

INDIAN BULK TEA INDUSTRY

Drop in tea prices, along with wage rate hike to impact margins for tea estates in North India; sector outlook revised to Negative

DECEMBER 2023



Highlights

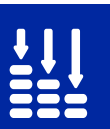


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ICRA estimates NI estates to witness an average decline in realisation of Rs. 10 to Rs. 15/kg in FY2024 on a YoY basis.

Increase in wage rates for NI-based players is estimated to have raised the cost of manpower by ~Rs. 9/kg at present, although for the full financial year the impact would be ~Rs 5/kg.

Consequently, operating profitability of NI bulk tea producers is projected to decline significantly in FY2024. Any material improvement over the medium term appears unlikely at present.



- All-India cumulative auction average of orthodox (ODX) tea in 10M CY2023 declined significantly by Rs. 51/Kg (~21%) on a YoY basis. This was primarily driven by a sharp drop in the North India (NI) ODX tea prices by Rs. 70/kg (~25%). The South India (SI) ODX tea variety also witnessed a price fall, but the same was limited to only Rs. 7/kg (~5%). The fall was on the back of lower export demand, primarily from Iran.
- Prices of all-India crush-tear-curl (CTC) tea also witnessed a decline of Rs. ~6/kg (~3%) in 10M CY2023 on a YoY basis. Sluggish rural demand, along with headwinds in exports markets due to oversupply of Kenyan teas, India's main competitor in CTC teas, has contributed to this fall.
- Introduction of the 'Bharat' auction system in NI auction centres is also likely to have weighed on prices in FY2024. The Tea Board of India has reverted to the earlier 'English' auction system from Nov '23 and the trend in prices in recent auctions, post the change, seems to be encouraging.
- Given the current production trend, black tea production in India in CY2023 is likely to be lower by ~1% on a YoY basis. Tea output in Kenya may increase in CY2023, with production during 8M CY2023 already up by ~7% on a YoY basis. The Sri Lankan output during 10M CY2023 is also up by 5 Mkg (~2%) on a YoY basis. However, full-year production would still remain materially lower than the CY2019 level.
- West Bengal (WB) and Assam have hiked the wage rates from June '23 and Oct '23 respectively. ICRA estimates the cost of labour to increase by ~Rs. 9/kg, although the full-year impact would be lower at ~Rs. 5/kg. The OPM of NI-based bulk tea players of the ICRA sample set in FY2024 is likely to contract by ~280 basis points on the back of an increase in cost due to the wage rate hike and decline in tea realisation. Given the current operating environment in the industry, both domestic and international, any material improvement in OPM during FY2025 appears unlikely at present. Accordingly, **ICRA has revised the sector outlook to Negative from Stable.**

