

Building momentum for tomorrow

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The Andhra Pradesh Paper Mills Limited

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Building momentum for tomorrow

The strengths were always known. Large production capacity, top of the market quality, improving productivity, environment friendliness, regeneration of resources, committed team - these have been the fundamentals that helped report handsome performance results. APPM has a healthy track record.

The market is changing. Demand for quality paper is increasing while the competitive pressure needs to be met. APPM saw the dynamics, the challenges and the opportunities and is executing plans and building momentum to face the future.

In less than two years, the Company has created additional capacity, improved efficiencies, enhanced quality, reduced waste, become cost effective and more significantly, environment friendly.

We recognise that our stakeholders expect a healthy and responsible company. We have effective systems that monitor standards, processes and performance. We follow through to ensure compliance. We have gone beyond compliance needs.

The past was good. It cannot however be extrapolated to measure the future. While quarterly results are important, it is not the only measure for which the Company works. APPM is striving to enhance competitive strengths, profitability and accelerate its growth.

The efforts are to be one of the best players in the paper industry, achieve sustainable long term growth, and improve shareholder value.





From the desk of the Chairman

Paper industry needs to maintain growth momentum

Dear friends,

We at Andhra Paper had an exciting year. We implemented the Phase I of the MDP and stepped up pulp and paper production volumes, achieved significant level of efficiencies, improved productivity and saved on utilities. We showed immediate improvement in all performance parameters.

Unfortunately, we had a setback in the last quarter when the recovery boiler was damaged, and as a temporary measure we have reverted to the old boiler to support our production. The volume levels were affected impacting the financials in the recent quarters. We are confident that we shall soon resume our modernisation programme and stay on course to be one of the best performing companies in the industry.

I must reiterate that we have the most contemporary and environment friendly technology and we would be delivering consistently high quality paper with better strength properties. Our endeavour would be to demonstrate that Andhra Paper and indeed Indian paper quality can be as good as that produced anywhere in the world.

Indian paper industry has the best entrepreneurial skills and professional talents in this country and produces paper of international standards. In fact, in some of the grades we offer better quality to the customers.

We have a large population, but do not have large consumption. This needs to be addressed, both from the industry level as well as by the government. As the Indian economy grows and the aspiration levels of our people rises, Indian paper industry needs to be ready to meet the expectations of the consumer.

We need to anticipate and generate demand, build production capacity, and deliver volume and quality. Larger market for paper needs to be supported and the industry has to scale up its technology, volumes, productivity and be more cost competitive.

The issue needs to be addressed from the raw material stage. While all the larger companies encourage and motivate farm forestry, today manufacturers have no control on raw material availability, quality or price.

Despite the best brains in the industry, Indian paper industry has not optimised its economies and fresh investments in greenfield projects have been slower than desired. Command over supply chain is critical for investment decisions.

Seen in the correct perspective, investment in technology and capacity building in the paper industry is constrained by the lack of control on its key raw material, supplies of good quality wood. Large investors need reassurance on



raw material supplies and their forward plans and strategies are not limited by avoidable uncertainties.

Growth of the paper industry would get accelerated if the government permitted corporate farming, and allowed manufacturers to plan their raw material supplies. State and central governments need to appreciate that corporates would improve the land usage, rural economics and create wealth.

I believe not only would the paper industry add volumes and enhance efficiencies, there would be larger forest cover, cultivation of fallow wastelands, improvements in soil productivity, increased employment potential to farm hands, and considerable benefits to the rural economy.

Many of the Asian and European countries have large sized mills, the latest in technology, access to better varieties of wood and economies of scale, and Indian producers have considerable handicap in competing with them. We have talent, technology and mind set for quality but do not have control over the most important component of

paper production. Indian industry needs a level playing ground to be globally competitive.

In the interest of the Indian consumer, we at Andhra Paper seek and look forward to growth of Indian paper industry, assured raw material availability, high end quality, larger reach and market size, cost competitiveness, and long term sustainability of all paper manufacturers. India needs to step up volume availability at affordable prices.

Indian industry deserves support from the governments and other stakeholders to meet the challenges ahead. We need to address the situation now to manage some part of the future. The momentum needs to be built soon. I am sure the authorities and industry associations would work for the long term interest of the paper industry. I stay optimistic.

Warm regards

H. Manoj





The Executive Director reflects on the year under review

Review of Operations

How would you describe 2006-07?

The financial year 2006-07 was remarkable for the major initiatives that APPM took to build momentum for the future. While APPM did well on many of the operating parameters, the thrust was to hugely improve the production processes, systems and facilities, increase raw material security and ensure that environmental needs were adequately met. We worked on improving the fundamentals and the long term sustainability of the Company.

What were the highlights of operations?

