November 16, 2023

N R Agarwal Industries Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Cash Credit	127.12	204.10	[ICRA]A (Stable) reaffirmed
Long-term Fund-based – Term Loan	529.80	501.80	[ICRA]A (Stable) reaffirmed
Short-term Non-fund based	118.08	69.10	[ICRA]A1 reaffirmed
Total	**775.00**	**775.00**	

**Instrument details are provided in Annexure-I*

Rationale

The ratings reaffirmation of N R Agarwal Industries Limited (NRAIL) remains supported by the established track record of its promoters (more than 30 years in the paper industry), its large scale of operations, and its strong presence in western India. The company reported revenue growth of 9% to Rs. 1,766.1 crore in FY2023 on a YoY basis owing to healthy realisation levels of its writing and printing paper (PWP) segment. Further, the operating margins also improved to 10.5% in FY2023 and 13.3% in H1 FY2024 over 8.9% in FY2022 owing to healthy sales realisation and discontinuation of lower margin products. However, the top line is expected to moderate in FY2024 over FY2023, given the declining sales realisations from Q1 FY2024, and closure of unit III, which is also reflected in the YoY decline of 29% in the top line in H1 FY2024. ICRA notes that the company had a comfortable capital structure and debt protection metrics in FY2023. ICRA expects NRAIL's revenue and earnings performance to be supported by stable demand, its strong distribution network and healthy capacity utilisation levels.

The ratings, however, remain constrained by the vulnerability of revenues and margins to net sales realisation of paper, which has been volatile recently, along with susceptibility of margins to wastepaper prices and foreign exchange (forex) rates. For FY2023, around 46% of the company's raw material requirements were met through imports. While NRAIL derives around 14% of its revenues through exports, which provides a natural hedge to an extent, it remains exposed to sharp volatility in forex rates in the absence of any firm hedging mechanism.

ICRA notes that the company is in the middle of a sizeable debt-funded capex towards capacity enhancement of duplex paper board. Though the repayment is likely to start in FY2025, after the moratorium period, the company's ability to timely execute the project without any material impact on its capital structure and coverage indictors will remain key rating factors, going forward. The debt protection metrics are expected to moderate from current levels in the near to medium term, hence NRAIL's ability to successfully ramp up its new facility remains critical from the earnings and improving debt protection metrics perspective. ICRA also notes that the promoter has pledged its entire holding for availing term loans from the bank for new capex plans, which limits NRAIL's financial flexibility on an aggregate basis.

The Stable outlook reflects ICRA's expectations that NRAIL will benefit from the extensive experience of its promoters, its large scale of operations and growing demand for its product portfolio of duplex boards, wherein it is carrying out its ongoing capex.

Key rating drivers and their description

Credit strengths

Established track record in the paper industry – NRAIL has been manufacturing paper products since 1993 and has developed an established presence and distribution network over the past three decades. Its operations are managed by Mr. RN Agarwal, the Chairman and Managing Director, who has an extensive experience of more than three decades in the paper industry.

Healthy capacity utilisation levels – NRAIL had four manufacturing units at Vapi and Sarigam, Gujarat, with a total production capacity of 2,88,000 MTPA. However, the company had permanently shut down unit III, which had a production capacity of 42,000 MTPA, owing to muted demand for low margin Grams per Square Meter (GSM) products. Thereafter, it decided to optimally utilise its other units. NRAIL, at present, has a total production capacity of 2,46,000 MTPA. With healthy demand for PWP products, its capacity utilisation levels improved to more than 100% in FY2023 from 86% in FY2022. Going forward, with favourable demand for its products, the utilisation levels are expected to remain healthy as reflected by capacity utilisation of more than 100% in H1 FY2024 for PWP and duplex boards. NRAIL intends to raise its production capacity by ~1,50,000 MTPA for boards, which will enable it to cater to the growing domestic demand and increase its market share in the paper industry.