Bulk Tea Sector – Indicative thresholds for outlook revision

OPBDITA in Rs. per kg of made tea



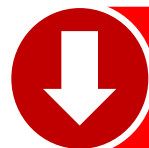
Positive Outlook

More than Rs. 25/Kg



Stable Outlook

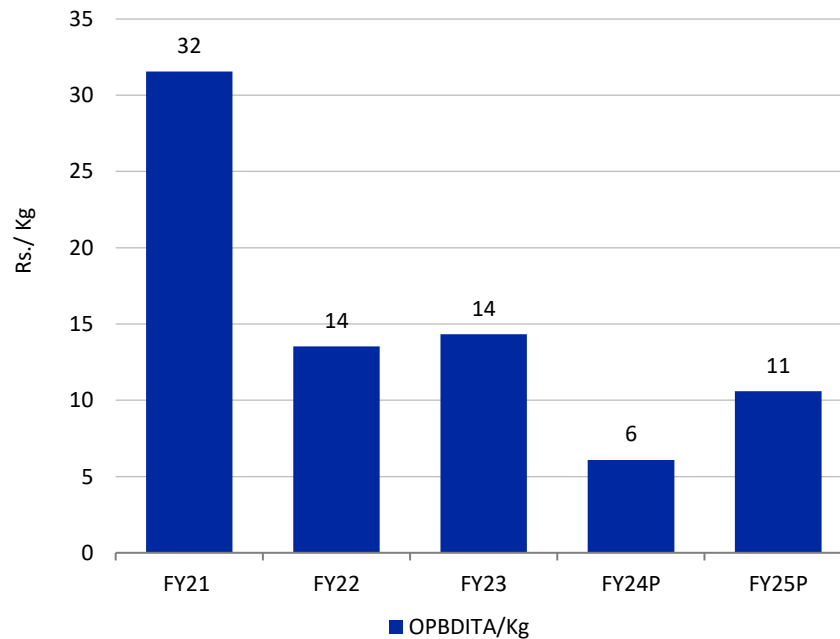
Between Rs. 15/Kg to Rs. 25/Kg



Negative Outlook

Less than Rs. 15/Kg

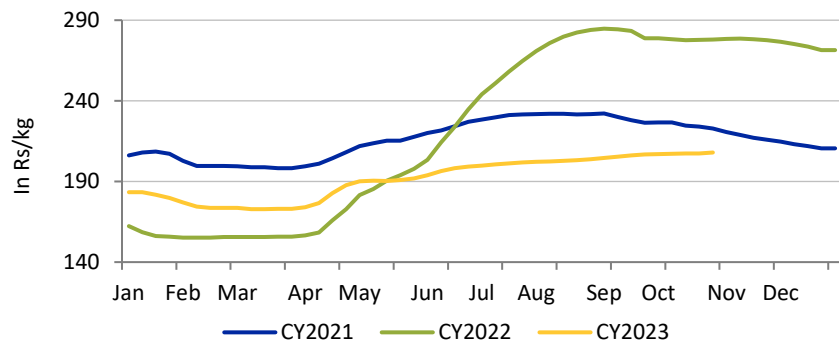
Trend in yearly movement of OPBDITA/ Kg



Source: ICRA Research, Based on aggregate of ICRA sample set of 13 entities

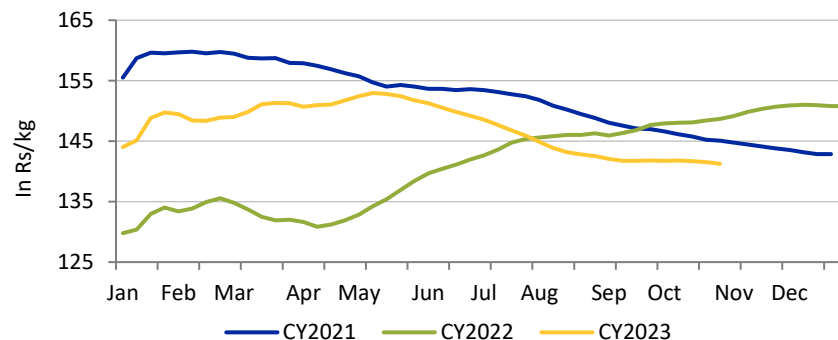
Sharp YoY drop in NI ODX prices; SI ODX prices witness limited decline

Exhibit: Trend in cumulative ODX auction prices in North India (in Rs./kg)



Source: ICRA Research

Exhibit: Trend in cumulative ODX auction prices in South India (in Rs./kg)

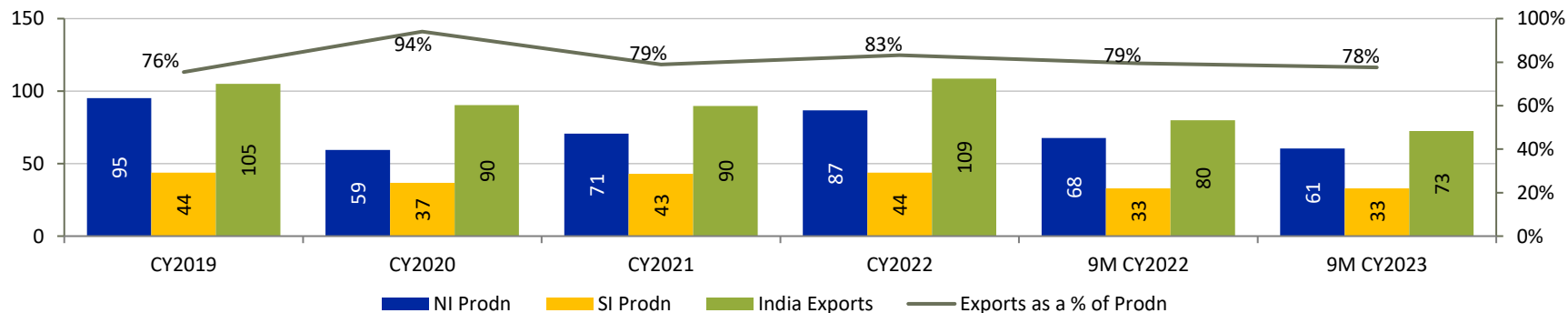


Source: ICRA Research

- The cumulative NI ODX auction price in 10M CY2023 declined sharply by ~Rs. 70/kg (~25%) on a YoY basis, on the back of lacklustre export demand, primarily because of stoppage of orders from Iran. On a YoY basis, the cumulative NI ODX prices in CY2023 remained moderately higher by ~Rs. 16/kg till April 2023, but the price differential turned negative from end-May 2023 and the gap widened thereafter.
- Cumulative SI ODX auction prices remained firm till May 2023, but slipped subsequently primarily due to a muted export demand for orthodox teas, which also affected the prices of NI ODX teas. Nevertheless, the extent of moderation in the cumulative SI ODX prices, on a YoY basis, has so far remained lower than the drop in NI ODX prices. In 10M CY2023, the cumulative SI ODX price declined by ~Rs. 7/kg (~5%).

Slowdown in ODX tea export in CY2023 due to lower demand from importing nations

Exhibit: ODX production trend vs. export (in Mkg)

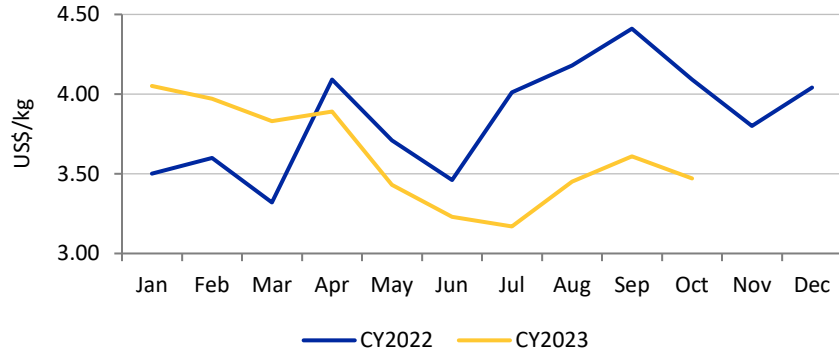


Source: ICRA Research

- Although ODX tea produced in India is primarily exported, the overall tea export from India during CY2013 to CY2020 comprised approximately 18% of the total production. However, the same dropped to less than 15% in CY2021 primarily due to an increase in the overall output, post the pandemic, besides an ~11% decline in CTC export.
- In CY2022, exports from India rose substantially (by ~15%) due to a surge in export of ODX tea (by ~21%) because of buoyant demand in the international market amid production loss in Sri Lanka, the main exporter of ODX teas in the global market.
- Due to non-remunerative prices, ODX tea production in 9M CY2023 moved down by ~7% on a YoY basis and in addition, during the same period export also declined by ~9%, primarily because of lower demand from importing nations.

