

## India Ratings Assigns The West Coast Paper Mills 'IND A'; Outlook Stable

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By Khushbu Lakhota

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India Ratings and Research (Ind-Ra) has assigned The West Coast Paper Mills Limited (WCPM) a Long-Term Issuer Rating of 'IND A'. The Outlook is Stable. A full list of rating actions is at the end of this commentary.

The ratings reflect WCPM's well-established position in the Indian paper industry as well as its strong and improving credit profile, on the back of robust EBITDA margins and debt reduction.

### KEY RATING DRIVERS

**Established Industry Position:** WCPM is among India's top five paper manufacturers in terms of the scale of operations, with a total capacity of 320,000mtpa for paper and paperboards. It has a share of around 10% in the domestic uncoated paper market.

**Divestment Boosts Credit Profile:** WCPM sold its entire 36.3% stake in the loss-making Shree Rama Newsprint Limited (SRNP) to Riddhi Siddhi Gluco Biols Ltd in May 2015. The share transfer and release of corporate guarantees worth INR2.5bn that were extended towards SRNP's bank facilities were completed in August 2015, resulting in an improvement in WCPM's net adjusted leverage to 2.9x in FY16 (FY15: 4.7x). WCPM did a total write-off of INR970m on this account (FY15: INR516m; FY16: INR454m), including all inter corporate deposits extended to SRNP and loss on sale of stake.

**Expected Improvement in Credit Profile Due to Higher Margins:** Ind-Ra expects WCPM's net adjusted leverage (net adjusted debt/EBITDA) to improve to around 2.2x in FY17 (FY16: 2.9x) due to term loan repayments, which would keep reducing each year. Ind-Ra also expects its EBITDA margin to improve in FY17 due to lower raw material costs, which coupled with a reduction in interest costs would lead to an improvement in the EBITDA interest coverage (EBITDA/gross interest expense; FY16: 3.6x; FY15: 3.5x). Ind-Ra has considered the expected improvement in credit metrics in FY17 to arrive at the ratings.

**Raw Material Price Volatility:** WCPM's EBITDA margin was volatile during FY13-FY15 as a result of fluctuations in wood procurement costs. Its EBITDA margin declined to 13.3% in FY14 (FY13: 18.5%), due to a nearly 30% increase in wood procurement costs, before recovering to 14.9% in FY15. WCPM's EBITDA margin remained stable at 14.9% in FY16 as it could not benefit from the decline in wood prices in 4QFY16 on account of its annual fixed-price contracts with overseas suppliers. However, Ind-Ra expects WCPM's EBITDA margin to improve in FY17 on account of lower wood prices, which it has fixed with suppliers for the year. Such fixed-price contracts constitute around 50%-60% of WCPM's total raw material requirements. However, the company remains exposed to wood price fluctuations for the rest of its requirements, since it is a price taker for its finished products.

**Unhedged Forex Exposure:** WCPM imports 50%-60% of its raw material requirements and keeps its forex exposure unhedged, exposing itself to currency fluctuations. However, the actual forex loss suffered by the company has been modest (FY16: INR37.6m; FY15: INR27.6m) and significantly lower than the cost it would have otherwise incurred on hedging the exposure.

**Low Capital Expenditure Supports Liquidity:** WCPM has a comfortable liquidity position, as reflected by its free cash flow (FCF) of INR1.7bn for FY16. The company's average maximum utilisation of its fund-based working capital limits was 65%-70% in the 12 months ended June 2016, indicating a significant liquidity cushion. Ind-Ra expects both cash flow from operations and free cash flow to remain positive in the near term as the company has indicated that it does not plan to take up any major capacity expansions during this period.

**Capex Required for Volume Growth:** WCPM's capacity utilisation in the paper division stood at 95.9% in FY16 (FY15: 93.9%), indicating the need to increase its capacity to achieve meaningful volume growth and maintain its market share over the near-to-medium term. Management has not planned any major debt addition for expansion in the next few years; so, Ind-Ra expects the company's leverage to continue to improve. However, any major debt-funded capex could lead to deterioration in the company's credit metrics.

**Integrated Facility:** WCPM has an integrated plant to produce pulp from wood and then manufacture paper from pulp. It also has steam-based captive power to meet its entire power requirements. It has cultivated more than 45,000 acres of land as part of its farm forestry programme, which currently covers around 5% of its wood requirements.

## RATING SENSITIVITIES

**Positive:** Growth in the scale of operations, along with a sustained improvement in the net adjusted leverage to below 2x, could lead to a positive rating action.

**Negative:** The net adjusted leverage being sustained above 2.75x could lead to a negative rating action.

## COMPANY PROFILE

Incorporated in 1955, WCPM is the flagship company of the SK Bangur Group. Its integrated paper manufacturing facility is located in Dandeli (Karnataka) and produces pulp, writing and printing paper as well as cup stock, paperboards and duplex boards. It also manufactures fibre optic cables and has six windmills totalling 1.75MW in Tamil Nadu; it has a contract with the Tamil Nadu State Electricity Board to sell power. The paper division accounted for around 95% of its total revenue in (FY15: 94.5%).

### WCPM's ratings:

- Long-Term Issuer Rating: assigned 'IND A'; Outlook Stable
- INR1,893.1m long-term loans: assigned 'IND A'; Outlook Stable
- INR2,900m fund-based limits: assigned 'IND A'/Stable/'IND A1'
- INR2,350m non-fund-based limits: assigned 'IND A1'
- Proposed INR500m non-fund-based limits: assigned 'Provisional IND A1'
- Proposed INR756.9m bank loan: assigned 'Provisional IND A'/Stable/'Provisional IND A1'

## SOLICITATION DISCLOSURES

Additional information is available at [www.indiaratings.co.in](http://www.indiaratings.co.in). The ratings above were solicited by, or on behalf of, the issuer, and therefore, India Ratings has been compensated for the provision of the ratings.

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## Rating Outstanding

(As on 22/Jul/2016)

Long Term Issuer Rating	IND A / Stable	
Bank Loan	Provisional IND A / Stable	INR 756.9 m
Bank Loan	Provisional IND A1	INR 756.9 m
Fund Based Working Capital Limit	IND A / Stable	INR 2900.m
Fund Based Working Capital Limit	IND A1	INR 2900 m
Non-Fund Based Working Capital Limit	IND A1	INR 2350 m
Non-Fund Based Working Capital Limit	Provisional IND A1	INR 500 m
Term loan	IND A / Stable	INR 1893.1 m

## Applicable Criteria

### Corporate Rating Methodology

## Analyst Names

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