

Indian Paper Scenario – July 2004

The Indian paper industry, excluding newsprint, is estimated at around Rs. 140 billion, and is expected to grow at about 6% -8% per annum, in line with the GDP growth, due to increased demand for printing and writing paper (PWP) and marginally higher demand for packaging paper. Among the various segments of PWP, the demand for coated paper (comprising coated chromo paper, art paper and art boards), branded copier paper and maplitho is expected to increase at a high rate due to the expected increase in expenditure on advertisement, marketing and other high quality printing by the corporate sector. However, the supply of paper in India will not be able to grow as fast as the demand primarily due to the high capital cost of new paper production capacity. Paper production capacity would grow approximately 2% annually from 2002 to 2006, and production is expected to grow 5% annually, primarily through increased operational efficiencies at existing production facilities. These growth rates will be below the expected rate of growth in the PWP market of over 6% over similar periods. Further, any gap between supply and demand will be met through increased capacity utilisation, currently 84% by domestic producers. The Indian paper industry has a total installed capacity of seven million tonnes and consists of over 500 producers, with production capacities ranging from less than 1,000 tonnes to over 100,000 tonnes. Of these, the 10 largest producers accounted for 32% of total industry production in fiscal 2001. The fragmentation of the Indian paper industry can be traced to the government excise concession in the 1970s, which encouraged the proliferation of many small capacity mills. The total installed capacity includes non-operational capacity of about 0.8 million tonnes. This non-operational capacity is either uneconomical to operate or has become obsolete.

Presently the average effective capacity utilisation is by smaller players operating in the small-scale and the unorganised sectors. The larger players are operating very close to their full capacity. Bilt is one of the few paper companies operating at more than full capacity utilisation in the past few years. The demand for paper in the past has grown at a compounded annual growth rate (CAGR) of about 6%, while the supply side only grew at a CAGR of about 4.6% in the past. The increased supply of paper came from better utilisation of the existing paper mills as the installed capacity addition in the past has been at a CAGR of 2.2%, going by the current trend, it is expected that demand would outstrip supply, leading to a demand supply gap. The large players in the industry, which are already operating close to full capacity utilisation, are looking to grow and capture the increased demand expected in the future. The expansion of capacity by large players is a step to bridge the demand-supply gap. The pulp and paper prices have increased globally in the recent past and are further expected to improve. The Indian paper industry will stand to gain by way of improved margin. The large players in the industry stand to gain more as most have integrated pulp-manufacturing facilities and are hedged against the volatility of pulp prices. Any increase in paper prices will translate in an improvement in their margin. The small and medium players are dependent on waste paper and bought-out pulp. Thus, an increase in pulp/waste paper prices can have an adverse impact on margins.

The market for paper products in India can be classified into three broad product segments: PWP, industrial paper and newsprint paper. In 2003, India's PWP, industrial paper and newspaper production capacity totalled 7.2 million tonnes and the total demand for such products was 6.1 million tonnes, with each such product segment comparison 35%, 50% and 15%, respectively, of the total demand. The PWP segment,

which is the category on which Bilt is focused, can be further classified into segments for coated, uncoated and speciality paper, each comprising 11%, 79% and 10% respectively, of the total PWP production capacity. As per Jaakko Poyry Consulting, the total demand growth for the paper industry in India in 2000-2015 is expected to be 6.8 million tonnes. The supply is estimated to increase by about six million tonnes during the same period (depending on investments). Thus, the difference in the demand and supply is likely to be filled by higher capacity utilisation of existing facilities as imports are expected to cater to only a small market. The value added segments such as coated paper, branded copier and business stationery etc. are expected to grow faster than the market growth rate. Global pulp and paper prices are witnessing an upward trend. Domestic coated paper prices follow the international trends closely. As there is some gap between the international and domestic prices of uncoated paper, this segment does not have an impact. The paper and pulp prices are expected to continue to rise till the second and third quarter of calendar year 2005. The price increase will have a positive impact on Bilt margin as it is insulated to a large extent from pulp price increase due to its captive production capacities.

The Indian Paper industry find itself face-to-face with crises, both on the international as well as domestic fronts. While the domestic paper industry fears the Indonesian and Chinese onslaught due to free trade agreements (FTAs) with Asian nations, the recent decision of the coal ministry to cut supply of coal (one of the main inputs) is likely to raise production cost manifold. The fear of FTA with Asian nations, including Singapore and Thailand, is far greater than the World Trade Organisation (WTO) regime specially in the light of high input costs for domestic producers. Demanding adequate safe guards against imports of paper, paper board and paper products from neighbouring Asian countries, IPMA has demanded that the stationary items should be excluded from the list of FTA's and if that is not feasible, then imported products should be impacted with the countervailing duty applicable to paper. Duty concessions contained in FTAs should be in consonance with the internal reforms in India mostly in areas of infrastructure improvement and dilution of state control on utilities. Coal India and coal ministry has advised the industry to rely on imported coal for their future energy needs. The energy cost (both power and steam) in paper industry constitutes about 30 per cent of total production cost. Being a core sector, the government must ensure adequate supply of coal to the industry. In the view of coal shortage, some paper manufacturers have already started importing coal for their facilities located at coastal belts, but it is completely uneconomical for facilities in the hinterland. Meanwhile, IPMA has submitted a pre- Budget memorandum to the finance minister demanding a zero duty on coal import to meet impending shortage. The import duty on coal is 5 per cent. On WTO obligations, IPMA requested the government to maintain status quo, "Since, over the years, the domestic industry had taken the full brunt of non-competitiveness, the government should not show any undue haste in lowering the basic custom duty further from the current level of 20 percent when the WTO bound rate for paper remain at 40 per cent.

ANDHRA PRADESH PAPER MILL LIMITED: This company has signed a loan agreement recently with International Finance Corporation of USA (IFC) in connection with foreign currency loan of \$ 35 million sanctioned by IFC to part finance its mill development plan. It has embarked upon the development plan involving an outlay of Rs. 5540 million to be implemented in two phases. While the first phase is scheduled to be completed by 2006, the second phase will be completed by march 2007. The plan envisages increase in the company's installed capacity from 1,53,500 tonnes per annum

to 1, 90,700 tpa and modernisation of its two mills located at Rajahmundry and Kadiam in Andhra Pradesh. The Plan would be financed through the internal accruals of over Rs.2400 million and the remaining Rs.3100 million by way of term loans, debentures and equity

CENTURY TEXTILES AND INDUSTRIES LIMITED: This company is contemplating increasing the capacity of its paper pulp production by 200 tonne per day. The capacity increase was being examined and a decision would be taken on it by the end of this year. The company has decided to reduce the number of looms from the existing 1,600 to 1, 250 in the next one year. He added that the company would focus on high quality cotton. The company would also focus on ready made garments and has already made a beginning by manufacturing shirts, which was sold through its retail outlets. The company plans to set up more retail outlets though no numbers were specified.

HINDUSTAN PAPER CORPORATION LIMITED: This paper mill has finalised an ambitious plan for its wholly owned subsidiary, Hindustan Newsprint Limited, to double its newsprint manufacturing capacity to 200,000 tonnes per annum. The capacity will be expanded at an investment of about Rs.6000 million. Production facilities at HNL's pulp mill and deinking plant will be doubled. A captive power plant will also be set up based on gas or imported coking coal. Similarly, the company has plans to increase writing and printing production capacity by at least 60,000 tonnes. The company has two mills in Assam – one at Cachar and another at Naogaon. Each has an annual production capacity of 100,000 tonnes. The capacity will be expanded with an export commitment of at least 30 percent of total production from both the mills.