

INDIAN BULK TEA INDUSTRY

Drop in orthodox tea price and a wage rate hike in West Bengal to intensify margin pressure for tea estates in North India

SEPTEMBER 2023





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Low export demand, particularly from Iran, has led to a sharp decline in orthodox (ODX) tea prices in the current calendar year. However, crush-tear-curl (CTC) tea prices are largely ruling at the last year's level. The impact of ODX price drop on the weighted average realisations of bulk tea players is expected to be limited. However, an increase in wage rates for NI-based players is likely to result in margin pressure.



- All-India cumulative auction average of orthodox (ODX) tea in 8M CY2023 declined significantly by ~21% (Rs. 50/Kg) on a YoY basis. This was primarily driven by a sharp drop in the North India (NI) ODX tea prices by ~27% (Rs. 76/kg). South India (SI) ODX tea also witnessed a price fall, but the same was limited to only ~3% (Rs. 4/kg). The price fell on the back of lower export demand, primarily from Iran, which is reportedly sourcing a large part of its requirement from Sri Lanka.



- On the contrary, prices of all-India crush-tear-curl (CTC) tea witnessed a marginal decline of ~2% (Rs. ~4/Kg) in 8M CY2023 on a YoY basis on the back of continued healthy domestic demand. No material deviation in all-India CTC tea prices is expected in CY2023 as production is likely to remain flat.



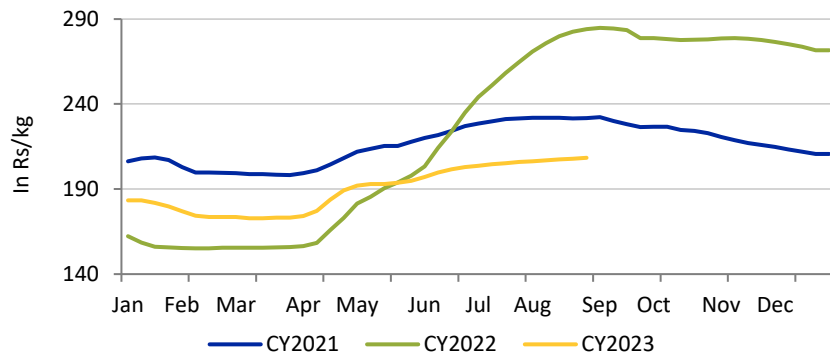
- Given the current production trend, no material increase in black tea output is likely in India and Kenya in CY2023 vis-à-vis CY2022. Although monthly production in Sri Lanka has been moderately higher on a YoY basis since April 2023, a meaningful recovery in the same is unlikely in CY2023 over CY2022 and the same would still remain materially lower than the CY2019 level.



- West Bengal (WB) has hiked the wage rate, effective June 2023. Given the historical trend, Assam is also likely to follow suit shortly although the impact of the same would be limited in FY2024. The operating margin of NI-based bulk tea players of the ICRA sample set in FY2024 is likely to contract by ~250 basis points on the back of an increase in cost due to wage rate hike and a sharp decline in ODX prices, notwithstanding the low (~8%) share of ODX in NI production. Also, ICRA expects some traction in the export demand of ODX teas in the coming months, which is likely to reduce the YoY price gap.

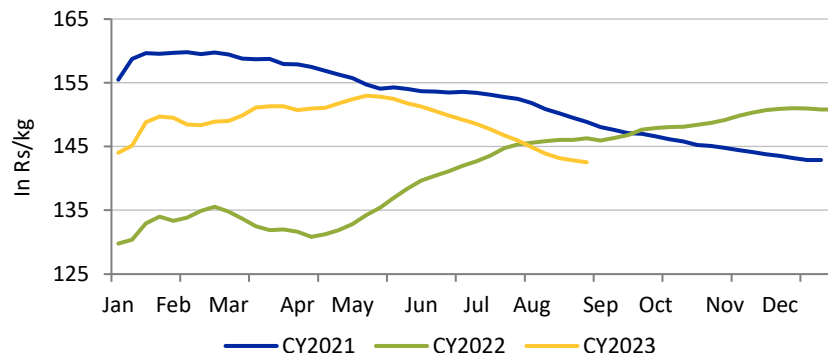
Sharp YoY drop in NI ODX prices, but SI ODX prices witness limited decline

