Emami Paper Mills Limited

November 26, 2020

Ratings

Facilities	**Amount (Rs. crore)**	**Ratings[1]**	**Rating Action**
Long Term Bank Facilities	990.75 (Enhanced from 915.75)	**CARE BBB+; Stable (Triple B Plus; Outlook: Stable)**	**Reaffirmed**
Short Term Bank Facilities	380.00	**CARE A2 (A Two)**	**Reaffirmed**
Total Bank Facilities	**1,370.75 (Rs. One Thousand Three Hundred Seventy Crore and Seventy-Five Lakhs Only)**		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Emami Paper Mills Limited (EMPL) continue to drive strength from long operational track record of the company with established promoter group. CARE factors in improvement in the financial flexibility of the Emami group, financial support from the group and its promoters and willingness of continuity in the future as and when required. The ratings continue to factor in diversified product basket of EMPL with partial flexibility to change product mix resulting in diversified customer base with presence in diverse end-user industries and initiatives taken to reduce power and fuel cost. The ratings are, however, constrained by moderation in capacity utilization along with financial performance in FY20 (refers to the period April 01 to March 31) and H1FY21 due to tepid demand scenario in Newsprint (NP) and Printing and Writing Paper (PWP) and disruption of operations and supply chain due to the lockdown announced by the Government in view of the spread of the COVID-19 pandemic. The ratings are further constrained by high leverage position, high debt repayment obligation of EPML over the period of next three years resulting in weak coverage ratios, working capital intensive nature of business, forex risks, and susceptibility of business to volatility in input and finished goods prices. The ratings further factors in the uncertainty regarding the timing of the on-going Covid-19 pandemic clearing out affecting the revival of demand for paper products in the near term.

Rating Sensitivities

Positive Factors - Factors that could lead to positive rating action/upgrade:

- Repayment of debt resulting in improvement of the gearing ratio below 1.00x.
- Improvement in PBDILT margin by more than 20% on continuous basis and improvement in return ratios on sustained basis.

Negative Factors- Factors that could lead to negative rating action/downgrade:

- Deterioration in debt coverage indicators by debt funded capex and increase in borrowing beyond current levels.
- Further losses in subsequent quarters.
- Inability to infuse funds on timely manner by the promoter group.

Detailed description of the key rating drivers

Key Rating Strengths

Established group along with demonstrated financial support from the group and its promoters with improved group financial flexibility

Emami Group is a leading industrial group with major interest in cosmetics, healthcare, edible oil, paper, retail, and real estate sectors. The flagship company of the group, Emami Ltd. (rated CARE AA+; Stable/ CARE A1+), has presence in personal and healthcare products. The promoters of the group, Mr R S Agarwal and Mr R S Goenka, are qualified professionals with business experience of over four decades. Emami group has demonstrated support and infused funds to meet various fund requirements of the company, including working capital and capex. The promoters /group companies had infused money in the form of non-cumulative redeemable preference shares towards setting up of its board plant (BV: Rs.309.60 crore as on March 31, 2020). In FY20, the group has demonstrated support by infusing funds to the tune of Rs120 crore by way of Inter-Corporate Deposits (ICDs). Further as on September 30, 2020 the ICDs stands at Rs.138.98 crore.

The financial flexibility available to the group improved over the last few months. The company's promoters sold its power and cement business to reduce the promoter level debt and the pledge of promoter shareholding. Consequently, the outstanding loan against pledge of promoter's shares reduced from Rs.2,408 crore as on July 29, 2019 to Rs.1,145 crore as on October 29, 2020. The pledge of shares stands at 41.7% of promoter shareholding as on October 29, 2020 (46.8% as on June 30, 2019).

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

Long track record of the company
EPML is engaged in paper manufacturing business since three decades and has an established position in the paper market with an installed capacity of NP/PWP [along with fungible capacity of Kraft Paper(KP) of 39,000 MTPA] of 1,60,000 MTPA and that of board paper of 2,00,000 MTPA. EPML has started the production of speciality KP with Burst Factor (BF) of 28 – 35, from Q3FY20.

