

Cheaper feedstock, urea price decontrol must for shoring up fertiliser projects

By Uttam Gupta

RECENTLY, PIB is reported to have termed the proposed Rs 1570 crore Nellore urea project of IFFCO as highly risk-prone. This is on the basis that urea can be imported at C&F price of US \$100 per tonne as against a projected price of about US \$200 per tonne by IFFCO in its proposal. The argument is shortsighted and seriously flawed.

The price of imported urea cannot be a logical basis for deciding whether we should set up a plant here or not. This is because the price is not related to cost of production in exporting countries; instead, it depends primarily on global demand-supply balance. When it is tight, price increases and when it is easy, price decreases.

In the last two-and-a-half decade or so, C&F price of urea imported by us has fluctuated widely from US \$275 per tonne in 1974-75, US \$97 per tonne in 1986-87, US \$225 per tonne in 1995-96 to US \$100 per tonne currently. These, in turn, have been influenced by developments in China and India, two major buyers of urea in the world market.

Thus, in 1974-75, when prices skyrocketed to about US \$275 per tonne, we were importing about 50 per cent of our consumption needs. In the early 80s, world ammonia/urea capacity was built on a large scale, even as demand did not grow that fast. This resulted in a glut, in the mid-80s, and an all-time low price of US \$97 per tonne in 1986-87.

Thereafter, price increased until the early 90s, primarily due to China increasing its import demand. After a drop in 1993-94

—due to happenings within Russia and other CIS countries—price went up again to a high of US \$225 per tonne during 1995-96 due to heavy imports by both India and China. During 1996-97 also, prices remained high at about US \$206 per tonne.

During 1997-98, China has drastically reduced its purchases due to excess availability at home consequent to recent commissioning of a couple of plants and heavy imports in the previous two years. India, too, has not increased its imports beyond the 1996-97 level due to domestic capacity addition — from IFFCO Aonla/NFL Vijaipur exp., (December 1996/March 1997) — meeting the bulk of the incremental demand.

This is, however, temporary and, according to available indications, China may enter the market sometime in middle of 1998. During 1998-99, India will also step up its imports as there is no significant fresh addition to capacity — except full year production from IFFCO, Phulpur exp., commissioned in December 1997.

As for the future, in India, except for the expansion of Chambal Fertilisers plant at Gadepan — likely to be set up by 1999-2000 — all the other contemplated projects have been dropped/kept on hold due to continuing policy uncertainties/adversities. In China, its much-trumpeted plans to become totally self-sufficient in urea by the turn of century would not be easy to realise given its feedstock supply and logistics constraints.

About 5.5 million tonnes of existing urea capacity in India is

from plants more than 20 years old. These are in dire need of timely revamping and modernisation. But the huge resources required for this are nowhere in sight and the policy environment is not conducive to attract private capital. As a result, there is a serious risk of losing this capacity. In that event, our import demand will increase sharply.

Thus, we may face an extremely tight global demand-supply balance. Much will depend on whether we care for our own industry. If we do not, this would lead to heavy dependence on imports and that, in turn, would cause prices to rise sharply. Even JVs, e.g., in Oman, cannot come to our rescue as, on supplies from these under buy-back, we have to pay the prevailing world market price.

The decision on setting up projects in India has to be primarily strategic keeping in view the goal of maintaining self-sufficiency as was the position until the end of the 80s. While, it is nobody's case that these should be allowed to be set up and produce at any cost, ground realities, especially in regard to high pricing of feedstock, cannot be ignored.

Nellore is based on naphtha, the cost of which, delivered at the factory gate, is about Rs 8,500 per tonne. Using 0.7 tonne needed to produce a tonne of urea, the energy cost alone is about Rs 6,000 per tonne. In view of this, if you set a totally unrelated/arbitrary benchmark, i.e. farmgate cost of imported urea at US \$100 per tonne C&F or Rs 5,400 per tonne, the project is bound to be unviable. This will be so even if someone were to gift the plant to

IFFCO.

Let us not forget that because of the high feedstock price, the reasonable cost of production of almost all existing naphtha-based plants is Rs 8,000 per tonne-plus; and feedstock cost alone accounts for about 75-80 per cent of this. So, if you assess them according to PIB methodology, all will be highly risk-prone.

The gas-based plants may be slightly better placed with the present delivered cost of energy of about US \$2.9 per million Btu to on-shore/landfall and US \$3.4 per million Btu to HBJ plants — as against US \$5.5 per million Btu for naphtha. However, with the steep increase in gas price — already in the pipeline — energy cost even to these plants would eventually reach the level closer to naphtha.

Due to high feedstock prices on the one hand, and control on urea selling price at an artificially low level of Rs 3,600 per tonne on the other, viability of the entire fertiliser industry is at stake. There is an urgent need to bring down former to internationally comparable levels and to increase latter in small steps.

These measures will help in narrowing the present huge gap — more than 100 per cent — between the reasonable cost of supplying domestic urea and the selling price. In turn, this would enable smooth transition to a non-price control scenario without affecting the viability of the existing plants. It would, then, also be possible to pronounce judgements on projects like the Nellore, in an objective and reasonable manner.

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