Established network of agents across western India – NRAIL operates through an established network of agents and dealers with focus on sales in western India. These agents have tie-ups with printing and designing companies who make boxes as per the specifications of various end-user industries such as pharmaceuticals and FMCG. NRAIL's customer base remains moderately diversified with its top 10 customers generating ~37% of its revenues in FY2023.

Demand dynamics remain favourable amid healthy demand for boards 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. Moreover, since the company is amid capex plans in the board segment for growing its manufacturing capacity by two times, this augurs well for the company in terms of the demand scenario.

Credit challenges

Pressure on coverage metrics in near to medium term – Although, the company has a comfortable coverage indicator as reflected by interest coverage of 13.5 times and total debt/ OPBITDA of 0.7 time in FY2023, its profitability remains vulnerable to cyclicality in the paper business, availability of water and raw materials, and volatility in 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, pressuring the coverage metrics in the near to medium term. Also, the company is amid debt-funded capex plans, wherein the debt will be fully drawn from FY2025 onwards, impacting the debt protection metrics in the near to medium term, till the scale up benefits start flowing in from the said capex.

Commensurate returns from planned debt-funded capex remain critical for NRAIL's credit profile – NRAIL is planning to set up a new manufacturing unit at an estimated cost of Rs. 650.0 crore over FY2022-FY2024 towards capacity enhancement of its duplex paper boards. Through the capacity expansion, NRAIL intends to raise its production capacity by ~1,50,000 MTPA in the segment, enabling it to cater to the growing domestic demand and increase its market share in the paper industry. Given the sizeable capex in relation to the gross block, NRAIL is exposed to project execution risk. Further, its ability to complete the project within the stipulated timeline of Q4 FY2024, without any cost overruns or material impacts on its capital structure and coverage indictors will remain key rating factors, going forward. The project cost is proposed to be funded through a term loan of Rs. 425.0 crore and the remaining through internal accruals. With the onboarding of the debt, NRAIL's debt-coverage metrics are likely to moderate over FY2024-FY2026. The ability of the company to generate commensurate returns from the new capex, which will strengthen its overall financial profile, will remain a key monitorable.

Profitability remains exposed to volatility in prices of key raw materials, wastepaper and coal – The main raw material used in NRAIL's manufacturing process is wastepaper, which accounts for 75-80% of its total raw material costs. The prices of wastepaper vary with changes in related regulations as well as the overall availability scenario. The other key input for the entity is coal, which is largely imported. Both raw materials have reported unprecedented price rises in the last one year. However, owing to healthy realisation levels, the operating margins improved in FY2023 and H1 FY2024. Hence, its ability to protect its margin through price hikes in case of any rise in input prices, will remain a key rating sensitivity.

Profitability exposed to forex rate movements in the absence of any hedging policy – NRAIL sources wastepaper from both domestic and international markets. Imports are primarily made from North America, West Asia and Europe through various indenting agents and account for ~56% of its total raw material requirements. Thus, NRAIL's margins remain vulnerable to any adverse fluctuations in forex rates, in the absence of any hedging mechanism. Also, the company remains exposed to imported coal price fluctuations. However, it derives nearly 14% of its revenues through exports, which provides a natural hedge to an extent.

Environmental and Social Risks

Environmental considerations: The paper manufacturing industry is exposed to environmental risk of air, water and land pollution, with discarded paper and paperboard make up a sizable portion of solid municipal waste in landfills. Manufacturing paper out of wastepaper requires a lot of resources such as water and power, creating a lot of wastewater and solid waste in the process. As a result, environment management is critical for sustainable business operations. The company had received a closure order from Gujarat Pollution Control Board for unit V at its Sarigam facility, because the sample waste water from the septic tank did not meet regulatory norms. The company had already commissioned sewage treatment plant (STP) of 10 KLD and took necessary actions before receiving a revocation of the said order. 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. NRAIL uses wastepaper as a primary raw material, which effectively reduces the demand for wood, a natural resource that plays a pivotal role in maintaining ecological balance. Also, water treatment is extremely important because the pulping and bleaching process can release complex organic and inorganic pollutants that need to be properly treated. The company's environment management philosophy aims to cater to the necessary guidelines and requirements of the Central and State Pollution Control Boards and fulfil all Government norms related to air, water and solid waste management.

