Press Release

Kherani Paper Mills Private Limited

August 31, 2020

Rating Assigned

Total Bank Facilities Rated*	Rs.55.00 Cr.
Long Term Rating	ACUITE BBB+/ Outlook: Stable (Assigned)

** Refer Annexure for details*

Rating Rationale

Acuité has assigned the long-term rating of **'ACUITE BBB+' (read as ACUITE triple B plus)** on the Rs.55.00 crore bank facilities of Kherani Paper Mills Private Limited (KPMPL). The outlook is **'Stable'.**

Mumbai based KPMPL is promoted by the G.N. Agarwal group and is engaged in the manufacturing of duplex board. The company was incorporated in 1988 and had its factory situated at Vapi, Gujarat and registered office at Mumbai, Maharashtra. KPMPL manufactures Duplex Boards in different grammages ranging from 180 GSM to 550 GSM. The manufacturing capacity of the plant is 36,000 metric tonne per annum (MTPA).

Analytical Approach

To arrive at the rating, Acuité has consolidated business and financial risk profiles of Gayatrishakti Paper and Boards Limited (GPBL) and KPMPL, hereinafter referred to as G.N. Agarwal group. The consolidation is on account of common management, significant cross-holdings, a similar line of business and significant financial linkages among the two entities. The differential rating is mainly on account of difference in scale of operations of these entities. Extent of consolidation is full.

About the group Company- Gayatrishakti Paper and Boards Limited

Mumbai based GPBL incorporated in 1996 is promoted by the G.N. Agarwal group. The company manufactures Premium Coated Paper Boards (duplex board) & Kraft paper. It has manufacturing units located in Gujarat Industrial Development Corporation (GIDC), i.e. duplex board unit at Vapi and Kraft paper unit at Sarigam. The combined manufacturing capacity of the plants is 216000 metric tonne per annum (MTPA). It sells its products through a dealership network to outlets. GPBL also has a duplex board unit operated under its associate company Kherani Paper Mills Private Limited (KPMPL), which caters to a local market while GPBL caters to premium segment.

GPBL offers coated packaging board (grey back) that find its application in serial packing, toys, appliances, industrial packing, top liner on corrugated boxes, garment and shoe packing, medicine boxes, kitchen spices, book covers, and other products; and white back (silkia) that are used for dry fruit products, soaps and cosmetics packing, publication covers, among others. The company also provides a blister pack board (grey and white back) that are used for a toothbrush, shaving blades, toys, electronic items, and other applications; and playing cards.

Key Rating Drivers

Strengths

- **Extensive experience of promoters, established position in the paper industry and established dealer network**

  GPBL is the flagship company of the G. N. Agarwal group, which is engaged into manufacturing of Premium Coated Paper Boards (duplex board). The Chairman and Managing Director of the company Mr. G. N. Agarwal has been associated with the paper industry for more than three decades. The extensive experience of the promoters and the management has helped the company build a strong presence in the market. GPBL and KPMPL have diversified presence on a pan-India basis with more than 150 distributor and dealer networks. The sales for duplex boards and kraft paper are through dealers to reputed clients for manufacturing of packaging products. GPBL and KPMPL have tied up with the printing companies who in turn carry out printing jobs for the end-user. The group has a healthy relationship with the dealers over two decades that further reduces the counterparty risk. The group has an advantage of the distribution network as dealers provide access to a wide range of packing industries such as Food Products, Personal Care, FMCG products, Oral Care & Hygiene Products, e-commerce industry among others. The group caters to a healthy portfolio of end consumers including AMUL, Hindustan Unilever Ltd, Colgate Palmolive India Ltd, Kellogg Company, Anchor Health and Beauty Care Pvt Ltd, among others.

Acuité believes that the group will continue to benefit from its extensive experience in the paper industry and established market presence through a healthy network of dealers and distributors. In addition, the business risk profile of the group will continue to derive support from a strong dealer network.