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)

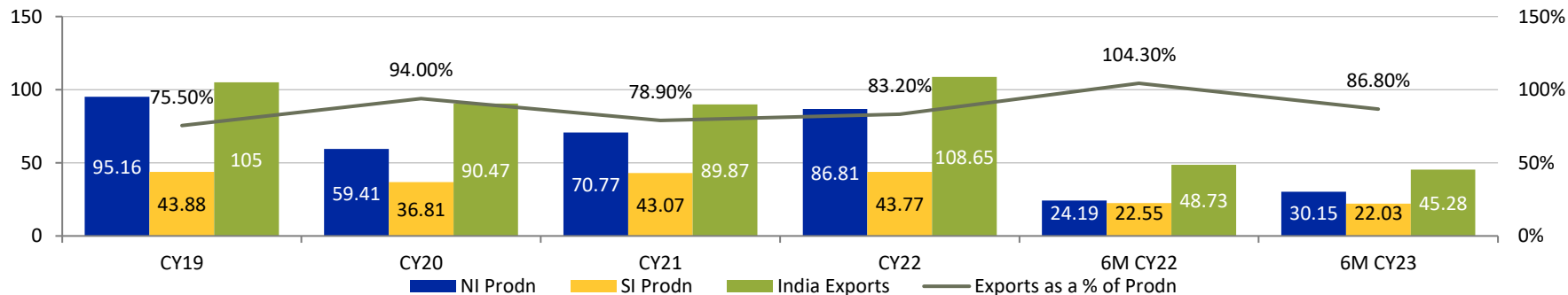


Source: ICRA Research

- The cumulative NI ODX auction price in 8M CY2023 declined sharply by ~Rs. 76/kg (~27%) on a YoY basis, on the back of lacklustre export demand, primarily because of stoppage of orders from Iran, which is reportedly sourcing a large part of its requirement from Sri Lanka. On a YoY basis, the cumulative NI ODX price 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. Nevertheless, given no signs of a meaningful recovery in production in Sri Lanka, and the likely uptick in export demand in the coming months, the YoY gap for NI ODX auction prices may reduce, going forward, from the current level.
- 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 8M CY2023, the cumulative SI ODX price declined by ~Rs. 4/kg (~3%).

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

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

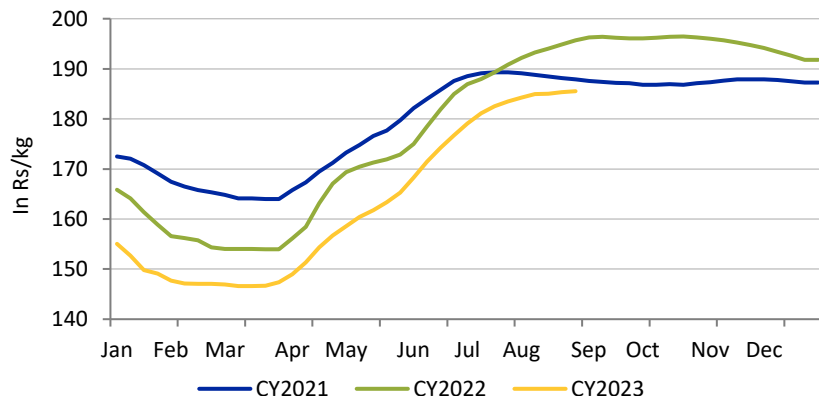


Source: ICRA Research

- 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, export 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.
- While ODX tea production in 6M CY2023 moved up by 12% on a YoY basis, ODX tea export has declined by ~7% during the same period, primarily because of lower demand from importing nations, impacting ODX tea realisation.

