

## **Price Increases – Natural Ingredients**

Below, we demonstrate a justification for the price increases of natural ingredients exported from Sri Lanka, despite devaluation of local currency. It serves as a justification of the prices quoted by exporters at present.

### **1. Currency Devaluation**

#### **Point (1)**

Pre-crisis exchange rate of LKR against USD was at 203LKR/USD. However, due to the economic downturn the Central Bank of Sri Lanka revised the exchange rate to 355-360LKR/USD in March 2022.

While some exporters use grey channels to receive/exchange money, where the exchange rate of 410LKR/USD is offered, this is prohibited by exchange control laws of Sri Lanka.

P.T.C Agro as a registered business entity with strict principals and bound by our internal code of conduct are unable to use such means to gain undue advantages in the currency market.

**Therefore, we forego 10-13% of margin compared to some other compatriot exporters.**

#### **Point (2)**

Certain exporters who are exporting blended oils are also using the foreign exchange earned to import isolated compounds etc. to be added in the oils.

We, P.T.C Agro are only exporting pure essential oils, thus are unable to make such foreign currency advantages/gains either.

### **2. Production Delays**

#### **Point (1)**

Due to power interruptions that have ranged between 3-14 hours per day so far since January 2022, we as a distiller have fallen behind on all our production schedules.

**For Example – to produce a Pure Natural Cinnamon Bark Oil lot of 200kg – our facility requires 28 days with 4 distillation sessions per day utilizing 3,600kg of raw material.**

However, over the past few months due to power interruptions - daily distillations on average have been 2 per day. Also given the timings of power interruptions, the distillery has only operated on 3-4 days per week.

The power interruptions have delayed our QA-QC processes as the sensitive equipment had to be shut down during the interruptions as the line voltages become unstable.

Point (2)

Our distillery runs on biomass – mostly uprooted old rubber wood, which is usually abundantly available. However, due to the fuel crisis, suppliers have not been able to saw firewood as well as transport the biomass to our factory.

**In the month of June and July the average working days per month was less than 16 days due to the above reason.**

Point (3)

Due to fuel crisis private as well as public transport is dysfunctional. Our employees have not been able to attend to work for weeks on due to fuel shortages.

Furthermore, supply of raw materials to the distillery has also been very irregular.

Owing to the unavailability of a fair fuel distribution mechanism, average time to obtain fuel on a que varied between 24-72 hours – some employees using motorbikes or other forms of private transport have not reported to work. A recent system has brought down the wait time to an average of 4 hours, provided fuel arrives at the pumping station.

As a registered legal entity that cares for our employees, P.T.C Agro has yet paid complete salaries to all our workers during the COVID-19 pandemic period as well as during the ongoing crisis.

Despite production meeting only 50-60% of the usual capacity or lower on some instances, the increase in overheads and wages have been fully absorbed by the company. **Therefore, for certain lots of production, the wages and overhead factored contribution have been accounted as threefold the usual rate.**

**Given the above factors of electricity interruptions, shortages in firewood and inability of work force to report to work, time spent to produce a 200kg lot of bark oil has increased from 28 days to over 55-60 days.**

**The overhead and wages contribution per lot of 200kg cinnamon bark oil for example has increased by nearly 60-70%.**

### **3. Shipping Delays**

Due to fuel shortages moving cargo from the production facility to port has been delayed considerably on certain occasions raising holding costs of the company.

Due to the non-payment for imported cargo including government import of fuel, fertilizer etc. delays at the port have been considerable. 6 out of 10 vessels that usually transit at port of Colombo avoid sailing to Sri Lanka, which has been confirmed by our usual freight partners – Expeditors, USA (local agent – Expelogix).

**Therefore, some of our cargo has been delayed by over 30 days to ship and issue Bill of Lading. Such delays have had an effect of 2.5-3% cost increase on the total value of a shipment as finance cost increase.**

#### **4. Price Increases by Farmers**

##### Point (1)

Due to the ban on fertilizer importation, certain crop harvests have reduced by nearly 30%. In case of cinnamon quills exported as a spice, for example Hamburg Grade quills doubled in price.

