

The South India Paper Mills Ltd

63rd Annual General Meeting, 22nd September 2022

Chairman's Speech

Ladies and Gentlemen

A very Good Morning to all of you on this virtual 63rd Annual General Meeting of our Company.

I am sure all of you have received a copy of the 63rd Annual Report with the Accounts and Auditors' Report and hope you have had time to study it carefully and cast your votes electronically on the Resolutions proposed.

In this address, I would now like to report on how the year went, the Current situation and Future Prospects.

The financial year that went by, in a nutshell, was characterized by a steep, debilitating surge in the cost of raw material, energy and other commodity inputs even as demand remained lacklustre.

The CoVid 19 Pandemic continued to be disrupting with the detection of the Omicron variant in October-November 2021. Before it could be assessed that this variant although more virulent, was relatively benign and signalled the beginning of the end of the pandemic, there was the usual disruption in economic activity that had been observed in the previous variants. This also affected the speed of implementation of our expansion project but not as much as in the previous waves.

Operations in the year that was: A bumpy ride up the steep slope of rising costs.

During the year, there was an unprecedented and steep increase in the cost of recycled fibre and energy for paper making. The underlying factor for the rise in raw material prices was the high freight rates arising out of supply chain bottle necks, coupled with a sharp revival in global demand after the initial lock downs during the Pandemic.

Fuel prices went up very steeply from the third quarter onwards and remained high for the rest of the financial year as the geopolitical situation in Europe deteriorated with the Russian invasion of Ukraine in February 2022. Energy costs rose to two and a half times of the average of the preceding 5 years.

Revisions sought in paper prices to counter these cost increases were received with a substantial delay as downstream buyers of packaging pushed back against the increases sought and often threatened to divert business elsewhere to do so.

You will observe from the accounts that although the turnover improved substantially during the year, the operating margin declined as we could only revise prices to the extent of the increase in costs that were steep and frequent. There was neither the time nor the scope to push through increases large enough to retain operating margins in terms of a percentage of sales realisation.

The Status of the Global Containerboard Industry, Recycled Paper Demand and Supply and its impact on the Indian Industry:

The Global Scenario in the Containerboard (referred to as "Kraft Paper" in India) has seen a huge change over the year. The decline of the Pandemic and the change in the pattern of consumer spending has had a significant impact on the Containerboard Industry in terms of demand. From an unprecedented high in demand for boxes in the North American and European markets during 2021, the market has, during the last 90 days or so, fallen off a cliff. Whilst wastepaper prices have dropped hugely,

containerboard prices are yet to respond in full measure to the drop in demand. This is primarily due to energy costs that remain at unprecedentedly high levels due to the Russian strangle hold on European energy supply.

The Chinese market which is a major consumer of corrugated boxes and containerboard is also seeing a decline in demand from North America and Europe, its main export markets for manufactured consumer goods.

Current Operations: A Roller Coaster Ride

In my address to you in our last AGM, I had mentioned that it was a matter of concern that costs of raw material and energy were rising rapidly. Unfortunately, this concern was valid and in fact, this concern translated into reality during the last two quarters of the year when both raw material (recycled fibre) and energy costs saw all time highs with energy cost rising to twice the average of the preceding 5 years.

Recycled paper (OCC 11) rose to a historic high of \$380 for bookings in April, May, and June 2022 before collapsing to around \$180 currently as demand “dropped off the cliff” in the source markets.

Inventory on hand remains at high cost and will have to be liquidated at a loss if prices continue to fall.

Outlook: Sustained High Energy Costs, Stagnant Demand and Excess Capacity will limit margins this year.

Before commenting on the current scenario in the industry, I must highlight the fact that the Paper Industry and indeed the Containerboard segment has several segments and sub-segments. The performance of each segment in terms of demand and costs is affected differently by both common and specific cost factors.

On the demand side, the packaging segment (corrugated particularly) showed a strong resilience on the back of demand for packaging for essential goods and for e-commerce during the Pandemic. In contrast, the graphics paper segment of the industry suffered at this time due to the closure of academic institutions and offices. The pendulum of demand is now swinging across as demand from the Education and Office Paper segments gets restored and demand for packaging from the e-commerce segment moves to a lower orbit with a return to traditional shopping and diversion of disposable incomes away from goods to services- particularly, travel and hospitality.

It is a matter of relief that we are forward integrated into packaging, particularly that of essential fast moving consumer goods. What is of concern though, is the steep increase in the number of new “Automatic” plants looking for business in a market that is growing too slowly to fully absorb the new capacities. The entry of new players seeking entry at “any cost” is limiting the pricing power and margins of existing, established players. To counter this situation, the Packaging Division is working on adding new higher value-added products to serve the new, fast-growing segment of the packaging business that addresses the demand arising out of the ban of single use plastic. The developments thus far are encouraging.

On the cost side, the prices of recycled brown and mixed papers collapsed in July and August 2022 and the reductions are likely to be passed on as the new material begins to arrive in October 2022. The prices of virgin pulp and virgin pulp-based grades have remained relatively insulated from the decline in global demand as there is a significant raw material demand-supply imbalance in these markets. Energy costs, nevertheless, are a matter of concern for producers in this segment as well and sustaining high prices to recover higher energy costs could hurt demand significantly.

In the paper division, we retain some of pricing power for the higher grades that substitute Kraft Liners with good value. We expect this to enable the liquidation of high-priced raw material inventory with better realisation.

Having set before you the harsh ground reality of the year that went by and the current scenario, I would like to strike a note of optimism when I bring to your attention the status of the Expansion Project.

Expansion Project and Future Prospects –Paper Machine 6 – Our Noah’s Ark

In the deluge of rising costs of raw material and energy in a crowded supply market, the Company’s investment in the state of art PM6 with a modern recycled fibre line with extensive value-added grade capabilities is reason for optimism. Your Company has completed the installation of machinery as envisaged in the original plan. The equipment under the enhanced scope of the project has been installed as on date and is under trial. This additional investment gives us the opportunity to exploit more lucrative opportunities due to the enhanced grade capability and savings in the water, raw material, and energy cost.

Our medium to long term prospects depend heavily on the successful operation of the new paper machine.

Gratitude:

At this time of much uncertainty, I must state that the mood of the Operating Personnel and the Company Management is one of cautious optimism and this gives me much hope and confidence that we will achieve all our objectives in due course.

I take this opportunity to thank all the employees of the Company who have strived hard to beat the odds in these troubled times.

We have been privileged to enjoy the wholehearted support of our Bankers in our ventures over the years and I thank them for supporting us on this new growth plan.

It is a strong testimony to our ethos of building win-win partnerships that many of our customers and vendors have worked with us continuously over a few decades. I would like to extend my thanks to them as we continue to seek their support.

I would like to thank all my colleagues on the Board of Directors for their help and guidance over the years.

Finally, I would like to thank all of you, the members, for your patience and wholehearted support of our Company.

Thank you All for attending this Meeting.

Manish M. Patel

Chairman & Managing Director,

The South India Paper Mills Ltd.

