August 22, 2024

Aryan Paper Mills Pvt. Ltd.: Ratings Downgraded; Outlook revised to Stable from Negative; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based – Term loans	141.42	166.50	[ICRA]BBB- (Stable); Rating Downgraded from [ICRA]BBB (Negative), Outlook revised to Stable from Negative; assigned for enhanced limits
Fund-based – Cash credit	20.00	20.00	[ICRA]BBB- (Stable); Rating Downgraded from [ICRA]BBB (Negative), Outlook revised to Stable from Negative
Non-fund Based – Letter of credit	4.00	4.00	[ICRA]A3; Rating Downgraded from [ICRA]A3+
Non-fund Based – Credit exposure limit	2.40	2.40	[ICRA]A3; Rating Downgraded from [ICRA]A3+
Unallocated limits	4.00	-	-
Fixed deposit	6.00	15.00	[ICRA]BBB- (Stable); Rating Downgraded from [ICRA]BBB (Negative); Outlook revised to Stable from Negative; assigned for enhanced limits
Total	**177.82**	**207.90**	

**Instrument details are provided in Annexure-I*

Rationale

The downgraded ratings for Aryan Paper Mills Pvt. Ltd. (APML or the company) consider the continued pressure on the company's debt protection metrics in the near term, primarily due to the ongoing debt-funded capex related to capacity expansion. The project expansion witnessed a cost and time overrun and is now expected to commence in September 2024. APML's performance was affected in FY2024 amid volatility in wastepaper prices and subdued paper realisations, resulting in a decline of 23% in the top line for FY2024 compared to FY2023. The top line was also impacted by the drop in export sales, which declined by more than half in FY2024 due to reduced exports to key markets in West Asia. Such factors adversely impacted the margins and cash accruals in FY2024. The margin profile, however, is expected to improve in FY2025, backed by the commercialisation of the new plant in H2 FY2025 and stabilisation in paper prices. However, the margin profile is likely to remain well below the peaks witnessed before the pandemic. The stabilisation of the new plant with a steady ramp-up of operations, leading to better quality output, remains critical for the company's credit profile and will remain a key rating monitorable.

The ratings continue to remain constrained by APML's concentrated product portfolio (mainly kraft paper) and the vulnerability of its profitability to volatility in wastepaper prices, along with foreign exchange (forex) fluctuations; however, this is naturally hedged by exports to some extent. The company's ability to pass on any rise in input prices to improve its margins will be key from a credit rating perspective, going forward. The ratings also remain constrained by the stiff competition in the kraft paper segment from the unorganised players, resulting in pricing pressures.

The ratings, however, favourably factor in APML's extensive track record of operations and its promoters' experience in paper manufacturing, the company's established customer and dealership networks, as well as its healthy capacity utilisation levels.

The Stable outlook on the rating reflects ICRA's opinion that the company will continue benefitting from its established brand presence in the kraft paper industry, capacity and product diversification, as well as adequate liquidity levels, which are expected to be derived from the ongoing capex.

Key rating drivers and their description

Credit strengths

Established track record in kraft paper industry and extensive experience of promoters – APML has an established track record of more than three decades in the manufacturing of kraft paper. Mr. Sunil Shah, promoter, and Managing Director of the company, has three decades of experience in the industry and is also assisted by an experienced management team.

Healthy capacity utilisation levels and established network of dealers – The capacity utilisation remained healthy at over 90% over the past few fiscals, backed by healthy demand. Furthermore, the company is expanding its capacity, which is expected to reach 1,25,000 metric tonnes per annum (MTPA) in H2 FY2025 from the current level of 55,000 MTPA. Over the years, the company has established its presence as a preferred kraft paper supplier and has a wide dealership network in the industry.

Credit challenges

Sizeable debt-funded capex to keep coverage metrics under check in near term – APML is in the final stage of completing the capex of ~Rs. 220 crore, scheduled over FY2022-FY2025 to increase its kraft paper manufacturing capacity to 1,25,000 MTPA from 55,000 MTPA. It is noted that the project cost has escalated from ~Rs. 170 crore, which was initially envisaged. The cost escalations are for additional machinery and modifications in buildings. The initial capex was funded through a mix of a term debt of Rs. 120 crore and promoters' funds in the form of equity of Rs. 6.0 crore, unsecured loans of Rs. 4.0 crore and the rest through internal accruals. The funding for cost escalations has been made through a term debt of Rs. 36 crore, promoters' funds in the form of equity of Rs. 14.0 crore and unsecured loans of Rs. 2.0 crore. The project commercialisation is also delayed until September 2024 from the initial commencement date set for April 2024. Although the capex will be value accretive in terms of better efficiency, it is likely to keep the coverage indicators under pressure in the near term. The company's ability to generate commensurate returns from the capex and improve its debt protection metrics over the medium term remains key monitorable from the rating perspective.

Margins remain susceptible to volatility in adverse fluctuations in wastepaper and coal prices, as well as forex movements – APML's profitability remains exposed to sharp fluctuations in raw material prices, primarily wastepaper, which is largely imported. The volatility in the raw material prices and inventory build-up at higher prices resulted in a mismatch between raw material costs and price realisations, given the product's commodity nature. Consequently, the company`s margin fell sharply in the last two fiscals over FY2022, given its inability to fully pass on the increased cost to its end customers. Thus, APML's margins remain exposed to adverse fluctuations in wastepaper and coal prices. Further, the company uses imported wastepaper, making it vulnerable to movements in forex rates. The margins are expected to improve from H2 FY2025, backed by the commercialisation of the new manufacturing unit, which is expected to garner enhanced margins driven by better quality output and operational efficiencies.

