

JK Paper Ltd

Initiating coverage

MARKET DATA

NSE TICKER	JKPAPER
Net worth FY20 (Rs in Crs)	2,365.5
P/BV Ratio (FY20) (x)	0.8
EPS (FY20) (Rs.)	26.3
Market Price (Rs.)	100
P/E Ratio (FY20) (x)	3.7
52 Week High (Rs)	151
52 Week Low (Rs)	62
Market Capitalisation (Rs. Cr)	1,755

AVERAGE MONTHLY VOLUME ('000)

BSE	64.4
NSE	1,436

SHARE HOLDING PATTERN

Promoter	48.89
FII	6.96
DII	0.80
Public	43.35

RETURN (%)	3M	6M	12M
JKPL	-23.65	-21.43	-34.53
Nifty	-22.25	-21.31	-18.60

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JK Paper Ltd. (JKPL) is a leader in India's copier paper segment with a market share of 23%, second-largest in the coated paper segment (market share of 12%) and a leading player in the packaging board segment, having market share of 11%. On the back of a strong brand name, capacity expansion including acquisition of Sirpur Papers and financial strength, we believe that JKPL is fairly valued at current level with limited downside and can be a hold at current levels.

Formidable player with presence of high quality brands

JKPL has 23% market share in copier paper which is used extensively in printing and photocopying. The company has 16 warehouses, 250 distributors (including wholesalers and direct dealers) and over 4000 dealers to sell its products. JKPL enjoys positive brand recall for its products.

Backward Integrated with focus on farm forestry to support pulp supply

JKPL intends to increase the quantum of pulp derived from every tonne of wood from 41.7% to ~44% through the enhanced planting of clonal saplings. The rising cost of pulp is likely to be countered through the commissioning of a new pulp mill, enhancing raw material security. JKPL is a net wood and carbon positive company and it plants more trees than it harvests for manufacturing of papers.

Inorganic growth by Sirpur Acquisition

JKPL acquired Sirpur Paper for Rs 782 Cr in 2018-19 (settlement payout of Rs 371 cr and revival capex of Rs 411 cr). Sirpur Paper is one of the oldest paper mills in India, having a capacity of 108,000 TPA. Besides the additional paper manufacturing capacity that Sirpur adds, the acquisition comes with the benefit of excess land area for future expansion, water supply (which is key for paper manufacturing industry), access to coal, robust logistical network and area of organized plantation. In order to set up a new plant of similar capacity would have cost JKPL ~Rs 1500 cr and 2-3 years to make it operational.

Stellar financial performance and discipline followed over the past 7 years

From FY12 to FY20, JKPL reported 11% CAGR revenue growth, 23.9% CAGR EBITDA growth and 32.9% CAGR profitability growth. Strong profitability growth along with improvement in working capital cycle translated into higher operating cash flows. This led to aggressive reduction in debt as D/E ratio fell from 2.9 in FY14 to 0.65 in FY20.

Going forward, company has an expansion plan of ~2 lakh TPA for a capital outlay of ~Rs 2,100 cr which is to be financed by a mix of internal accruals and debt. Also, recently, the company declared a buyback at Rs 130/shr in spite of Covid impact. All of it has been possible on back of financial discipline followed by JKPL over past 7 years.



Attractive valuation reduces down side risk

At current levels, JKPL is fairly valued and the downside move looks unlikely. JKPL is trading at 3.7X PE multiple and 0.8X Book Value which is not justified considering the fact that JKPL is a leader in widely copier paper.

Valuation & View

- We like JKPL on the back of (a) strong brand name in high demand copier paper, (b) backward integrated manufacturing process with in-house pulp supply, (c) value creation through Sirpur acquisition, (d) disciplined financial management and (e) attractive valuation insulating down side risk. However, the recent 50% upmove in the price has factored in most of the upside potential. Any dips going forward should be considered as a buying opportunity in JKPL
- We are valuing JKPL at 5X FY22's EPS of Rs 21.7 to arrive at our target price of Rs. 108 for the stock, which presents a potential upside of 11% from the CMP of Rs 97. Accordingly, we recommend a **Hold** on the stock.

