

**The Paper Products Ltd: Margins under pressure; Healthy growth ahead**

For 3QCY12, The Paper Products Ltd (PPL) has reported topline inline with our estimates; however, profitability has taken hit, led by various factors. Key highlights of result are as follow:

**Key Highlights**

- Net sales for 3QCY12 grew by 13.7% YoY to ₹2210.3 mn, comprising 8% volume growth and 5-6% price growth, which is led by combination of improvement in product mix and price hikes. Export contributed ~20% to the topline in 3QCY12. The sequential deceleration in volume growth (12% in June 2012 quarter) is mainly due to inventory correction exercise being done by FMCG players, in lieu of implementation of standard packaging and declaration norms, which is effective from 1st Nov12. In addition, delayed monsoon and weak consumer sentiments also impacted the volume growth of FMCG players, especially in rural areas, which in turn has impacted PPL's volume.
- Gross margin declined by 90 bps YoY to 28.1% mainly led by high inflationary effect in inks, solvents and adhesives, led by elevated crude derivative prices and depreciation of INR against USD and lag in passing on the increased cost pressure.
- Other expenditure increased by 25.7% YoY to ₹280.5 mn mainly led by increase in power and fuel cost. The increase in power tariffs in company's operation area coupled with lower supply from grid has led to surge in power cost.
- Overall, EBITDA declined by 7.6% YoY to ₹156.9 mn and EBITDA margin contracted by 164 bps YoY to 7.1%. The management has indicated that it is trying to get back to historical EBITDA levels of ~9%, by cost optimisation and trying to pass-on the increased cost burden to the end consumers.
- Other income increased by 21.9% YoY to ₹37.9 mn. This mainly includes income from current investments and sale of scrap. Tax rate in 3QCY12 was 18.2% vs 13.2% in 3QCY11. Adjusted PAT declined by 16.1% YoY to ₹87.8 mn.

**Outlook:** In the medium term, we expect volume for PPL to grow inline with the historical growth rate based on the strong underlying FMCG growth. Although, in short term, due to high inflationary scenario and weak consumer sentiments, we can see some down-trading possibly leading to change in product mix and slightly lower margins. So far the volume growth in the consumer business doesn't point towards a generic slowdown in consumption.

**Valuations:** At CMP, the business is available at P/E ratio of 9.2x and 7.3x CY12E and CY13E earnings respectively and on P/BV at 1.2x and 1.1x CY12E and CY13E book respectively. PPL is a quality MNC and a niche play on the packaging front, with consistent earnings growth and a healthy B/S and OCF and reasonable return ratios of ~15%. We reiterate our BUY rating on the stock with a rolled over Sept13 price target of ₹92/share.

**Standalone Financial Snapshot (₹ mn)**

In ₹ mn	Sales	YoY (%)	EBITDA	YoY (%)	Adj. PAT	YoY (%)	EPS (₹)	YoY (%)	EBITDA (%)	RoE (%)	RoCE (%)	P/E (x)	EV/EBITDA (x)	P/B (x)
CY10	7,040	21.9	709	(2.5)	361	(3.3)	5.8	(3.3)	10.1	13.0	15.6	11.7	6.1	1.4
CY11	7,973	13.3	814	14.8	502	39.0	8.0	39.0	10.2	16.1	18.9	8.4	5.2	1.3
CY12E	9,175	15.1	826	1.5	468	(6.8)	7.5	-6.8	9.0	13.6	16.9	9.1	5.2	1.2
CY13E	10,239	11.6	1,000	21.0	589	25.9	9.4	25.9	9.8	15.7	19.6	7.2	4.3	1.1

