

INDIAN BULK TEA INDUSTRY

**Proposed wage hike in West Bengal
to escalate margin pressure for tea
estates in the state**

MAY 2023





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The proposed hike in the basic wage rate for tea estate workers in West Bengal by ~8%, effective June 1, 2023, is estimated to increase the total wage cost (including bonus, other cash components and benefits) per day by ~6%.

As per ICRA estimates, the cost of production is likely to increase by ~Rs. 9/kg, which would have a negative impact on the margins of tea estates located in West Bengal.



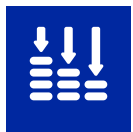
- **Quantum and effective date of proposed wage hike:** On April 27, 2023, the West Bengal Government's Labour Department came out with an advisory to increase the basic wage of tea estate workers in the state by 8% to Rs. 250/day from Rs. 232/day, with effect from June 01, 2023.



- **Trend in tea price vis-à-vis wage cost:** Tea players benefited in CY2020 due to a sharp rise in realisations post-pandemic in the absence of any wage hike. The increase in wage cost in North India (NI) and moderation in tea prices impacted the margins in CY2021. Further increase in wage cost in CY2022 exerted pressure on the cost structure despite a moderate improvement in realisations.



- **Rate hikes gave rise to cost pressures:** In CY2022, NI auction prices increased by ~6% on the back of supply shortage due to crop loss in Sri Lanka, aiding recovery in the profitability of domestic tea growers. However, cost pressures emerged after West Bengal and Assam hiked the basic wage rates by 15% and 13% from January 2022 and August 2022, respectively. In view of the proposed wage rate hike in West Bengal w.e.f. June 2023 and a flattish trend in tea prices, the profitability of the tea players in West Bengal would come under pressure.



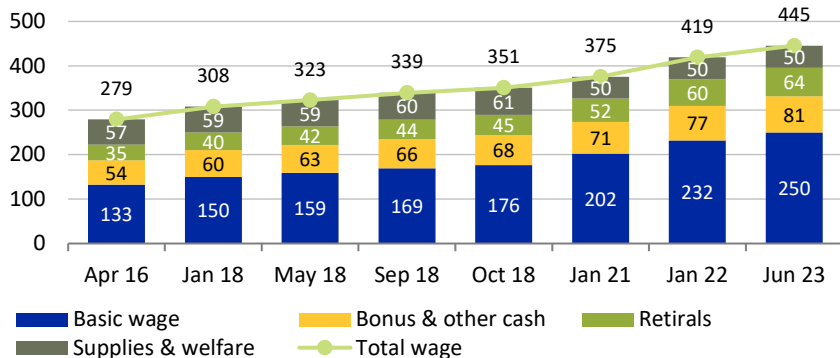
- **Estimated impact on cost of production and margins:** The cost of production for tea manufacturers in West Bengal is slated to increase by around Rs. 9/kg as a result of the wage revision. This is likely to reduce the operating margin of the West Bengal-based players by around 500 basis points at a steady state level of realisations.



- **Overall impact on the financial performance of the ICRA-rated portfolio:** The impact of the increase in the cost of production for the West Bengal-based estates on the overall financial performance of the ICRA-rated portfolio is estimated to be moderate because of the relatively low share of production from West Bengal. However, historically, wage rates in West Bengal and Assam have moved in tandem. In case there is a wage revision in Assam in the near term, the profitability of NI bulk tea companies, including ICRA-rated entities, will be materially impacted.

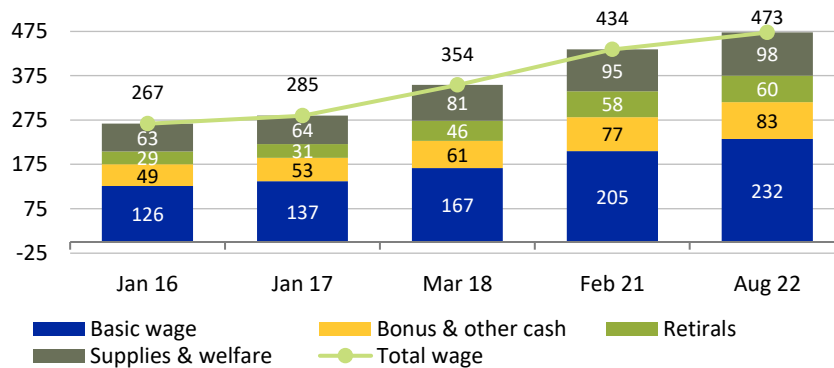
Wage rates in West Bengal and Assam moved almost concurrently in the past