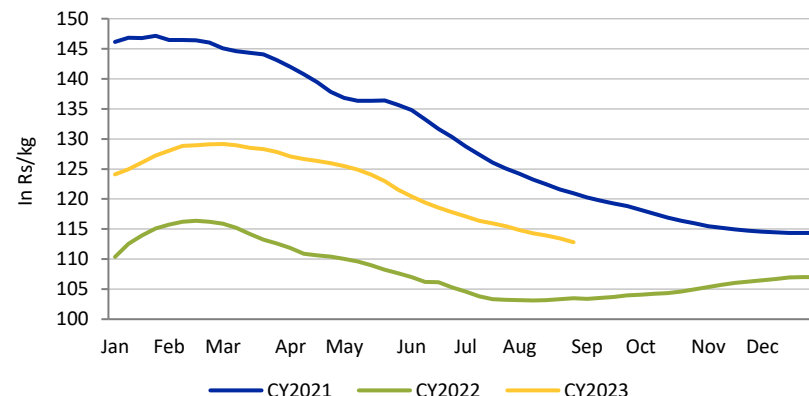
Moderate drop in NI CTC prices, but SI CTC prices rise in 8M CY2023 on a YoY basis

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)

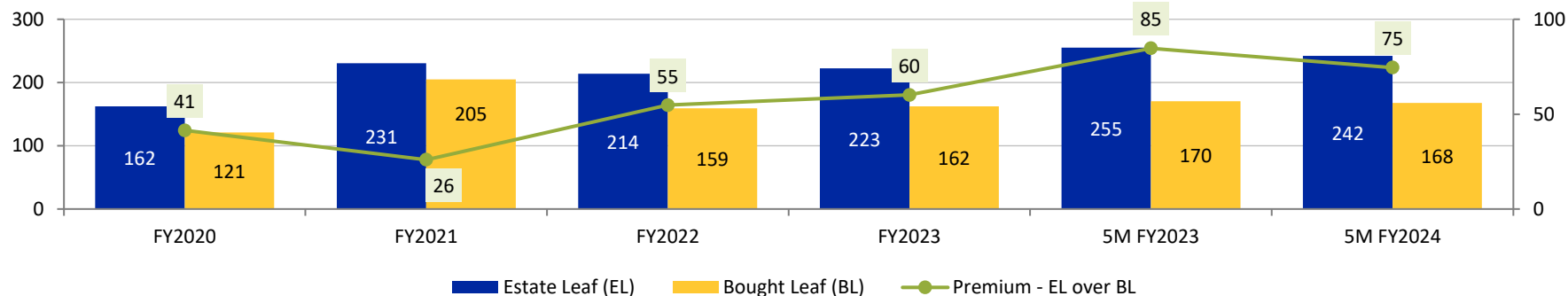


Source: ICRA Research

- The cumulative NI CTC auction price declined in 8M CY2023 on a YoY basis, however, the extent of fall was moderate at ~Rs. 10/kg (~5%), compared to a sharp drop in NI ODX auction prices (by ~27%).
- SI CTC auction price, on a cumulative basis, improved by ~Rs. 9/kg (~9%) in 8M CY2023, in contrary to the trend in NI CTC teas. However, compared to 8M CY2021, the cumulative SI CTC price in 8M CY2023 remained lower by ~Rs. 8/kg (~7%).

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

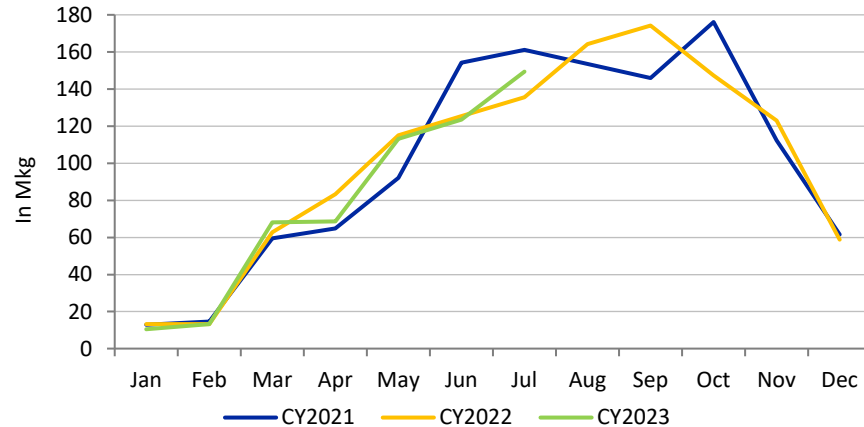


Source: ICRA Research

- 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 teas made from bought leaves.
- In FY2022, prices of teas of all categories declined with a recovery in output after a significant loss was 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 5M FY2024, the same moderated to Rs. 75/kg from Rs. 85/kg in 5M 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.