Diversified product basket with flexibility to change product mix
EPML has diversified paper product portfolio with manufacturing facilities for NP, PWP, KP and multi-layer coated board paper of both recycled and virgin grade catering to diverse end-user segments. Over the years the company has developed strong operational capabilities by undertaking continuous de-bottlenecking, expansion and up-gradation in its plants to achieve optimum production as well as flexibility to shift between products. Hence, EPML was able to reap benefits of rise in NP price from Q3FY18 by quickly shifting to NP from PWP. Furthermore, due to volatility in NP prices along with tepid demand due to shift into digital space followed by brunt of COVID-19, the company has successfully converted part of its Newsprint production capacity into Kraft Paper (KP) plant.
The plant wise installed capacity of the company and product flexibility is as under:

Gulmohar Plant	NP: 18,000 MTPA fungible with Absorbent Kraft paper 21,000 MTPA
PM I	NP: 18,000 MTPA fungible with Kraft/PWP of 18,000 MTPA
PM II	NP: 33,000 MTPA fungible with PWP of 36,000 MTPA.
PM III	NP: 85,000 MTPA
PM IV	Board Plant: 2,00,000 MTPA

Diversified customer base with presence in diverse end-user industries
EPML has an established position in the domestic paper industry, supported by its strong brand image and superior quality product. Given EPML's diversified product basket, the Company has diversified customer base from diverse end-user industries. Board Paper is used for packaging in various customer facing industries including pharmaceutical, health care, food and cosmetics etc. NP is used by print media for printing newspapers. PWP finds application in notebooks, textbooks, and copier paper (education sector). Kraft Paper is used in packaging operations for packing, wrapping individual items, bundling and void fill. The company caters to majority of the NP buyers in Eastern India. BP and PWP are sold through a network of 39 dealers and distributors.

Efforts to reduce power and fuel cost
Paper manufacturing is highly energy intensive with annual coal requirement of 3.4 lakh MT. EPML procures coal requirement through linkage and e-auction route. EPML entered into a Fuel Supply Agreement (FSA) in Q3FY19 for a period of 5 years with Mahanadi Coalfields Ltd (MCL) for supply of coal ensuring continuous availability and safeguarding from price volatility to an extent.
Hence, procurement of coal under linkage/FSA increased to 77% in FY20 which was around 30% till FY19. In H1FY21, EPML procured entire coal requirement through linkage. As a result, power and fuel cost as a % of sales reduced to 8.54% and 8.14% respectively during FY20 and H1FY21 (vis-à-vis 9.92% in FY19).

Key Rating Weaknesses
Moderation in capacity utilization in FY20 and H1FY21
EPML has manufacturing facility with five plants - four (PM-I, PM-II and PM-III, PM-IV) at Balasore and
one in Kolkata for manufacturing of NP,PWP, KP and Board Paper. The capacity of Board Plant increased from 1,80,000 MTPA to 2,00,000 MTPA in March 2019, however the commercial production started from October'2019. In addition to this EPML has Captive Power plants (CPP) with an aggregate installed capacity of 33.5 MW.
The effective capacity utilization decreased in FY20 to 87% from 97% in FY19 due to lower production of NP resulting from decline in demand for the product due to shut down of production due to lockdown in later half of March'2020. Further in H1FY21, the capacity utilization decreased to 60% due to continued intermittent lockdown imposed throughout Q1 and lower demand scenario. However, production for Board paper has reached pre-covid level on month-on-month basis, albeit lower production continues for NP/PWP.

Moderation in financial performance in FY20 and H1FY21
The total operating income of the company witnessed marginal de-growth of 1.02% on y-o-y basis from Rs.1539 crore in FY19 to Rs.1524 crore in FY20. Operating margin of NP reduced to 8.79% in FY20 vis-à-vis 18.85% in FY19 due to declining NP prices, impacting the overall PBILDT margin of the company, despite better performance of board segment. EPML incurred net loss of Rs.10.45 crore in FY20 mainly due to lower PBILDT margin and recognition of exceptional item of Rs.27 crore pertaining to pre-operative expenses incurred in FY18-19 for green-field multi-layer paperboard expansion project in

Bharuch, Gujarat which was discontinued in September, 2019. Furthermore, loss on foreign currency fluctuation also increased substantially to Rs.53.51 crore in FY20 from Rs.34.61 crore in FY19.
The interest coverage ratio deteriorated to 1.75x in FY20 vis-a-vis 2.10x in FY19 due to increase in finance cost and low accretion of profit.
In H1FY21, the company reported income from operation of Rs.491.24 crore with PBDILT of Rs.82.39 crore and PAT of Rs.0.85 crore as against income from operation of Rs.734.43 crore in H1FY20 and PBDILT and PAT of Rs.95.43 crore and Rs.2.10 crore respectively. The decline in sales was mainly on account of disruption caused due to lockdown to ensure containment of spread of COVID-19. As a result, the operation of the company was scaled down to 50%-60%. Further NP and PWP industry also suffered set back due to on-going sluggish demand. The GCA of the company in H1FY21 stood at Rs.39.54 crore. The adjusted GCA (after considering mark to market gain or loss on forex as non-cash in nature) stood at Rs.32.65crore.

