May 15, 2019

NLC India Limited: Rating assigned

Summary of rating action

Instrument	Previous Rated Amount (Rs. Crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term, Term Loans	1,400.0	1,400.0	[ICRA]AAA (Stable); outstanding
Long Term, Borrowing Programme	2,000.0	2,000.0	[ICRA]AAA (Stable); outstanding
Long Term, Non-Convertible Debentures	-	2,000.0^	[ICRA]AAA (Stable); assigned
Total	**3,400.0**	**5,400.0**	

^Company can raise NCD upto Rs. 2000 crore

Rationale

For arriving at the rating, ICRA has taken a consolidated view of NLC along with its subsidiaries NLC Tamilnadu Power Limited, which operates a 1000 MW power project at Tuticorin, and Neyveli Uttar Pradesh Power Limited, which is setting up a 1980 MW power project in Uttar Pradesh.

The rating continues to reflect NLC Group's strong business risk profile with respect to both lignite mining operations and power generation. While access to captive lignite mines reduces the fuel risks, operation of pit-head power stations linked to these mines enables NLC to have competitive energy costs. These operational strengths have resulted in a favourable financial risk profile characterized by healthy cash accruals and comfortable capital structure. The rating also continues to be supported by the dominant Government of India ownership.

These strengths are to some extent offset by the counterparty credit risk arising from the exposure to financially weak discoms; the resultant elevated working capital requirements and the large cash outgo in the recent past towards dividend & share buyback, which have impacted the liquidity profile of the company to an extent. The rating also factors in the pressure on NLC's profitability due to the lower PLFs and the adverse cost structure of the newly commissioned plants; the availability of low cost merchant power has further kept the PLFs of thermal players depressed and the ability of NLC to improve on its PLF levels in such an environment remains to be seen. The rating also considers NLC's large expansion plans with sizeable projects under execution which exposes the company to risks of cost overruns.

Outlook: Stable

ICRA believes NLC's credit profile will remain stable given the long track record of operations, financial flexibility arising out of sovereign ownership and also the regulated nature of mining / power generation where the company enjoys cost-plus pricing and regulated returns. The outlook may be revised to 'Negative' if NLC's working capital intensity remains elevated, due to further delays in receipt of the arrears amounts from the beneficiaries, thereby impacting the liquidity position. Also, continued technical issues in TPS II Expansion and Barsingsar projects & execution delays in under construction thermal / solar projects resulting in large under-recoveries as well as increase in the cost of NLC's power generation would have a material impact on the profitability going forward and would be key rating sensitivities.

Key rating drivers

Credit strengths

Navratna Govt of India PSU with a long operational track record - The Government of India holds a dominant share of ~82% in NLC which has been operational for more than 50 years in the lignite mining and power generation segments. NLC was also conferred the 'Navratna' status in 2011 which enables the management to take faster investment decisions

Integrated mining / power player with very low fuel supply risks - NLC is the Ministry of Coal designated nodal agency for lignite mining in India and currently operates mines with a total capacity of 30.6 MTPA across the states of Tamil Nadu and Rajasthan. Most of the company's thermal stations are pithead power plants and hence the fuel supply risks are very low considering the captive nature of the mines and large reserves. Even for the recently commissioned coal-based power plant in Tuticorin, the company has a Fuel Supply Agreement which mitigates fuel risks to a large extent.

Cost plus tariff structure for both mining and power generation ensuring steady profitability - NLC uses lignite mined from its captive mines to generate power and sells it to various beneficiaries. The lignite transfer pricing is determined by Ministry of Coal and it is based on Cost plus principles ensuring healthy profitability from the mining segment. The tariffs for the thermal power plants are determined by the Central Electricity Regulatory Commission (CERC) as per the classic two part tariff methodology whereas the fixed and energy charges are calculated and approved separately. The fixed charges include a stable return on equity and operation of the plants at desired parameters would result in a healthy profitability at the company level.

Risk profile diversified through renewable energy generation - NLC has been focused on thermal power generation since inception and this has exposed the company to risks specific to the sector. However, the company has ventured into renewable power generation and is commissioning / has recently commissioned 1,339 MW of solar power projects in TN in addition to the 61 MW renewable capacity that is already operational. These projects would largely not be affected by risks inherent in the mining and thermal businesses including labour strikes, wage increases and technical issues.

Financial profile characterised by healthy cash accruals and capital structure - The Company has reported healthy profitability over the years driven by operational efficiency and regulated tariffs. With fully depreciated plants and low interest burden, this has translated into healthy net cash accruals. NLC also has a large accumulated net worth due to profitable operation over the years and, notwithstanding the recent uptick, the outstanding debt levels are relatively low resulting in a healthy capital structure which the company intends to leverage for its expansion plans.

Credit challenges

Project execution delays and operational issues in recently commissioned power plants – NLC's older power plants (TPS I, TPS I Expansion & TPS II) continue to operate above normative parameters despite their vintage. However, the company has faced technical issues in the recently commissioned Barsingsar and TPS II power plants and hence the overall PLF levels of the company have remained lower than the normative PLF since FY 2016. This in addition to the fixed cost under recovery – CERC has disallowed some portion of the cost overruns incurred for the Barsingsar, TPS II Expansion & Tuticorin NTPL project – is expected to result in lower returns from these projects. Nevertheless, the plants constitute a minor portion of the overall power generation and hence the impact is expected to be moderate.