Financial Snapshot:

Year End	Revenue	EBITDA	EBITDA %	PAT	EPS	RoE (%)	RoCE (%)	P/E
FY19	3,256.7	868.1	26.7%	424.9	23.8	20.8%	21.8%	4.2
FY20	3,060.2	871.3	28.5%	468.3	26.3	19.8%	18.5%	3.8
FY21E	2,784.8	776.1	27.9%	346.8	20.3	13.6%	12.1%	5.0
FY22E	3,010.9	910.1	30.2%	369.8	21.7	13.1%	13.4%	4.7

- Going forward, we expect the revenue to remain flattish on account of drop in demand in FY21 on account of Covid related slowdown. However, cost rationalizations and improving pulp output per unit of wood as well as technological enhancements will lead to EBITDA margins to move up from 28.5% in FY20 to 30% by FY22E. On account of 2 lac TPA expansion at a capex of Rs 1,700 cr by mix of internal accruals and debt will lead to a jump in depreciation.
- FY20-FY22 will be a period of consolidation for the company after 6-8 years of continuous growth. The new capacity expected to come on stream in FY22 post which JKPL will revive its growth trajectory.
- Based on above, we expect the revenue to remain flat at Rs 3,011 cr. EBITDA is expected to grow at 2.2% CAGR at Rs 910 cr as margins improve by 180 bps to 30.2% by FY22E. PAT is expected to degrow at 11% CAGR to Rs 370 cr on account of higher depreciation. EPS after buyback adjustment is expected to be at Rs 21.7.
- The RoE and RoCE are expected to come down to 13% due to the heavy capital expenditure of ~Rs 2000 cr towards Gujarat Plant and Sirpur Plant which will be operational in FY22 and the revenues will start flowing only after FY22.

About Company

JK Paper Ltd. (JKPL) is a leader in India's copier paper segment with a market share of 23%, the second-largest in the coated paper segment (market share of 12%) and a leading player in the packaging board segment, having market share of 11%. JKPL enjoys a pan-India presence with distribution network of paper and packaging board products comprises four regional offices, 16 warehouses, 250 distributors (including wholesalers and direct dealers) and over 4000 dealers. The company was successful in acquiring Sirpur Paper mill (SPML) with an installed capacity of 1.38KT (30% of JK current capacity) by infusing Rs 370 cr. Uninterrupted supply of coal, raw material and water along with various cost benefits provided by state government (discussed later in the report) to revive the plant will benefit the company to improve the EBITDA margin at a company level.



Products

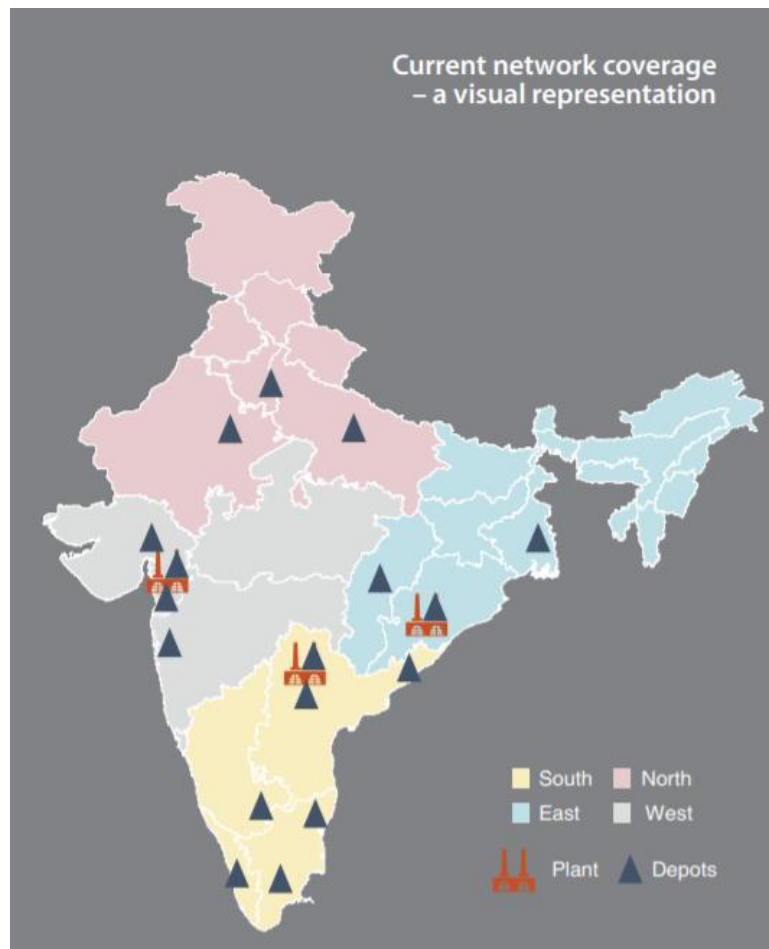
The Company's diverse product portfolio (office paper, packaging board, writing and printing paper and specialty paper, among others) is synonymous with high quality leading to superior applications. The Company's pulp and paper manufacturing operations are integrated.