Product concentration risk and fragmented industry structure with stiff competition – APML is involved in the manufacturing of a single product, i.e., kraft paper, which exposes the company to product concentration risk. Further, the kraft paper industry is highly fragmented, with stiff competition from numerous organised and unorganised players. However, APML produces kraft paper with a burst factor (BF) of 20-35. Competition in the higher BF range (above 20) is less intense than in lower BF range because of the complexity of the manufacturing process and the capital costs involved in setting up the production line for higher BF paper.

Liquidity position: Adequate

The company's liquidity is adequate, supported by the expected requisite generation of cash accruals compared to debt repayments. Its average working capital utilisation stood at ~78% for the 12-month period ending June 2024. Further, the company also enhanced its cash credit limit to Rs. 23 crore from July 2023, which further supports the liquidity profile. ICRA notes that the repayment for the new capex will begin from FY2026, by when the repayments for the existing term loans are expected to be largely completed. Also, the ballooning nature of the repayment structure for the new capex is expected to aid the liquidity profile.

Rating sensitivities

Positive factors – ICRA could upgrade the company's ratings if it registers a healthy ramp-up in operations, along with a sustained improvement in profitability, leading to enhanced credit metrics and liquidity.

Negative factors – Pressure on APML's rating could arise if there is a material decline in revenues or moderation in profitability leading to a stretch in coverage metrics. The company's inability to scale up after the commercialisation of the new unit leading to delay in commensurate returns, will also be a negative. Specific credit metrics for ratings downgrade will include a DSCR of less than 1.2 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	Not applicable
Consolidation/Standalone	The rating is based on the standalone financial profile of the company

About the company

Aryan Paper Mills Private Limited was incorporated in 1990 by Mr. Sunil K. Shah and his friends. The company's manufacturing facilities are in the Gujarat Industrial Development Corporation (GIDC) area of Vapi, Gujarat. APML manufactures kraft paper in varying grammage and BF specifications, which are used to produce corrugated boxes for packaging material. With modifications and expansions over the years, the installed production capacity of the plant has gradually increased to 55,000 MTPA. The company also has a 4.8-MW power plant, a 1.25-MW wind power plant, 0.331-MW solar plant and 1.1-MW from the Gujarat Electricity Board, which are enough to support the energy requirements for its planned capacity addition.

Key financial indicators (audited)

APML	FY2023	FY2024
Operating income	224.3	172.2
PAT	5.2	1.3
OPBDIT/OI	5.8%	5.2%
PAT/OI	2.3%	0.8%
Total outside liabilities/Tangible net worth (times)	1.3	2.3
Total debt/OPBDIT (times)	4.2	16.3
Interest coverage (times)	3.0	2.2

Source: Company, ICRA Research; All ratios as per ICRA's calculations; Amount in Rs. crore

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Current (FY2025)			Chronology of rating history for the past 3 years					
				FY2024		FY2023		FY2022	
	Type	Amount Rated (Rs Crore)	Aug 22, 2024	Date	Rating	Date	Rating	Date	Rating	Date	Rating
Term loans	**Long term**	166.50	[ICRA]BBB-(Stable)	Aug 30, 2023	[ICRA]BBB (Negative)	Aug 29, 2022	[ICRA]BBB+ (Negative)	Jun 02, 2022	[ICRA]BBB+ (Stable)	Aug 26, 2021	[ICRA]BBB+ (Stable)
Cash credit	**Long term**	20.00	[ICRA]BBB-(Stable)	Aug 30, 2023	[ICRA]BBB (Negative)	Aug 29, 2022	[ICRA]BBB+ (Negative)	Jun 02, 2022	[ICRA]BBB+ (Stable)	Aug 26, 2021	[ICRA]BBB+ (Stable)
Letter of credit	**Short term**	4.00	[ICRA]A3	Aug 30, 2023	[ICRA]A3+	Aug 29, 2022	[ICRA]A2	Jun 02, 2022	[ICRA]A2	Aug 26, 2021	[ICRA]A2
Credit exposure limit	**Short term**	2.40	[ICRA]A3	Aug 30, 2023	[ICRA]A3+	Aug 29, 2022	[ICRA]A2	Jun 02, 2022	[ICRA]A2	Aug 26, 2021	[ICRA]A2
Unallocated limits	**Short term**	-	-	Aug 30, 2023	[ICRA]A3+	Aug 29, 2022	-	Jun 02, 2022	-	Aug 26, 2021	-
Fixed deposit	**Long term**	15.00	[ICRA]BBB-(Stable)	Aug 30, 2023	[ICRA]BBB (Negative)	Aug 29, 2022	[ICRA]BBB+ (Negative)	Jun 02, 2022	[ICRA]BBB+ (Stable)	Aug 26, 2021	MA (Stable)

Complexity level of the rated instruments

Instrument	Complexity Indicator
Term loans	Simple
Cash credit	Simple
Letter of credit	Very simple
Credit exposure limit	Very simple
Fixed deposit	Very simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Term loans**	FY2016	NA	FY2033	166.50	[ICRA]BBB-(Stable)
NA	**Cash credit**	NA	NA	NA	20.00	[ICRA]BBB-(Stable)
NA	**Letter of credit**	NA	NA	NA	4.00	[ICRA]A3
NA	**Credit exposure limit**	NA	NA	NA	2.40	[ICRA]A3
NA	**Fixed deposit**	NA	NA	NA	15.00	[ICRA]BBB-(Stable)

Source: Company

[Please click here to view details of lender-wise facilities rated by ICRA]

Annexure II: List of entities considered for consolidated analysis – Not applicable

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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