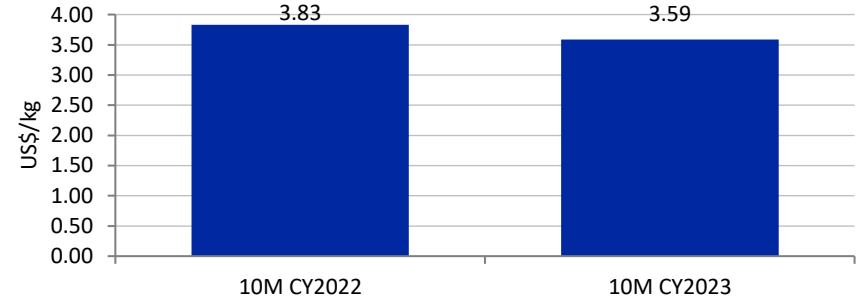
Sri Lanka, the largest ODX tea supplier in the global market, witnessed a lower price moderation compared to a sharp drop in North Indian auction prices

Exhibit: Trend in monthly prices in Sri Lanka (in USD/kg)



Source: ICRA Research

Exhibit: Cumulative prices in Sri Lanka (in USD/kg)

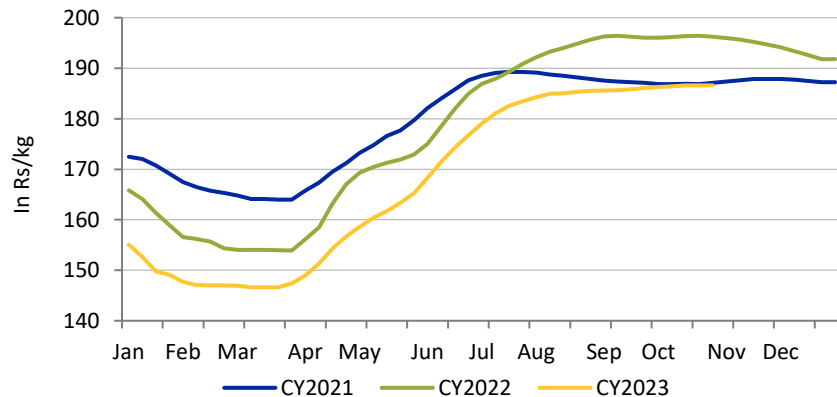


Source: ICRA Research

- Sri Lanka, mainly an ODX tea producer, is the largest supplier of ODX teas in the global market. Tea production in Sri Lanka in the current year has not registered any meaningful recovery from a historically low production level witnessed in CY2022, induced by a ban on fertiliser import and an economic crisis in the island nation. In 10M CY2023, the country's production rose marginally by ~2% compared to 10M CY2022. However, tea exports from the country declined by ~6% (11.9 mkg) in 10M CY2023 on a YoY basis, due to sluggish demand in the global market, leading to a drop in the cumulative tea prices in Sri Lanka by ~6% in 10M CY2023 compared to 10M CY2022.
- The drop in Sri Lankan tea prices, however, has remained far lower than the YoY price decline in NI ODX price (~25% drop in cumulative auction price in 10M CY2023). This may be partly attributed to an increase in offtake of Sri Lankan tea by some of the countries like Turkey, Russia, Chile, Saudi Arabia, Syria, etc. in the current year. On the other hand, there has been a significant drop in demand from Iran, the main importer of ODX tea from NI, adversely impacting NI ODX prices.

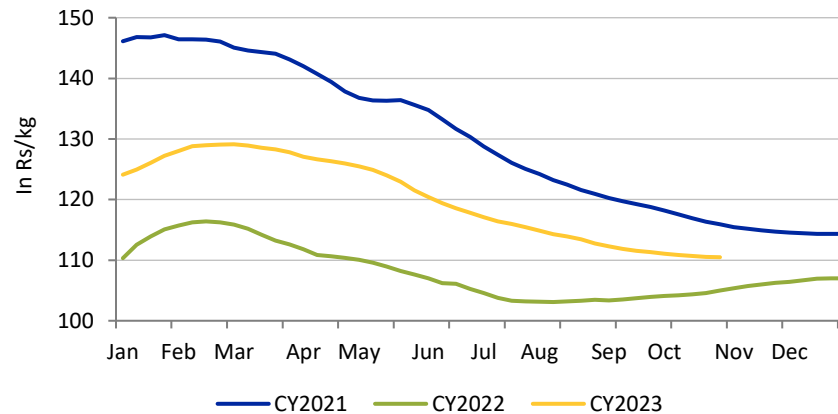
Moderate drop in NI CTC prices, but SI CTC prices rise in 10M CY2023 on a YoY basis

Exhibit: Trend in cumulative CTC auction prices in North India (in Rs./kg)



Source: ICRA Research

Exhibit: Trend in cumulative CTC auction prices in South India (in Rs./kg)

