October 27, 2023

Tamil Nadu Newsprint & Papers Limited: Long-term rating upgraded to [ICRA]A+(Stable) and short-term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Term Loans	1,717.05	1,623.11	[ICRA]A+(Stable); upgraded from [ICRA]A(Stable)
Long-term/ Short-term, Fund/ Non-fund Based Limits	700.00	775.00	[ICRA]A+(Stable)/ [ICRA]A1; Long-term rating upgraded from [ICRA]A(Stable) & Short-term rating reaffirmed
Long-term, Unallocated Limits	217.95	311.89	[ICRA]A+(Stable); upgraded from [ICRA]A(Stable)
Long-term/ Short-term, Unallocated Limits	298.00	223.00	[ICRA]A+(Stable)/ [ICRA]A1; Long-term rating upgraded from [ICRA]A(Stable) & Short-term rating reaffirmed
Total	**2,933.00**	**2,933.00**	

**Instrument details are provided in Annexure-I*

Rationale

The upgrade in the long-term rating considers the improvement in operational and financial profile of Tamil Nadu Newsprint & Papers Limited (TNPL) in FY2023 and expectation of the same to be sustained, going forward. The strong performance in FY2023 and Q1 FY2024 was aided by a healthy demand for the writing and printing paper (PWP) segment and turnaround for its paper board division. High-capacity utilisation amid favourable demand, higher realisations, cost saving triggered by start of commercial operations of the in-house pulp unit and better working capital management resulted in better earnings and sharp reduction in TNPL's debt levels, thereby improving its debt protection metrics. Although the average realisations are expected to be lower in FY2024 over FY2023, the operating margins in FY2024 are expected to be supported by in-house pulp manufacturing, healthy demand for the PWP segment and value-added product mix in the board segment. ICRA notes that TNPL has deferred its capex plan on phase 2 expansion of its PWP/ board segment. However, the company will carry on with a curtailed capex programme in the range of ~Rs. 1,000 crore in the next three years. The ratings also continue to factor in TNPL's long operational history, strong management profile, dominant market position in the domestic PWP segment and diversified sales and distribution network.

The ratings are, however, constrained by the vulnerability of revenues and margins to net sales realisation of paper, which has been volatile recently, susceptibility of margins to pulp and waste paper prices along with fuel (primarily coal). ICRA also notes that with the next expansion phase going on hold, the debt levels in the near to medium term are expected to be at lower levels than earlier expectations. ICRA, however, will continue to monitor the development related to capex plans and will assess the impact once definite clarity emerges on the matter.

The Stable outlook on the rating reflects ICRA's opinion that TNPL will continue to benefit from its established position, competitive advantages in the PWP segment and healthy financial flexibility with the lenders.

Key rating drivers and their description

Credit strengths

Healthy revenue growth and profitability in FY2023 resulting in sharp improvement in debt protection metrics – The company reported healthy revenue growth of 29% to Rs. 5,179.9 crore in FY2023 owing to favourable demand and high average sales realisation levels for the PWP and board segments in FY2023. TNPL's manufacturing capacity utilisation remained healthy at more than 100% for the PWP plant and more than 80% for boards in FY2023. TNPL has increased the manufacturing capacity of its PWP plant to 4.4 lakh MTPA from 4.0 lakh MTPA by debottlenecking and making minor modifications in the plant after having received consent to operate (CTO) for higher production capacity. Further, the operating margins also witnessed significant improvement to 18.8% in FY2023 and 24.5% in Q1 FY2024 owing to healthy sales realisations, lower dependence on high-cost imported pulp due to commencement of its new pulp mill in Unit II and sale of value-added products in the board segment. Although the average realisations are expected to be lower in FY2024 compared to FY2023, the operating margins in FY2024 are expected to be supported by in-house pulp manufacturing, healthy demand scenario for the PWP segment and value-added product mix in the board segment. Coupled with better working capital management, which provided the much-needed flip to its earnings, the company witnessed sharp reduction in debt levels, thereby improving its debt protection metrics. The coverage indicators also improved as reflected by interest coverage of 5.4 times in FY2023 (2.4 times in FY2022) and total debt/ OPBITDA of 1.9 times in FY2023 (6.0 times in FY2022). The same is expected to continue in the near term given the truncated capex programme and healthy margin expectations.

Leading market position in PWP segment – The company has an operating track record of more than three decades and an established brand name in the PWP segment. It has a well-diversified sales and distribution network across India, consisting of non-exclusive dealers who account for ~45-60% of its sales (PWP). While the sales are directly handled by TNPL for Government and private sector entities, which account for ~15-25% of PWP sales, exports account for the remaining ~10-20% of PWP sales. The company started board production from May 2016, which drove ~26% of its operating income in FY2023.