JKPL has two manufacturing capacities apart from the newly acquired Sirpur facility. Key highlights of these two facilities for FY19 is as follows:

Unit – JK PAPER MILLS

- JKPM reported ~104.4% capacity utilisation.
- Increased pulp production by 2% to 2.24 Lac Bone Dry Metric Tonnes (BDMT).
- Increased paper production by 1% to 3.04 Lac tonnes.
- Improved raw material yield.
- Started recovering methanol and using it in lime kilns to halve furnace oil consumption.
- Became one of the earlier paper companies in the country to commission a methanol plant.
- Undertook debottlenecking initiatives and upgraded from the old gear system to a silent drive system.





Unit – CENTRAL PULP MILLS

- Paper machine reported ~123.5% capacity utilisation.
- Increased pulp production by 7% BDMT.
- Increased paper production by 6% in 2018–19.
- Increased packaging board production by 9%.
- Moderated steam, water and coal consumption.
- Debottlenecked capacities, strengthening throughput. Substituted ~21% pulp requirement with fillers, reducing costs

Industry Overview

India’s per capita paper consumption is at 13kg compared 57kg globally. The domestic demand for paper and paperboards in India is estimated at 17.1 million tonnes at ₹80,000 cr in 2017–18, growing at a CAGR of 6.5% (fastest in the world). India’s share in the world production of paper is about 3.7%. Growth of the paper industry moves in tandem with GDP growth. Indian manufacturing is uncompetitive compared to global peers due to regulatory bottlenecks, poor infrastructure, higher fuel costs, technology obsolesce, lack of scale, etc. and hence, threat of cheaper imports lure over domestic manufacturers. The paperboard imports have increased from ~0.5 million tonnes in 2010–11 to ~1.7 million tonnes in 2017–18 growing at a CAGR of ~20%. To mitigate the interest of domestic players, government on Dec 5th, 2018, imposed anti-dumping duty on uncoated copier paper imported from Indonesia, Thailand, and Singapore for a period of 3 years.

S N	Product	Volume (Mn Tons)			Share %			Projected Growth%		
		2018-19	2018-19	2022-23	2018-19	2018-19	2022-23	(2023/2019)		
		Global	India		Global	India		Global	India	
		1	2	3	4	5	6	7	8	
1	Coated	25.5	0.84	1.0	6.2	4.4	4.0	-0.5	4.0%	
2	Uncoated	53.9	4.6	5.3	13.0	23.9	21.7	-0.3	3.7%	
2.1	Creamwove		2.1	2.4		11.0	9.6			3.0%
2.2	Copier & High Bright Maplitho		2.5	3.0		13.0	12.0			4.4%
3	Packaging Board	45.4	4.7	6.4	11.0	24.3	26.1	2.0	8.3%	
3.1	Virgin Fiber Based		1.0	1.6		5.2	6.4			12.7%
3.2	Recycled Fiber Based		3.7	4.8		19.2	19.7			7.1%
4	Tissue	35.8	0.2	0.3	8.6	0.9	1.2	3.2	15.5%	
5	Industrial incl. Kraft	174.0	5.7	8.0	42.0	29.6	32.6	2.2	9.1%	
6	Newsprint	44.0	2.6	2.7	10.6	13.7	11.1	-2.8	1.0%	
7	Others	36.0	0.6	0.8	8.7	3.2	3.4	-1.0	7.5%	
8	Total	414.7	19.2	24.6	100.0	100.0	100.0	1.0	6.5%	