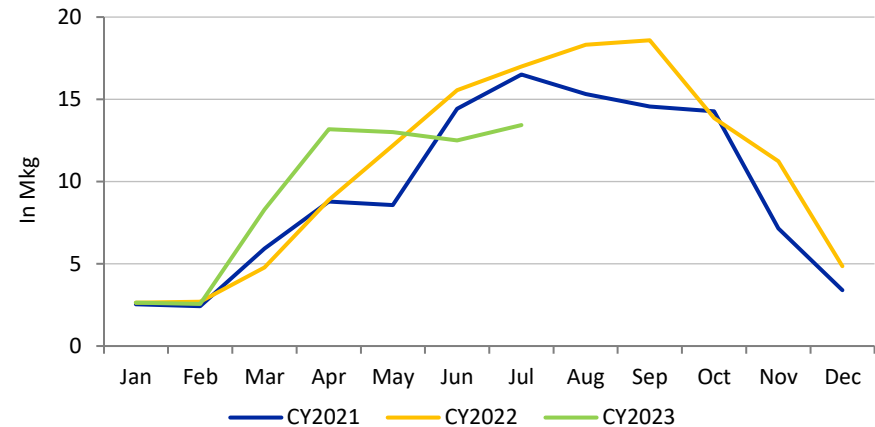
All India bulk tea production to remain largely flat in CY2023 on a YoY basis, given the current trend

Exhibit: Trend in All India ODX production



Source: Tea Board of India, ICRA Research

Exhibit: Trend in All India CTC production

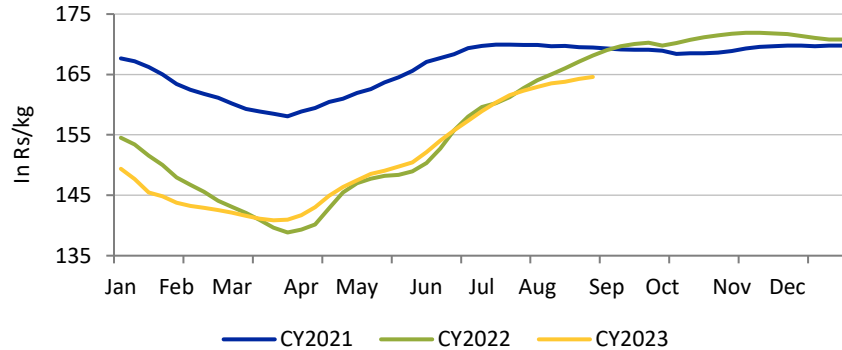


Source: Tea Board of India, ICRA Research

- All India bulk tea production in 7M CY2023 was down by ~2 million Kg on a YoY basis despite a substantial higher output in July 2023 vis-a-vis July 2022. In July 2023, all India production of CTC rose by ~10% but that of ODX fell by ~21% as there has been a partial shift from ODX to CTC production due to the former's unremunerative prices.
- All India bulk tea production in CY2023 is likely to remain largely flat, given the current trend; although CTC output may witness a marginal uptick.

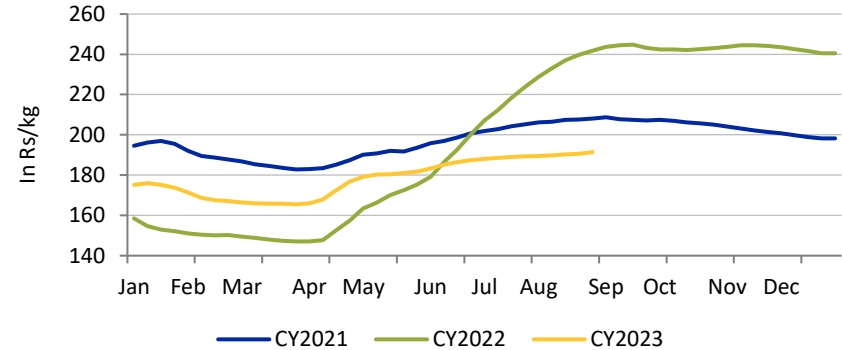
Sluggish all-India ODX prices resemble the trend in NI ODX prices, but all-India CTC prices remain relatively resilient in 8M CY2023

