Seshasayee Paper and Boards Limited

April 06, 2021

Ratings

Facilities	**Amount (Rs. Crore)**	**Rating[1]**	**Rating Action**
Long Term Bank Facilities – Term Loan	82.50	**CARE A+; Stable [Single A Plus; Outlook: Stable]**	**Reaffirmed and Outlook revised from Positive to Stable**
Long Term Bank Facilities - Fund Based	205.00	**CARE A+; Stable [Single A Plus; Outlook: Stable]**	
Short Term Bank Facilities - Non Fund Based	205.00	**CARE A1+ [A One Plus]**	**Reaffirmed**
Total Facilities	**492.50 [Four hundred ninety two crore and fifty lakh only]**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision in outlook factors in the lower than expected increase in the revenue of the company in FY20 led by adverse effects of the Covid-19 pandemic. The revenue as well as profitability continued to decline in 9MFY21 led by slowdown of demand in the paper industry. However, the same is expected to improve during FY22 with the likely and gradual opening of educational institutions as well as commercial establishments.
The reaffirmation of the ratings assigned to the bank facilities of Seshasayee Paper and Boards Limited (SPBL) continue to factor in the established track record of the company along with extensive experience of the promoters in the paper industry as well as a strong and well-qualified technical team, well-established distribution network, its moderate operating performance backed by operating efficiencies as well as synergies derived from integrated manufacturing operations. The ratings also derive strength from the healthy financial risk profile marked by robust capital structure along with comfortable debt coverage indicators in FY20 and 9MFY21.

The aforementioned strengths are however tempered by susceptibility of profit margins to volatile input prices, inherent industry cyclicality and the potential impact of any latent capacity coming on stream in the industry or threat of imports in the paper industry.

Rating Sensitivities:

Positive

- *Significant improvement in scale of operations while sustaining the current level of PBILDT margins and capital structure*

Negative

- *Sustained decline in PBILDT margin below 10% on account of reduced sales realization*
- *Deterioration in overall gearing beyond 0.5x on account of debt funded organic or inorganic growth*

Detailed description of the key rating drivers

Key Rating Strengths

Long track record coupled with vast promoter experience in the paper industry: Incorporated in 1960, SPBL has a well-established track record of around six decades in the Indian paper industry. The company is the flagship company of the Esvin group, which is engaged in other industries like sugar, chemicals, project consultancy, etc. Currently, the day-to-day operations of the Erode and Tirunelveli units are handled by professional management and are ably supported by team of qualified and experienced personnel instrumental in providing technical and managerial inputs. The company is supported by its in-house project consultancy company named SPB Projects and Consultants Limited (SPB-PC), which is the project consultant for almost all major paper companies in India.

[1] *Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

Well established distribution network: The company has a strong marketing set-up and a well-established distribution network to support the manufacturing activities. SPBL commands a strong goodwill in South India which is evident from the revenue contribution of around 65-70% of its total sales. The company has a well-built network of more than 50 dealers appointed on commission basis and one depot in Bengaluru. The company also exports its products to countries like United States of America, Sri Lanka, Nepal and Middle East countries. The company's production is largely order based procured by its dealer network.
Synergies between manufacturing facilities led to enhanced operating efficiency: The two manufacturing units of the company situated at Erode and Tirunelveli share significant synergies, wherein the company has an excess capacity of pulp manufacturing at its Erode facility, which is deployed at Tirunelveli unit, thereby reducing the latter's dependency on imported pulp. The excess pulp production at the Erode unit caters to around 60% of the pulp requirement of the Tirunelvelii plant. Moreover, the captive power plant of 21 MW at Erode unit is able to supply power to the extent of 3MW to the Tirunelveli unit and reduces its dependence on external sources. The aforementioned synergies have led to savings in the raw materials as well as power cost thereby positively impacting the profit margins.
Moderate operating and financial performance: The total revenue during FY20 has declined by around 10% led by decrease in production as well as sales volume. This reduction in volume was mainly due to shut down of one of the Paper Machines during the year for upgradation works, poor market conditions and on account of plant operations being shut down in the last week of March 2020 due to Covid-19 lockdown. However, the PBILDT margin remained constant during FY20 primarily led by higher sales realization during the year as well as operating efficiencies.
During 9MFY21, the revenue as well as profitability has decreased significantly on a Y-O-Y basis mainly on account of adverse impact of the lockdown imposed in the first half of the year to contain the spread of Covid-19 as well as planned shutdown of the paper machines to undertake upgradation works as part of the planned capex during the year. The continued closure of commercial establishments, schools, colleges and educational institutions has adversely affected the demand of writing paper in the country. Consequent slowdown in the Indian economy, coupled with poor offtake in export markets resulted in significant reduction in demand for Printing and Writing Paper. The PBILDT margin declined from 25.07% during 9MFY20 to 19.07% during 9MFY21 primarily due to lower sales realizations.
Comfortable capital structure and debt protection metrics: The overall capital structure of the company continues to remain robust marked by an improved overall gearing of 0.08x at the end of FY20 led by healthy accretion to the networth as well as reduction in borrowings. The total debt to GCA also stood healthy at 0.35x as compared 0.84x in FY19, while total debt to PBILDT ratio was at 0.29x at the end of FY20 as compared to 0.66x in FY19. The company has undertaken a capex of Rs. 315 crore, funded by term loan of Rs. 82.50 crore and the balance through internal accruals or cash reserves. Overall gearing is expected to remain comfortable despite this additional term loan, which would be drawn down in FY22.