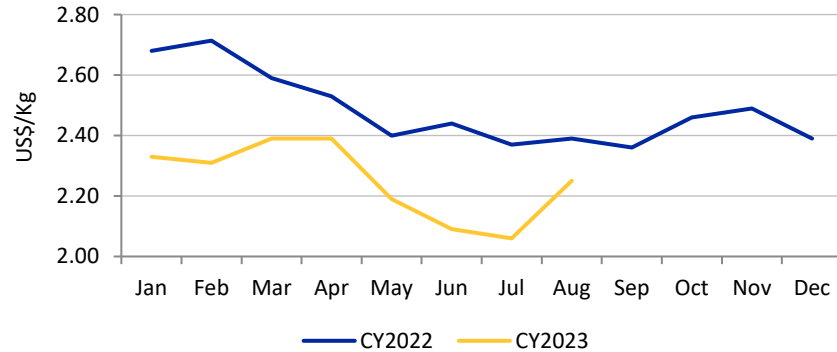


Source: ICRA Research

- The cumulative NI CTC auction price declined in 10M CY2023 on a YoY basis, however, the extent of the fall was moderate at ~Rs. 10/kg (~5%), compared to a sharp drop in NI ODX auction prices (by ~25%).
- SI CTC auction price, on a cumulative basis, improved by ~Rs. 6/kg (~5%) in 10M CY2023, in contrast to the trend in NI CTC teas. However, compared to 10M CY2021, the cumulative SI CTC price in 10M CY2023 remained lower by ~Rs. 5/kg (~5%).

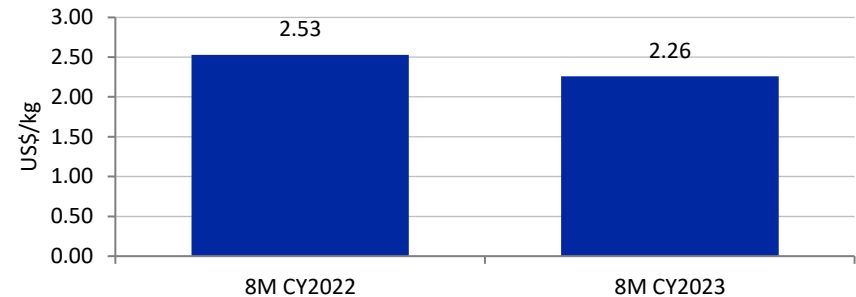
Auction prices in Kenya moderated on the back of a YoY dip in export by ~11% and increase in production by ~7% in 8M CY2023

Exhibit: Trend in monthly prices in Kenya (in USD/kg)



Source: ICRA Research

Exhibit: Cumulative prices in Kenya (in USD/kg)

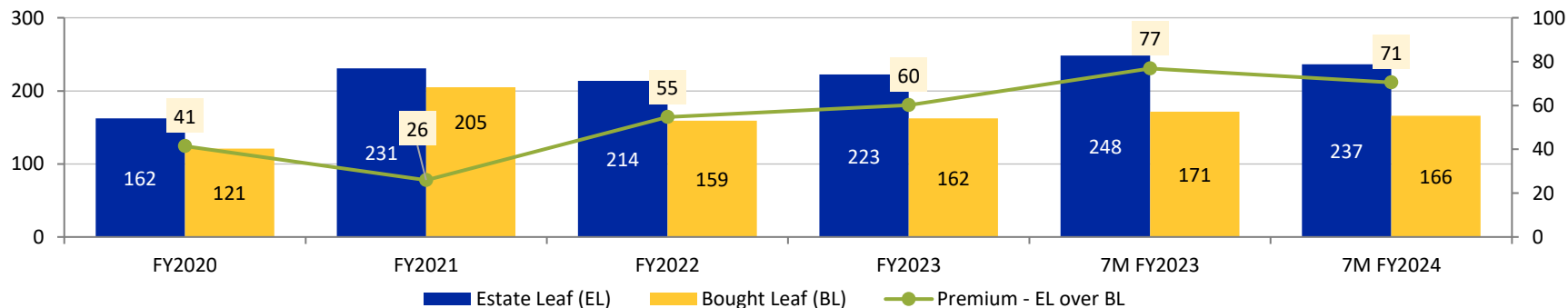


Source: ICRA Research

- Tea production in Kenya grew by ~7% in 8M CY2023 on a YoY basis, however, tea exports from the country contracted by ~11% in 8M CY2023 on a YoY basis on the back of a lacklustre demand from some of the key importing nations like Pakistan, Egypt, Sudan, Russia etc. on account of an economic slowdown and geo-political tensions.
- A rise in production and a decline in exports have kept the auction prices of Kenyan tea under pressure. The prices moderated significantly from May 2023. An uptick in the prices was witnessed in August 2023, however, the cumulative price in 8M CY2023 dropped by ~11% on a YoY basis. The same had a bearing on the CTC tea prices in the global market, with Kenya being the largest exporter of CTC tea.

Healthy price premium for CTC teas made from estate leaves over bought leaves

Exhibit: Trend in Assam Valley CTC tea prices made from estate leaf (EL) and bought leaf (BL) – in Rs./kg



Source: ICRA Research

- The demand for quality CTC teas has increased after the pandemic, leading to a consistent rise in the price premium for teas made from estate leaves over the prices of those made from bought leaves.
- In FY2022, prices of teas of all categories declined with a recovery in output after a significant loss witnessed in FY2021 due to the pandemic. However, the decline in bought leaf tea prices in FY2022 was sharper than tea produced from estate leaf, mainly due to increased demand for quality tea. The cumulative price differential between Assam Valley CTC teas made from estate leaf and bought leaf stood at Rs. 55/kg in FY2022 vis-à-vis Rs. 26/kg in FY2021. The price differential widened to Rs. 60/kg in FY2023. In 7M FY2024, the same moderated to some extent to Rs. 71/kg from Rs. 77/kg in 7M FY2023 due to a relatively higher drop in the prices of estate leaf teas compared to bought leaf teas; however, the price premium for estate leaf teas still remained healthy.