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



Source: ICRA Research

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

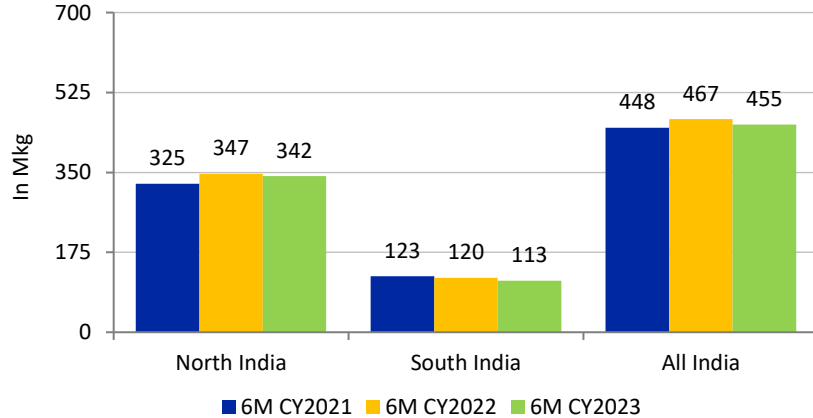


Source: ICRA Research

- All-India tea auction prices are largely influenced by the NI auction prices, as NI accounts for ~83% of the total tea produced in the country.
- All-India ODX auction prices, on a cumulative basis, replicated the trend witnessed for NI ODX prices and remained significantly lower by ~Rs. 50/kg (~21%) on a YoY basis, with a widening YoY price differential continuing from June 2023.
- The cumulative all-India CTC prices, however, have remained resilient in the current year, almost in line with CY2022 prices. In 8M CY2023, the cumulative all-India CTC auction price stood marginally lower by ~Rs. 4/kg (~2%) over 8M CY2022. Higher SI CTC prices on a YoY basis supported the all-India CTC prices to some extent, resulting in a lower YoY decline in all-India CTC prices than NI CTC prices.

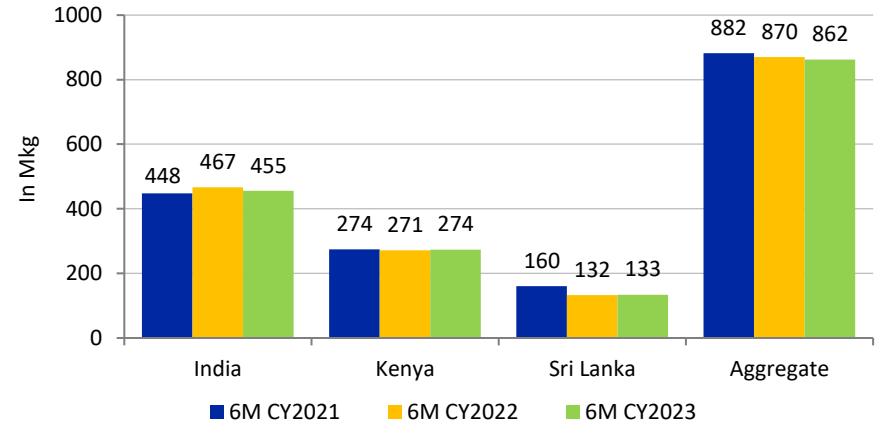
Global black tea production till 6M CY2023 dips ~1% on a YoY basis due to lower output in India

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)