Volatile raw materials and finished goods price
Wastepaper and pulp are the most critical raw materials for NP and BP, constituting around 58% of cost of sales. This is followed by power & fuel cost and chemicals. These raw materials and finished goods are globally traded commodities and so prices are volatile in nature. EPML procures wastepaper mainly through indigenous sources and imports entire pulp requirement. Further, EPML does not have its own plantation and pulping capacity and is dependent on the market for procurement of its pulp requirements. Any shortage in the pulp market might lead to plant shutdown which would impact the profitability of the company.
Domestic NP prices are based on import price parity given majority of domestic NP industry demand (55-60%) is met through imports. EPML resets NP prices on a quarterly basis based on international prices and the exchange rate (Rs./USD) prevailing during the last week of the previous quarter.
However, the Chinese government restricting the import of significant levels of waste paper in 2017 due to environmental concerns has resulted in a decline in the global waste paper prices. This has in turn benefitted domestic manufacturers who use waste paper /pulp as a key raw material. As a result, EPML's cost per MT of waste paper decreased from Rs.14,434 in FY19 to Rs.11,693 in FY20, thereby preventing further decline in operating margin of the company.
The prices of packaging board has been in the range of Rs.55,000/MT to Rs.50,000/MT during the period for FY20 & FY19. The prices however dropped to ~Rs46,000/MT in H1FY21.

High leverage ratio and sizeable long-term debt repayment obligations next three years
The debt equity ratio and overall gearing ratio deteriorated to 4.28x and 6.90x as on March 31, 2020 respectively as against 4.14x and 6.17x respectively as on March 31, 2019 due to abatement of net worth on account loss in FY20 and increase in working capital borrowing, inter corporate deposit (from Pan Emami Cosmed Limited and Emami Capital Markets Limited) and LC backed creditors. The TD/GCA deteriorated from 11.41x as on March 31, 2019 to 17.85x as on March 31, 2020 mainly due to decrease in GCA and increase in total debt. The adjusted debt equity ratio and overall gearing ratio (considering preference shares neither as a part of net worth not debt) stood at 2.86x and 5.48x respectively as on March 31, 2020 vis-à-vis 2.98x and 5.01x respectively as on March 31, 2019. Also, adjusted debt/GCA deteriorated from 9.21x as on March 31, 2019 to 9.99x as on March 31, 2020 on account of decline in GCA in FY20.
The company has sizeable portion of debt repayment obligation of in the range of Rs.170 crore- Rs.200 crore in FY21- FY23. The Company expects higher cash accruals going forward to meet the debt repayment obligation. CARE also derives comfort from EPML being a part of Emami group, financial flexibility and established relationship with lenders, which will enable it to arrange for financing to fund any shortfalls in accruals for servicing debt obligations, as has been adequately demonstrated in the past.

Exposed to foreign exchange fluctuation risk
The company has availed ECB's and avails loans in foreign currency working capital loans for working capital and imports raw materials and chemicals. Since the newsprint prices move in line with landed cost of imported newsprint due to import parity prices, it act as a natural hedge. However, with the reduction in newsprint production the natural hedge available to the company for its forex liabilities was also reduced. Hence the company from April'20, through its board resolution has approved new hedging policy wherein the company takes forward cover for 70% of net forex exposure for import bills. Further the company is also developing export market for its packaging board segment.
Over the years, the gap has moved unfavourably with increase in foreign currency payables vis-à-vis lower foreign currency payables. In FY20, due to rupee depreciation EPML incurred forex loss of Rs.85.26 crore in FY20 (charged to P/L Rs.53.51 crore and MTM loss of Rs.31.75 crore which is capitalised in fixed assets) vis-a-vis Rs75.07 crore in FY19 (charged to P/L Rs.34.06 crore and MTM loss of Rs.40.46 crore which is capitalised in fixed assets).
However, in H1FY21 the company has been able to reverse notional loss position into notional gain by recording foreign exchange gain of Rs.10.64 crore in H1FY21 by passing on loss incurred by import of raw materials.

