

July 28, 2020

Eco Tech Papers: Ratings reaffirmed

Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|---|-----------------------------------|----------------------------------|---------------------------------|
| Fund Based Limits – Cash Credit | 20.00 | 15.00 | [ICRA]BBB+ (Stable); Reaffirmed |
| Non-fund Based – Letter of Credit | 5.00 | 5.00 | [ICRA]A2+; Reaffirmed |
| Fund Based/ Non-Fund Based – (Credit Exposure Limit/Derivative) | 0.20 | 0.10 | [ICRA]A2+; Reaffirmed |
| Total | 25.20 | 20.10 | |

*Instrument details are provided in Annexure-1

Rationale

The reaffirmation of the ratings continues to factor in the strong management and parentage of Eco Tech Papers (ETP), co-promoted by the Lohia Group, which has an established presence in North East India with business interests across diverse sectors. It also considers ETP's prominent market presence in the kraft paper industry, particularly in North East India despite a moderate operational track record since FY2014. The ratings also consider the firm's optimum capacity utilisation and the presence of a captive power plant, which positively impact its cost structure. ICRA notes ETP's conservative capital structure, strong debt coverage metrics and the firm's entitlement to various fiscal incentives for setting up a plant in Assam, though the same will be expiring in the near to medium term.

However, the ratings are constrained by the stiff competition in the fragmented kraft paper industry that restricts its pricing flexibility. A limited geographical diversification of the firm's revenue stream and vulnerability of its profitability to volatility in waste paper prices, which is the key raw material consumed by ETP, remain credit challenges. ICRA also notes the risks associated with ETP's legal status as a partnership firm including the risks of capital withdrawal by the partners, as witnessed in the recent years.

The Stable outlook on the [ICRA]BBB+ rating reflects ICRA's opinion that ETP will continue to benefit from its established presence in the kraft paper industry, particularly in North East India and its strong parentage.

Key rating drivers and their description

Credit strengths

Strong management profile and parentage – The firm is co-promoted by the Lohia Group and Mr. Pradeep Jain. The Lohia Group has an established presence in the north-eastern region (NER) across various industries including manufacturing of steel, cement, coke, fly-ash bricks, retailing of lifestyle products, textile processing, flour mills, etc. Mr. Pradeep Jain is involved in FMCG distribution business and production of plastic disposable containers in the NER.

Prominent market presence in the kraft paper industry, particularly in North East India – ETP commenced operations in FY2014, implying its moderate operational track record. Nevertheless, the firm has emerged as a prominent player in the kraft paper market in the NER. Over the last few years, it has been able to expand its customer base consistently. The firm's capacity utilisation remained high at around 118% in FY2020, notwithstanding a decline from around 128% in FY2019. ETP is in the process of expanding its capacity further, which is likely to result in an increase in its scale of

operation, going forward. However, a challenging operating environment due to the Covid-19 pandemic may negatively impact its operations, to some extent, in the near term.

Presence of captive power plant positively impacts cost structure – ETP has a co-generation based captive power plant (CPP) of 4 mega-watt capacity, which meets almost its entire power requirement. The availability of power from the CPP at a cheap rate positively impacts the firm's cost structure.

Conservative capital structure and strong debt coverage metrics – The firm's limited working capital borrowings and absence of any long-term loans led to a conservative capital structure. Its gearing stood at 0.07 times as on March 31, 2020 (as per the provisional results). The conservative capital structure and healthy profits at an absolute level resulted in a strong debt coverage metrics, as reflected by an interest coverage of 32.99 times, net cash accrual relative to total debt of 74% and total debt relative to OPBDITA of 0.26 times in FY2020 (provisional).

Entitlement to various fiscal incentives for setting up a plant in Assam, however, the tenure of such benefits will expire in the near to medium term – ETP is entitled to various Government subsidies available in Assam for setting up its plant. The tenure of some of the subsidies have expired. Receipt of the residual fiscal benefits, in a timely manner, are likely to positively impact the firm's profitability and cash flows. However, the tenure of the remaining benefits will expire in the near to medium term.

Credit challenges

Stiff competition in a fragmented industry limits pricing flexibility – The Indian kraft paper industry is highly fragmented with the presence of many unorganised players. A significant price-based competition among the players impairs the pricing flexibility, to some extent.

Vulnerability of profitability to volatility in waste paper prices – Waste paper is the major raw material consumed by ETP for manufacturing kraft paper. The price of waste paper depends on the demand-supply situation in the domestic market as well as the international price trends. This impacts the firm's profitability, as reflected by the volatility in its operating margin in the recent years.

