

December 19, 2022

## The Sandur Manganese & Iron Ores Limited: Ratings reaffirmed; [ICRA]A1 assigned for the enhanced amount

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	400.00	400.00	[ICRA]A (Stable); reaffirmed
Cash Credit	10.00	10.00	[ICRA]A (Stable); reaffirmed
Non-fund-Based Facilities	341.00	486.00	[ICRA]A1; reaffirmed/assigned
<b>Total</b>	<b>751.00</b>	<b>896.00</b>	

\*Instrument details are provided in Annexure-1

### Rationale

The reaffirmation of the ratings factors in the established track record of The Sandur Manganese & Iron Ores Limited (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 105 million tonnes (mt) and manganese ore reserves of 17 mt, which, along with its mining lease validity till December 31, 2033, provide long-term revenue visibility to its mining operations. The company posted its best-ever operating and financial performances in FY2022 with the profits touching an all-time high, aided by all-time high iron ore, manganese ore prices and first full year operations of the coke oven plant. Besides, the benefits of the waste heat recovery-based (WHRB) power plant, which operates on the flue gas generated by the coke oven plant, resulted in an extremely competitive cost of power generation. Moreover, benefits of low-cost captive manganese ore amid all-time high ferro alloy prices led to robust profitability of the ferro alloys division. An earnings surge across all divisions and a negative working capital intensity aided in strong free cash flow generation of almost Rs.803 crore in FY2022, which was channelised to strengthen its balance sheet liquidity. Consequently, SMIORE's liquidity profile remains strong, as reflected in the large cash balance and liquid investment portfolio, which impart a high degree of financial flexibility to the company. The company's overall leverage was negative on a net debt basis as on March 31, 2022 and September 30, 2022, leading to a comfortable financial risk profile.

The financial performance of the company has been significantly impacted in H1 FY2023 owing to factors including the recent regulatory changes post the Supreme Court's recent judgment that allowed miners' transition to a direct sale mechanism as opposed to only e-auctions conducted by the Monitoring Committee in the earlier regime. This led to a temporary period of uncertainty, which resulted in significantly lower sales of ores than the production levels recorded in H1 FY2023. Besides, the reduced spreads in the ferro alloys and coke segments amid higher raw material consumption costs and falling realisations, inventory write-downs due to correction in spot coking coal/coke prices and reduced realisations of iron ore and manganese ore also contributed to the reduced profitability. ICRA understands that iron ore dispatches have started picking up from November 2022 post better clarity from the Government of Karnataka, which led to a gradual depletion of stocks. With steel demand increasing in the second half of the fiscal, ICRA expects demand for iron ore also to remain strong, which along with SMIORE's demonstrated past track record of achieving a sales dispatch in line with the maximum capacity, should lead to an improved operational and financial performance in H2 FY2023. Also, with input costs largely peaking out, the performance of the ferro alloy and coke segments should also improve going forward. Notwithstanding the overall moderation in earnings expected in FY2023 from the high levels of FY2022, ICRA expects SMIORE's absolute profitability and credit metrics to remain healthy over the near term.

The ratings are, however, constrained by the upcoming capacity expansion programme towards setting up a 0.3-million-tonne-per-annum (mtpa) ductile iron pipe (DIP) and a 0.4-mtpa hot metal facility along with matching sinter plant and other auxiliary facilities at a budgeted cost of Rs.2,634 crore (gross of input tax credit). The same would expose the company to project execution risks and increase the indebtedness of the company, leading to a moderation in the net leverage (Net Debt/OPBDITA) during the project execution phase. Besides, lack of track record in the steel business accentuates project execution risks and timely completion/ stabilisation of the project within the budgeted time and costs would remain key rating sensitivities. However, ICRA understands that SMIORE is in the process of seeking requisite regulatory approvals in increasing the mining capacity from 1.6 mtpa to 4.5 mtpa and tripling of the mining output can reduce the company's dependence on borrowings to fund its upcoming growth plans. Moreover, ICRA has noted the higher share of value-added products and integration benefits that would be accruing to SMIORE once the DIP facility gets operational on account of the captive iron ore and coke sourcing. The ratings have also factored in the risks arising from operating in a highly regulated iron ore and manganese ore mining industry, and the exposure of its margins to volatility in prices of iron ore, manganese ore, coking coal/coke and ferro alloys, given the inherent cyclicity in the end-user segments.

The Stable outlook on the long-term rating reflects ICRA's opinion that the company's credit metrics would continue to remain at comfortable levels, going forward, aided by steady accruals, notwithstanding the sequential moderation expected in the current fiscal.

## Key rating drivers and their description

### Credit strengths

**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. Yeshwantrao Hindurao Ghorpade. SMIORE produces iron ore with Fe content of around 56-58%, 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 ferro-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 31, 2033, with proven reserves of almost 105 mt of iron ore and around 17 mt of manganese ore. It has an annual production capacity of 1.6 mtpa and 0.28 mtpa for iron ore and manganese ore, respectively. 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 around Rs. 400 per MT, which support the profitability of the mining division.

**Comfortable financial risk profile and healthy liquidity** – SMIORE's healthy profits over the years and low capital requirements in the mining business kept its return indicators healthy, as reflected by its core Return on Capital Employed (Core RoCE) in the range of 38-75% during FY2017 to FY2021, which further rose to around 113% in FY2022, aided by robust profitability across divisions. The company's moderate debt levels compared to its sizeable net worth resulted in a comfortable capital structure, as reflected by a gearing of 0.2 times as on March 31, 2022. The company's overall leverage stood negative on a net debt basis as on March 31, 2022 and September 30, 2022, supported by a free/bank/liquid investment balance of ~Rs.586 crore and ~Rs.627 crore, respectively, leading to a comfortable financial risk profile.