Industry cyclicality & 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. Further, the industry is grappling with weak demand, shortage of raw material and limited availability of labour, which is affecting capacity utilization. Demand for paper and cardboards to contract 10-15 per cent on-year, affecting all categories of products. The shutdown of schools, colleges and majority of offices has crimped demand for writing and printing (W&P) paper. Though pulp prices have come off their highs and waste paper prices have declined further, the raw material prices are expected to remain stable. However, despite the eased out cost side pressures, the margins of the players are expected to be affected by subdued market conditions, lower realizations of finished goods, imports of finished paper and disruption in supply chain and production due to COVID-19.

Liquidity: Adequate

EPML earned adjusted GCA of Rs.120 crore in FY20 vis-à-vis debt repayment obligation of Rs.300 crore (incl. ST loan repayment of Rs.100 crore) in FY20. In view of inadequate GCA, the debt repayment was met out of infusion of Rs.120 crore by promoters through ICDs, and proceeds from refund from Gujarat Industrial Development Corporation of Rs.69.42 crore in November 2019 through surrender of land. The working capital utilization of the company stood at 89% for last 12 months ended October'2020.

In H1FY21, the company earned a GCA of Rs.32 crore against debt repayment of Rs.84crore, which was met out of realization of GST refund and infusion of funds by promoter. The company has sizeable position of debt repayment obligation of Rs.170 crore- Rs.200 crore each during the period FY21-FY23. In case of any shortfall, the promoters shall infuse funds to meet debt repayment obligations.

Current ratio has perennially been low and stood at 0.69x as on March 31, 2020 vis-à-vis 0.74x as on March 31, 2019 mainly because of high working capital requirement and significant term loan repayment obligation. The company is having cash and bank balance of Rs.20.41 crore as on March 31, 2020 vis-à-vis Rs.10.28 crore as on March 31, 2019. As on September 30, 2020, the cash and bank balance of the company stood at Rs.6.40 crore.

EPML has opted for moratorium of interest and principal payments under RBI COVID-19 package scheme for some its facilities and the same has been approved till August 31, 2020.

Analytical approach: Standalone. Ratings factor in the financial flexibility of the Emami group in raising resources and demonstrated fund support by the group investment Companies.

Applicable Criteria

CARE's Policy on Default Recognition
Financial ratios – Non-Financial Sector
Criteria on assigning Outlook and Credit watch to Credit Ratings
CARE's methodology for manufacturing companies
Criteria for Short Term Instruments
Liquidity analysis of Non-financial sector entities
Rating Methodology: Factoring Linkages in Ratings

About the Company

Emami Paper Mills Ltd (EPML) is engaged in manufacturing of Newsprint (NP), Printing & Writing Paper (PWP), Kraft Paper (KP) with an aggregate installed capacity of 1,60,000 MT per annum (MTPA), packaging board of 2,00,000 MTPA and captive power plant of 33.5 MW. It belongs to the Kolkata-based Emami group. Emami Group is a leading industrial group with major interest in cosmetics, ayurvedic medicines, pharmaceuticals, hospital, edible oil, paper, retail and real estate sectors. The flagship company of the group, Emami Ltd. has presence in personal and healthcare products.

Brief Financials (Rs. crore)	FY19(A)	FY20(A)
Total operating income	1,539.68	1,524.00
PBILDT	240.05	217.26
PAT	43.99	-10.45
Adjusted Overall gearing (times)	5.01	5.48
Interest coverage (times)	2.10	1.75

A: Audited

Status of non-cooperation with previous CRA: Not Applicable
Any other information: Not Applicable
Rating History for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: *Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3*
Complexity level of various instruments rated for this company: Annexure 4

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-Cash Credit	-	-	-	310.00	CARE BBB+; Stable
Non-fund-based - ST-BG/LC	-	-	-	355.00	CARE A2
Fund-based - LT-Term Loan	-	-	June 2026	625.75	CARE BBB+; Stable
Non-fund-based - LT-Letter of credit	-	-	-	10.00	CARE BBB+; Stable
Fund-based - LT-Cash Credit	-	-	-	20.00	CARE BBB+; Stable
Non-fund-based - ST-Letter of credit	-	-	-	25.00	CARE A2
Fund-based - LT-Working Capital Demand loan	-	-	-	25.00	CARE BBB+; Stable