The production volume at 1,59,574 MT was 9 per cent higher over the previous year. The quantity sold was 1,55,750 MT and the turnover was a new high for the Company at Rs.533 crore. The realisation per MT was higher at Rs.34,223 as against Rs.32,795 in the previous year. The incremental revenue per tonne was a function of both

improved market conditions as well as better realisation from higher grades of paper sold.

The profit before interest, depreciation and tax (PBIDT) was Rs.76.30 crore, a new milestone for the Company. With the completion of the Phase I of the MDP, interest and depreciation charges were higher and were booked against revenue. The profit before tax (PBT) was hence lower.

Members will appreciate that in line with prudential accounting standards, the Company has charged all costs while the revenues would commence gradually as the mill modernisation programme stabilises. Costs are incurred and booked early, while revenues would have a lag in time.

Unfortunately, in the last quarter of the financial year under review, there was a mishap in the recovery boiler and the damage reduced the throughput, created a set back in stabilisation programme and impacted the profitability levels. Every effort necessary is being made to resume operations early and step up the pace of growth.

Can you describe the initiatives to improve the manufacturing processes?

APPM has embarked on a growth plan that will increase production volumes, improve quality of paper produced, boost productivity, reduce use of expensive utilities, lower the operating costs and thereby step up margins. The fundamentals of the Company are expected to change when the Mill Development Plan is fully operational.

Rs.76.30 crore

Profit before interest,
depreciation and tax (PBIDT)

A new milestone

2006 - 07

For an integrated paper mill, major part of the costs is incurred in producing pulp and in consumption of fuel, power and water. APPM addressed these components and invested into larger production lines which give economies of scale, while increasing the production capacity. The manufacturing technology was improved by installing modern energy efficient and environment friendly plants.

What were the other initiatives regarding sustainability and long term growth?

At APPM, we believe long term strategy is a function of assurance of long term productive assets. Apart from ensuring that the production systems cater to our long term needs, we worked on raw material security by clonal propagation of pulpable tree species, by selecting elite parental trees with desirable qualities such as fast and uniform growth, high yielding disease and pest resistant and drought tolerant varieties.

Rs.533 crore

Turnover

A new high

2006 - 07

We distributed 71.5 million seedlings to the farmers at very low cost to them, guided them in plantation techniques and are seeing huge improvement in farm productivity. The farmers are at liberty to sell the wood to any one. Our experience is we do get a large volume of their harvest since we are in their vicinity. They are also positively responsive to the assistance that we provide them.



Realisation

Rs. per MT

34,223
2006-07

32,795
2005-06

During the year, we also worked towards lowering the consumption of water. We have consistently ensured that harmful emissions are low. Improvements made in processes and emission treatment facilities have helped to reduce discharges.

All these initiatives and activities have helped improve the long term fundamentals of APPM.

What do all these mean to the outlook and shareowner value?

As said earlier, APPM's fundamentals are set to change. The MDP includes a programme for cost savings and profitability improvement, but more significantly, it is an investment to improve the competitiveness of APPM's products and services. The MDP enhances the long term sustainability of the Company.

In fact, I believe, APPM will be a much stronger company producing larger volumes of high margin, high grade paper. Not only do we see APPM coming out of commoditisation, we expect to have pricing power as we upgrade our product lines.

Members would find visibility of growth and profits from the second half of the current fiscal followed by full benefits from the financial year 2008-09. The cost and income profiles upon which our annual valuations are based will undergo comprehensive revision. We shall work to create an APPM that will be the investor's preferred choice.



India the next growth market

- The global industry is increasingly centered in Asia and India is the next growth market to be pursued.
- Asian demand growth continues to dominate the global industry.
- India is yet only a small part of the story, with potential to expand much further.
- Supply development in Asia is also out-stripping all other regions.
- Structure of the Asian industry is strong, but India lags behind.
- There is a need to improve the overall competitiveness of the industry by investing more boldly.
- Consolidation and capacity restructuring is also one avenue of growth.
- International acquisition opportunities exist but need to be driven by a clear strategy.
- International players are more focused on India having missed the "boat to China".
- Raw materials remains a major issue but the industry can still grow without total control over pulp supply.
- Per capita paper consumption is expected to climb from the present 7 kilograms to 12 kilograms in 2020.

Excerpts from Poyry presentation on Developments in the Global Pulp and Paper Industry (January 2007)



Building momentum for tomorrow

We planned where we wanted to go; we got our plans ready; we worked out our strategies. We estimated the resources required for the transformation to be one of the most efficient pulp and paper mills in the country; and, we got going.

Indian paper industry is forecast to have increasing market size, rising demand for better quality paper as well as have a compelling need to stay ahead of both domestic and imported competition.

APPM's endeavor to remain competitive over the long term necessitates flexibility, problem solving approach and ability to adapt to the dynamics of moving targets. The Company is conscious of the need for renewal in production processes, improvement in manufacturing efficiencies as well as upgradation of the business model.

A Mill Development Plan (MDP) was drawn up to create the infrastructure that would keep APPM ahead of the curve.