**For Example - Hamburg Grade cinnamon quills were selling a 2000LKR/kg approx. in late 2021/early 2022, whereas the prices at present range 3800-4000LKR/kg.**

Cinnamon chips and quillings used for distilling cinnamon bark oil have followed a similar pattern and our observation and experience is a 50-60% increase in the cost.

##### Point (2)

In terms of cinnamon leaf oil, unavailability of fertilizer has resulted in some landowners insisting the leaves and twigs be left in the fields to compost as fertilizer, than be collected for distilling cinnamon leaf oil.

Fuel shortages and electricity interruptions have had a similar impact on smaller field distillers who predominantly produce cinnamon leaf oil in Sri Lanka.

##### Point (3)

Other contributory factors such as transport issues, daily wage-earning labourers who work in plantations demanding higher wages in proportion to living cost increases etc. field distilled oils such as cinnamon leaf oil and citronella have increased in price significantly.

**In support of the above Point (3) as per Central Bank of Sri Lanka Headline Inflation (Year on Year change from June 2021 to June 2022) stood at 54.6% as at 30/June/2022.**

The combined effect of Points 1|2|3 has been astounding especially for cinnamon leaf oil as it is the mostly traded and exported essential oil from Sri Lanka. The effect on cinnamon raw materials used for distilling oil and field distilled citronella oil has been moderate, whereas the effect on nutmeg oil, clove oils have not been considerable. (Due to demand for Sri Lankan material not being considerable for clove and nutmeg oils of Sri Lankan origin).

#### **5. Supply and Demand Equilibrium**

The demand seen since December 2021 to date has been usual despite Russian and Ukraine crisis. Anticipated slowing down of the US and European economies have still not translated to the ingredients markets in Sri Lanka.

Given all the supply side obstacles – the prices have continued to grow more rapidly for some products than others.

The disproportionate price increases and stock holding by farmers and field distillers in anticipation of further price increases are also contributing to the current surge in ingredient prices.

**While some suppliers and farmers may offer cheaply than others, at P.T.C Agro – we are compelled to purchase our raw materials ONLY from our site visited, audited approved suppliers, especially for field distilled oils.**

Contamination of cinnamon leaf oil with Diethyl Phthalate has been an ongoing problem due to bad storage as well as deliberate adulteration and to avoid such issues, our company has initiated a strict sourcing approach, which dictates terms that prevents us from alternating to cheaper suppliers without auditing.

## **6. Increase in Cost of Finance and Other Costs**

**Pre-crisis business lending rates were nudging above 8.5% in January 2022, which has spiked to over 22.5% per annum as at today.**

To put this into perspective with the help of an example of exporting 1000kg of cinnamon leaf oil to port of New York, USA by Sea as follows:

CIF price of Cinnamon Leaf Oil : 22.50USD/kg

Transit and Sailing time : 50 days under present conditions

Credit terms : Payment within 30 days from receipt of goods by buyer

Therefore, in the case of such an order – the cost increase is over 800USD approx.

**As a business entity producing multiple products and paying all our farmers and field distillers 100% of funds at the time of accepting raw materials or oils after quality inspection, the finance costs for P.T.C Agro has increased significantly due to the crisis dragging the time taken to produce and export ingredients.**

Furthermore, fuel price increase by three-fold is affecting all other costs related to production and logistics.

*Overall impact in terms of cost increases and hurdles to produce and export ingredients have been considerable. The devaluation of currency is a consolation against such, yet the indirect cost increases may not be obvious to many buyers.*

*We make this an opportunity to thank all our buyers, supporters and well-wishers who have continued to support our business over the many years. We look forward to your continued support and encouragement more than ever during this time of crisis.*

*Best Regards*

*P.T.C Agro (Private) Limited.*