Access to diversified raw material sources and integrated production facility – The company has a long-term tie-up with several sugar mills near its manufacturing unit/s for the supply of bagasse against commensurate exchange of steam or coal. Additionally, TNPL enters short-term tie-ups with other sugar mills during periods of reduced availability of bagasse. The prices of bagasse are dependent on sugar cane production in Tamil Nadu and cost of coal, mainly imported. It has also been using wood for pulping. To ensure availability of wood, TNPL initiated farm forestry and captive plantation schemes in FY2005. Apart from the farm forestry programme and captive sources, significant quantities of wood are currently being procured from the two State Government of Tamil Nadu entities— Tamil Nadu Forest Plantation Corporation Limited (TAFCORN) and Principal Chief Conservator of Forests (PCCF). Procurement of raw materials from diversified sources mitigates raw material availability risks. Earlier, the company used to enjoy stronger profitability than its peers, mainly because of predominant usage of bagasse as a key raw material, which is cheaper than wood or imported pulp. Further, availability of wood from captive sources at competitive rates also aids comfort in raw material procurement cost.

High financial flexibility and competitive borrowing costs from healthy standing among lenders – Given its established presence in the domestic PWP segment and its strong management profile, TNPL continues to enjoy high financial flexibility with lenders, evident from the competitive borrowing costs and general corporate loans availed at short notice to support its liquidity profile.

Demand dynamics remain favourable amid healthy demand for paper and board from end-user sectors – Long-term demand outlook for paper in the domestic market remains favourable because of its low per-capita usage as on date, compared to global standards and increasing usage of packaging products. Growing demand for packaging from e-commerce, food and food products, FMCG, textiles and pharmaceutical sectors augurs well for the company. However, rising digitisation remains a threat for the growth of the PWP segment on a longer term basis.

Credit challenges

Relatively leveraged but improving capital structure – TNPL had undertaken debt-funded capex in the last few years for setting up a new board plant, expanding its cement plant and new pulp unit, which impacted its gearing. Although, the company's capital structure improved to 1.0 time as on March 31, 2023 from 1.4 times as on March 31, 2022 owing to significant debt reduction and healthy accretion to reserves, it continues to remains leveraged.

Susceptibility to cyclicality in paper industry – Paper, being a commodity, is exposed to economic cycles. While its demand is expected to be favourable in India because of its low per-capita consumption in domestic markets compared to global standards, there could be aberrant years, given the cyclical nature of the industry. Any increase in imported coal prices and reduced availability of bagasse and wood at competitive rates can offset the advantage enjoyed by TNPL with respect to its operating profit margins. Steep volatility in imported coal prices or reduced availability of wood or bagasse at competitive rates could lead to erosion of the competitive advantage it enjoys and adversely impact margins, as witnessed recently.

Margins remain exposed to fluctuations in input costs, primarily bagasse, pulp and coal – The profitability of the company remains vulnerable to cyclicality in the paper business, availability of water and raw materials, and volatility in bagasse, pulp, chemicals and international coal prices, as well as exchange rates. The company is also exposed to vulnerability of revenues and margins to net sales realisations of paper, which has been volatile in recent times.

Exposed to project execution risk related to tissue paper and revamping of power plants – TNPL is planning to set up a tissue manufacturing plant at a cost of ~Rs. 300 crore and capex for revamping its steam and power system at an estimated cost of Rs. 500-550 crore, to be completed in medium term. Hence, it remains exposed to project execution risk. Further, timely commencement of the project without any cost overrun remains a key rating monitorable. The project cost is proposed to be funded through a mix of term loan and internal accruals. Despite the onboarding of the debt, the debt-coverage metrics are likely to remain at similar levels over FY2025–FY2026. The company's ability to achieve financial closure at favourable terms to keep capital structure and coverage indicators under check, will remain a key rating sensitivity, going forward. ICRA also notes that given the phase II expansion on hold, the debt levels in near to medium term is expected to be at lower levels compared to earlier expectations. ICRA, however, will continue to monitor the development related to this and will assess the impact on credit metrics once clarity emerges on the same.