Exhibit: Composite wage rate trend in West Bengal (in Rs./man-day)



Source: ICRA Research

Exhibit: Composite wage rate trend in Assam valley (in Rs./man-day)

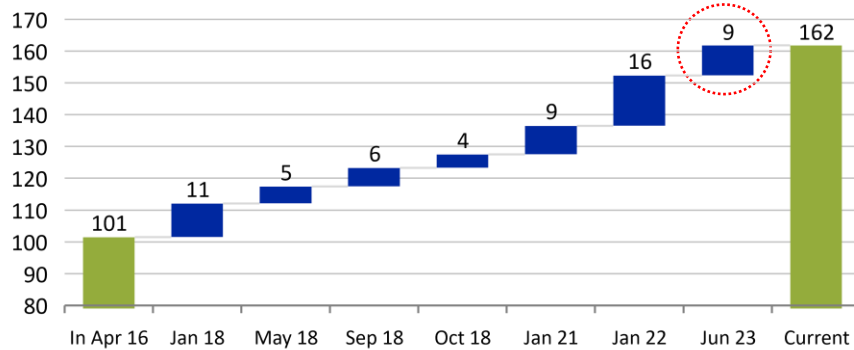


Source: ICRA Research

- Apart from daily cash wages, tea workers receive a host of other benefits, such as housing and medical facilities, ration, firewood etc. Considering these facilities and other benefits viz. bonus, provident fund, gratuity and leave with pay, the total wage per day, as per ICRA estimates, works out to around Rs. 445 for West Bengal and Rs. 473 for Assam valley, at present.
- The wage rates in West Bengal and Assam, the two largest tea-producing states, have remained aligned historically. In 2018, there were frequent but smaller interim wage rate hikes in West Bengal, while a larger one-time hike happened in Assam. Both West Bengal and Assam hiked the basic wage rates by 15% and 13% from January 2022 and August 2022, respectively. The total wage rate in West Bengal after the proposed hike (w.e.f. June 2023) will still be somewhat lower than the rate in Assam.

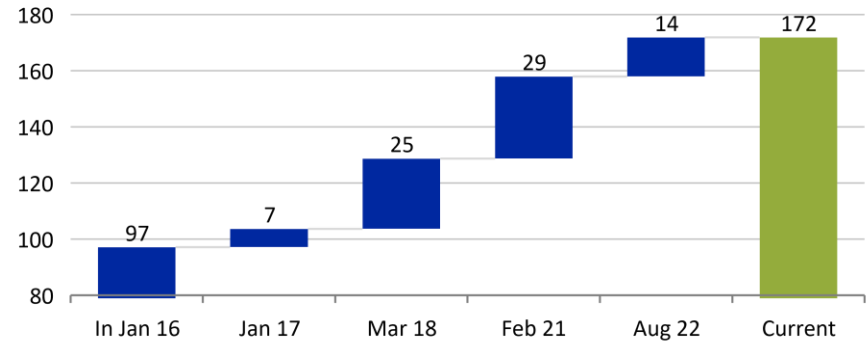
Proposed wage hike in West Bengal likely to increase cost of production by ~Rs. 9/kg of tea

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)

