

Rating Rationale
Quality Paper Industries Private Limited

Rating

Facility/ Instrument	Amount (Rs. In Million)	Rating ¹	Rating Action
Long Term Bank Facilities	480.38	CARE-NP BB- [Double B Minus]	Assigned
Short Term Bank Facilities	170.30	CARE-NP A4 [A Four]	Assigned
Total Facilities	650.68		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned rating of ‘CARE-NP BB-’ to the long-term bank facilities and ‘CARE-NP A4’ to the short-term bank facilities of Quality Paper Industries Private Limited (QPIPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of QPIPL is constrained by nascent stage of operations, leveraged capital structure, project stabilization risk, raw material price volatility risk. The rating is also constrained by working capital intensive nature of the business, competition from existing players in the market and exposure to the volatile interest rate. The ratings, however, derives strength experienced promoters and management team in the various sectors, diversified product profile of the company and healthy demand for paper products in the country. The ability of the company to manage raw material price fluctuation and satisfactory generation of operational cash flows from the existing plant are the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Nascent stage of operations

QPIPL has started its commercial operation from August 31, 2020 producing Kraft Paper. QPIPL reported the total sales of Rs. 21.42 Mn from production of Kraft paper during Q1FY20 (refers to quarter ended October 16, 2020).

Leveraged Capital Structure

QPIPL has leveraged capital structure with the overall gearing ratio of 4.20x during Mid-July 2020. The total term loan availed by the QPIPL is Rs. 481.60 Mn. For the additional capex procurement like generators, sheet cutter etc. to increase the efficiency of the plant, the company is planning to avail the additional loan amount of Rs.110 Mn. Out of the total proposed equity capital of Rs. 200 Mn, the company has already infused Rs. 145 Mn as on November 30, 2020. The overall gearing ratio of the company is likely to be high followed by the weak debt service coverage ratio during initial years of

¹Complete definitions of the ratings assigned are available at www.careratingsnepal.com

operations. Being in the first year of operation, total debt to Gross Cash Accruals (GCA) is also likely to be high in FY21.

Project stabilization risk

The plant came into an operation on August 31, 2020 and is in the initial stage of the operation. Currently the company is manufacturing only Kraft paper since there is no market for the writing paper recently due to the impact of COVID-19. Company plans to manufacture writing paper and duplex paper in future simultaneously. The main targeted customer for Kraft papers will be packaging industry who makes packaging materials for the manufacturing industries. Although the plant has come into an operation, the project is still exposed to stabilization risk. Satisfactory operations and generation of the cash flows from the plant are the key rating sensitivities.

Raw material price volatility risk

Waste paper is the most critical raw materials for QPIPL for manufacturing Writing papers, Kraft papers and Duplex paper. This is followed by the power & fuel cost and chemicals. Around 92-95% of the total raw material for the production of the paper is purchased domestically. However, only 5-7% of the raw materials are imported from India. Raw material cost is the major cost component of QPIPL as cost of goods sold constitute around major portion of the total sales. Hence, any adverse movement in raw material price without any corresponding movement in finished goods price is expected to affect the profitability of the company. Further, the company does not have any long term contracts with domestic suppliers for the purchase of raw materials. Being a new player in the industry, the ability of the company to pass through changes in raw material prices to the finished products will be the key rating sensitivity.

Competition from existing players in the market

Paper industry is competitive with presence of few domestic players and import of papers from India. Further, with the low entry barriers and low product differentiation, QPIPL will have low pricing power which may impact the profitability of the company. Also, to penetrate the market, QPIPL may have to provide higher credit period leading to high debtors' collection period which could stress working capital of the company. The ability of QPIPL to sustain competition and achieve projected revenue will be key rating sensitivity.

Working capital intensive nature of operation

The operations of the company are working capital intensive in nature. QPIPL is involved in the manufacturing of paper by locally purchased raw materials. Only 5-7% of the raw materials are imported. Payments for majority of imports are done through Letter of Credit (LC). The company has to make payment for the raw materials within 7 days and the company has to fund inventory and debtors which leads to reliance on working capital limits. QPIPL generally allows 45 days of credit period to its customers. The company also has to keep huge amount of the inventory of the raw materials since there is

no organized sector for the supply of the waste paper. This leads to reliance of the company on the bank financing for working capital needs. The working capital utilization against the drawing power of the company for the month Mid-October 2020 to Mid-November 2020 was 91.59%.