Environmental and Social Risks

Environmental considerations: The paper manufacturing industry is exposed to environmental risks of air, water and land pollution, as discarded paper and paperboard make up a sizeable portion of solid municipal waste in landfills. Pulp and paper generate a notable amount of industrial air, water, and land emissions. While these risks have not resulted in any material implications so far, any breaches in waste management or higher-than-permissible emissions could have cost implications for the company. Also, water treatment is extremely important because the pulping and bleaching process can release complex organic and inorganic pollutants, which need to be properly treated. However, the waste generated in the co-processing is effectively utilised in the production of value-added products, such as cement and fly ash bricks. A mini cement plant has been built to convert the waste into value-added products. TNPL sources wood through its captive plantation and farm forestry model, as well as from the Tamil Nadu Forest Plantation Corporation. Further, pulpwood is certified by both the Forest Stewardship Council Forest Management (FSC-FM) and Forest Stewardship Council Chain of Custody (FSC-COC), which ensures that paper manufactured from wood is managed socially and environmentally in a responsible way. Further, the company tries to monitor the emission levels by online data collected continuously from final treated effluent stream and stack emissions from power boilers, which are regularly uplinked to the TNPCB and CPCB servers and displayed in the electronic board installed. The mill has implemented several water-conservation measures and reduced water consumption to 30 KL per tonne of paper during FY2023, which is one of the lowest in the paper industry.

Social considerations: Being a labour-intensive segment, entities operating in the paper industry are exposed to the risk of disruption from their inability to properly manage human capital in terms of their safety and overall well-being. Further, any significant wage rates adversely impacting the cost structure of paper manufacturing companies can impact their margins. TNPL is also exposed to the shortage of a skilled workforce and exposure to hazardous chemicals, which can impact operations. However, TNPL has adopted a clearly defined occupational health and safety policy. Suitable personal protective equipment (PPE) is provided to all employees. Periodical training programmes are conducted on the handling of hazardous chemicals, material handling, usage of PPE, electrical safety, road safety, first aid, firefighting, etc, to improve safety awareness among employees, including contract workmen.

Liquidity position: Adequate

During FY2023, the fund flow from operations improved to ~Rs. 698.3 crore (PY: ~Rs. 209.0 crore) along with significant improvement in the free cash flows of the company on account of judicious working capital management, which was also supported by prepayment of term loans that reduced TNPL's overall debt levels. The company has repayment of Rs. 308.8 crore in FY2024, which is expected to be sufficiently funded from cash accruals. Further, the absence of any major capex plans in FY2024 and sufficient buffer in working capital borrowings are expected to support the liquidity profile of the company, in addition to healthy flexibility with lenders.

Rating sensitivities

Positive factors – ICRA could upgrade TNPL's rating if the company demonstrates further improvement in operating margins along with growth in top line on a sustained basis, leading to an improvement in capital structure and coverage indicators.

Negative factors – Pressure on TNPL's rating could arise if there is significant moderation in revenue and profitability on a sustained basis. Any large, debt-funded capex leading to sustained pressure on profitability and credit metrics, or material moderation in liquidity levels will also be a negative rating trigger.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	Not applicable
Consolidation/Standalone	Standalone

About the company

TNPL was promoted by the State Government of Tamil Nadu and the Industrial Development Bank of India (IDBI) in 1979 to manufacture newsprint and PWP, using bagasse as the principal fibre source. Its plant at Kagithapuram in Tamil Nadu has a production capacity of 4.40 lakh tpa. The plant is the largest single location paper plant in India. Following the sale of IDBI's stake, the Tamil Nadu government is now the single largest shareholder with a stake of 35.32%. TNPL has three production units with a total manufacturing capacity of 4.40 lakh MTPA for the PWP segment. The company has also set up a new board plant near Trichy, with an annual capacity of 2.00 lakh MTPA, which commenced production from May 2016.

Key financial indicators (audited)

	FY2022	FY2023
Operating income	4,020.3	5,179.9
PAT	14.3	387.9
OPBDIT/OI	9.3%	18.8%
PAT/OI	0.4%	7.5%
Total outside liabilities/Tangible net worth (times)	2.6	2.2
Total debt/OPBDIT (times)	6.0	1.9
Interest coverage (times)	2.4	5.4

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

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as of March 31, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
					Oct 27, 2023	August 24, 2022	September 09, 2021	December 29, 2020
1	**Term loans**	Long term	1,623.11	1,373.4	**[ICRA]A+(Stable)**	**[ICRA]A(Stable)**	**[ICRA]A (Negative)**	**[ICRA]A(Stable)**
2	**Fund /Non fund Based-Limits**	Long term and short term	775.00	--	**[ICRA]A+(Stable)/ [ICRA]A1**	**[ICRA]A(Stable)/ [ICRA]A1**	**[ICRA]A (Negative)/ [ICRA]A1**	**[ICRA]A(Stable)/ [ICRA]A1**
3	**Unallocated Limits**	Long term	311.89	--	**[ICRA]A+(Stable)**	**[ICRA]A(Stable)**	**[ICRA]A (Negative)**	**[ICRA]A(Stable)**
4	**Unallocated Limits**	Long term and short term	223.00	--	**[ICRA]A+(Stable)/ [ICRA]A1**	**[ICRA]A(Stable)/ [ICRA]A1**	**[ICRA]A (Negative)/ [ICRA]A1**	**[ICRA]A(Stable) /[ICRA]A1**