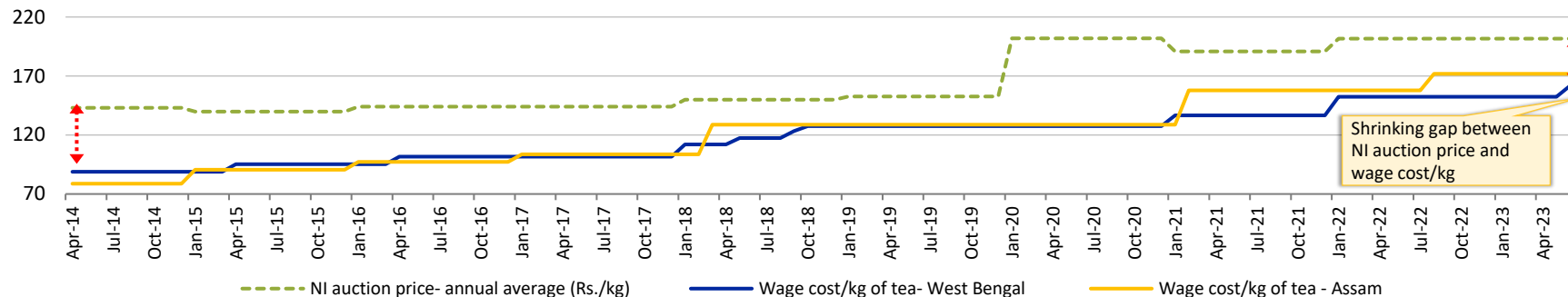


Source: ICRA Research

- The basic daily wage of the tea estate workers in West Bengal is proposed to be increased by Rs. 18 to Rs. 250, as a part of a long-term wage settlement, effective from June 01, 2023, pending finalisation of the revision in minimum wages.
- With the proposed 8% increase in the basic wage rate, the total wage per day (including other benefits) in West Bengal is estimated to increase by around 6%.
- The overall wage cost per kg of tea is estimated to increase by around Rs. 9/kg in view of the proposed wage hike. Nevertheless, the estimated wage cost per kg of tea in West Bengal still remains lower than Assam.

Wage rate hike outpaced realisation growth in recent years

Exhibit: Trend in NI auction prices (annual average) vis-à-vis wage cost (per kg of tea) in West Bengal and Assam valley

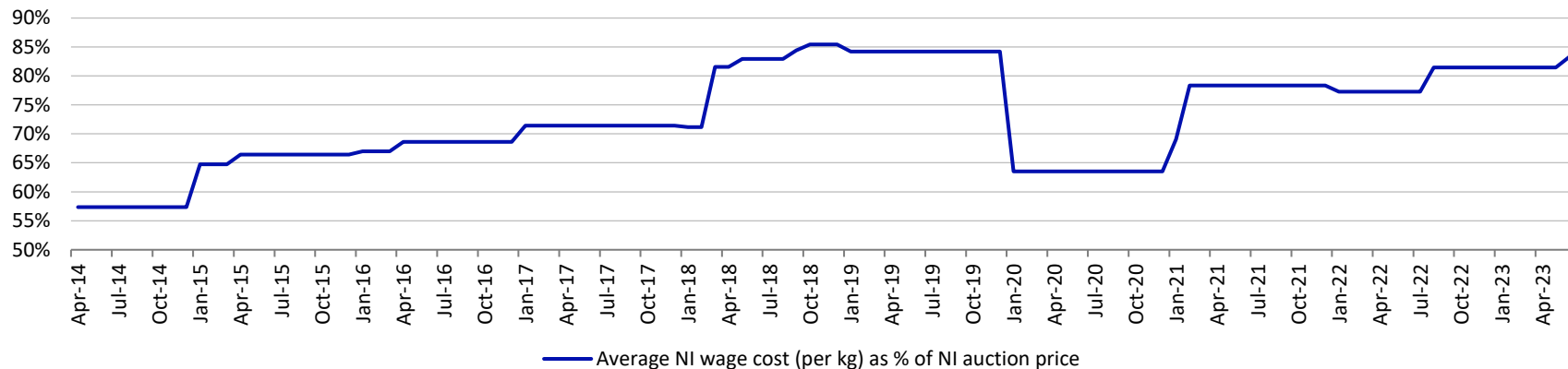


Source: ICRA Research

- The total wage per man day in West Bengal and Assam increased at a CAGR of 7% and 10%, respectively, during CY2014-CY2019, which continued to squeeze the margins of the tea players as the average NI auction prices remained stagnant during the same period, with a CAGR of only 1%.
- In CY2020, tea prices increased sharply following the production disruption due to the pandemic, but the wage rates remained unchanged, benefitting the tea players. However, a moderation in tea prices coupled with the increase in wage rates both in West Bengal and Assam in CY2021 exerted pressure on tea producers' cost structure. In CY2022, NI auction prices increased by 6%, primarily on the back of supply-shortage due to production loss in Sri Lanka because of political unrest, aiding recovery in the profitability of tea players. However, cost pressures emerged after West Bengal and Assam hiked the basic wage rates by 15% and 13% from January 2022 and August 2022, respectively.
- The proposed wage rate hike, if implemented, and a flattish trend in tea prices would lead to further pressure on the operating margins of the tea players in West Bengal.