Source: JK Paper Company Presentation, Dimensional Securities Research

Within the coated paper segment of Printing & Writing paper, Ballarpur Industries enjoys the highest market share of ~40% while JKPL stands second with ~23% share. The paper board segment is largely commanded by ITC followed by TNPL, Century and Emami. News print paper demand is expected to severely impact due to Covid and demand is expected to stay flat or decline. JKPL does not have its presence in news print paper segment.



Sr No	Companies	Printing and Writing		Paper Board		Tissue	News Print	Mfg Units
		Coated	Uncoated	Industrial	Consumer			
1	Ballarpur Industries Ltd	316	540	0	0	0		5
2	ITC	0	140	109	457	36		3
3	Tamil Nadu Newsprint	0	400	0	200	0		1
4	JKPL	54	397	0	121	0		3
5	Century	0	198	0	180	36		1
6	Emami	0	18	0	180	0	127	2
7	WCPM + IP APPM	0	497	0	64	0	0	2
8	Tirdent	0	175	0	0	0		1
9	Orient	0	55	0	0	50		1

Manufacturing Locations of Large Paper Companies across India



Source: Indian Paper Manufacturers Association, Dimensional Research



❖ Covid-19 Impact on Paper Industry

Covid is expected to have a mixed impact on paper industry. On one side, the demand for newspaper will drop drastically as lockdown will lead to increasing usage of online newspaper. Also, emerging trend of work from home and online lectures for students will bring down the demand for copier paper. However, usage of disposable paper cup and plates will increase. Moreover, growth in online shopping will lead to demand for packaged board and packaging paper. We expect overall growth in paper industry as a whole to come down from 6.5% (pre covid levels) to sub 4% as it will grow at a 20% lower rate than the GDP growth rate.

❖ Investment Rationale:

❖ Formidable player with presence of high quality brands

JKPL is a leader in India's copier paper segment with a market share of 23%, the second-largest in the coated paper segment (market share of 12%) and a leading player in the packaging board segment, having market share of 11%. JKPL enjoys positive brand recall for its products. Also, the company has a very strong distribution network across India.

Segment	Application	Key Brands	Market Share	Revenue
Copier Paper	Printing & Photocopying	JK Copier & JK Easy copier: High-end customers JK Sparkle: Middle segment JK Copier Plus: Govt & PSU JK Cedar: High-end Digital printing JK C Max & JK Max- Value for money	23%	50%
Coated Paper	Publishing & Magazines	JK Cote	12%	25%
Packaging board	FMCG, Pharma & food processing industry	JK Ultima & JK Tuffcote	11%	25%

We believe that company is well poised to capitalize the Sirupur acquisition with its own brand name and distribution network to further strengthen the market share and optimize margins as incremental S&D expenses are lower.

❖ Backward Integrated with focus on farm forestry to support pulp supply

JKPL intends to increase the quantum of pulp derived from every tonne of wood from 41.7% to ~44% through the enhanced planting of clonal saplings. Increase pulp capacity is mainly to address growing packaging board demand. Also, JKPL intends to increase pulp substitution with fillers. JKPL used ~65% imported pulp for the manufacture of packaging board. Commissioning of a new pulp mill enhances pulp security. Consequent to better operating parameters the Company's cost of production is competitive and competes well in the market.

The Company's farm forestry within a 200 kms radius of its manufacturing plants covered over 160,000 hectares cumulatively and more than 5,000 farmers in 2018-19, accounting for a major portion of the



Company's raw material procurement. JKPL helped plant eucalyptus, casuarina and subabul clones / saplings. JKPL is net wood and carbon positive; it plants more trees than it harvests for paper manufacture.