Reintroduction of 'English' auction system in NI is likely to lead to better price discovery

Salient features of English auction system



- Bids can be made till a lot is sold



- Division of lots is allowed enabling smaller buyers to participate in the bidding process

Salient features of Bharat auction system



- Bids are entered before the lots offered go live and no option to modify

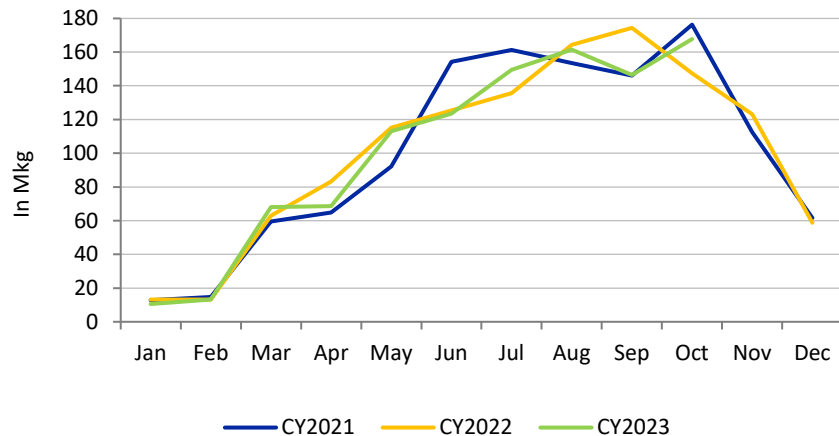


- Smaller buyers are not able to participate in the bidding process as division of lots are not allowed

- Introduction of the 'Bharat' auction system in North India auction centres from April 2023 is likely to have weighed on the auction prices in the current year.
- Based on the representations made by various stakeholders on the inefficient price discovery, under the 'Bharat' auction system, the Tea Board of India has reverted to the earlier 'English' auction system from November 2023.
- While the trend in prices in recent auctions, post the change, seems to be encouraging the long-term impact of the same remains to be seen.

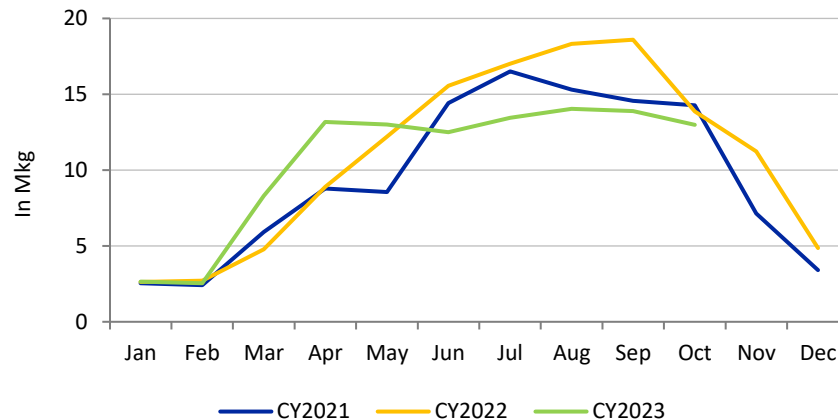
All-India bulk tea production to remain lower in CY2023 on a YoY basis, given the current trend

Exhibit: Trend in All India CTC production



Source: Tea Board of India, ICRA Research

Exhibit: Trend in All India ODX production

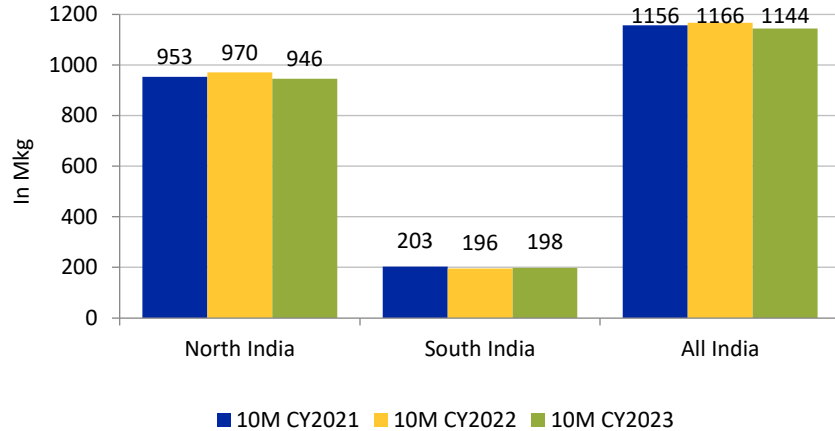


Source: Tea Board of India, ICRA Research

- All-India bulk tea production in 10M CY2023 declined by ~22 million Kg on a YoY basis, largely driven by a substantial lower output in September 2023 in YoY terms. In September 2023, all-India production of CTC fell by ~16% while that of ODX fell by ~25%.
- Despite some improvement witnessed in October 2023, all-India bulk tea production in CY2023 is likely to remain lower compared to CY2022, given the current trend.

