Indian Paper Scenario – May 2008

World paper demand growth is subdued and is between 2-3 per cent, against India's 8 per cent. This high growth rate has been possible by a strong emphasis on literacy, increase in per-capita income, increasing use of photocopiers and printers, higher export growth and demand for high quality packaging. India's total production and consumption of paper and paper board is around 8 million tonnes – barely 2 per cent of global production. It is projected that India's paper demand would reach 17 million tonnes by year 2015. The Indian paper industry started facing heat from the reforms initiated by the Government in the 1990s and till then the protection provided by the Government was helping the sector record inflated profits and giving it a false feeling of competitive strength. And the industry did not seem interested in taking timely initiatives to face the challenges emerging from globalisation. The government is on record in bringing import tariff to the levels prevailing among Asian members, putting the industry in a real tight corner. Productivity trends in India/s Manufacturing sectors in last two decades – a study done by Unel for the IMF working paper WP/03/22 concluded that at the paper sub-sector had the second lowest productivity growth in the 13 major manufacturing sub-sectors analysed. Most of the paper mills in India were found not competitive against imports. Several factors have brought the industry to such a pass.

The industry uses different fibres for paper-making, namely bamboo, hard-wood, bagasse, agri-residues (wheat/rice straw) and recycled paper. India is deficient in all these fibres. Bamboo is now almost extinct, excepting in the North-Eastern States mainly Mizoram and Assam. Hard-wood is no more accessible from forests but can be grown in India in large quantities due to fine tropical climate, good rainfall, abundant unemployed youth and large expanses of degraded lands needing immediate restoration, as has been done successfully by Brazil, Chile, Argentina and Indonesia. But the Government has not agreed to industry's proposal to allow degraded forest lands for industrial plantations. Some initiatives were taken by paper mills to engage farmers in hard-wood plantations, but for potentially more valuable sectors, only a small share of wood harvest reaches the paper mills. The landed cost of hardwood of a paper mill is not less than $90 per tonne, against $40-45 in other countries. Taking 2.5 tonnes of wood needed for a tonne of paper, India starts with a disadvantage of $120 per tonne. The story is no different with bagasse. Sugar mills find it more attractive to burn it as fuel for power generation. Similar is the case with agri residues. Wheat and rice straws primarily used as animal feed-stock for the growing animal population are mostly in short supply. Prices are never stable and have of late, shown unduly large variations. Recycled paper is being increasingly used worldwide for paper-making. But, here too, India does not have an advantage, as a proper collecting system for waste paper is not in place. India collects just 22 per cent of total paper consumed in the country – one of the lowest recovery figures in South-East Asia.

Energy is around 18-20 per cent of total cost of manufacturing paper. Indian mills consume, on an average, 1600 units per tonne of paper, while it is only 920 units in Europe. Here, due to excessive gird power cost, several large paper mills have set up their own power generating units. The cost of own power generation is increasing due to consistent increase in coal prices. Wood bark unsuitable for paper making and having no fibre can be used for power generation as an input in place of fossil fuels such as coal. Several wood based paper companies are using it in Europe, Latin America and in South East Asia. Thus Indian mills are going on two counts: high cost of power (either girds or own) and higher power consumption. Paper manufacturing is a highly capital

intensive activity and also a long gestation one. The Indian Paper sector has been always investor-shy as it has rarely rewarded its shareholders, even banks and financial institutions are also not favourably disposed towards the sector. Thus cost of capital is high for Indian corporate. Poor roads and bridges and ports mean high transportation costs. And many of the paper mills source inputs from distant places and ship finished paper to all Indian cities, pushing up the logistics costs. In fact, huge internal transportation costs are also an entry barrier for imported products in the country. The small scale of production and out dated technology have been the main features of Indian paper units, and are still so. On an average, to produce 100,000 tonnes in a year, an Indian mill manages five paper machines in one or more location, while abroad, paper-making machines of 500,000 tonnes per annum, or more, and are the norm.

Economies of scale, after considering the impact of higher capital cost, are 3-5 per cent of total conversion cost. In addition, large modern machines produce internationally accepted paper, difficult with smaller machines. Thus India loses out on both counts-quality and cost. Apart from the high cost of manufacturing paper in India, employing environment-friendly technology with outdated machines and pulp mills is also not easy. The Government is forcing paper mills to upgrade the effluent plants and follow the strict norms being notified from time to time. But the impact of such steps is still not visible. The investment needed for such activities generally yields much lower returns and impacts the bottom-line. The industry must become transparent and adopt a sharing mindset. Apart from a company's unique strategy of how differently it serves its customers, it should be able to initiate synergies with others in the sector, be it in sourcing, logistics or distribution. Rival newspapers such as Times of India and Hindustan Times are co-producing a daily 'Metro News" in Delhi. Three top US paper companies are e-procuring chemicals needed jointly. New initiatives are emerging. The industry also needs to have a fresh look at vertical disintegration-associating its employees and associates in growing pulp –wood plantation; and at he value-chain-reducing its internal logistic cost by having national distribution networks. Other problem areas such as economies of scale, pollution control and capital costs also demand innovative solutions. Regulatory agencies must also extend their assistance in helping the industry solve problems rather than offering temporary sops such as tariff cuts.

BALLARPUR INDUSTRIES LIMITED: This company is mulling to increase the price of coated paper by at least Rs.2000 a tonne. The company has posted a 14.81% growth in its net profit at Rs.745 million for the third quarter ended March 2008 against Rs. 649 million for the corresponding period a year ago. The total revenue rose to Rs.7350 million for the quarter (Rs.6050 million) For the nine months ending March the company announced a net profit of Rs.221.70 a 18.86% growth over the year ago period. For the corresponding period the previous year the company had a net profit of Rs. 1865 million The total income rose to Rs. 21956 million for the nine month periods (Rs.17905 million).

TAMIL NADU NEWSPRINT AND PAPERS LIMITED: This company has reported a 23 % growth in net profit for the fourth quarter ended March 2008 over the net profit in the corresponding period in the previous year. Its annual production of printing and writing paper is 2,45,000 tonnes, representing a capacity utilisation of 107% and 14, 310 tonnes more than in 2006-07. The company has completed the Rs 5650 million mill development plan that would see its captive pulp production capacity increase to 720 tonnes a day form 500 tonnes. The benefit of this expansion would start accruing from May 2008.