❖ Inorganic growth by Sirpur Acquisition

JKPL acquired Sirpur Paper for Rs 782 Cr in 2018–19 (settlement payout of Rs 371 cr and revival capex of Rs 411 cr). Sirpur Paper is one of India's oldest and most respected paper mills, acquired a large pre-used paper machine that was subsequently redesigned. This redesigned facility could not stabilise production across its expanded capacity, reported suboptimal utilisation, failed to cover fixed costs and eventually eroded the Company's net worth. However, the Company's pulp mill (108,000 TPA) with sophisticated Andritz technology possessed viable fundamentals but could not achieve its desired potential. JKPL is capitalizing on long-standing intangible advantages of the acquired company and for fast-tracking its investment, given that it is time-consuming and expensive to commission a Greenfield paper manufacturing facility. The Company was acquired for five principal reasons.

- Sirpur possessed access to ample land for future expansion
- Abundant water availability with river Peddavagu
- Access coal from Singareni Collieries (only about 40 kms away)
- Access to a robust logistical network – highways not more than 14 kms away and being upgraded from undivided two lanes to divided four lanes.
- Proximate catchment area is virtually devoid of organised plantations, representing an excellent resource-enhancing opportunity.

JKPL plans to enhance the average production capacity of the four acquired machines to 1,36,000 tonnes per annum by various measures of debottlenecking, higher speed and productivity. JKL is also investing in a new power boiler and turbine. The full result of these improvements is expected to manifest from the second half of FY21. In order to set up a new plant of similar capacity would have cost JKPL ~Rs 1500 cr and 2–3 years to make it operational.

JKPL to receive numerous benefits on Sirpur acquisition such as uninterrupted supply of coal at a concession of ₹ 1,000 for 10 years, raw material and water along with various cost benefits provided by government to revive the plant such as 100% gross State GST reimbursement for 10 years, 100% exemption on stamp duty, exemption of electricity duty for 10 years, reimbursement of power cost at ₹ 3 per unit for three years, capital subsidy at 20% of investment (subject to a maximum of ₹ 50 crore) and interest subvention of 2% per annum on amount of new investments for 5 years. Moreover, the government has agreed to reimburse the liquidation value of workmen's priority dues while reimbursement of all other dues to be decided by it later. All these benefits will help the company to improve the EBITDA margin at a consolidated level.

❖ Stellar financial performance and discipline followed over past 7 year

- From FY12 to FY20, JKPL reported growth of 11% CAGR in its top line to Rs 3,060 cr.
- Over the same period, the EBITDA has grown at 23.9% CAGR to Rs 871 cr. EBITDA margin improved by 1670 bps from 11.7% in FY12 to 28.4% in FY20.
- Net profit recorded a jump of 33% CAGR over 8 years to Rs 468 cr in FY20 mainly on back of improved operating profitability and lower interest cost as the company mainly focused on deleveraging the balance sheet.



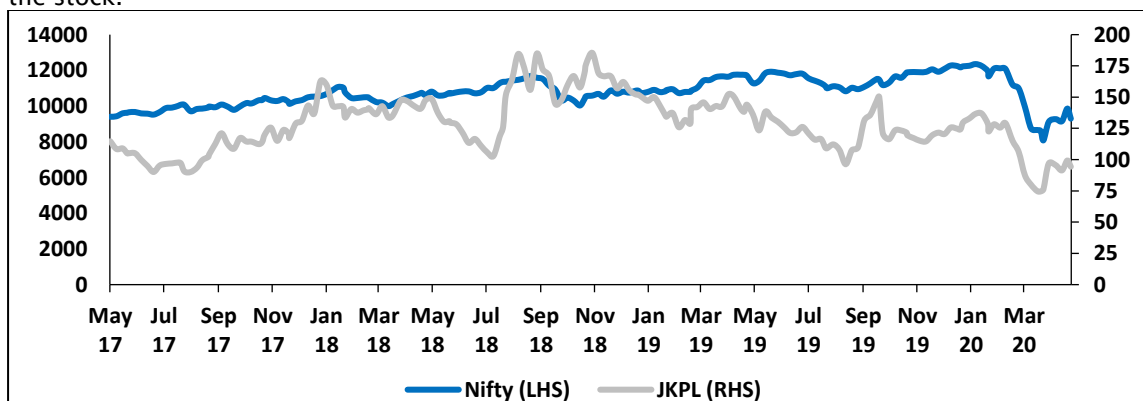
- Operating cash flows improved drastically and the incremental cash generation was used to repay debt. At the same time, company has also started paying dividends and has also announced buy back at Rs 130/share recently.
- Deleveraging focus reduced the D/E ratio from 2.9 in FY14 to 0.65 in FY20 leading to better interest coverage from 0.1 in FY14 to 5.6 in FY20.
- Working capital days also improved as receivable days went down from 29.5 days in FY12 to 8.8 days in FY20. Over the same period, payable days went up from 38.9 in FY12 to 39.1 in FY20.

