September 06, 2021

The Sandur Manganese & Iron Ores Limited: Ratings upgraded

Summary of rating action

Instrument^	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund based-Term Loan	400.00	400.00	[ICRA]A (Stable); upgraded from [ICRA]A- (Stable)
Long term - Fund based-Cash Credit	10.00	10.00	[ICRA]A (Stable); upgraded from [ICRA]A- (Stable)
Short Term - Non-fund based	341.00	341.00	[ICRA]A1; upgraded from [ICRA]A2+
Total	**751.00**	**751.00**	

^Instrument details are provided in Annexure-1

Rationale

The ratings upgrade reflects a sustained improvement in The Sandur Manganese & Iron Ores Limited's (SMIORE) operating and financial performances on the back of remunerative iron ore prices, turnaround in the ferro alloys business, and stabilisation of operations of the coke oven plant, which is expected to lead to a strong earnings growth in FY2022. SMIORE has a comfortable financial risk profile, characterised by a conservative capital structure and strong coverage indicators due to healthy profitability of mining operations, and adequate liquidity supported by unencumbered cash and liquid investments of Rs. 600 crore as on June 30, 2021. The ratings also favourably factor in the established track record of SMIORE for over six decades in the mining industry and its status as one of the leading merchant miners of manganese and iron ore. The company has access to estimated iron ore reserves of 118.5 million tonnes (mt) and manganese ore reserves of 14.7 mt, which, along with its mining lease validity till December 2033, provide long-term revenue visibility to its mining operations.

The ratings are, however, constrained by the proposed capacity expansion programme towards setting up a 1-million-tonne-per-annum (mtpa) steel plant (in two phases), which would increase the indebtedness and expose the company to project execution risks. The company also remains exposed to offtake risks for its coke manufacturing capacity. While the company has signed a memorandum of understanding (MoU) with a pig iron manufacturer in Karnataka to sell about 50% of its coke output on a conversion basis, its ability to offload the agreed quantity and sell the balance production to other steel plants would remain critical to mitigate offtake related risks. ICRA has also factored in the risks arising from operating in a highly regulated iron ore and manganese ore mining industries, and the exposure of its margins to volatility in prices of iron ore, manganese, coking coal and coke, given the inherent cyclicality in the end-user segments. The ratings also factor in sizeable contingent liabilities, which if crystallised, could adversely impact the financial risk profile of SMIORE. ICRA also notes that a large part of the promoters' shareholding in SMIORE has been pledged to the lenders of the company, which constrains its financial flexibility to some extent.

The Stable outlook on the [ICRA]A rating reflects ICRA's opinion that demand from the steel industry is expected to remain steady in the near-to-medium term, which coupled with SMIORE's low-cost mining operations, would lend comfort to its overall financial risk profile.

Key rating drivers and their description

Credit strengths

Strong operating and financial performances – The company's operating income and profits rose significantly in Q4 FY2021 and Q1 FY2022, supported by large iron ore price hikes owing to favourable domestic demand and turnaround in the ferro alloys business. The company commissioned its 400,000-metric-tonnes-per-annum (MTPA) coke oven plant and 30-MW waste heat recovery boiler (WHRB)-based captive power plant (CPP) in FY2021. It also increased its ferro-alloys capacity from 36,000 MTPA to 48,000 MTPA in that fiscal. The power generated from the WHRB covers the entire power requirement of the ferro-alloys division, which was loss making till FY2020 due to high power costs. The company reported better-than-expected operating profit margin of 36.4% in FY2021 and 53.5% in Q1 FY2022. While the profitability is likely to witness some moderation in the coming quarters owing to correction in iron ore prices, the same is likely to remain significantly better than ICRA's earlier estimates, supported by healthy ferro alloys and coke realisations. The company's financial risk profile remains comfortable, marked by a conservative capital structure with a strong net worth of Rs. 993.1 crore as on March 31, 2021 and healthy coverage indicators. It has a comfortable liquidity position, supported by healthy cash and liquid investments of Rs. 600 crore as on June 30, 2021. Going forward, despite the proposed debt-funded capex, the capital structure and liquidity position are expected to remain comfortable due to healthy free cash flow generation from the mining business.