- **Location advantage**

The group's manufacturing units are located in Vapi and Sarigam (Gujarat) which is one of the most developed Industrial Zone of Gujarat connected by rail and road. Also, the distance from nearest port, i.e. Adani Hazira port is 142 kms for Unit I in Vapi and 160 kms from Unit II in Sarigam. As the group imports waste paper and exports finished goods, the location of the units provides an advantage of low transportation cost up to the ports. The presence of unit in GIDC provides a competitive advantage in terms of proximity to raw material, trained workforce and marketing. Further, the group has a pan-India presence and caters to international markets through exports.

- **Moderate financial risk profile**

The group's financial risk profile is marked by healthy net worth, high gearing and moderate coverage indicators. The net worth stood at Rs.145.15 crore as on March 31, 2020 (Provisional) against Rs.120.13 crore as on March 31, 2019. The gearing of the company improved to 2.54 times as on March 31, 2020 (Provisional) 2.88 times as on March 31, 2019. The total debt of Rs.368.87 crore as on March 31, 2020 (Provisional) comprises long-term loans from bank worth Rs.289.11 crore, unsecured loans worth Rs.8.50 crore and short-term working capital debt from the bank of Rs.71.26 crore. Due to high-interest cost and huge repayment obligations in the long term, coverage indicators stood moderate. Interest Coverage Ratio (ICR) has improved to 2.14 times for FY2020 (Provisional) from 1.92 times for FY2019. Similarly, Debt Service Coverage Ratio (DSCR) has improved to 1.99 times for FY2020 (Provisional) 1.85 times for FY2019. Further, the net cash accruals of the group stood healthy in the range of Rs.37.5– Rs. 50.00 crore for the last three years through FY2017 – FY2019 against minimal debt repayment obligations. This has reduced reliance on external debt to a large extent.

Acuité believes that the financial risk profile of the group will continue to improve in the near to medium term backed by healthy revenue levels, improvement in profitability and healthy net cash accruals.

- **Efficient working capital management**

The working capital management of the group is efficient, marked by Gross Current Assets (GCA) of 108 days for FY2020 (Provisional) as against 99 days in FY2019. The group has established customers and its strong distribution network, with around 90% of the sales closed through dealers. The GCA days are dominated by credit extended to its dealer network of around 30 - 60 days. Inventory majorly includes raw material and work in progress. Since the production is order based, finished goods inventory is low. The inventory and debtor levels stood at 39 days and 65 days in FY2020 (Provisional) as against 34 days and 62 days in FY2019, respectively.

Acuité believes that efficient working capital management will be crucial to the group in order to maintain a stable credit profile.

Weaknesses

- **Large capital requirement**

The business involves regular capex on facilities and innovation. GPBL has been undergoing capex from time to time to increase its capacity and upgrade technology. GPBL has increased its kraft paper manufacturing capacity from 90,000 MTPA to 1,44,000 MTPA over the last four years. The same is expected to increase to 1,80,000 MTPA in the near term.

Acuité draws comfort from the group's comfortable liquidity profile, as well as its low debt repayment obligations in the near term. Acuité notes that the capex has been funded with long tenure term loans with up to a seven-year repayment period. Hence, despite the increase in annual repayment burden from Q2 FY2021, Acuité believes the group has sufficient liquidity cushion, operating profits and cash accruals for capital requirements.

* **Susceptibility of margins to fluctuations in raw material prices**

  Operating margins of the group have remained moderate in the range of 10~13 percent during the past 3 years. The company reported an operating margin of 12.30 percent during FY2019, as against 10.62 percent in the previous year. The duplex board and kraft paper manufacturers in India are exposed to the risk of volatility in waste paper prices, largely due to intense competition. On account of competitive pressures, players face challenges in passing on increased costs to end-users. In addition, the profitability of players with power plants is exposed to fluctuation in the prices of coal. The business risk profile will remain constrained by exposure to the downturn in the paper industry. The rise in the prices of duplex paper over that of waste paper is expected to be gradual, rendering the profitability susceptible to volatility in the price of paper.