West Bengal-based players may witness around 500 basis point margin contraction

Exhibit: Average NI wage cost (per kg) as % of NI auction price

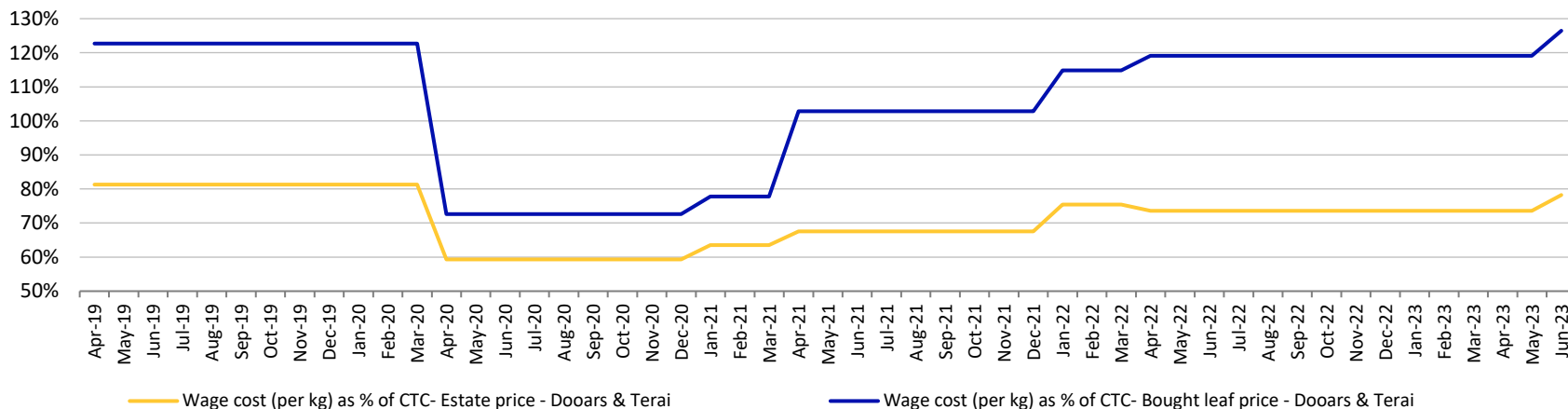


Source: ICRA Research

- At present (before the proposed increase), the weighted average wage cost per Kg of tea (of both Assam and West Bengal) as a percentage of annual NI auction price (taking the current year price at par with CY2022) is at a high level of around 81%. For West Bengal, the ratio stood at ~84% for FY2023. The proposed increase in West Bengal's wage cost, effective June 2023, would result in a significant 500 basis point decline in margin (based on an average of both estate and bought leaf teas), unless there is a commensurate improvement in realisations.
- A sharp rise in tea prices after the pandemic led to a significant decline in the above-mentioned ratio to 64% from 84% prior to the pandemic. However, the subsequent normalisation in tea prices coupled with the multiple wage hikes in both West Bengal (from Jan-21 and Jan-22) and Assam (from Feb-21 and Aug-22) have exerted pressure on the cost structure of the tea producers.

Top-quality tea producers less vulnerable to impact of wage hike

Exhibit: Wage cost (per kg) in West Bengal as % of yearly (FY) CTC price in the Dooars & Terai region- Estate leaf vs bought leaf



Source: ICRA Research, Contemporary Brokers

- The impact of the wage rate hikes on quality tea producers has been somewhat limited, with wage costs at ~74% when only estate leaf teas are considered. Nonetheless, even for those teas, the wage costs, as a percentage of realisations, are also likely to witness a material increase. Moreover, the proportion of top quality teas is only 10-15% of the overall production and may not be representative of the overall industry.



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Analytical Contact Details

Name	Designation	Email	Contact Number
Jayanta Roy	Senior Vice-President	jayanta@icraindia.com	033 7150 1120
Kaushik Das	Vice-President	kaushikd@icraindia.com	033 7150 1104
Sujoy Saha	Vice-President	sujoy.saha@icraindia.com	033 7150 1184
Sovanlal Biswas	Assistant Vice-President	sovanlal.biswas@icraindia.com	033 7150 1181
Sandipan Das	Assistant Vice-President	sandipan.das@icraindia.com	033 7150 1190





ICRA

Business Development/Media Contact Details

Name	Designation	Email	Contact Number
L Shivakumar	Chief Business Officer	shivakumar@icraindia.com	022-61693304
Neha Agarwal	Head – Research Sales	neha.agarwal@icraindia.com	022-61693338
Rohit Gupta	Head Business Development - Infrastructure Sector	rohitg@icraindia.com	0124-4545340
Vivek Bhalla	Head Business Development - Financial Sector	vivek.bhalla@icraindia.com	022-61693372
Vipin Saboo	Head Business Development – Corporate Sector - West & East	vipin.saboo@icraindia.com	022-61693348
Shivam Bhatia	Head Business Development – Corporate Sector - North & South	shivam.bhatia@icraindia.com	0124-4545803
Naznin Prodhani	Head – Media & Communications	communications@icraindia.com	0124-4545860





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