

## Seshasayee Paper & Boards Limited

April 5, 2019

### Ratings

Facilities	Amount (Rs. Crore)	Rating <sup>1</sup>	Rating Action
Long Term Bank Facilities – Term Loan	120.34	<b>CARE A+; Positive</b> [Single A Plus; Outlook: Positive]	<b>Reaffirmed</b>
Long Term Bank Facilities - Fund Based	205.00	<b>CARE A+; Positive</b> [Single A Plus; Outlook: Positive]	<b>Reaffirmed</b>
Short Term Bank Facilities - Non Fund Based	205.00	<b>CARE A1+</b> [A One Plus]	<b>Reaffirmed</b>
<b>Total Facilities</b>	<b>530.34</b> [Five hundred thirty crore and thirty four lakh only]		

Details of instruments/facilities in Annexure-1

### Detailed Rationale & Key Rating Drivers

The reaffirmation of ratings assigned to the bank facilities of Seshasayee Paper and Boards Limited (SPBL) continue to take into account established track record of the company along with extensive experience of the promoters in the paper industry, well-established distribution network and its continued healthy operating performance backed by operating efficiencies and synergies derived from integrated manufacturing operations. Furthermore, the ratings derive strength from the healthy financial risk profile marked by strong network base leading to favorable capital structure along with robust liquidity/debt coverage indicators in FY18 (refers to the period April 01 to March 31) and 9MFY19 respectively.

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.

Going forward, SPBL's ability to sustain healthy operating performance and favorable capital structure through effective management of working capital cycle as envisaged shall remain key rating sensitivities. Furthermore, any unplanned debt funded capex/acquisition leading to significant deterioration in capital structure or liquidity position remains a key rating monitorable.

### Outlook: Positive

The outlook continues to remain positive owing to expected improvement in scale of operations, profit margins and capital structure along with sustenance of healthy liquidity position as envisaged. The outlook may be revised to stable in case of any deviation in the operating performance or improvement in overall financial risk profile as envisaged.

### 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, Seshasayee Paper & Boards Limited has well established track record of close to approximately 6 decades and commands a good reputation in Southern India. The company is promoted by Mr. Vishwanathan of Seshasayee Brothers Private Limited and is currently spearheaded by Mr. N Gopalratnam in the role of Chairman. The promoters have a rich experience of close to 5 decades in the Indian paper industry. 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.

#### 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 ~65-70% of its total sales. The company has a well-built network of more than 50 dealers appointed on commission basis and 1 depot

<sup>1</sup>Complete definition of the ratings assigned are available at [www.careratings.com](http://www.careratings.com) and other CARE publications

in Bengaluru. The company has presence in export market with substantial exports to countries like United State of America, Sri Lanka, Nepal and Middle East countries. The company's production is largely order based procured from its dealer network.

#### **Synergies between manufacturing facilities has enhanced operating efficiency**

In FY12, SPB acquired a defunct paper manufacturing unit in Tirunelveli and has successfully revived its operations leading to increased scale of operations. The revival of the acquired unit has aided SPBL in overcoming project execution risk and also concurrently maintaining its market share in competitive/growing paper industry.

From operations perspective, the Erode and Tirunelveli facilities share significant synergies, wherein the company has an excess capacity of pulp manufacturing at its Erode facility is deployed at Tirunelveli unit thereby reducing the latter's dependency on imported pulp. Also, with a retrofit carried out in power boiler to generate additional steam and power has enabled the company to wheel 3 MW of power from Erode to Tirunelveli plant there by aiding the unit on power front as well. The aforementioned synergies have led to savings in the raw material as well as power cost thereby positively impacting the profit margins.

#### **Healthy operating performance**

Owing to synergies derived across its manufacturing operations and reduced dependency on imported pulp, SPBL has maintained a healthy profitability during FY18. The PBILDT margin for FY18 stood at 19.25% as compared to 19.78% in FY17. Over the past couple of years, improved captive power generation eliminated purchase of costly third party power and furthermore the raw material synergies between the two units have aided in reducing the overall cost structure. The company is thus reaping benefits of both backward integration as well as economies of scale. The company reported a sharp increase in profitability margins during 9MFY19 primarily marked by increase in realizations. During the period the blended realizations increased by 8.68% on a y-o-y basis while the cost increase was marginal at 2.52%; this enabled the company to clock a PBILDT margin of 23.07% higher by 462 bps y-o-y (9MFY18 PBILDT margin of 18.45%). The PAT margin for 9MFY19 stood at 13.14% (9MFY18: 10.37%).