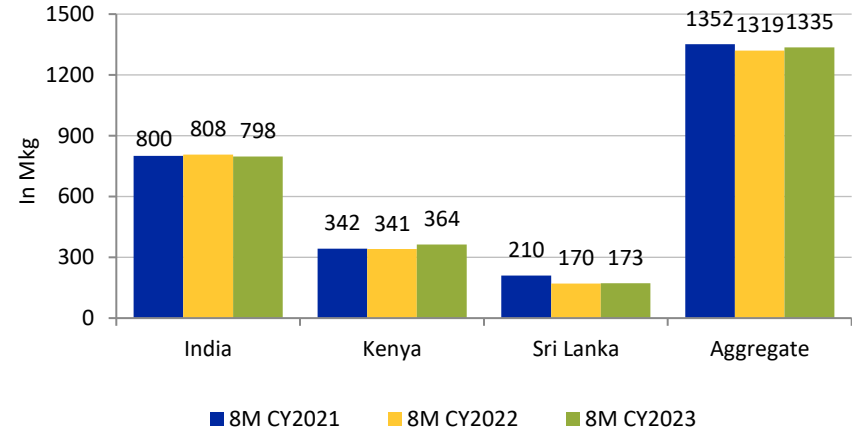
Global black tea production till 8M CY2023 up ~1% on a YoY basis due to higher output in Kenya

Exhibit: Indian Tea Production



Source: Tea Board of India, ICRA Research

Exhibit: Tea Production of India, Kenya & Sri Lanka in Jan-Jun (CY2021 to CY2023)

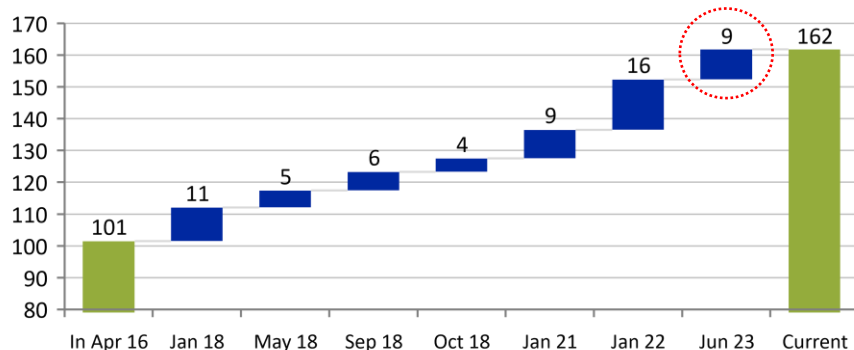


Source: Tea Board of India, Sri Lanka and Kenya, ICRA Research

- All India bulk tea production in 10M CY2023 dropped by ~2%, due to lower production in North India.
- In Kenya, tea production, in 8M CY2023, grew by ~7%, on a YoY basis, resulting in a ~1% increase in global black tea production.
- Sri Lankan tea production in 8M CY2022 witnessed a significant drop of ~19% to 170 Mkg on a YoY basis due to the adverse political and economic scenario in the country. There has not been any meaningful recovery in the current year as well.
- Indian tea production in 8M CY2023 marginally declined by ~9 Mkg (~1%) on a YoY basis.

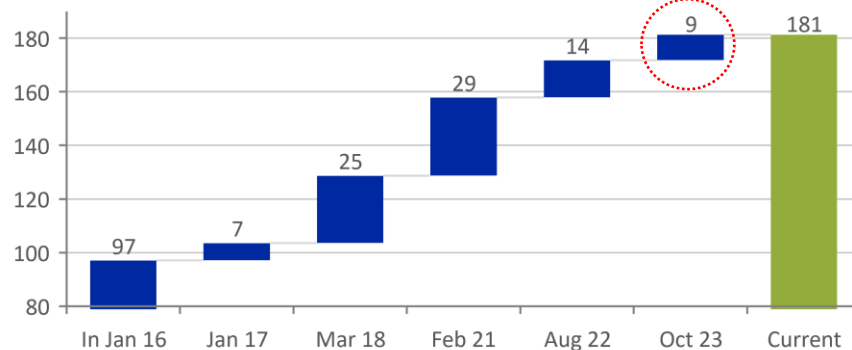
Wage rate hike to impact the margin for tea estates in NI in FY2024

Exhibit: Wage cost increase trajectory in West Bengal (in Rs./kg of tea)



Source: ICRA Research

Exhibit: Wage cost increase trajectory in Assam valley (in Rs./kg of tea)

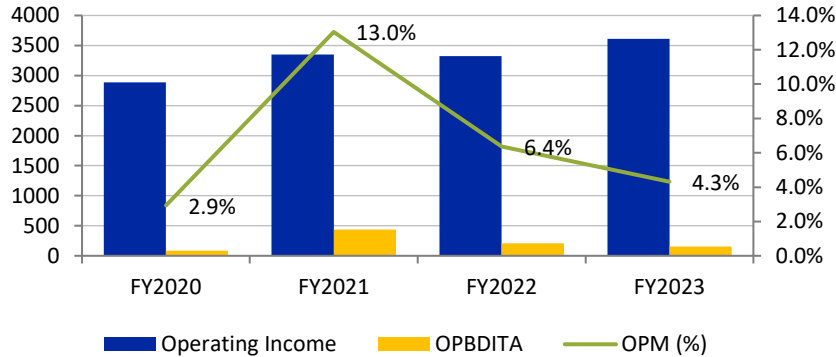


Source: ICRA Research

- The basic daily wages of the tea estate workers in West Bengal and Assam have moved up by Rs. 18 to Rs. 250, as a part of a long-term wage settlement, effective from June 01, 2023 and October 1, 2023, respectively. With an 8% increase in the basic wage rate, the total wage per day (including other benefits) has increased by around 6% in West Bengal and Assam.
- The overall wage cost per kg of tea is likely to rise by around Rs. 9/kg in view of the wage hike in both West Bengal and Assam. This may escalate the margin pressure for the tea estates based in North India, given a moderation in prices in the current year. However, the impact of wage rate hike in the current fiscal will be lower for the tea estates in Assam as the wage hike in Assam has come into effect after a gap of four months, post the wage hike in West Bengal.

