

# N R Agarwal Inds.

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## Hardest worker in the room

### *Business Background*

Established in 1993, the Company is engaged in the manufacturing of duplex boards and writing and printing paper. The Company's production facility is located in Gujarat and comprises five paper units. The Company is environmentally-conscious and utilizes waste paper as a raw material. During the year under review, the Company produced 3,38,988 TPA of paper (95.8% utilization). The Company's products are primarily used in FMCG packaging, textbooks and notebooks and print media applications.

Headquartered in Mumbai (India), the Company has its manufacturing facilities located in Vapi and Sarigam, Gujarat. The Company has a total manufacturing capacity of 3,54,000 TPA paper as on current date and has its own cogeneration power plant of 24MW total installed capacity to produce power as well as steam in all units of board, news print and writing & printing paper required for pulp and paper process.

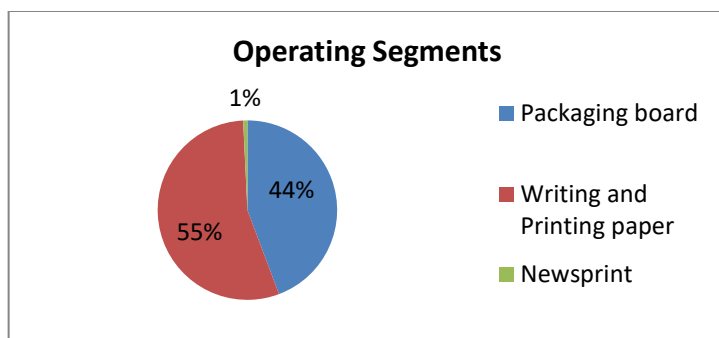


\*Sum of capacity above does not add up to total capacity.

### *Products*

The Company manufactures recycled paper based products addressing mainly three categories:

- **Duplex Boards:** Manufactured with recovered grades of raw material, used in multi-purpose post-print applications and quality duplex boards are suitable for gravure printing, embossing and foil stamping. End application is packaging for FMCG products.
  - 7-8% market share and second largest manufacturer in India, as stated by management
- **Writing and Printing:** Manufactures writing and printing paper products that are high in brightness, shade stability and smoothness. The high tensile strength and surface properties of the products make them suitable for high-speed multi-color printing.
  - **Copier:** The Company manufactures copier paper with high bulk and good stiffness suitable for both side printing and Hi-speed copying with perfect A4 line finish.
- **Newsprint:** The Company manufactures A-grade newsprint which is used by the leading Newspaper publications of India.



## Snapshot

Nov-2020

Market Cap (₹ Cr.)	332.72
P/E	3.20
Book Value (₹)	265
Div (%)	-
5 Year Median P/E	5.4
Price/FCF	4.49
Price/Book	0.72

## SWOT Analysis

### Strengths

- Use of recycled paper and allows the Company to have more stable gross margins (unadjusted margin of 36%-44%) which have improved over time
- Well diversified paper products after converting majority of its Newsprint capacity into Writing and Printing paper which has higher growth prospects
- Has a reasonably low working capital cycle of ~36 days (AR + Inv - AP) with a Net Profit to FCF convertibility of 65% on average over the last 5 FYs with majority of Profit used to fund Capex
  - Working Capital Days for FY20 (Current Assets - Current Liabilities) is 16 days below the Median industry cycle of 55 days
- Management has allocated capital well by shifting from Newsprint to Writing and Printing paper while maintaining strong returns and managing debt levels
- Highly efficient in making the assets sweat with best-in-class Asset Turnover of 2.37x compared to industry average of 1.09x
- Positive y-o-y Sales growth in the last 10 FYs (may not be achievable due to pandemic related closures in this FY)
  - Not all sales growth has been profitable as it reported a loss in FY15 due to low margin (3% OPM) and interest expenses

### Weaknesses

- Highly capital intensive business with an average of ₹51cr in the past 5 years and with more to come in order to expand the writing and printing paper capacity
- Highly prone to raw material sourcing issues especially with regards to the availability of water
- Manufactures a very low margin and generic product with little to no control over the selling price
- Sales growth rate is on a steady decline over the past 4 years and profit has been driven by margin improvements expected to taper off
- Management claims very large salaries which increase sharply y-o-y and now stands at 11% of Net Profit

### Opportunities

- Further improvement in product mix or increase in capacity could improve margins or increase sales, respectively
  - Debt levels are reasonable and reducing which gives enough room to borrow
- Growth of the paper industry has closely tracked the economic growth rate and India is the fastest growing paper market in the world
- Industry has a large number of fragmented companies and this could be a strong target to acquire given the capacities, efficiency in operations and reasonable debt levels
- E-commerce and FMCG are one of the strongest drivers for the future of packaging paper demand

### Threats

- Market down cycles will erode profitability on the bottom line has seen in the past
- Short-term or structural reduction in demand for writing and printing paper post Covid lockdown
- Higher imports from China and relaxation of environmental norms in the industry there
- Environmental and compliance issues for the operations of the plant