Limited geographical diversification with a bulk of its sales confined to Assam – The firm's customers are primarily manufacturers of corrugated boxes. In FY2020, ETP derived around 63% of its revenues from the customers based in Assam, reflecting a limited geographical diversification.

Risks related to a partnership firm including the risks of capital withdrawal – ETP would remain exposed to the inherent risks associated with its legal status as a partnership firm, including the risks of capital withdrawal by the partners, as witnessed in the recent years.

Liquidity position: Adequate

ETP's liquidity position is adequate. The firm's liquidity is supported by its healthy cash flow from operations (around Rs. 21 crore in FY2020), absence of any long-term debt repayment obligation and cushion in its working capital utilisation, as reflected by an average working capital limit utilisation of 32.03% during April 2019 to June 2020. However, a significant capital withdrawal by the partners negatively impacted the firm's retained cash flows in the recent years. The ongoing capital expenditure (estimated at around Rs. 12 crore, being internally funded) for capacity expansion is likely to have a bearing on the firm's free cash flows in the current fiscal.

Rating Sensitivities

Positive triggers – ICRA may upgrade ETP’s ratings if its sales volume improve significantly, aided by the ongoing capacity addition and if its debt coverage metrics remain strong.

Negative triggers – A significant deterioration in the firm’s profit margins on a sustained basis may trigger ratings downgrade. Weakening of ETP’s liquidity position due to a sizeable capital withdrawal, a significant debt-funded capital expenditure and/or a stretch in the firm’s working capital cycle may also result in ratings downgrade.

Analytical approach

| Analytical Approach | Comments |
|---------------------------------|---|
| Applicable Rating Methodologies | Corporate Credit Rating Methodology Paper Industry |
| Parent/Group Support | Not Applicable |
| Consolidation/Standalone | The ratings are based on the standalone financial statements of ETP |

About the company

Eco Tech Papers (ETP), a partnership firm, was established in 2014 at Kamalpur in Guwahati, Assam. It is co-promoted by the Lohia Group, which has an established presence in North East India, and Mr. Pradeep Jain. ETP manufactures multi-layered kraft paper with an installed capacity of 48,840 tonnes per annum. The firm supplies kraft paper to the manufacturers of corrugated boxes. It manufactures various qualities of kraft paper ranging from 100 to 150 gram per square metre (GSM) and 16 to 28 burst factor (BF). ETP is in the process of increasing its manufacturing capacity significantly by around 90% in the current fiscal.

Key financial indicators

| | FY2019 (Audited) | FY2020 (Provisional) |
|--|------------------|----------------------|
| Operating Income (Rs. crore) | 175.68 | 152.70 |
| PAT (Rs. crore) | 30.87 | 12.73 |
| OPBDITA/OI (%) | 21.82% | 16.04% |
| PAT/OI (%) | 17.57% | 8.33% |
| Total Outside Liabilities/Tangible Net Worth (times) | 0.22 | 0.13 |
| Total Debt/OPBDITA (times) | 0.33 | 0.26 |
| Interest Coverage (times) | 74.51 | 32.99 |

Source: ETP

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

| Instrument | Current Rating (FY2021) | | | | Rating History for the Past 3 Years | | |
|------------|-------------------------|--------|--------|--------|-------------------------------------|--------|--------|
| | Type | Amount | Amount | Rating | FY2020 | FY2019 | FY2018 |

| | | | Rated | Outstanding | 28-Jul-2020 | 29-Apr-2019 | - | - |
|---|----------------------------------|------------|--------------|--------------------|---------------------|---------------------|---|---|
| 1 | Cash Credit | Long Term | 15.00 | - | [ICRA]BBB+ (Stable) | [ICRA]BBB+ (Stable) | - | - |
| 2 | Letter of Credit | Short Term | 5.00 | - | [ICRA]A2+ | [ICRA]A2+ | - | - |
| 3 | Credit Exposure Limit/Derivative | Short Term | 0.10 | - | [ICRA]A2+ | [ICRA]A2+ | - | - |

Amount in Rs. crore

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

| ISIN | Instrument Name | Date of Issuance / Sanction | Coupon Rate | Maturity Date | Amount Rated (Rs. crore) | Current Rating and Outlook |
|------|----------------------------------|-----------------------------|-------------|---------------|--------------------------|----------------------------|
| NA | Cash Credit | - | - | - | 15.00 | [ICRA]BBB+ (Stable) |
| NA | Letter of Credit | - | - | - | 5.00 | [ICRA]A2+ |
| NA | Credit Exposure Limit/Derivative | - | - | - | 0.10 | [ICRA]A2+ |

Source: ETP

Annexure-2: List of entities considered for consolidated analysis: Not applicable

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