Social considerations: Being a labour-intensive sector, 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. NRAIL is also exposed to the shortage of a skilled workforce as well as to hazardous chemicals, which can impact operations. NRAIL invests in training and skilling at all levels to align employees with requirements on safety, customer support, market needs, operational excellence, technology upgradation, process improvements, innovation and behavioural competencies.

Liquidity position: Adequate

The liquidity position of the company is **adequate** with healthy cash accruals and low working capital requirements. The average working capital utilisation stood at 13% for its fund-based limits in the last 12-month period ending in September 2023, providing sufficient cushion to its liquidity position. The liquidity position is also supported by nil repayment obligations in FY2024, as the repayment for NRAIL's new debt will start from FY2025, following the one-year moratorium period. The capex requirements are expected to be funded by internal accruals and tied-up term loans.

Rating sensitivities

Positive factors – The ratings may be upgraded in case the company registers a sustained growth in revenues along with stabilisation of the new unit on a timely basis, resulting in an improved financial risk profile.

Negative factors – The ratings may be downgraded if there is a significant decline in earnings due to lower off-take from the new unit. Pressure on the ratings could also emerge in case of any material delay in commissioning the new unit, leading to cost overruns that may impact the liquidity profile and debt metrics. Specific credit metrics, which could trigger a negative rating, include a DSCR of 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 rating is based on standalone financial statements.

About the company

Incorporated in 1993, N R Agarwal Industries Limited manufactures various duplex paper boards, writing and printing paper as well as newsprint. However, the company discontinued its newsprint business in FY2020. NRAIL has three manufacturing facilities at Vapi and Sarigam, Gujarat. It is listed on NSE and BSE. All the utilities are in place for its manufacturing plants and most of its energy requirement is met through captive power generation, while the rest is purchased from the Gujarat Electricity Board (GEB).

Key financial indicators (audited)

NRAIL Standalone	FY2022	FY2023	H1 FY2024
Operating income	1,616.5	1,766.1	710.3
PAT	61.0	99.3	78.4
OPBDIT/OI	8.9%	10.5%	13.3%
PAT/OI	3.8%	5.6%	11.0%
Total outside liabilities/Tangible net worth (times)	0.9	0.6	0.9
Total debt/OPBDIT (times)	1.0	0.7	1.9
Interest coverage (times)	5.7	13.5	29.8

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	
					Nov 16, 2023	Sep 27, 2022	Feb 23, 2022	Jan 20, 2022	Oct 26, 2021	Jul 21, 2021	Jan 05, 2021	Dec 22, 2020
1	**Cash Credit**	Long term	204.10	--	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	-
2	**Term loans**	Long term	501.80	131.71	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	-
3	**Non-Fund Based**	Short term	69.10	--	**[ICRA]A1**	**[ICRA]A1**	**[ICRA]A1**	**[ICRA]A1**	**[ICRA]A1**	**[ICRA]A1**	**[ICRA]A1**	-
4	**Issuer rating**	Long term	0.00	--	-	-		**[ICRA]A (Stable) withdrawn**	-	-	-	**[ICRA]A (Stable)**

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund-based – Cash Credit	Simple
Long-term fund-based – Term Loans	Simple
Short-Term – Non-Fund Based	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	Cash Credit	NA	NA	FY2024	204.10	[ICRA]A(Stable)
NA	Term Loan – I	FY2022	NA	FY2032	226.80	[ICRA]A(Stable)
NA	Term Loan-II	FY2022	NA	FY2032	200.00	[ICRA]A(Stable)
NA	Term Loan-III	FY2023	NA	FY2030	75.00	[ICRA]A(Stable)
NA	Non- Fund Based	NA	NA	NA	69.10	[ICRA]A1

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:

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