Annexure-2: Rating History of last three years

Sr. No.	Name of the 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-Cash Credit	LT	310.00	CARE BBB+; Stable	1)CARE BBB+; Stable (17-Nov-20)	1)CARE BBB+; Stable (19-Aug-19)	1)CARE A; Stable (08-Jan-19)	1)CARE A; Stable (15-Dec-17)
2.	Non-fund-based - ST-BG/LC	ST	355.00	CARE A2	1)CARE A2 (17-Nov-20)	1)CARE A2 (19-Aug-19)	1)CARE A1 (08-Jan-19)	1)CARE A1 (15-Dec-17)
3.	Fund-based - LT-Term Loan	LT	625.75	CARE BBB+; Stable	1)CARE BBB+; Stable (17-Nov-20)	1)CARE BBB+; Stable (19-Aug-19)	1)CARE A; Stable (08-Jan-19)	1)CARE A; Stable (15-Dec-17)
4.	Non-fund-based - LT-Letter of credit	LT	10.00	CARE BBB+; Stable	1)CARE BBB+; Stable (17-Nov-20)	1)CARE BBB+; Stable (19-Aug-19)	1)CARE A; Stable (08-Jan-19)	1)CARE A; Stable (15-Dec-17)
5.	Fund-based - LT-Cash Credit	LT	20.00	CARE BBB+; Stable	1)CARE BBB+; Stable (17-Nov-20)	1)CARE BBB+; Stable (19-Aug-19)	1)CARE A; Stable (08-Jan-19)	1)CARE A; Stable (15-Dec-17)
6.	Non-fund-based - ST-Letter of credit	ST	25.00	CARE A2	1)CARE A2 (17-Nov-20)	-	-	-
7.	Fund-based - LT-Working Capital Demand loan	LT	25.00	CARE BBB+; Stable	1)CARE BBB+; Stable (17-Nov-20)	-	-	-

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities

CC Limit	**Detailed explanation**
Financial covenants	The margin applicable is 20%-25% on stock and 30% on book debts (cover period 90 days)
	Penal Interest at 2% for all overdue /delays of any monies payable.
Non-financial covenants	
Standard reporting, affirmative and negative covenants.	Furnishing of monthly stock statements and book debt statements with 21 days from last day of the preceding month.
WCDL Limit	
Financial covenants	The margin applicable is 20% on RM/FG/WIP and 25% on stores and spares.
Major Non-financial covenants	
Standard reporting, affirmative and negative covenants.	Repayable on demand subject to review at annual intervals or as may be decided by the bank
	Furnishing of monthly stock statements and book debt statements with 21 days from last day of the preceding month.
LC limit	
Financial covenants	To maintain a minimum net working capital of 25% of current assets.
Major Non-financial covenants	The borrower shall seek prior approval from lender before any amalgamation /merger /change in management control
	The company to submit information on UFCE on quarterly basis within 30 days from quarter end.
LC/BG Limit	
Financial covenants	Bank Guarantee for disputed liabilities shall be issued only against 100% margin in the form of fixed deposit duly lien marked in favour of bank
Major Non-financial covenants	Borrower to submit undated cheque(UDC) for the entire sanctioned amount along with declaration
	Financial BG/SBLC to be utilized only for availing buyers credit from overseas bank
Term Loan Limit	NA

Annexure 4: 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 - LT-Letter of credit	Simple
4.	Non-fund-based - ST-BG/LC	Simple
5.	Non-fund-based - ST-Letter of credit	Simple

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

Contact us

Media Contact
Name:-Mradul Mishra
Contact no. :-022-68374424
Email ID:- mradul.mishra@careratings.com

Analyst Contact
Name:-Richa Bagaria
Contact no.:-033-40181653
Email ID:- richa.jain@careratings.com

Relationship Contact
Name:- Lalit Sikaria
Contact no.:- 033-40181607
Email ID:- lalit.sikaria@careratings.com

About CARE Ratings:
CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

For detailed Rationale Report and subscription information, please contact us at www.careratings.com