Established track record of over six decades in mining industry; considerable experience of promoters – SMIORE was incorporated in 1954 by the former ruler of the Princely state of Sandur, Mr. Yashwanthrao Hindurao Ghorpade. SMIORE produces iron ore with Fe content of around 58-60%, with lump to fine production ratio of 1:2. The company is also among the large miners of manganese ore in India. In addition, SMIORE manufactures ferro-alloys (silico-manganese) and coke, providing a diversified revenue stream.

One of the largest private sector iron ore and manganese ore miners in Karnataka with adequate reserves – The company has two mining leases, valid up to December 2033, with proven reserves of almost 118.5 mt of iron ore and around 14.7 mt of manganese ore. It has an annual production capacity of 1.6 mtpa and 0.4 mtpa for iron ore and manganese ore, respectively. While the company has applied for an increase in production capacity to 3.85 mtpa, clearance from the Ministry of Environment, Forest and Climate Change (MoEFCC) is still pending. ICRA takes comfort from the vast reserves, long validity of the mining licence and established presence of the company in the mining industry. ICRA also positively considers the low-cost iron ore mining operations of Rs. 400 per MT, which supports the profitability of the mining division.

Credit challenges

Proposed capacity expansion programme towards setting up a 1-mtpa steel plant to increase indebtedness – SMIORE has plans to set up a 1-mtpa integrated steel plant in two phases. The proposed debt-to-equity mix would be 50:50. The entire iron ore and coke requirement for the steel plant would be met through captive sources. Given the significant investment in setting up a steel plant, the debt-funded nature of the capex programme would increase the indebtedness and constrain the financial risk profile of the company. Also, lack of track record in setting up a steel plant would expose the company to project execution risks.

Exposure to coke offtake risks – The company remains exposed to coke offtake risks given the large coke manufacturing capacity. While the company has signed an MoU with a pig iron manufacturer in Karnataka to sell 50% of its coke output on a conversion basis, its ability to offload the agreed quantity and sell the balance production to other steel plants would remain important to mitigate offtake related risks.

Exposure to price risks and risks arising from operating in a highly regulated mining industry – SMIORE is exposed to fluctuation in coking coal and coke prices, given the large lead time of the entire process, from ordering coking coal to selling coke, which is expected to keep the company's profitability and cash flows volatile. Nevertheless, such price risks are limited to 50% of SMIORE's output as it has signed an MoU with a pig iron manufacturer in Karnataka to sell about 50% of its coke output on conversion basis. SMIORE's earning from the mining business also remains volatile, as it is exposed to fluctuation in the prices of iron ore and manganese ore and to changes in the regulatory framework (as witnessed by the mining restriction imposed in Karnataka in the past). Metal ores and ferro-alloy prices exhibit considerable cyclicality and are highly sensitive to global demand patterns and general macro-economic factors.

High share pledge – The pledge of the promoters' shareholding in SMIORE remained elevated at 53.1% as on June 30, 2021, which constrains the financial flexibility of the company to some extent. The shares have been pledged to the lenders of SMIORE for the Rs. 400-crore term loan for the coke oven project.

Sizeable contingent liabilities – SMIORE has sizeable contingent liabilities, which primarily include disputed income tax claims of Rs. 68.4 crore and payments related to forest development tax of Rs. 68.2 crore as on March 31, 2021. While the company has been paying the income tax claims under protest, the materialisation of the same could adversely impact its net worth. On the other hand, crystallisation of its forest development tax liability could affect both cash generation and net worth as the same has not been paid by the company so far.

Liquidity position: Strong

SMIORE's liquidity position is **strong**, supported by healthy cash accruals from the mining operations. The company had unencumbered cash and liquid investments of Rs. 600 crore as on June 30, 2021 against repayment obligations of Rs. 57 crore in the current fiscal. The liquidity profile is further supported by unutilised fund-based limits of Rs. 10 crore. While a large part of the free cash available as on date would be utilised for the proposed steel plant capex, the cash generation in the coming quarters would keep the overall liquidity position comfortable.

