

Seshasayee Paper & Boards Limited (Revised)

April 07, 2018

Ratings

Facilities	Amount (Rs. crore)	Ratings ¹	Rating Action
Long term Bank Facilities (Term Loan)	195.55	CARE A+; Positive (Single A Plus; Outlook: Positive)	Reaffirmed
Long term Bank Facilities (Fund based)	205.00	CARE A+; Positive (Single A Plus; Outlook: Positive)	Reaffirmed
Short term Bank Facilities (Non-fund based)	205.00	CARE A1+ (A One Plus)	Reaffirmed
Short term Bank Facilities (Fund based)	-	-	Withdrawn
Total Facilities	605.55 (Rs. Six hundred Five crore and Fifty Five lakhs only)		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The reaffirmation of rating assigned to the bank facilities of Seshasayee Paper and Boards Limited (SPBL) continues to factor in its long track record coupled with vast experience of the promoters in paper industry, strong distribution network and well established position in the South Indian paper market. Furthermore, the ratings also derive comfort from improved profitability margins as a result of majority of capex being completed resulting into synergies derived from integrated manufacturing operations, comfortable capital structure/debt coverage indicators, comfortable liquidity position and shortened operating cycle.

The rating strengths are however tempered by concerns over profit margins susceptible to volatility in prices of key raw materials and presence in cyclical and competitive nature of paper industry.

Going forward the ability of SPBL to increase its scale of operations, improve profit margins and maintain its comfortable capital structure through effective management of its working capital cycle are the key rating sensitivities. Any unplanned debt funded capex or higher reliance on debt to support the operations resulting into deterioration in capital structure is a key rating monitorable.

CARE has withdrawn the rating assigned to the short term bank facility (fund based) of SPBL with immediate effect, as the company has repaid the aforementioned short term bank facility (fund based) in full and there is no amount outstanding under the bank facility as on date.

Outlook: Positive

The outlook is revised to positive owing to expected completion of ongoing project resulting in improvement in scale of operations coupled with sustainability of healthy profitability margins and comfortable capital structure. The outlook may be revised to stable if the company is unable to sustain healthy profit margins and improvement in overall financial risk profile of the company.

Detailed description of the key rating drivers**Key Rating Strengths****Long track record coupled with vast experience of promoters in the paper industry**

Incorporated in 1960, SPBL, promoted by Mr. Vishwanathan of Seshasayee Brothers (Pvt.) Limited and currently spear-headed by Shri N Gopalaratnam as Chairman, has an established position in Southern India. The promoters have over five decades of experience in Indian paper industry. The company has professional management which oversees the overall operations of Erode and Tirunelveli units. They are ably assisted by a team of qualified and experienced professionals which are instrumental in providing technical and managerial inputs.

Well established distribution network

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

The company also has a strong marketing team and well established distribution network to support its off-take. The company is having strong presence in Southern India which contributes majority i.e. 65-70% of its total sales. The company primarily divides its markets as primary (Southern India), Secondary (Rest of India) and Export. The company has network of approximately 30 dealers appointed on commission basis and 8 depots in other parts of India and exports too (majorly in Sri Lanka, Nepal and Middle East countries). Total production is based on orders procured by these dealers.

Synergies between manufacturing sites resulting into improved business performance

The inorganic growth route adopted by SPBL through the acquisition of defunct paper manufacturing unit at Tirunelveli in FY12 and reviving its operations have helped SPBL to overcome project execution risk and provided the opportunity to maintain its market share in a competitive and growing paper industry. Moreover, Erode unit has integrated pulp manufacturing capacities which are higher than its requirements for paper manufacturing capacities. As a result, SPBL is utilizing the excess pulp production for manufacturing paper at Tirunelveli unit thus reducing its dependency on imported pulp thereby providing synergies to the company as a whole. Besides, the power requirement for the Tirunelveli plant has been met by the captive power generation at Erode plant. Thus, all these synergies have resulted in lower raw material and power costs and improved profit margins.

Substantial improvement in profitability margins

The overall profitability of the company has substantially improved with PBILDT margins from 10.64% in FY16 and 19.32% in FY17. The improvement is on account of improved captive power generation in its captive power plant after retrofit and wheeling of power to Tirunelveli unit, thereby eliminating purchase of costly third party power. Further benefit is derived from increased pulp supply from Erode unit that resulted in reduced consumption of costly imported pulp. The same has resulted in lower raw material costs. Hence, with all these cost saving benefits and economies of scale has resulted in improvement in profit margins.