## *Porter's 5 Forces Industry Analysis – Total Score: 3/10*

### Threat of new entrants – **Low**

- Not an attractive industry and very capital and resource intensive with a cyclical nature
- Consolidation is the way forward in the long-term as existing companies struggle with scale

### Threat of substitutes – **Medium**

- Strength of substitutes has increased with the Covid pandemic as end users shift to electronic means of display and communication
- Substitutes to paper are lower in recurring cost and environmentally friendly
- No substitutes for paper used in textbooks and notebooks

### Bargaining power of Suppliers – **High**

- Pulp and water are a key input for the product which could affect margins
- Suppliers selling a generic product but operate on an international level and are able to pass on costs to buyers

### Bargaining power of Buyers – **High**

- Product is quite generic and brands hold little importance for buyers

- Large number of customers who place large orders generally on a contract basis as they either use it for their inputs or distribution
- Buyers can easily substitute and are also price sensitive especially since the product is used as a material input
- Switching costs are low

Rivalry amongst competitors – **High**

- Large number of local players offering a very generic product
- Industry is highly fragmented locally with large number of unorganized players competing as well
- Relatively high barriers to exit since the industry is capital intensive
- Competition majorly done in terms of price

## **Management Overview**

### **R N Agarwal – Chairman and MD**

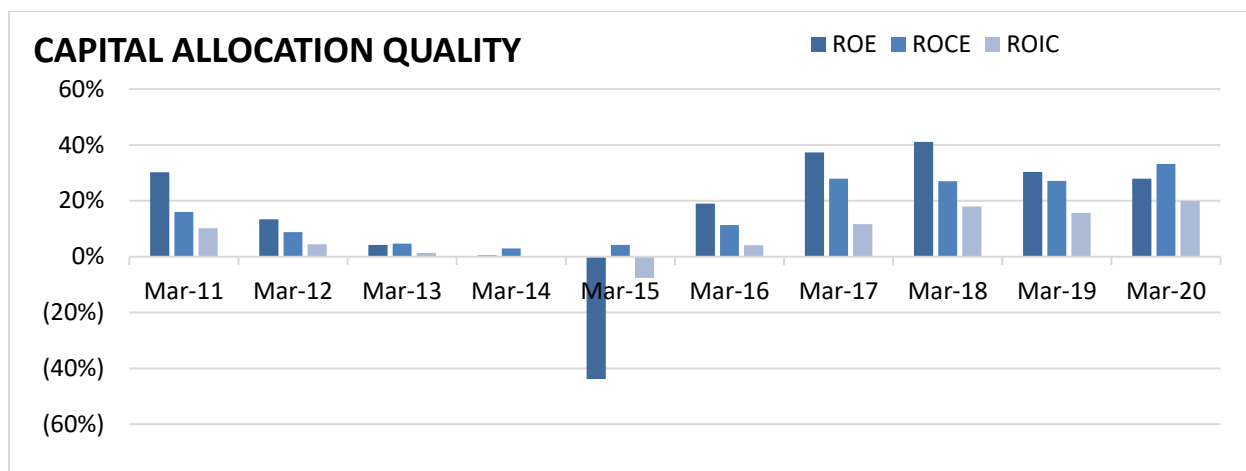
Mr. R N Agarwal, is the Promoter and Chairman & Managing Director of the Company. He is an Electrical Engineer and an MBA from USA. He has an overall experience of around 24 years in the field of Product Development, Marketing, Finance and Administration. He is actively involved in the business of the Company since its inception. He has been instrumental in playing a key role in the Company's growth with his inputs in Strategic Planning and Business Development, especially in the shift towards manufacturing writing and printing paper. Over the years, he has played a vital role in expanding the operations and directing the Company's growth in a defined manner. Started as Director on Board (1993–2004), followed by Managing Director (2005-2009) and finally Chairman & Managing Director in 2010, he has been largely responsible for the strong turnaround of the Company's operations as well as development of new project activities.

Management has a strong focus on expansion while maintaining high efficiency. This is represented by best in class Asset Turnover of 2.4x. This in turn plays a key role in pushing up the return ratios of the Company with ROE of 31.9% and best in class ROCE of 32.8%. The Company

