 per litre under the Ethanol Blending Programme (EBP)

**Production of Alcohol**

	Year 2010-2011			Year 2009-2010		
	Hargaon	Narkatiaganj	Total	Hargaon	Narkatiaganj	Total
Alcohol Produced (lacs Ltrs.)	233.24	112.12	345.36	136.26	62.57	198.83
Recovery % (Ltrs. Per Qtl.)	22.46	21.63	22.19	23.74	21.34	22.93

- The Company sold 541.15 units of power in 2010-11 against 343.54 units in 2009-10, owing to increase in co-generation; the electricity generated was sold at Rs. 3.98/unit

## Power Sold

	Year 2010-2011				Year 2009-2010			
	Hargaon	Narkatiaganj	Hata	Total	Hargaon	Narkatiaganj	Hata	Total
<b>Power Sold (in lac Units)</b>	246.97	87.73	210.45	545.15	245.25	32.95	65.34	343.54

## Internal control

The company has a wide spread internal control system to ensure smooth functioning of each and every department of the organization. The internal control system is totally in alignment with the business nature and the size of the company. It tracks various financial transactions effectively and certifies the compliance with rules and regulations, thus contributing to the operational efficiency of the company.

## Human resources and industrial relations

Human Resources are the greatest assets that the Company possesses. In order to leverage the actual potential of every employee, the Company has built an encouraging working environment and has nurtured and appreciated individual talents to enable them to grow professionally as well as personally.

Vigorous efforts were made to upgrade and improve skills and knowledge of Company's employees and to fill up specific knowledge and skill gaps. The Company also continued to maintain cordial relations in all the mills and offices during the year under review.

## DE-RISKING AT OUDH

### Risk: Higher operating cost

**Measures:** In order to bring down the operating costs, the Company undertook various production optimisation techniques and installed various cutting edge technologies that resulted in a significant control over operational cost.

### Risk: Lower revenues resulting out of poor realisations

**Measures:** The integrated business model of the Company enables additional revenue streams in the event of lower sugar realisations.

### Risk: Stalling of regular operations due to high level of debt.

**Measures:** After witnessing a negative growth in the past (due to adverse external scenario), the Company undertook a Corporate Debt-Restructuring program during the year to increase the financial leverage of the Company. The resultant benefit will be seen in the coming years.

## ANNEXURE - B

### Statement showing particulars pursuant to the Companies (Disclosure of particulars in the Report of the Board of Directors) Rules, 1988 and forming part of the Directors' Report for the year ended 30th June, 2011

#### I. CONSERVATION OF ENERGY :

- i) Following initiatives have been taken by the Company to conserve Energy during the year 2010-11:
  - a) The Company has installed various machineries and equipments which besides increasing generation of steam are also dedicated to reduce consumption of steam and fuel.
  - b) The Company has installed auto control system on all boilers to reduce the consumption of bagasse by putting auto control combustion system.
  - c) The Company has modified system of heating of juices and bleeding of vapors for pan boiling to considerably reduce consumption of steam and fuel.