❖ Attractive valuation at current level

After the recent rally of 50% in JKPL, the near term upside has been captured. Having said that, the stock is available at 3.7X PE multiple and 0.8X Book Value which is fair considering the fact that the growth in paper industry is expected to taper down due to rapid digitization post Covid-19. However, over long term, we expect JKPL to move back to the growth trajectory post 2 years of consolidation in FY21 and FY22 as the new capacity becomes operational and company is able to grab higher market share. Any dips in the near future can be considered as a buying opportunity in JKPL.

➤ Valuation and View:

- We like JKPL on the back of (a) strong brand name in high demand copier paper, (b) backward integrated manufacturing process with in-house pulp supply, (c) value creation through Sirpur acquisition, (d) disciplined financial management and (e) attractive valuation insulating down side risk. However, the recent 50% upmove in the price has factored in most of the upside potential. Any dips going forward should be considered as a buying opportunity in JKPL.
- Going forward, we expect the revenue to remain flattish on account of drop in volumes demand is expected in FY21 on account of Covid. However, cost rationalizations and improving pulp output per unit of wood as well as technological enhancements will lead to EBITDA margins to move up from 28.5% in FY20 to 30% by FY22E. On account of 2 lac TPA expansion at a capex of Rs 1,700 cr by mix of internal accruals and debt will lead to a jump in in depreciation.
- Based on above, we expect the revenue to remain flat at Rs 3,011 cr. EBITDA is expected to grow at 2.2% CAGR at Rs 910 cr as margins improve by 180 bps to 30.2% by FY22E. PAT is expected to degrow at 11% CAGR to Rs 370 cr on account of higher depreciation. EPS after buyback adjustment is expected to be at Rs 21.7.
- We are valuing JKPL at 5X FY22's EPS of Rs 21.7 to arrive at our target price of Rs. 108 for the stock, which presents a potential upside of 11% from the CMP of Rs 97. Accordingly, we recommend a **Hold** on the stock.