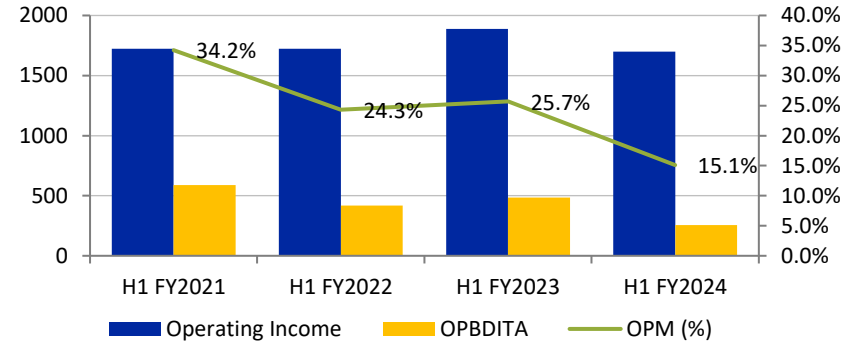
Decline in operating margin in H1 FY2024 due to muted realisation and hike in wage rate; full-year margin likely to compress compared to FY2023

Exhibit: Trend in yearly result of nine listed bulk tea players



Source: BSE, NSE, ICRA Research

Exhibit: Trend in H1 result of nine listed bulk tea players

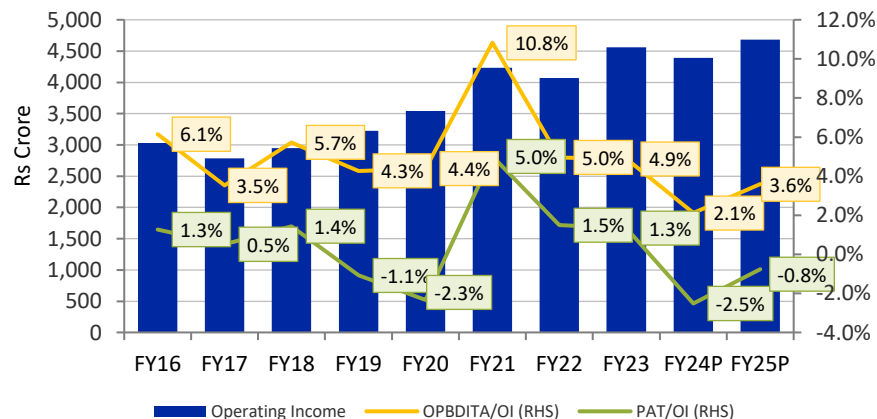


Source: BSE, NSE, ICRA Research

- Despite an improvement in the overall realisation of tea, a sharp hike in the wage rate in North India led to a decline in the operating margin (OPM) to 4.3% in FY2023 from 6.4% in FY2022.
- An increase in the wage rate and a fall in tea realisation, particularly ODX tea, resulted in a drop in the operating profits during H1 FY2024.
- The OPM in H1 FY2024 was lower by ~1,059 bps compared to H1 FY2023, while the same was lower by ~918 bps compared to H1 FY2022.
- Muted realisation along with a wage hike in West Bengal and Assam, effective from June 2023 and October 2023 respectively, would lead to a significant moderation in the OPM in FY2024 over FY2023.

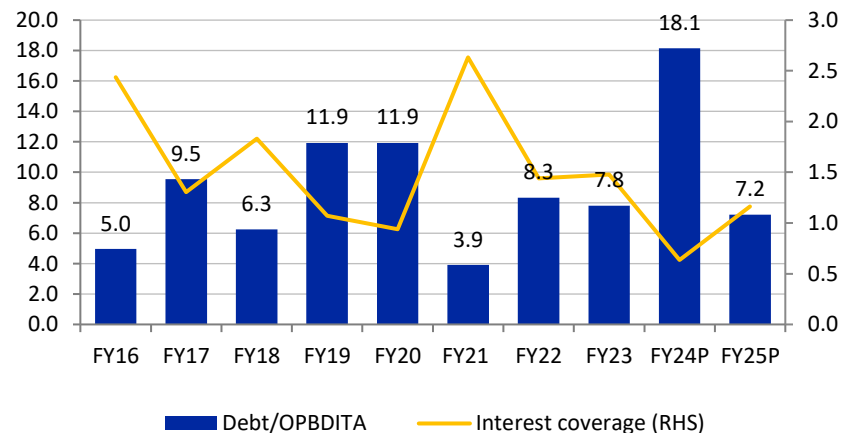
Expected performance of ICRA's sample set

Trend in revenue growth and margins



Source: ICRA Research, Based on aggregate of ICRA sample set of 13 entities

Trend in coverage metrics

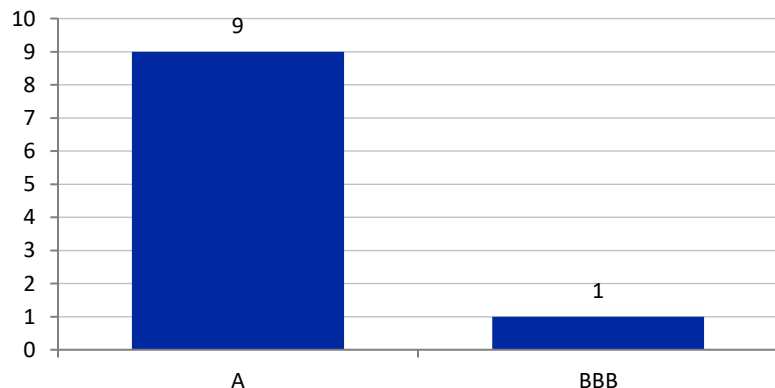


Source: ICRA Research, Based on aggregate of ICRA sample set of 13 entities

- Lower production and increase in realisation led to a significant increase in the OPM to ~11% in FY2021. The same witnessed a decline in the subsequent years and is expected to weaken further to ~2% in FY2024 driven by the drop in realisation and increase in wage cost. The NPM is expected to remain negative in FY2024 and FY2025.
- Interest coverage and Debt/ OPBDITA, which improved substantially in FY2021, are likely to deteriorate in FY2024 and FY2025.