Source: Company, ABML Research

Rating	Closing Price (₹)	Target Price (₹)	Upside / Downside %
BUY	68.5	92.0	34.3

Source: ABML Research

**Company Data**

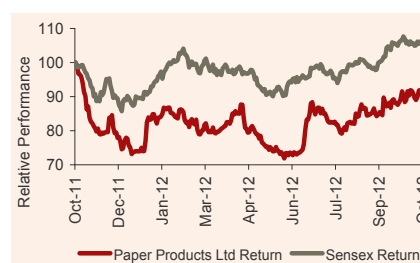
BSE Code	509820
NSE Code	PAPERPROD
Equity Capital (₹ mn)	125.4
Face Value (₹)	2
Market Cap (₹ bn)	4.2
Avg Daily Volume (Qty)	48842
52 week H/L (₹)	84.5/58.0

Source: NSE, BSE

**Shareholding (%)**

Holders	Sept 12	Jun 12	Mar 12
Promoters	63.7	63.7	63.7
FII's	0.1	0.1	0.1
MFs/Banks & FI's	6.4	5.8	5.7
Public & Others	29.8	30.4	30.5

Source: BSE

**Chart: PPL vs. Sensex**


Source: Capitaline

**Analyst Details**

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## Standalone Financial Results (3QCY12)

Particulars (₹ mn)	3QCY12	3QCY11	YoY%	2QCY11	QoQ%
<b>Net Sales</b>	<b>2210.3</b>	<b>1944.0</b>	<b>13.7</b>	<b>2367.8</b>	<b>-6.7</b>
(Inc)/Dec in Stock in trade	-24.7	25.7	-196.1	-12.3	100.8
as a % of Net Sales	-1.1	1.3		-0.5	
Raw Material Cost	1613.3	1354.4	19.1	1678.3	-3.9
as a % of Net Sales	73.0	69.7		70.9	
Employee Cost	181.9	166.9	9.0	179.2	1.5
as a % of Net Sales	8.2	8.6		7.6	
Other Expenditure	280.5	223.1	25.7	287.7	-2.5
as a % of Net Sales	12.7	11.5		12.2	
Foreign exchange loss/ (gain)	2.4	4.1	-41.5	10.9	-78.0
as a % of Net Sales	0.1	0.2		0.5	
<b>Total Expenditure</b>	<b>2053.4</b>	<b>1774.2</b>	<b>15.7</b>	<b>2143.8</b>	<b>-4.2</b>
<b>EBITDA</b>	<b>156.9</b>	<b>169.8</b>	<b>-7.6</b>	<b>224.0</b>	<b>-30.0</b>
<b>as a % of Net Sales</b>	<b>7.1</b>	<b>8.7</b>		<b>9.5</b>	
Other income & Other Ops.Income	37.9	31.1	21.9	43.8	-13.5
as a % of Net Sales	1.7	1.6		1.8	
Depreciation & Amortization	87.4	78.7	11.1	86.4	1.2
<b>PBIT</b>	<b>107.4</b>	<b>122.2</b>	<b>-12.1</b>	<b>181.4</b>	<b>-40.8</b>
Interest Expense	0.0	1.6	-100.0	0.1	-100.0
Exceptional Item	0.0	29.4		0.0	
<b>PBT</b>	<b>107.4</b>	<b>150.0</b>	<b>-28.4</b>	<b>181.3</b>	<b>-40.8</b>
as a % of Net Sales	4.9	7.7		7.7	
Tax Expenses	19.6	19.8	-1.0	47.7	-58.9
Tax rate %	18.2	13.2		26.3	
<b>PAT</b>	<b>87.8</b>	<b>130.2</b>	<b>-32.6</b>	<b>133.6</b>	<b>-34.3</b>
as a % of Net Sales	4.0	6.7		5.6	
<b>Adjusted PAT</b>	<b>87.8</b>	<b>104.7</b>	<b>-16.1</b>	<b>133.6</b>	<b>-34.3</b>
<b>EPS-Basic (Rs)</b>	<b>1.4</b>	<b>2.1</b>	<b>-32.6</b>	<b>2.1</b>	<b>-34.3</b>
<b>EPS-Diluted (Rs)</b>	<b>1.4</b>	<b>2.1</b>	<b>-32.6</b>	<b>2.1</b>	<b>-34.3</b>
<b>Adjusted EPS (Rs)</b>	<b>1.4</b>	<b>1.7</b>	<b>-16.1</b>	<b>2.1</b>	<b>-34.3</b>