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term Term Loans	Simple
Long-term/ Short-term, Fund/Non fund-Based Limits	Simple
Long-term, Unallocated Limits	Not Applicable
Long-term/Short-term, Unallocated Limits	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	**Term Loans**	FY2018	NA	FY2027	1,623.11	[ICRA]A+(Stable)
NA	**Fund/Non fund-Based Limits**	NA	NA	NA	775.00	[ICRA]A+(Stable)/ [ICRA]A1
NA	**Unallocated**	NA	NA	NA	311.89	[ICRA]A+(Stable)
NA	**Unallocated**	NA	NA	NA	223.00	[ICRA]A+(Stable)/ [ICRA]A1

Source: Company

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

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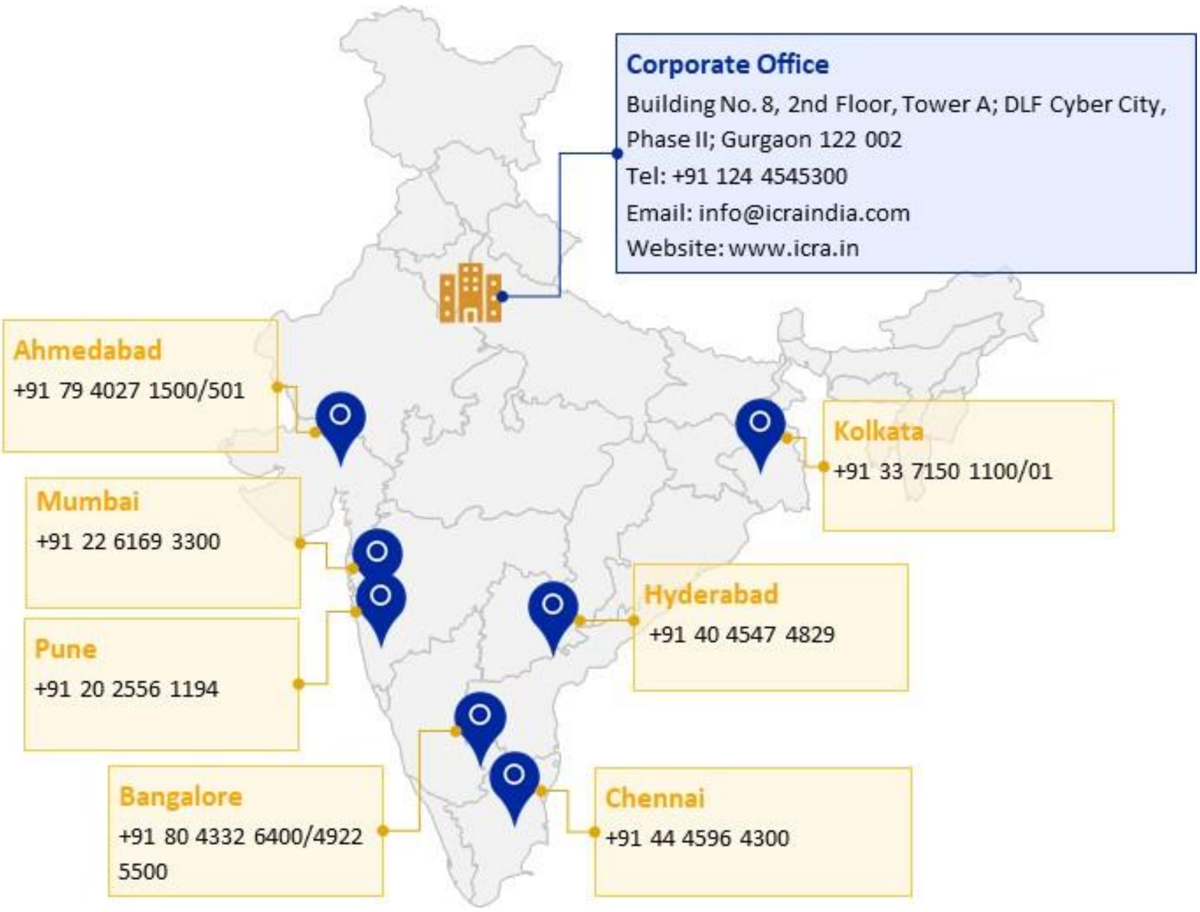

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