Rating sensitivities

Positive factors – ICRA could upgrade SMIORE's ratings in case of a significant increase in its scale of operations while maintaining the profitability at the current level.

Negative factors –Pressure on SMIORE's ratings could arise in case of any large unanticipated debt-funded capex, resulting in increased debt-to-operating profit ratio of more than 1.5 times and/or lower-than-expected cash accruals because of unfavourable movement in prices of iron ore/manganese ore.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Mining Entities Rating Methodology for Entities in the Ferrous Metals Industry
Parent/Group Support	Not applicable
Consolidation/Standalone	Standalone

About the company

The Sandur Manganese & Iron Ores Limited (SMIORE), the flagship company of the Karnataka-based Sandur Group, was promoted in 1954 by the former ruler of the Princely state of Sandur, Mr. Yashwanthrao Hindurao Ghorpade (YHG). Mr. Bahirji Ghorpade, grandson of Late Shri M Y Ghorpade has been appointed as the Managing Director of the company with effect from June 17, 2020.

SMIORE is involved in mining of low phosphorous manganese and iron ore in the Hosapete-Ballari region of Karnataka. It has large mines with two leases, ML-2678 and ML-2679, with an area of 1860.10 hectares (ha) and 139.20 ha, respectively. The entire lease area is in the forest land, falling under Swamy Mallai (SM) and Rammana Mallai (RM) forest blocks of Sandur Range. The permissible production capacity is 1.6 mtpa for iron ore and 0.4 mtpa for manganese ore. In addition, SMIORE manufactures ferro-alloys (silico-manganese) at its 48,000-MTPA plant in Vyasankare, near Hospet.

Key financial indicators

Consolidated financials (Ind AS)	FY2020 (Audited)	FY2021 (Audited)	Q1 FY2022
Operating Income (Rs. crore)	591.6	746.6	475.1
PAT (Rs. crore)	147.4	153.9	148.8
OPBDIT/OI (%)	33.0%	36.4%	53.5%
PAT/OI (%)	24.9%	20.6%	31.3%
Total Outside Liabilities/Tangible Net Worth (times)	0.7	0.7	-
Total Debt/OPBDIT (times)	2.1	1.4	-
Interest Coverage (times)	29.0	20.8	24.6

Source: Company; P – Provisional; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; Source: SMIORE

Status of non-cooperation with previous CRA – Not Applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2022)				Chronology of Rating History for the past 3 years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in	Date & Rating in FY2021		Date & Rating in FY2020	Date & Rating in FY2019
					Sep 6, 2021	Nov 6, 2020	May 11, 2020	Jul 8, 2019	Jun 22, 2018
1	Term Loans	LT	400.0	364.1*	[ICRA]A (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Stable)
2	Cash Credit	LT	10.0	-	[ICRA]A (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Stable)
3	Letter of credit	ST	341.0	-	[ICRA]A1	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+

*Amount in Rs. crore; *As on March 31, 2021; LT – Long Term; ST – Short Term*

Complexity level of the rated instrument

Instrument	Complexity Indicator
Term Loans	Simple
Cash Credit	Very Simple
Letter of credit	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analyzing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, is available on ICRA's website: www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (RS Crore)	Current Rating and Outlook
NA	Term Loans	FY2018	-	FY2028	400.0	[ICRA]A (Stable)
NA	Cash Credit	-	-	-	10.0	[ICRA]A (Stable)
NA	Letter of credit	-	-	-	341.0	[ICRA]A1

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis – Not applicable

ANALYST CONTACTS

Jayanta Roy
+91 33 2287 6617
jayanta@icraindia.com

Priyesh Ruparelia
+91 22 6169 3328
priyesh.ruparelia@icraindia.com

Ritabrata Ghosh
+91 33 71501107
ritabrata.ghosh@icraindia.com

Anshuman Bharati
+91 22 6169 3351
anshuman.bharati@icraindia.com

RELATIONSHIP CONTACT

L Shivakumar
+91 22 6114 3406
shivakumar@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

ICRA Limited

Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

Branches