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Vegetable Oils: Likely to see recovery

It was a healthy 2007-08 for the vegetable oil industry, but the downturn in the following year caused due to a fall in consumer demand and high input prices, hurt financials. However, today, the industry can already smell the aroma of recovery this year with rising consumer demand and its increased thrust on branded and value-added space yielding positive results.

The big five players in the sector - Ruchi Soya, JVL Agro, KS Oils, Sanwaria Agro and Gujarat Ambuja Exports - saw their aggregate net profit fall by 14% in 2008-09 on 15% higher aggregate sales due to rising prices.

The high volumelow margin nature of the business took its toll on the companies during the December 2008 quarter when their operating margins were hit the most due to a drop in consumer demand for vegetable oil and poultry demand for the largely-exported oilmeal.

High prices of oilseeds also increased their procurement costs. Oilmeal exports were down 49% to 15.8 lakh tonnes during January-April 2009 compared to the corresponding period in the previous year on declining production of meat and lower demand for compound feeds and, thus for oilmeals, according to the Solvent Extractors' Association of India.

While the operating margins collapsed for all the five large companies during the December quarter, only a handful, such as KS Oils and Sanwaria Agro, could salvage their profit margins in the March quarter. KS Oils recovered fast because the company commands a dominant share of the lesscluttered mustard oil market and has a prominent presence in the branded market, securing 40-50 % of its edible oil revenues from the branded business. Last year's downturn has changed the way vegetable oil companies run their business: not only have the large players started building brands and manufacturing value-added derivative products such as soya granules and soya nuggets, they are now also selling their branded products to the new retail chains and contract-manufacturing for their private labels. Lower duties too have played a role in changing the fortunes of the industry. The zero customs duty on crude palm oil and the recent scrapping of 20% import duty on crude soybean oil have made it cheaper for the companies to

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import and refine oil than buy oilseeds locally for crushing and then refine the oil. Also, this being an off-season for kharif oilseeds, profit margins in the import business are better as compared to the domestic business of procuring oilseed and processing it into oil.

Another positive sign for the investor is that large players such as KS Oils, Ruchi Soya and Sanwariya Agro are planning capital expenditure to fund capacity expansion. KS Oils is going ahead with its backward integration project to develop palm plantations in Indonesia and Malaysia. For this, the company recently announced its plan to raise Rs 450 crore, and has received a term-sheet commitment of Rs 390 crore from its promoters and the three private equity investors. Similarly, Ruchi Soya has raised Rs 350 crore, by issuing Rs 245-crore preferential warrants to promoters and Rs 105-crore preferential equity shares to foreign institutional investors. Sanwariya Agro is planning to raise Rs 100 crore for manufacturing value-added soy derivatives.

The next quarter is likely to be better for the sector with a possible recovery in operating margins. Companies establishing presence in branded space in oil and oilseed derivatives stand a better chance of growth rather than ones that operate in the unbranded space or are only into pureplay trading.

