December 29, 2022

Subam Papers Private Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund Based - Cash Credit	50.00	50.00	[ICRA]A- (Stable); reaffirmed
Long-term Fund Based - Term loan	7.38	33.23	[ICRA]A- (Stable); reaffirmed
Long-term Unallocated	26.12	0.27	[ICRA]A- (Stable); reaffirmed
Total	**83.50**	**83.50**	

**Instrument details are provided in Annexure-I*

Rationale

The rating reaffirmation favourably factors in Subam Paper Private Limited's (SPPL/the company) established market presence in the paper industry in Tamil Nadu; the favourable demand outlook; and the company's integrated production facility, expansion into margin accretive segment and access to diversified raw material sources which are likely to support accruals going forward. The company currently has around 450 direct customers and caters to several end-user industries including breweries and distilleries, e-commerce, fast-moving consumer goods (FMCG), healthcare, textiles and pharmaceuticals to name a few. It has had history of low churn rates and added multiple new customers as well in the last few years, although its geographic concentration within Tamil Nadu remains. The growing demand for packaging augurs well for the company and this, along with the recent entry into duplex paper manufacturing would drive revenue growth and customer expansion in the near to medium term.

The company has integrated manufacturing setup with adequate captive renewable power capacity (10 MW of solar power and 1.7 MW of wind power), which ensures availability of power and provides cost advantages. Also, the recent expansion into the margin-accretive duplex paper segment and access to diversified raw material sources are likely to be favourable for the company. However, SPPL's operating profit margins (OPM) remain vulnerable to the inherent cyclicality in the paper business and volatility in raw material costs, fuel prices and exchange rates (OPM reduced to 13.8% in FY2022 from 18.5% in FY2021). The elevated raw material and fuel prices, albeit some softening in the recent months, are expected to limit benefits accruing from usage of low-cost captive power and favourable product mix in FY2023 to an extent. Also, the company faces stiff competition from both organised and unorganised players in the paper industry, which limits its pricing flexibility and bargaining power with customers to an extent.

The rating is constrained by the moderation in the coverage metrics because of the debt-funded capex of Rs. 147.6 crore undertaken in FY2022 and H1 FY2023. As a result of increase in debt levels, SPPL's debt/OPBDITA moderated to 3.4 times for FY2022 (PY: 0.2 times) and its net cash accruals/Total debt was 24.2% for the same period (PY: 250.7%). ICRA expects SPPL's debt metrics to improve going forward, with anticipated improvement in accruals and in the absence of significant capex plans.

Key rating drivers and their description

Credit strengths

Established presence with a strong customer base in the packaging industry; caters to a variety of end-user segments – With almost three decades of presence, SPPL is an established player in the kraft paper industry in Tamil Nadu. The company currently has around 450 direct customers and caters to several end-user industries including breweries and distilleries, e-commerce, fast-moving consumer goods (FMCG), healthcare, textiles and pharmaceuticals to name a few. The company has had history of low churn rates and has added multiple new customers as well in the last few years.

Favourable demand outlook – The growing demand for packaging from e-commerce, food and food products, FMCG, textiles and pharmaceutical sectors, augurs well for the company in the near to medium term. Further, the long-term demand outlook for the domestic market remains favourable because of low per-capita usage and increasing usage of packaging products.

Access to diversified raw material sources, integrated production facility and expansion into margin accretive segments to support margins going forward – The company procures wastepaper from multiple suppliers in both domestic and overseas markets, mitigating risks arising from supply-chain challenges and unfavourable forex movements to an extent. Further, it has an integrated manufacturing setup with adequate captive renewable power capacity (10 MW of solar power and 1.7 MW of wind power), ensuring availability of power and providing cost advantages. The company met 47.5% of its power requirements from captive sources in H1 FY2023. Also, SPPL has expanded into the margin-accretive duplex paper manufacturing from February 2022. All of these are likely to benefit the company's margins going forward.

Credit challenges

Sizeable debt-funded capex moderates coverage indicators – The company has undertaken debt-funded capex of Rs. 105.0 crore in FY2022, primarily for expansion into manufacturing of duplex papers and building captive solar power capacity. Further, it has undertaken capex of ~Rs. 45.8 crore in H1 FY2023, primarily for expansion of kraft paper capacity, and around Rs. 30.0 crore is remaining in H2 FY2023 as part of the planned capex. As a result of increase in debt levels, the company's coverage metrics have moderated from previous levels. SPPL's debt/OPBDITA stood at 3.4 times for FY2022 (PY: 0.2 times) and its interest coverage was 8.7 times for the same period (PY: 21.0 times). ICRA, however, expects the debt metrics to improve going forward, with anticipated improvement in accruals and in the absence of significant capex plans going forward.

Susceptibility of profit margins to input costs – The company's profit margins remain vulnerable to cyclicality in the paper business and volatility in raw material costs, fuel prices and exchange rates. The same is reflected via a dip in operating margins to 13.8% in FY2022 from 18.5% in FY2021. The elevated raw material and fuel prices, albeit some softening in the recent months, are expected to limit benefits accruing from usage of low-cost captive power and favourable product mix in FY2023 to an extent.

High geographic concentration; fragmented industry structure with stiff competition – The company has moderate scale of operations with relatively high geographical concentration in Tamil Nadu. Further, the company faces stiff competition from both organised and unorganised players in the paper industry, which limits its pricing flexibility and bargaining power with customers to an extent. The former risk, however, is partially mitigated by SPPL's established customer base, history of low churn rates and periodic addition of customers. The company's measures for improving its cost structure are likely to mitigate pressure on profits because of competition to an extent.