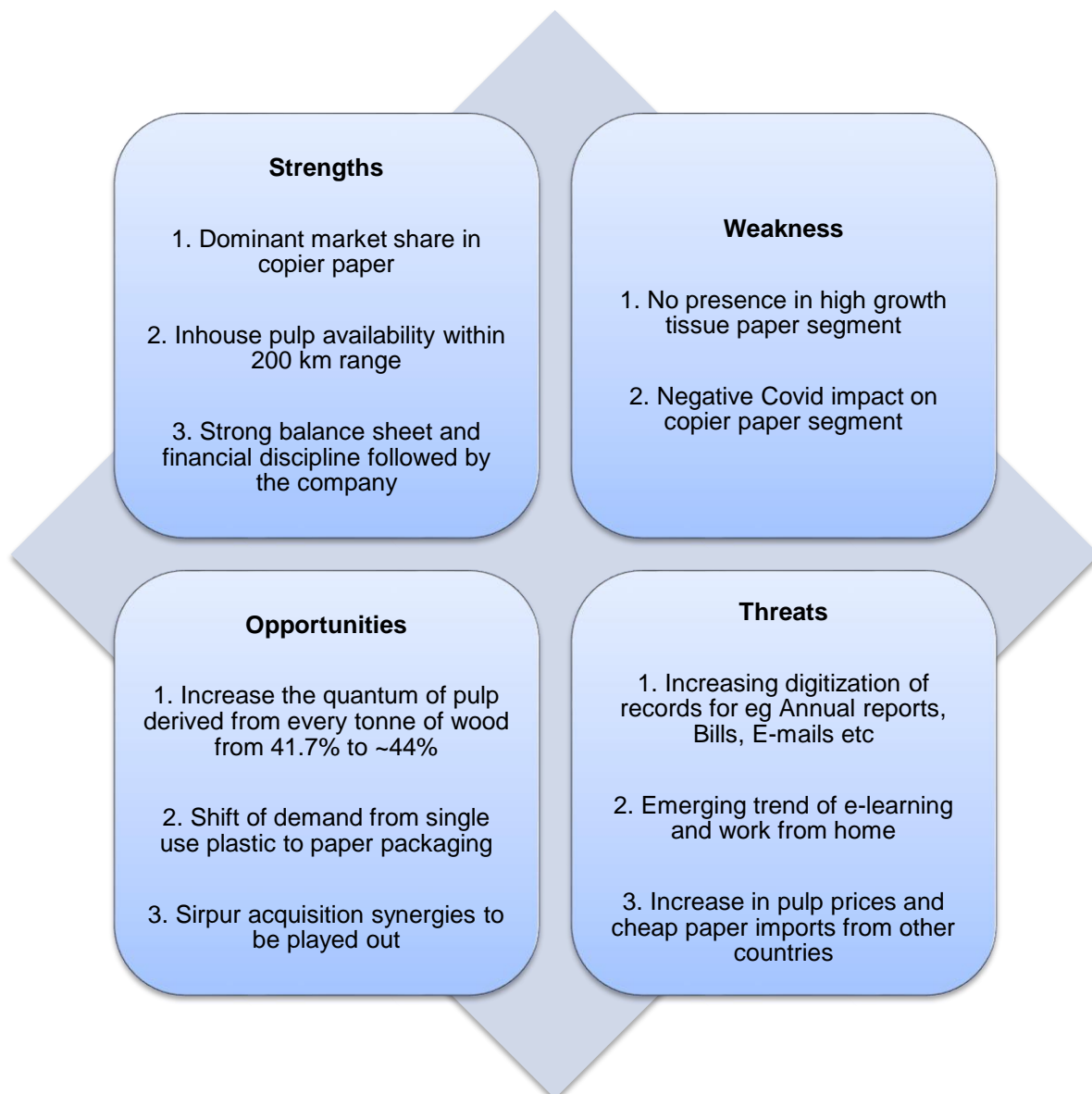




Key Risks

- In a rapidly digitising world, paper demand could decline as online learning and digitization of records can lead to reduced paper requirement.
- Raw material scarcity and rising pulp prices can affect the profitability
- Competition from imports is high since imports of paper and paperboard have increased from ~0.5 million tonnes in 2010-11 to ~1.7 million tonnes in 2017-18.

SWOT Analysis





Financials:

JK Paper Ltd.– Statement of Profit & Loss					
DESCRIPTION	FY18	FY19	FY20	FY21E	FY22E
Net Sales	2844.0	3256.7	3060.2	2784.8	3010.9
EXPENDITURE					
Raw Material Cost	1528.0	1627.5	1364.0	1235.7	1293.9
<i>as % of Sales</i>	<i>53.7%</i>	<i>50.0%</i>	<i>44.6%</i>	<i>44.4%</i>	<i>43.0%</i>
Fuel & Manufacturing overheads	246.0	258.7	295.3	265.1	276.0
<i>as % of Sales</i>	<i>8.6%</i>	<i>7.9%</i>	<i>9.6%</i>	<i>9.5%</i>	<i>9.2%</i>
Employee Cost	232.0	262.7	287.7	296.3	308.2
Other Expenses	225.0	239.7	241.9	211.6	222.8
EBITDA (Ex OI)	613.0	868.1	871.3	776.1	910.1
<i>EBITDA Margin</i>	<i>21.6%</i>	<i>26.7%</i>	<i>28.5%</i>	<i>27.9%</i>	<i>30.2%</i>
Depreciation	121.0	127.7	149.5	196.2	278.5
EBIT	492.0	740.4	721.8	579.9	631.7
Other Income	26.0	50.0	103.8	44.6	36.3
Interest	143.0	124.4	129.3	161.1	173.9
Profit Before Taxation	375.0	666.0	696.3	463.4	494.1
Provision for Tax	115.0	241.1	228.0	116.6	124.4
Profit After Tax	260.0	424.9	468.3	346.8	369.8
Adjusted EPS	14.6	23.8	26.3	20.3	21.7