Source: Company data, ABML Research

## Estimate Variance

Particulars (₹ mn)	CY12E - New	CY12E - Earlier	% Chg	CY13E - New	CY13E - Earlier	% Chg
Net Sales	9175	9175	0.0	10239	10239	0.0
EBITDA	826	953	-13.3	1000	1054	-5.2
PAT	468	561	-16.5	589	627	-6.0

Source: ABML Research, Company data

## Recommendation summary

Date	Reports	Rating	Last Closing Price (₹)	Target Price (₹)	Upside/(Downside) %
26 <sup>th</sup> June 2012	Initiating Coverage	BUY	65.3	95.0	45.5
1st Aug 2012	Result Update (2QCY12)	BUY	64.2	96.0	49.6
2 <sup>nd</sup> Nov 2012	Result Update (3QCY12)	BUY	68.5	92.0	34.3

Source: ABML Research

## Standalone Financials – The Paper Products Ltd (PPL)

Profit & Loss				
In ₹ million	CY10	CY11	CY12E	CY13E
<b>Net sales</b>	<b>7,040</b>	<b>7,973</b>	<b>9,175</b>	<b>10,239</b>
YoY (%)	21.9	13.3	15.1	11.6
<b>Total expenses</b>	<b>6,331</b>	<b>7,159</b>	<b>8,349</b>	<b>9,239</b>
Incl/dec in stock	(64)	9	12	0
Raw material cost	5,030	5,628	6,532	7,239
Purchase of finished goods	0	0	0	0
Employee Cost	591	643	730	828
Other expenses	774	879	1,074	1,172
<b>EBIDTA</b>	<b>709</b>	<b>814</b>	<b>826</b>	<b>1,000</b>
YoY (%)	(2.5)	14.8	1.5	21.0
<b>EBIDTA (%)</b>	<b>10.1</b>	<b>10.2</b>	<b>9.0</b>	<b>9.8</b>
Depreciation	324	320	349	385
Other income	83	137	140	161
<b>EBIT</b>	<b>469</b>	<b>631</b>	<b>617</b>	<b>776</b>
Interest	6	6	1	1
Extraordinary income/(exp.)	153	29	0	0
<b>PBT</b>	<b>616</b>	<b>654</b>	<b>616</b>	<b>775</b>
(-) Tax	135	128	148	186
Current Tax	153	168	148	186
Deferred Tax	(18)	(39)	0	0
FBT & Provision for earlier yrs & MAT Credit	0	0	0	0
Tax/ PBT (%)	21.9	19.6	24.0	24.0
<b>PAT</b>	<b>481</b>	<b>526</b>	<b>468</b>	<b>589</b>
YoY (%)	28.7	9.3	(11.0)	25.9
Preference Dividend	0	0	0	0
<b>Adjusted PAT</b>	<b>361</b>	<b>502</b>	<b>468</b>	<b>589</b>
YoY (%)	(3.3)	39.0	(6.8)	25.9