**Age:** 54 years

**Remuneration (FY20):** ₹6.41cr; 5.5% of Net Profit (R N Agarwal – Chairman and MD)

Combined family income of ₹12.2cr; 11.0% of Net Profit



### Peer Comparison (FY20 data)

S.No.	Name	Mar		EV/	P/E	PEG	NPM Ann %	Asset	Debt / Eq	ROE %	ROIC %	ROCE %	Sales Grw		Profit Grw		CMP / FCF	OPM %	WC Days
		CMP Rs.	Cap Rs.Gr.										EBITDA	Turnover	5Yrs %	5Yrs %			
1	JK Paper	96.8	1688.57	4.18x	4.9x	0.05x	15.3%	0.74x	0.72x	20.2%	15.4%	20.8%	7.2%	107.7%	7.09x	24.7%	107.2		
2	West Coast Paper	181.2	1196.50	3.46x	4.6x		16.3%	1.16x	0.54x	32.7%	18.8%	26.3%	0.0%	0.0%	3.81x	20.7%	61.8		
3	Satia Industries	116.8	1167.50	8.17x	15.2x	0.23x	11.4%	1.32x	0.55x	26.1%	25.2%	24.0%	15.6%	65.6%	16.69x	21.8%	23.2		
4	Seshasayee Paper	142.6	899.04	2.20x	5.6x	0.10x	15.4%	1.14x	0.01x	19.0%	17.7%	26.0%	3.5%	57.8%	5.03x	22.6%	51.5		
5	Andhra Paper	206.1	819.66	3.42x	6.3x	0.05x	16.8%	1.29x	0.01x	24.5%	21.8%	27.4%	1.8%	117.4%	4.07x	17.3%	70.2		
6	T.N. Newsprint	110.4	764.08	5.95x	22.5x	n.m.	3.8%	0.89x	1.29x	7.8%	7.0%	11.0%	10.2%	(4.7%)	1.52x	15.4%	38.4		
7	Emami Paper	70.1	423.80	7.51x	51.3x		(0.7%)	0.94x	2.06x	(3.5%)	8.4%	8.2%	23.8%	0.0%	3.79x	14.1%	97.1		
8	Kvantum Papers	43.4	378.29	11.78x	10.2x	0.43x	9.6%	0.53x	0.63x	8.7%	8.6%	7.5%	8.3%	23.5%	(5.35x)	11.5%	39.6		
9	Orient Paper	17.5	371.32	15.30x			3.3%	0.54x	0.03x	1.8%	1.9%	2.3%	(18.3%)	22.3%	5.83x	2.6%	92.1		
10	N.R. Agarwal Inds	193.1	328.64	2.29x	3.0x	0.07x	8.3%	2.37x	0.41x	31.9%	22.5%	32.8%	14.2%	40.6%	4.55x	16.4%	16.3		
11	Shree Rama News.	14.3	210.96	n.m.			(13.3%)	0.42x	0.97x	(10.4%)	(1.7%)	(1.6%)	(2.1%)	8.8%	13.26x	1.4%	85.9		
12	Yash Pakka	59.3	208.80	5.52x	10.2x	0.40x	10.9%	1.28x	0.69x	26.3%	20.7%	25.5%	7.9%	25.6%	8.26x	19.8%	7.8		
13	Astron Paper	44.6	207.16	8.01x	19.2x	0.72x	3.8%	1.60x	0.37x	8.6%	12.9%	14.0%	18.8%	26.8%	n.m.	9.2%	28.8		
	Mean	99.7	666.49	6.48x	13.9x	0.26x	7.8%	1.09x	0.64x	14.9%	13.8%	17.2%	7.0%	37.8%	5.71x	15.2%	55.4		
	Median	96.8	423.80	5.74x	10.2x	0.17x	9.6%	1.14x	0.55x	19.0%	15.4%	20.8%	7.9%	25.6%	4.79x	16.4%	51.5		

- Best in class return ratios for ROCE and Asset Turnover and P/E
  - Second in class EV/EBITDA
- Better figures compared to the industry on all metrics

### Valuation (Price as on 20/07/20: ₹201.4)

Discounted Cash Flow Total Valuation	EBITDA Method	Perpetuity Method
Total of Present Value of Cash Flows (₹cr)	385.86	385.86
Present Value of Terminal Value (₹cr)	409.62	704.63
Total Enterprise Value (₹cr)	<b>795.47</b>	<b>1,090.49</b>
Net Debt, Non-controlling interests, preferred securities (₹cr)	216.51	216.51
Equity Value (₹cr)	<b>578.96</b>	<b>873.98</b>
Adjusted Share Count (millions)	1.70	1.70
Estimated Equity Value per Share	<b>340.19</b>	<b>513.53</b>

### Conclusion (Bigger picture)

NR Agarwal Industries is a paper manufacturer traditionally into newsprint and duplex boards but shifted into writing and printing paper which has better margins and growth prospects. This helped in the Company achieving sustained topline growth and improved margins since the change in business mix. Today the Company has been

able to manufacture a generic product like paper at very high rate of efficiency through which it has now become highly differentiated in terms of its returns.

However with the nature of the business that it operates in, this rate of return is not very sustainable as growth is always going to demand a continuous and high rate of capital investment due to the capital intensive nature of the industry. Although efficiency is very high, new capital investments will take time to become 100% productive and downturn in the business cycle can occur at any time. Despite this the Company should be expected to provide sufficient Free Cash Flow given its strong track record and low valuations.

On the metrics front, the Company is an outright leader in efficiency (Asset Turnover) which is paramount to success in a commodity industry. The Company also has relatively better margins than most peers. Combined with a reasonable Debt to Equity ratio, this produces strong ROE, ROCE and ROIC. If the Company can profitably sustain a large fraction of its current growth then it could be poised to provide shareholder with high returns.

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