Comfortable capital structure and debt coverage indicators

The overall capital structure of the company has improved from 0.89x as on March 31, 2016 to 0.48x as on March 31, 2017 and further to 0.39x owing to higher accretion of profit to networth and reduction in debt owing to decrease in working capital borrowings and term loans. This has also resulted in improvement in the debt coverage indicators.

Comfortable liquidity position as a result of short operating cycle

The overall liquidity profile of the company has improved with the negative operating cycle in FY17. Moreover the average working capital utilization level for the past twelve months ending February 2018 has been at around 5% for fund based limits while 42% for non-fund based limits.

Key Rating Weaknesses

Profit margins susceptible to volatile input prices

Raw material (bamboo and wood) cost is the major cost of paper manufactures which is volatile in nature and has witnessed a major uptrend during the last three years except for FY16. The supply of wood to domestic paper industry from natural forest resources is restricted by strict government regulations and causing raw material availability issues. In order to ensure long-term raw material security, the company has taken steps to step-up production of clonal seedlings and bare-rooted seedlings by the company's nursery as well as by the company sponsored nurseries, to support planting of nearly 12 crores of Casuarina and Eucalyptus seedlings in about 7000 ha by small and marginal farmers in Tamil Nadu. Thus, with the company increasing its emphasis on development and plantation of clonal saplings and excessive production of wood pulp at the Erode plant, SPBL's reliance on imported pulp has come down thereby mitigating the risk to an extent. Nevertheless, the company's profit margins is exposed to fluctuations in key raw material prices of bamboo, wood, wood pulp, waste paper and bagasse depending on the supply side i.e. availability and demand for raw material.

Competitive industry with paper players facing import threat

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 small paper mills are mainly based on recycled fibre, medium size mills are based on agro-residues and large mills on forest-based fibre. The increased competition will restrict 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 the 2.5% customs duty on paper in India has been brought down to zero; from 1st January 2014, as per the terms of the free trade agreement with the Association of Southeast Asian Nations (ASEAN). Due to this, there has been a rise in paper imports from ASEAN countries which has resulted in increasing share of imports in paper consumption in India. Earlier only few special grade paper and newsprint were imported but now, P&W paper is too being imported. Thus, inability of SPBL to pass-on the high input prices may further put pressure on its operating 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

Incorporated in 1960 and founded by Shri S. Viswanathan, Seshasayee Paper & Boards Limited (SPBL) belongs to 'Esvin Group'. It operates an integrated pulp and paper mill located at Pallipalayam, Erode and paper manufacturing mill at Tirunelveli. It commenced with a capacity of 20,000 TPA (tons per annum) at Erode (during 1962) and over the years the paper production capacity has been expanded in stages to 120,000 TPA. During February 2011, SPBL acquired Tirunelveli (Tamil Nadu) based defunct paper mill Subburaj Papers Limited (SPL) having a paper manufacturing capacity of 60,000 TPA (based on imported pulp and waste paper pulp). SPL was amalgamated with SPBL w.e.f April 1, 2012 after the high court order and the Tirunelveli unit is operating since then. SPBL manufactures a variety of papers such as printing and writing (P&W) grade papers (WPP), packing and wrapping grade papers, specialty grade papers, etc. Erode manufacturing unit is based on hardwoods and utilizes 'Eucalyptus' and 'Casuarina' trees for wood pulp besides bagasse.

Brief Financials (Rs. crore)	FY16 (A)	FY17 (A)
Total operating income	1,028.24	1,140.46
PBILDT	110.03	220.37
PAT	35.58	128.84
Overall gearing (times)	0.89	0.48
Interest coverage (times)	3.41	10.22

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. Investors/market intermediaries/regulators or others are welcome to write to 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-Cash Credit	-	-	-	205.00	CARE A+; Positive
Fund-based - LT-Term Loan	-	-	Jan 2021	195.55	CARE A+; Positive
Fund-based - ST-Term Loan	-	-	-	0.00	Withdrawn
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	195.55	CARE A+; Positive	-	-	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+; 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+ (23-Jan-17)	1)CARE A1 (21-Jan-16)
4.	Fund-based - ST-Term Loan	ST	-	-	-	-	1)CARE A1+ (23-Jan-17)	1)CARE A1 (21-Jan-16)

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