Key Rating Strengths

Experienced promoters and management team in the various sectors

QPIPL has 5 board of directors chaired by Mr. Sukesh Kumar Gupta, has more than 30 years of experience in various sectors such as trading, manufacturing, poultry industry etc. Mr. Rupak Shrestha, Director, has more than 15 years of experience in paper & packaging industry and is also director at Ratnashree Packaging & Daily Polymers Pvt. Ltd.

Diversified Product Profile of the company

QPIPL is manufacturing Writing Paper, Kraft Paper and Duplex Paper in the ratio 60:30:10 with the total production capacity of 20,020 metric ton per annum. Currently, company has covered its market share in different location with the majority of sales in Kathmandu Valley. Company is also planning to create its own brand, as one of the shareholder is linked with almost all the biggest educational institution where these writing copies are consumed at maximum.

Healthy Demand for paper products in the country

The Nepalese paper industry has tremendous potential for growth since wide range of Kraft papers and writing papers are imported annually from India whereas the waste papers are exported from Nepal which is the major raw material for the paper production. The fortune of the paper industry is closely linked with the economic growth as demand of paper for packaging increases with the increase in the industrial output. Also, with Government's prioritization for the development of education sector, there comes a opportunity for the paper manufacturers in Nepal. Further, as per Department of Customs Nepal, Kraft papers and writing papers are majorly imported from India which shows that demand of paper is yet to be fully met through internal production. Also, there is price competitiveness for the domestic manufacturer due to the 15% custom duty and transportation cost in import of paper. The outlook for the paper industry in the long term remains stable cause of key demand drivers such as increased economic activity, increasing government spending on education and greater use of paper packaging over plastic packaging.

About the Company

QPIPL is a private company, incorporated in December 19, 2016, for setting up paper manufacturing plant at Nawalparasi District of Nepal. The commercial operation of the plant was August 31, 2020 with the total installed capacity of 20,020 metric tons. Company plans to manufacture writing paper, kraft paper and Duplex paper in the ratio 60:30:10 with primary raw material as waste paper. QPIPL is currently engaged in the manufacturing and selling of Kraft Paper and plans to start manufacturing writing paper and duplex paper soon. Additionally, in future company has plans to diversify its business

into packaging industry after successful operation of the existing plant. Total equity capital of the company is Rs. 145.13 Mn as on November 30, 2020. Ms. Renu Kumari Kalwar (holds 29.38%), Mr. Sukesh Kumar Gupta (holds 26.72%) and M/S Pro Capital Investment Pvt. Ltd (holds 18.42%) are the major shareholders of the company.

Analyst Contact Ms. Elisha Lamichhane elisha.lamichhane@careratingsnepal.com Tel No.: +977-01-4012629	Group Head Ms. Shalini Sanghai shalini.sanghai@careratingsnepal.com Tel No.: +977-01-4012628	Relationship Contact Mr. Sajan Goyal sajan.goyal@careratingsnepal.com Tel No.: 9818832909/+977-01-4012628/29/30
---	--	---

Disclaimer CRNL's ratings are opinions on credit quality and are not recommendations to sanction, renew, disburse or recall the concerned bank facilities or to buy, sell or hold any security. CRNL has based its ratings on information obtained from sources believed by it to be accurate and reliable. CRNL does not, however, guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. Most entities whose bank facilities/instruments are rated by CRNL have paid a credit rating fee, based on the amount and type of bank facilities/instruments.
--

Annexure 1: Details of the Facilities rated

S. N.	Nature of the Facility	Type of the Facility	Amount (Rs. in Million)	Rating
1	Long Term Bank Facilities	Term Loan	480.38	CARE-NP BB-
2	Short Term Bank Facilities	Overdraft	50.00	CARE-NP A4
3	Short Term Bank Facilities	Demand Loan	70.00	CARE-NP A4
4	Short Term Bank Facilities	Letter of Credit/ Bank Guarantee	50.30	CARE-NP A4
	Total		650.68	