#### **Strong networth base, favorable capital structure and debt coverage indicators**

The overall capital structure of the company continues to remain robust marked by healthy networth of Rs.699.60 crore as on March 31 2018 and Rs. 827.34 crore as on December 31 2018. The overall gearing remained stable at the end of FY18 at 0.21 times (FY17: 0.29 times). The total debt to GCA also stood healthy at 0.87 times as against 1.05 times in FY17, while total debt to PBILDT ratio was at 0.70 times at the end of FY18 as against 0.77 times in FY17. An overall decrease in the term loans and working capital borrowings has led to improvement in the debt coverage indicators.

#### **Robust liquidity and short operating cycle**

The overall liquidity improved on account of steady cash accruals owing to healthy profitability and short operating cycle. Furthermore, the average working capital utilization level for last twelve months for fund based facility has been negligible while for non-fund based facilities has remained low at ~49%. The company thus has a large liquidity buffer at its disposal in the form of unutilized bank limits.

The company reported cash and bank balance of Rs.141.90 crore as on March 31, 2018 and Rs.243.07 crore as on December 31, 2018; this provides a boost to company's financial flexibility.

#### **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 witnessed an upward trend. Domestically, the supply of wood to the paper industry from natural forest resources is restricted by government regulations leading to raw material availability issues. 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 industry cyclicity; potential impact of idle capacity coming on stream**

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. In the past cyclical downturn, the industry witnessed scarcity of raw material thereby negatively impacting the profitability margins. While the company is well placed in terms of raw material availability near its plant, the company remains exposed to sharp increase in hardwood prices due to higher minimum support prices of agricultural commodities. Furthermore, technology led efficiency improvements require periodic capacity modernization; leading to high capital intensity.

Currently, the Indian paper industry has some capacity lying idle; any restitution of the said capacity can have bearing on the supply-demand dynamics and lead to increased competitive intensity thereby impacting the realizations and margins.

#### **Analytical approach: Standalone**

#### **Applicable Criteria**

[Criteria on assigning Outlook to Credit Ratings](#)

[CARE's Policy on Default Recognition](#)

[Criteria for Short Term Instruments](#)

[Financial ratios – Non-Financial Sector](#)

[Rating Methodology-Manufacturing Companies](#)

#### **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 year, through organic expansion the company expanded its Erode facility to its current capacity of 115000 TPA. The company in February 2011 acquired a defunct paper mill (Subburaj Papers Limited, SPL) having a paper manufacturing capacity based on waster paper pulp of 60000 TPA; SPL was subsequently merged with the operations of SPB from April 2012.

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 brand in southern India.

The company is managed by Mr. N. Gopalaratnam in the capacity of Chairman and Managing Director and is ably supported by well qualified and seasoned industry experts providing technical and managerial inputs.

<b>Brief Financials (Rs. crore)</b>	<b>FY17 (A)</b>	<b>FY18 (A)</b>
Total operating income	1114.36	1111.42
PBILDT	220.43	213.96
PAT	128.04	122.89
Overall gearing (times)	0.60	0.46
Interest coverage (times)	9.5	14.96

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**

**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](http://www.careratings.com). Investors/market intermediaries/regulators or others are welcome to write to [care@careratings.com](mailto:care@careratings.com) for any clarifications.

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**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	-	-	December 2021	120.34	CARE A+; Positive
Fund-based - LT-Cash Credit	-	-	-	205.00	CARE A+; Positive
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 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Fund-based - LT Term Loan	LT	120.34	CARE A+; Positive	1)CARE A+; Positive (07-Apr-18)	-	1)CARE A+; Stable (23-Jan-17)	1)CARE A+ (21-Jan-16)
2.	Fund-based – LT Cash Credit	LT	205.00	CARE A+; Positive	1)CARE A+; Positive (07-Apr-18)	-	1)CARE A+; Stable (23-Jan-17)	1)CARE A+ (21-Jan-16)
3.	Non-fund-based – ST BG/LC	ST	205.00	CARE A1+	1)CARE A1+ (07-Apr-18)	-	1)CARE A1+ (23-Jan-17)	1)CARE A1 (21-Jan-16)

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