Key Rating Weaknesses
Profit margins susceptible to volatile input prices: Wood Pulp forms a key raw material for all paper manufacturers, the prices of which have been volatile and witnessed a downward trend in the current year. Another major raw material required is wood for production of pulp. Domestically, the supply of wood to the paper industry from natural forest resources is restricted by government regulations leading to raw material availability issues. The company also remains exposed to sharp increase in hardwood prices due to higher minimum support prices of agricultural commodities. In order to mitigate the risk and ensure long term raw material availability, SPBL has taken steps to step up production of clonal seedlings and bare-rooted seedlings at its nursery and other company sponsored nurseries. With excess production of pulp at Erode plant, the company has also lowered the dependence on imported pulp to a certain extent as well. Nonetheless, SPBL's profit margins remain exposed to the fluctuations in key raw material prices (wood, wood pulp, waste paper and bagasse) depending on demand-supply dynamics.
Inherent cyclicality; competitive industry with paper players facing import threat: The paper industry is inherently cyclical owing to the long gestation period in capacity addition and lead time for raw material generation, among other factors. The demand is dependent on education and corporate sectors which are affected by the overall macroeconomic situation.
Indian Paper industry has a fragmented structure consisting of small, medium and large paper mills, having capacities ranging from 5 to 1,150 tonnes per day. The increased competition restricts companies' ability in the paper industry to pass on the rise in input cost to the end consumers and keep margins under check in the near-term. Further, there has been a rise in paper imports from ASEAN countries which has resulted in increasing share of imports in paper consumption in India thereby affecting the profitability margins of the domestic players.

Industry Outlook
The Indian paper and paper industry has continued to witness steady growth in FY20, and the domestic demand grew from 9.3 million tonnes in FY08 to 18.6 million tonnes in FY20 at a CAGR of 6.4%. However, subdued and diverse trading conditions caused by geopolitical uncertainties including the current coronavirus outbreak have impacted the overall global demand. With the ongoing vaccination program in India and with people now adapting to Covid-19 norms and environment, it is

expected that the sales of paper & paper products industry will witness an uptick during FY22 on y-o-y basis backed by better paper demand and increase in its prices.

Liquidity: Strong
The company has no term loans as on December 31, 2020 except the interest free sales tax loan. Further, the company has negligible repayment obligations in FY21 as well as FY22. The company has planned a capex of Rs. 315 crore which will be funded by debt only to the extent of 26% and balance through its cash reserves. As on December 31, 2020, the company had cash balances to the extent of Rs.127 crore. With a gearing of 0.08 times as of March 31, 2020, the issuer has sufficient gearing headroom, to raise additional debt for its capex. Moreover, the company has nil fund based utilization which provides more than adequate liquidity cushion.

Analytical approach: Standalone

Applicable Criteria
Criteria on assigning Outlook and Credit Watch to Credit Ratings
CARE's Policy on Default Recognition
Rating Methodology: Manufacturing Companies
Rating Methodology – Paper Industry
Financial ratios – Non-Financial Sector
Criteria for Short Term Instruments
Liquidity Analysis of Non-Financial Sector Entities

About the Company
Seshasayee Paper and Boards Limited (SPB) operates an integrated pulp, paper and paper board mill at Pallipayam (Erode, Tamil Nadu) and a paper manufacturing mill at Tirunelveli. SPB was incorporated in 1960 and commenced commercial production in December 1962 with a modest capacity of 20000 tonne per annum (TPA) integrated facility comprising of a pulp mill and two paper machines (PM 1 and PM 2). Over the years, through organic expansion, the company expanded its Erode facility to its current capacity of 1,32,000 TPA.
The company in February 2011 acquired a defunct paper mill (Subburaj Papers Limited, SPL; located in Tirunelveli) having a paper manufacturing capacity based on wastepaper pulp of 60000 TPA; SPL was subsequently merged with the operations of SPB from April 2012. During FY19, the company undertook capacity expansion to increase the capacity to 90,000 TPA.
SPB manufactures a variety of papers such as printing and writing (P&W) grade papers (WPP), packing and wrapping grade papers, specialty grade papers, etc. The company markets its paper products in the domestic market under the brand name of Sprint, Sprint Plus, Swift and Success; which are amongst leading brands in Southern India.

Brief Financials (Rs. crore)	FY20 (A)	FY19 (A)
Total operating income	1205.25	1343.80
PBILDT	288.12	314.40
PAT	174.61	190.00
Overall gearing (times)	0.08	0.24
Interest coverage (times)	41.81	22.77

A: Audited; Classified as per CARE Standards
Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Term Loan	-	-	March 2026	82.50	CARE A+; Stable
Fund-based - LT-Cash Credit	-	-	-	205.00	CARE A+; Stable
Non-fund-based - ST-BG/LC	-	-	-	205.00	CARE A1+

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Fund-based - LT-Term Loan	LT	82.50	CARE A+; Stable	1)CARE A+; Positive (07-Apr-20)	1)CARE A+; Positive (05-Apr-19)	1)CARE A+; Positive (07-Apr-18)	-
2.	Fund-based - LT-Cash Credit	LT	205.00	CARE A+; Stable	1)CARE A+; Positive (07-Apr-20)	1)CARE A+; Positive (05-Apr-19)	1)CARE A+; Positive (07-Apr-18)	-
3.	Non-fund-based - ST-BG/LC	ST	205.00	CARE A1+	1)CARE A1+ (07-Apr-20)	1)CARE A1+ (05-Apr-19)	1)CARE A1+ (07-Apr-18)	-
4.	Fund-based - ST-SLC-WC	ST	-	-	-	-	1)Withdrawn (07-Apr-18)	-

Annexure 3: Complexity level of various instruments rated for this company

Sr. No.	Name of the Instrument	Complexity Level
1.	Fund-based - LT-Cash Credit	Simple
2.	Fund-based - LT-Term Loan	Simple
3.	Non-fund-based - ST-BG/LC	Simple

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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