Liquidity position: Adequate

SPPL's liquidity position is adequate supported by anticipated healthy cash flow from operations. The company had undrawn working capital lines of Rs. 10.9 crore as on September 30, 2022, and its working capital utilisation was 77% of drawing power for the period October 2021 to September 2022. The company had negligible cash and bank balances as on September 30, 2022. In relation to these sources of cash, SPPL has repayment obligations of around Rs. 5.0 crore in H2 FY2023, Rs. 15.1 crore in FY2024 and 25.4 crore in FY2025 on its sanctioned term loans. The company does not have significant capex commitments over the medium term, post completion of the pending capex of around Rs. 30.0 crore for the kraft paper capacity enhancement project in H2 FY2023.

Rating sensitivities

Positive factors – SPPL's ratings could be upgraded if the company is able to significantly scale up its operations leading to improvement in profit margins and debt coverage metrics. Specific credit metrics include net debt/OPBDITA less than 1.8 times on a sustained basis.

Negative factors – Negative pressure on SPPL's rating could emerge with sharp deterioration in the earnings or significant rise in net debt, due to working capital intensity, higher capex or increase in advances to Group entities. Specific credit metrics that may lead to a rating downgrade include DSCR less than 2.0 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 ratings are based on the consolidated financials of the company - Details of consolidation is given in Annexure-2

About the company

SPPL is involved in manufacturing kraft and duplex papers and has had presence for almost three decades. While the company was engaged only in kraft paper manufacturing earlier, it has currently expanded its capacities to duplex paper manufacturing. Further, there is also an ongoing capacity enhancement in its kraft paper capacity which is expected to be operational from Q1 FY2024. Post this, it will have a cumulative capacity of 1.95 MTPA, in its plants located in Tirunelveli. The company has about 450 customers currently and caters to multiple end-user industries including breweries and distilleries, e-commerce, fast-moving consumer goods (FMCG), healthcare, textiles and pharmaceuticals to name a few.

The company has 2 subsidiaries – namely Subam Paper and Boards Private Limited (SPBPL) and Subam Agro Ventures Private Limited (SAVPL). SPBPL was formed in FY2021, houses 0.2 lakh MTPA of kraft paper capacity and is the entity where the ongoing kraft paper expansion is being undertaken. SAVPL holds the land parcel where the solar capacity has been installed. This apart, SPPL also has two associates – B.M.M Paper Board Private Limited and Saradhambika Paper and Board Mills Private Limited – which are also into manufacturing of paper based products. SPPL is managed by Mr. T. Balakumar, who is a first-generation entrepreneur with close to three decades of experience in the industrial paper industry.

Key financial indicators (audited)

Consolidated	FY2021	FY2022
Operating income	270.4	328.2
PAT	21.6	28.6
OPBDIT/OI	18.5%	13.8%
PAT/OI	8.0%	8.7%
Total outside liabilities/Tangible net worth (times)	0.4	1.3
Total debt/OPBDIT (times)	0.2	3.4
Interest coverage (times)	21.0	8.7

Amount in Rs crore; Source: Company, ICRA Research; Financial ratios in this document are ICRA adjusted figures and may not be directly comparable with results reported by the company in some instances; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; total debt includes lease liabilities

Status of non-cooperation with previous CRA:

CRISIL Ratings in its rationale published on January 29, 2022, stated the following:

CRISIL Ratings has been consistently following up with Subam Papers Private Limited (SPPL) for obtaining information through letters and emails dated November 13, 2021 and January 12, 2022 among others, apart from telephonic communication. However, the issuer has remained non cooperative. Despite repeated attempts to engage with the management, CRISIL Ratings failed to receive any information on either the financial performance or strategic intent of SPPL, which restricts CRISIL Ratings' ability to take a forward looking view on the entity's credit quality. CRISIL Ratings believes that rating action on SPPL is consistent with 'Assessing Information Adequacy Risk'. Based on the last available information, the ratings on bank facilities of SPPL continues to be 'CRISIL B/Stable Issuer Not Cooperating'.

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2023)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as of Sep 30, 2022 (Rs. crore)	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020
					Dec 29, 2022	Sep 06, 2021	July 15, 2020	-
1	**Cash Credit**	Long term	50.00	-	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	-
2	**Term Loan**	Long term	33.23	33.23	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	-
3	**Unallocated**	Long term	0.27	-	[ICRA]A- (Stable)	[ICRA]A- (Stable)	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund-based – Cash Credit	Simple
Long-term – Term Loan	Simple
Long-term – Unallocated	Not Applicable

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	**Cash Credit**	NA	NA	NA	50.00	[ICRA]A- (Stable)
NA	**Term Loan**	FY2018	NA	FY2029	33.23	[ICRA]A- (Stable)
NA	**Unallocated**	NA	NA	NA	0.27	[ICRA]A- (Stable)

Source: Company

Annexure II: List of entities considered for consolidated analysis

Company Name	SPPL Ownership	Consolidation Approach
Subam Agro Ventures Private Limited	100.00%	Full Consolidation
Subam Paper and Boards Private Limited	99.88%	Full Consolidation
B.M.M Paper Board Private Limited	28.57%	Equity Method
Saradhambika Paper and Board Mills Private Limited	28.13%	Equity Method

Source: Company

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About ICRA Limited:

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