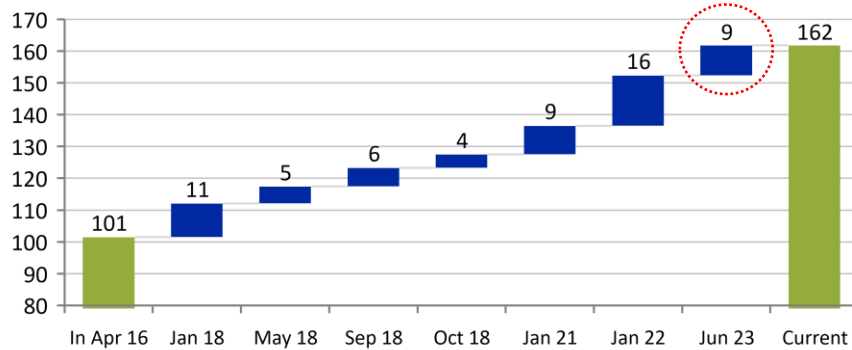


Source: Tea Board of India, Sri Lanka and Kenya, ICRA Research

- In India, tea production, in 6M CY2023, fell by ~2%, on a YoY basis, resulting in a ~1% decline in global black tea production.
- Sri Lankan tea production in 6M CY2022 witnessed a significant drop of ~17% to 132 Mkg on a YoY basis due to adverse political and economic scenario in the country. There has not been any meaningful recovery in the current year as well.
- Kenyan tea production in 6M CY2023 increased marginally by ~3 Mkg (~1%) on a YoY basis.

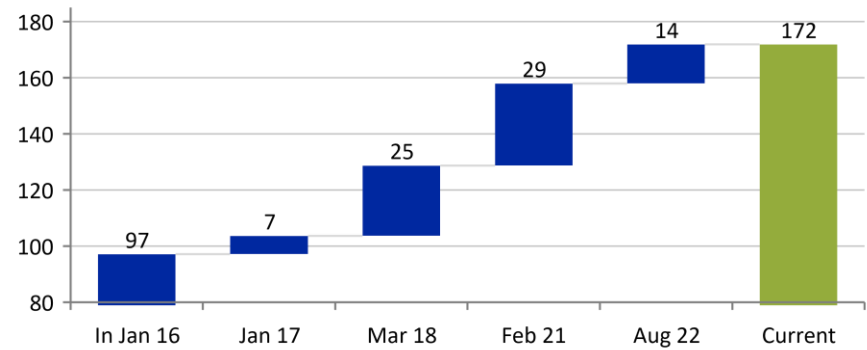
Wage hike in West Bengal from June 2023 to increase tea production cost by ~Rs. 9/kg

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)

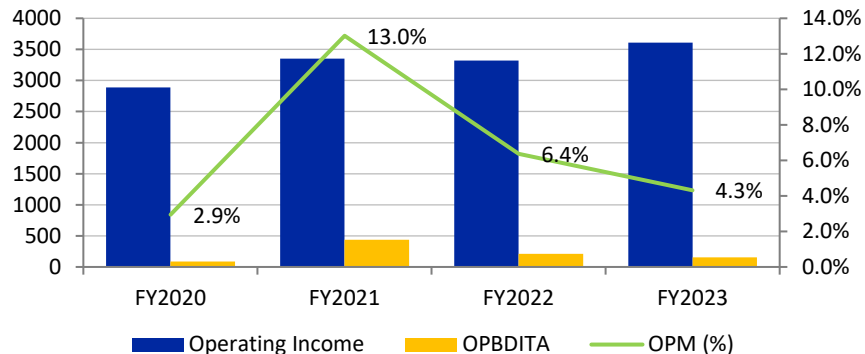


Source: ICRA Research

- The basic daily wage of the tea estate workers in West Bengal has moved up by Rs. 18 to Rs. 250, as a part of a long-term wage settlement, effective from June 01, 2023. With an 8% increase in the basic wage rate, the total wage per day (including other benefits) in West Bengal has increased by around 6%.
- The overall wage cost per kg of tea is likely to rise by around Rs. 9/kg in view of the proposed wage hike in West Bengal. This may escalate the margin pressure for the tea estates based in West Bengal, given a moderation in prices in the current year. The estimated wage cost per kg of tea in West Bengal still remains lower than Assam. However, there is a high likelihood of a wage hike in Assam, too, in the near term, given the recent rise in West Bengal.