* **Exposure to intense competition**

  Competition from large and established players is intense in the fragmented packaging industry. This is because of low capital and technology requirements, and therefore, low entry barriers. Also, the lead time to set up a small unit is low at 12-18 months. Overcapacity and limited product differentiation add to the competitive pressure. However, the group has been able to sustain and improve its operational performance over the years.

Liquidity position: Adequate

The group has adequate liquidity marked by healthy net cash accruals in the range of ~ Rs.37.5– Rs.50.00 crore crores against minimal debt obligations during the last three years. Major debt repayment obligations will begin only from the second quarter of FY2021 due to moratorium period. The working capital operations are efficiently managed, marked by Gross Current Asset (GCA) days of 108 in FY2020 (Provisional). The working capital facilities of the company remained utilized at ~75 per cent during the last six months period ended in July 2020. The unencumbered cash and bank balances stood at Rs.1.40 crore as on March 31, 2020 (Provisional). The current ratio stood at 1.16 times as on March 31, 2020 (Provisional). Acuité believes that the liquidity of the group will further improve on account of increasing net cash accruals sufficient to service maturing debt obligations and improving financial risk profile.

Rating Sensitivities

* Continuous improvement in the scale of operations while maintaining profitability leading to improvement in overall financial risk profile.
* Stretch in working capital cycle, leading to an increase in working capital borrowing and weakening of financial risk profile.

Material Covenants

1. DSCR >= 1.20 times.
2. TOL / TNW <= 2.75 times.
3. Net FA / Term Debt >=1.50 times.
4. Net Debt / EBITDA < 3.50 times.

Outlook: Stable

Acuité believes that the group will maintain a stable outlook over the near to medium term owing to its experienced management and established market position. The outlook may be revised to 'Positive' in case the company registers healthy growth in revenues while maintaining profitability margins, improvement in capital structure and working capital management. Conversely, the outlook may be revised to 'Negative' in case of a significant decline in revenue, profit margins or deterioration in the financial risk profile, particularly its liquidity most likely as a result of higher than envisaged working capital or capex requirements.

About the Rated Entity - Key Financials

	Unit	FY20 (Actual)	FY19 (Actual)
Operating Income	Rs. Cr.	789.98	817.85
PAT	Rs. Cr.	25.02	19.97
PAT Margin	(%)	3.17	2.44
Total Debt/Tangible Net Worth	Times	2.54	2.88
PBDIT/Interest	Times	2.14	1.92

Status of non-cooperation with previous CRA (if applicable)
None

Any other information
None

Applicable Criteria

- Default Recognition - https://www.acuite.in/view-rating-criteria-52.htm
- Manufacturing Entities - https://www.acuite.in/view-rating-criteria-59.htm
- Financial Ratios And Adjustments - https://www.acuite.in/view-rating-criteria-53.htm
- Consolidation Of Companies - https://www.acuite.in/view-rating-criteria-60.htm

Note on complexity levels of the rated instrument
https://www.acuite.in/view-rating-criteria-55.htm

Rating History (Upto last three years)
Not Applicable

***Annexure – Details of instruments rated**

Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Crore)	Ratings/Outlook
Cash Credit	Not Applicable	Not Applicable	Not Applicable	15.00	ACUITE BBB+/Stable (Assigned)
Cash Credit	Not Applicable	Not Applicable	Not Applicable	10.00	ACUITE BBB+/Stable (Assigned)
Term loans	Dec 2019	Not Applicable	Dec 2026	10.00	ACUITE BBB+/Stable (Assigned)
Term loans	Dec 2019	Not Applicable	Dec 2026	20.00	ACUITE BBB+/Stable (Assigned)

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About Acuité Ratings & Research:

Acuité Ratings & Research Limited is a full-service Credit Rating Agency registered with the Securities and Exchange Board of India (SEBI). The company received RBI Accreditation as an External Credit Assessment Institution (ECAI), for Bank Loan Ratings under BASEL-II norms in the year 2012. Since then, it has assigned more than 6,000 credit ratings to various securities, debt instruments and bank facilities of entities spread across the country and across a wide cross section of industries. It has its Registered and Head Office in Mumbai.