### Credit challenges

**Upcoming capacity expansion programme to expose the company to project execution risks and increase indebtedness and moderate business return indicators** – The company is embarking upon a large-sized capex programme towards setting up a 0.3-mtpa ductile iron pipe (DIP) and 0.4-mtpa hot metal facility along with matching sinter plant and other auxiliary facilities at a budgeted cost of Rs.2,634 crore (gross of input tax credit), which would expose the company to project execution risks

and would also increase the indebtedness of the company, leading to a moderation of net leverage (Net Debt/OPBDITA) during the project execution phase. Besides, the lack of track record of setting up and running a DIP plant, which remains a differentiated product being subject to BIS/ customer approvals could also expose the company to execution/ operating risks. However, ICRA has also noted the integration benefits that would be accruing to the DIP facility, once operational, on account of the captive iron ore and coke sourcing. However, given the high capital cost intensity of the DIP plant, the company's business return indicators are expected to moderate during the intervening period when the plant gradually ramps up to the peak rated capacity and is able to generate returns commensurate with the quantum of the investment.

**Exposure to price and regulatory risks** – 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 30-35% of SMIORE's output as the balance output is processed on a conversion basis, where the company earns a fixed conversion rate per tonne of production. SMIORE's earnings 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 restrictions imposed in Karnataka in the past). Metal ores and ferro-alloy prices exhibit considerable cyclicalities and are highly sensitive to global demand patterns and general macro-economic factors.

**Exposure to forex risks** – The company remains entirely dependent on coking coal imports for its coke manufacturing operations (to the extent of direct sales), thus exposing the company's earnings to fluctuations in foreign currency. As on March 31, 2022, the company had a foreign currency exposure of around Rs.457 crore mainly towards payables for coking coal, which remained unhedged. Subsequently, with the Indian rupee depreciating significantly against the US dollar in the current fiscal, the company's earnings in H1 FY2023 were impacted due to adverse forex fluctuations.

### Liquidity position: Strong

SMIORE's liquidity profile remains strong, as reflected in the large free cash, bank balance and liquid investment portfolio of ~Rs.627 crore as of September-end 2022, which impart a high degree of financial flexibility to the company. SMIORE has been generating positive operating cash flows, which are expected to continue going forward as well. This, along with the on-balance sheet liquidity available would lower dependence on external sources of funds to finance the upcoming capex.

### Rating sensitivities

**Positive factors** – ICRA could upgrade SMIORE's ratings in case of a significant increase in its scale of operations while maintaining healthy profitability and credit metrics.

**Negative factors** – Pressure on SMIORE's ratings could arise in case of any large debt-funded capex, resulting in increased net debt-to-operating profit ratio of more than 2 times or a deterioration in cash accruals because of unfavourable movement in prices of iron ore/manganese ore.

### Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Corporate Credit Rating Methodology</a> <a href="#">Rating Methodology for Entities in the Ferrous Metals Industry</a> <a href="#">Rating Methodology for Mining Entities</a>
Parent/Group Support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the standalone financials of SPL. The company has formed one new subsidiary in the current financial year, Sandur Pellets Private Limited, which is a non-operating entity at present.

## 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. Yeshwantrao Hindurao Ghorpade (YHG). Mr. Bahirji Ghorpade, grandson of Late 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 1,860.10 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 0.28 mtpa for manganese ore. In addition, SMIORE manufactures ferro-alloys (silico-manganese and ferro manganese) and coke at its plant in Vyasankare, near Hospet.

## Key financial indicators

SMIORE	Standalone		
	FY2021 (Audited)	FY2022 (Audited)	H1 FY2023 (Provisional)
Operating Income (Rs. crore)	746.6	2,248.7	1,130.2
PAT (Rs. crore)	153.9	675.1	55.7
OPBDIT/OI (%)	37.0%	43.3%	8.0%
PAT/OI (%)	20.6%	30.0%	4.9%
Total Outside Liabilities/Tangible Net Worth (times)	0.7	0.6	-
Total Debt/OPBDIT (times)	1.3	0.3	-
Net Debt/OPBDIT (times)	0.0	-0.3	-
Interest Coverage (times)	21.2	25.3	6.5

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation;

## Status of non-cooperation with previous CRA – Not Applicable

Any other information: None

## Rating history for past three years

Instrument	Type	Current Rating (FY2023)			Chronology of Rating History for the past 3 years				
		Amount Rated (Rs. crore)	Amount Outstanding as on Mar 31, 2022 (Rs. crore)	Date & Rating in Dec 19, 2022	Date & Rating in FY2022	Date & Rating in FY2021			Date & Rating in FY2020
						Sep 6, 2021	Nov 6, 2020	May 11, 2020	
1 Term Loans	Long Term	400.0	308.3	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Positive)	
2 Cash Credit	Long Term	10.0	-	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Positive)	
3 Non Fund-Based Limits	Short Term	486.00	-	[ICRA]A1	[ICRA]A1	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	

Amount in Rs. crore

## Complexity level of the rated instruments

Instrument	Complexity Indicator
Term Loans	Simple
Cash Credit	Simple

<b>Non Fund-Based Limits</b>	Very Simple
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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 analysing 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, are available on ICRA's website: [Click Here](#)

**Annexure-1: Instrument details**

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs Crore)	Current Rating and Outlook
NA	<b>Term Loans</b>	FY2018	NA	FY2028	400.00	[ICRA]A (Stable)
NA	<b>Cash Credit</b>	NA	NA	NA	10.00	[ICRA]A (Stable)
NA	<b>Non Fund-Based Limits</b>	NA	NA	NA	486.00	[ICRA]A1

Source: Company

[Please click here to view details of lender-wise facilities rated by ICRA](#)

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

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### Branches



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