TELMARK

Indian Paper Scenario – May 2003

Shareholders of Tamil Nadu Newsprint and Papers (TNPL) can stay invested at the current price levels, as there could be valuation gains. Investors with a penchant for risk can consider small exposures, especially on any price declines from the current level. Firm trends in the prices of paper and newsprint, despite a continuing slowdown in the global economy, may help TNPL turn healthy earnings numbers for 2002-03. The loss in production in the October –December 2002 quarter may, however, cap the earnings growth. There have been indications that global newsprint prices may firm up with producers facing higher costs. Newsprint prices have been caught in a fairly protracted and sharp downside. Even when prices of other varieties of paper started to recover in early 2002, sizeable over-supply and declining demand kept newsprint prices down. Now the worst appears to be over and newsprint prices at the international level have begun to consolidate. Prices of other varieties of paper have shown a slight weakness after firming up in the last one-year or so. But in the overall trends from the pulp market point to very limited risks on the downside and one or two possible spikes in prices. Domestic manufacturers have used the firm international price trends to effect three to four rounds of price hikes. The most recent one was effected just about a month back. If the relatively firm trends across categories continue into the next few months, TNPL may benefit with good earnings growth in the first half of fiscal 2003-04.

The risk of a protracted war remains a shadow over the global economy and commodity prices. The increase in fuel prices could have an adverse effect on costs. Due to TNPL's reliance on agri-residues for raw material and its self –sufficiency in power, it may be better placed than most other paper industry majors to ride out any pressures on the cost side. TNPL's earnings took a knock in the October-December 2002 quarter due to loss of production for 44 machine days due to shut down for rebuilding. Volumes suffered a 33 per cent decline during this period. Earnings fell 32 per cent to Rs. 30 million from Rs. 39 million in the corresponding previous period. Revenues fell 26 per cent. The company has indicated that the problems have been sorted out and volumes are likely being closer to normal levels in the next two quarters. The benefit of the capacity expansion by 50,000 tons from 182,000 tons may also get reflected in the revenue and earnings numbers over the next year or two. The enhanced flexibility in product profile with close to 85:15 mix in favour of non-newsprint papers and lower cost debt structure has also helped improve earnings levels in the last year or so. Going forward, these would continue to have a favourable impact.

The Union Ministry of Disinvestments has begun the process of disinvesting the Centre's 74 per cent of the total equity share capital holding in Hindustan Paper Corporation (HPC), thereby sending the clear message that the Government does not want to be directly involved in the manufacture of paper and newsprint. The Disinvestments Ministry has placed advertisements seeking expressions of interest (EOI) for selection of an advisor to assist the Union Government in the HPC disinvestments process. The company has two giant paper mills in Assam, each with an annual production capacity of 1,00,000 tons of writing and printing paper. In addition, it has three wholly owned subsidiaries, Hindustan Newsprint Limited (HNL), Nagaland Paper and Pulp Company Limited (NPPCL) and Mandiya Paper Mills Limited (MPML). Of the three subsidiaries, HNL, a 100 percent newsprint manufacturing company, is still running at a net profit, while the other two have closed down after incurring huge losses. In this situation, it remains to be seen whether the Government will prefer to disinvest its 74 per cent equity holding in HPC without separating all the subsidiaries from it or whether it will segregate the subsidiaries before disinvesting its equity stake in HPC. It may be noted that the Disinvestments Ministry, through its sole advisor, SBI Capital Ltd, is already processing EOI's for the purchase of HPC's 74 per cent. Altogether, nine bids were received for the equity stake, of these six bidders have opted out the race, leaving only two in the fray. Similarly, the Centre had invited EOI's for the purchase of Government's 100 per cent equity in NEPA Ltd., which falls under the administrative jurisdiction of the Union Ministry of Heavy Industry. The disinvestments process in NEPA has since been stalled because of technical reasons. A fresh notice inviting EOI's for the Government's entire stake in NEPA is likely to be circulated soon. Incidentally, NEPA is the first newsprint manufacturing company in the country, having commenced commercial production in 1956 with a total installed capacity of 30,000 tons per annum (TPA). The capacity had subsequently been raised to the level of 88,000 TPA. Initially, the company used raw materials such as Salai wood and Bamboo, which were available in abundance in the forests around the plant at Nepanagar in Madhya Pradesh. Currently, eco-friendly waste paper is used.

The legal process of the merger of BILT Graphic Papers Limited (BGPL), formerly Sinar Mas Pulp and Paper India, with Ballarpur Industries Ltd. (BILT) has almost been completed, with the Mumbai High Court and the Delhi High Court giving their assent to the proposed scheme of amalgamation. Industry circles see the merger, which was in the offing ever since Sinar Mas Pulp and Paper India was acquired by a private entity of the L.M. Thapar Group in association with ICICI Ltd. in May 2001, as one among the largest consolidation exercises undertaken in the domestic pulp and paper industry in recent times. Besides providing the operational synergies, the merger of BGPL with BILT will strengthen the latter company's position as a leading player in high value – added paper segments. It would also establish BILT as the market leader in the high-end coated paper segment with over 50 per cent market share. BGPL as an entity would be merged with BILT from the appointed date i.e. July 1, 2002 on filing of the court orders with the Registrar of Companies.

SIRPUR PAPER MILLS LIMITED: This Paper mill has improved its performance during the quarter to March 2003 on the back of a nine per cent increase in paper price realization to Rs. 26,400 per ton and 32 per cent increase in sales volume to 21,000 tons. Inventories (including work in progress) went up by 20.9 per cent to 961 ton. The company has also given consolidated results as per AS – 21 that relates to subsidiary companies AS-23 for the associate companies for the year to March 2003. But since the same for the fourth quarter are not given, stand-alone results have been considered for the analysis. Production was up 33.4 per cent to 2,000 tons, but raw material consumption per ton (without stock adjustment) declined by 6.5 per cent to around Rs. 5,900.

TAMIL NADU NEWSPRINT AND PAPER LIMITED: This Company is planning to expand its present capacity from 1,80,000 tpa to 2,30,000 tpa by spending Rs. 1400 million. The increase in capacity is likely to be operational by the 4th quarter of 2003 and is expected to benefit the company during 2004. Eco-friendly technology, abundantly available raw material base, captive power supply, highly flexible product mix and convertible paper machines are some of the factors that have enabled the company script this winning strategy.

PRICING