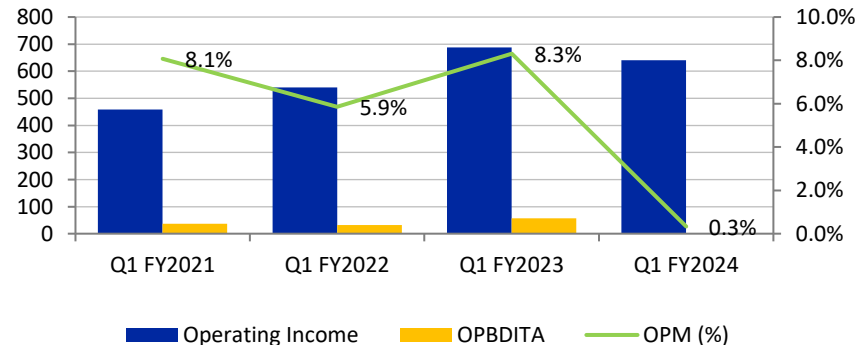
Decline in operating margin in Q1 FY2024 due to muted realisation and hike in wage rate; full-year margin likely to remain thin compared to FY2023

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



Source: BSE, NSE, ICRA Research

Exhibit: Trend in Q1 result of nine listed bulk tea players

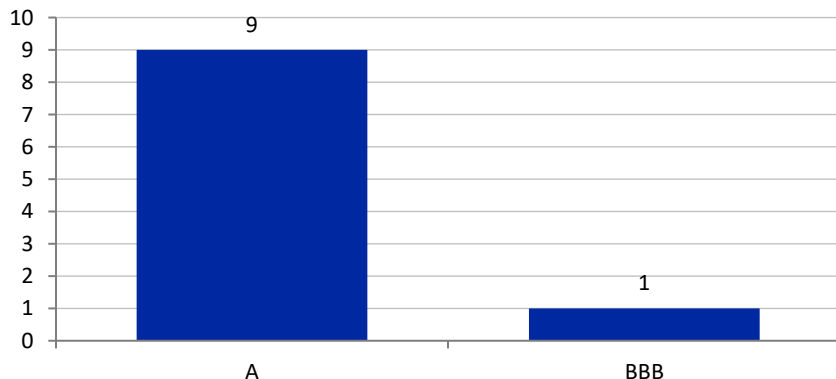


Source: BSE, NSE, ICRA Research

- 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 wage rate and a fall in tea realisation, particularly ODX tea, resulted in a drop in the operating profit in Q1 FY2024.
- The OPM in Q1 FY2024 was lower by ~796 bps on a YoY basis, while in Q1 FY2023, the same was higher by ~244 bps compared to Q1 FY2022.
- Muted realisation along with a wage hike in West Bengal, effective June 2023, would lead to a further moderation in the OPM in FY2024 over FY2023.

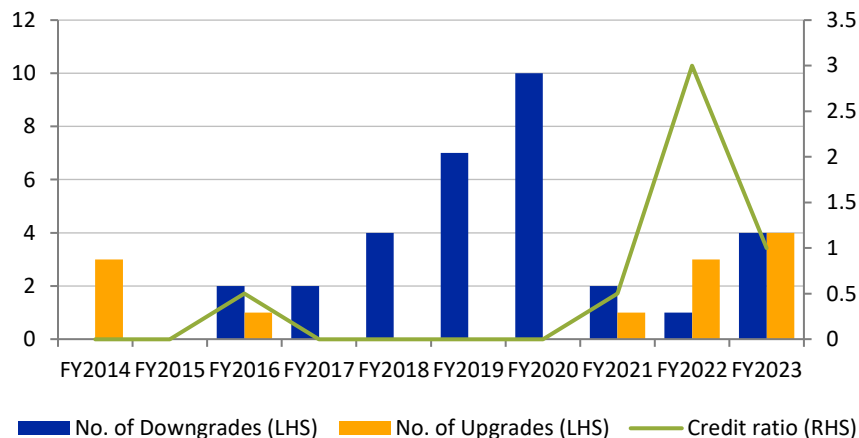
Credit rating movements in bulk tea sector

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+ considers 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.

Source: ICRA Research



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