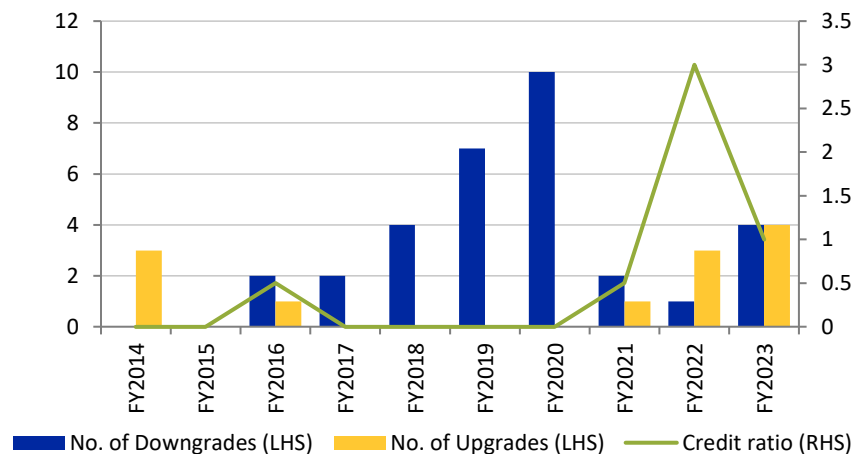
Credit rating movements in bulk tea sector

Exhibit: Rating Distribution of Bulk tea Industry



Source: ICRA Research

Exhibit: Trend In Credit Ratio



- All the entities rated by ICRA in the bulk tea sector are in the investment grade category, with 90% being in the A category and only 10% in the BBB category.
- ICRA's overall credit ratio declined to 1 times in FY2023 from 3 times in FY2022. All the four downgrades in FY2023 belonged to one group. The credit ratio of ICRA's rated portfolio of bulk tea remained low over the past years, except FY2022, owing to the challenging environment in the sector.



Key upgrades during FY2023:

- **Luxmi Tea Company Private Limited** from [ICRA]A/Stable/[ICRA]A1 to [ICRA]A+/Stable/[ICRA]A1 on account of significant growth in the consolidated revenues of the Group along with comfortable profitability, resulting in healthy cash accruals and improving debt coverage metrics
- **M. K. Shah Exports Limited** from [ICRA]A-/Stable/[ICRA]A2+ to [ICRA]A/Stable/[ICRA]A1 due to improvement in MKSEL's consolidated profitability and cash accruals, supported by buoyant realisations and a significant increase in its tea production.
- **The Jorehaut Group Limited** from [ICRA]BBB+/Stable/[ICRA]A2+ to [ICRA]A-/Stable/[ICRA]A2+ considering the consistent healthy performance of the company in terms of profits, return indicators, capital structure and coverage indicators.
- **Hasimara Industries Limited** from [ICRA]B/Stable to [ICRA]BB-/Stable on account of improvement in the financial performance driven by a significant increase in the tea prices, translating into a sharp rise in profitability, cash accruals and debt coverage metrics.



Key downgrades during FY2023:

- **Goodricke Group Ltd** from [ICRA]AA-/Stable/[ICRA]A1+ to [ICRA]A+/Stable/[ICRA]A1 on account of significant rise in wage and other input costs along with moderation in yields, which are likely to keep the consolidated profits and cash flows of the Group under pressure.
- **Amgoorie India Ltd** from [ICRA]A+/Stable/[ICRA]A1 to [ICRA]A/Stable/[ICRA]A1 due to moderation in the credit profile of the Goodricke Group.
- **Stewart Holl (India) Ltd** from [ICRA]A+/Stable/[ICRA]A1+ to [ICRA]A/Stable/[ICRA]A1 due to moderation in the credit profile of the Goodricke Group.
- **Koomber Tea Company Pvt Ltd** from [ICRA]A+/Stable/[ICRA]A1 to [ICRA]A/Stable/[ICRA]A1 due to moderation in the credit profile of the Goodricke Group.



Key upgrades during
FY2024:

- Not applicable



Key downgrades during
FY2024:

- **Goodricke Group Ltd** from [ICRA]A+/Stable/[ICRA]A1+ to [ICRA]A/Stable/[ICRA]A2+ on account of significant rise in wage rates along with drop in realisation, which are likely to keep the consolidated profits and cash flows of the Group under pressure.
- **Amgoorie India Ltd** from [ICRA]A/Stable/[ICRA]A1 to [ICRA]A-/Stable/[ICRA]A2+ due to moderation in the credit profile of the Goodricke Group.
- **Stewart Holl (India) Ltd** from [ICRA]A/Stable/[ICRA]A1 to [ICRA]A-/Stable/[ICRA]A2+ due to moderation in the credit profile of the Goodricke Group.
- **Koomber Tea Company Pvt Ltd** from [ICRA]A/Stable/[ICRA]A1 to [ICRA]A-/Stable/[ICRA]A2+ due to moderation in the credit profile of the Goodricke Group.



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