Key Ratios				
	CY10	CY11	CY12E	CY13E
EPS - Basic (Rs)	7.7	8.4	7.5	9.4
EPS - Diluted (Rs)	7.7	8.4	7.5	9.4
Adjusted EPS - Diluted(Rs)	5.8	8.0	7.5	9.4
CEPS (Rs)	12.8	13.5	13.0	15.5
Book value (Rs)	46.8	52.5	57.0	62.8
Dividend per share (Rs)	2.2	2.4	2.5	3.1
Net debt-equity (x)	(0.1)	(0.2)	(0.2)	(0.2)
Interest Coverage (EBIT/Int charges)	78.5	106.0	617.0	776.4
ROACE	15.6	18.9	16.9	19.6
ROAE	13.0	16.1	13.6	15.7
<b>Valuations</b>				
PE (x)	11.9	8.5	9.2	7.3
Cash PE (x)	5.3	5.1	5.3	4.4
Price/book value (x)	1.5	1.3	1.2	1.1
Dividend yield (%)	3.2	3.5	3.6	4.5
P/sales (x)	0.6	0.5	0.5	0.4
EV/sales (x)	0.6	0.5	0.5	0.4
EV/EBITDA (x)	6.2	5.3	5.2	4.3

Balance Sheet				
In ₹ million	CY10	CY11	CY12E	CY13E
Equity capital	125	125	125	125
Reserves	2,811	3,163	3,450	3,812
<b>Net worth</b>	<b>2,937</b>	<b>3,288</b>	<b>3,576</b>	<b>3,937</b>
Preference capital	0	0	0	0
Total Debt	225	221	216	210
Deferred tax	53	25	25	25
Minority Interest	0	0	0	0
<b>Total liabilities</b>	<b>3,215</b>	<b>3,535</b>	<b>3,817</b>	<b>4,173</b>
Asset Block	1,787	1,898	1,968	2,046
Investments	394	634	854	994
Goodwill	0	0	0	0
<b>Current assets</b>	<b>2,510</b>	<b>2,691</b>	<b>2,784</b>	<b>3,089</b>
Inventories	892	844	940	1,066
Debtors	1,188	1,296	1,336	1,512
Cash	108	223	179	182
Loans and advances	123	147	147	147
Other Current Assets	198	182	182	182
<b>Current liabilities</b>	<b>1,476</b>	<b>1,688</b>	<b>1,789</b>	<b>1,956</b>
Creditors	941	1,054	1,143	1,297
Provisions	227	241	253	265
Other current liabilities	308	394	394	394
<b>Net current assets</b>	<b>1,033</b>	<b>1,004</b>	<b>995</b>	<b>1,134</b>
Miscellaneous expenses	0	0	0	0
<b>Total assets</b>	<b>3,215</b>	<b>3,535</b>	<b>3,817</b>	<b>4,173</b>

Cash Flow				
In ₹ million	CY10	CY11	CY12E	CY13E
Net profit (before MI)	481	526	468	589
Depn and w/o	324	320	349	385
Change in working cap	387	(144)	35	136
Other income	83	137	140	161
Others	(171)	(69)	0	0
<b>Operating cash flow</b>	<b>164</b>	<b>785</b>	<b>642</b>	<b>677</b>
Other income	83	137	140	161
Capex	160	(410)	(420)	(462)
Investments	(84)	(239)	(220)	(140)
Others	(81.3)	20.2	0.0	0.0
<b>Investing cash flow</b>	<b>78</b>	<b>(492)</b>	<b>(500)</b>	<b>(441)</b>
Dividend	(160)	(174)	(181)	(228)
Equity	0	0	0	0
Debt	(14)	(4)	(6)	(6)
Others				
<b>Financing cash flow</b>	<b>(174)</b>	<b>(178)</b>	<b>(186)</b>	<b>(233)</b>
Net change in cash	68	114	(44)	3
Opening cash	41	108	223	179
<b>Closing cash</b>	<b>108</b>	<b>223</b>	<b>179</b>	<b>182</b>

Source: ABML Research, Company data

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ABML research is also accessible in Bloomberg at ABMR

## Our Rating Methodology

Stock Ratings	Absolute Returns (R)
Buy	$R > 15\%$
Accumulate	$5\% < R \leq 15\%$
Neutral	$-5\% < R \leq 5\%$
Reduce	$-10\% < R \leq 5\%$
Sell	$R \leq -10\%$

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Analyst holding in the stock: NIL