JK Paper Ltd.– Balance Sheet					
DESCRIPTION	FY18	FY19	FY20	FY21E	FY22E
Share Capital	175.5	178.2	178.2	170.5	170.5
Total Reserves	1,467.6	1,859.9	2,187.3	2,372.4	2,649.7
Shareholder's Funds	1,643.1	2,038.1	2,365.5	2,542.9	2,820.3
Minority Interest	0.0	50.9	8.0	8.0	8.0
Total Borrowings	1,029.7	1,353.9	1,544.8	2,244.8	1,894.8
Other Non-Current Liabilities	143.4	238.8	341.0	341.0	341.0
Total Non-Current Liabilities	1,173.1	1,592.7	1,885.8	2,585.8	2,235.8
Trade Payables	250.9	274.2	382.2	289.9	313.5
Other Current Liabilities	541.3	566.2	649.0	674.9	701.9
Total Current Liabilities	792.2	840.4	1,031.2	964.9	1,015.4
Total Liabilities	3,608.4	4,522.1	5,290.5	6,101.6	6,079.4
Fixed Assets	2,640.5	2,982.2	3,541.3	4,745.1	4,766.7
Other Non-Current Assets	115.7	139.5	140.4	140.4	140.4
Total Non-Current Assets	2,756.2	3,121.7	3,681.7	4,885.5	4,907.0



Inventories	394.2	346.3	498.2	366.2	387.7
Sundry Debtors	109.2	73.5	73.8	76.3	74.2
Cash and Bank	123.4	26.7	42.0	28.8	45.6
Other Current Assets	225.6	953.9	994.8	744.8	664.8
Total Current Assets	852.4	1,400.4	1,608.8	1,216.1	1,172.4
Total Assets	3,608.6	4,522.1	5,290.5	6,101.6	6,079.4

JK Paper Ltd.– Cash Flow Summary					
DESCRIPTION	FY18	FY19	FY20	FY21E	FY22E
PBT	375.4	666.0	696.3	463.4	494.1
Add: Depreciation	121.0	127.7	149.5	196.2	278.5
Add: Interest Paid	143.0	124.4	129.3	161.1	173.9
Less: Other Income	-26.0	-50.0	-103.8	-44.6	-36.3
Less: tax Paid	-69.2	-139.7	-130.3	-116.6	-124.4
Change in WC	629.5	869.0	688.0	1089.2	1021.2
Cash from Operating Activities	560.3	729.3	557.7	972.5	896.8
Cash from Investing Activities	40.3	-965.6	-394.9	-1400.0	-300.0
Cash from Financing Activities	-507.3	139.7	-147.5	414.2	-580.0
Net Change	93.3	-96.6	15.3	-13.3	16.9
Opening Cash Balance	30.1	123.4	26.7	42.0	28.8
Closing Cash Balance	123.4	26.7	42.0	28.8	45.6

JK Paper Ltd. – Key Ratios					
DESCRIPTION	FY18	FY19	FY20	FY21E	FY22E
EBITDAM (%)	21.6%	26.7%	28.5%	27.9%	30.2%
ROE (%)	15.8%	20.8%	19.8%	13.6%	13.1%
ROCE (%)	18.4%	21.8%	18.5%	12.1%	13.4%
Receivable days	14	10	9	10	9
Inventory Days	50	41	50	48	47
Payable days	31	29	39	38	38
Total Debt/Equity(x)	0.6	0.7	0.7	0.9	0.7
Current Ratio(x)	1.1	1.7	1.6	1.3	1.2
Interest Cover(x)	3.4	6.0	5.6	3.6	3.6
BV per share	92.2	114.3	132.7	149.1	165.4
Adjusted P/E Ratio	6.9	4.2	3.8	5.0	4.7
Price/ Book value	1.1	0.9	0.8	0.7	0.6



ANALYST CERTIFICATION

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