The execution of the 500 MW solar project in Tamil Nadu has also seen substantial delays, owing to land acquisition related issues, and this is expected to reduce the tariff applicable for a major portion of the capacity given that the bid tariff was subject to commissioning within the control period. This is expected to stress the standalone project metrics even though the project debt servicing would be met out of the accruals from other mines / power plants. With NLC also executing the 709 MW project, further slippages on execution could impact the financial profile adversely.

Current low power tariff scenario has increased the risks of power surrender by discoms – NLC's plants have traditionally been in the top of the Merit Order Position of its beneficiaries due to the lower fixed and energy charges. However, the tariff levels have increased following the increase in the lignite transfer prices and the higher capital costs for the recently commissioned plants. Concurrently, the overall demand supply position has changed in the power sector with the improvement in transmission network and availability of cheap renewable power. This has resulted in discoms increasingly surrendering high cost thermal power which has impacted the PLF levels of thermal plants. NLC has voluntarily reduced the lignite transfer price by Rs 300 / Tonne in FY 2019 to reduce the power tariff and improve its merit order position; however, this has impacted the profitability of the company's mining division.

Exposed to counterparty credit risks as majority of the discoms have weak financial profiles – Major portion of the sales of the company is to counterparties like TANGEDCO and Rajasthan discoms who have large accumulated losses and highly leveraged balance sheets. This has resulted in delayed payments especially from TANGEDCO which has stressed the working capital position in the past. The large arrears billing (~Rs 1500 crore) done in March 2017 has also been contested by TANGEDCO and not paid till date resulting in a substantial increase in working capital intensity in FY 2018 and current fiscal. Nevertheless, following a recent favourable order from the Court, these amounts are expected to be received in the current fiscal which would aid the liquidity.

Mining segment exposed to risks with regards to labour strikes and land acquisition – The mining segment has performed strongly over the years due to the high operational efficiency and the strong performance of the linked power plants. However, mining performance is heavily contingent on the company achieving continuous production – in the recent years there have been multiple stoppages of work due to flooding and labour strikes. Labour strikes especially pose a significant risk as the company has a large unionised and temporary labour base who have been demanding regularisation and wage revisions. Over the long term, the performance of the mining segment will also depend on speedy land acquisition to mine the identified reserves once the current mines are fully exploited.

Significant expansion plans in the mining, thermal power and renewable power segments: NLC has sizeable expansion plans with planned capex upwards of Rs 40,000 crore over the next five years, though most of the projects are in the nascent stages of development. The key ongoing projects are the 1000 MW New Neyveli TPS (which is nearing commissioning), NUPPL 1980 MW power plant, Mine I restructuring and the 500 & 709 MW solar projects. The company has also started initial works for coal mining in the allocated Pachwara and Talabira mines and timely commencement of mining would be critical to ensure fuel security for the UP and planned mega thermal project in Odisha. ICRA notes that the funding mix and execution risks associated with these projects would be the key rating sensitivities.

Liquidity Position:

NLC has traditionally maintained healthy cash balances owing to sizeable operational cash generation. In FY 2017, the company declared its higher ever dividend of 73% which led to an outgo of Rs 1350 crore. NLC also completed buyback of 9% of its then outstanding share capital, worth Rs 149 crore, in February 2017 at a substantial premium resulting in an outgo of Rs 1477 crore. In FY 2018, the company declared dividend of Rs 774 crore (inclusive of taxes) and has further spent Rs 1,249 crore in December 2018 to buyback a part of its equity shares. These outflows have decreased the overall liquid surplus available with the company. In addition, the company's working capital intensity has increased as the large arrears billing to discoms resulted in elevated receivables as of December 2018.

Though the cash balances have been depleted, the projected cash generation of NLC is expected to be largely adequate to meet the equity commitments of the ongoing and planned projects for the next three-year period. Also, the sanction of working capital limits, of which average utilisation remains at ~40%, is also expected to provide a substantial liquidity buffer to the company.

Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating methodology for thermal power producers
Parent/Group Support	NA
Consolidation / Standalone	Consolidated – Including the subsidiaries / JVs – NTPL & NUPPL

About the company:

NLC India Limited (NLC; erstwhile Neyveli Lignite Corporation Limited), a public sector undertaking incorporated in November 1956, is engaged in the activities of lignite mining and power generation. The company currently has lignite mining capacity of 30.6 million tons per annum (mtpa) and installed power generation capacity of 4731 megawatt (MW). NLC's power stations cater to the five southern states of Tamil Nadu, Andhra Pradesh, Kerala, Karnataka and Puducherry, as well as Rajasthan through its newly commissioned thermal plant in Barsingsar. The Government of India (GoI) holds ~82% stake in the company. The company works under the administrative control of the Ministry of Coal, GoI. In April 2011, the Government of India declared the company as a 'Navratna' enterprise.

Key financial indicators (audited) – NLC - Consolidated

	FY 2017	FY 2018
Operating Income (Rs. crore)	11,557.2	11,652.1
PAT (Rs. crore)	3,300.2	2,005.8
OPBDIT/ OI (%)	40.1%	37.6%
RoCE (%)	16.1%	14.5%
Total Debt/ TNW (times)	0.69	0.71
Total Debt/ OPBDIT (times)	2.48	3.02
Interest coverage (times)	7.87	7.99

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2020)				Chronology of Rating History for the past 3 years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating	Date & Rating in FY2019	Date & Rating in FY2018		Date & Rating in FY2017
					May 2019	Feb 2019	Nov 2017	Sep 2017	Apr 2016
1	Non Convertible Debentures	Long term	**600.0**	-	**-**	[ICRA]AAA (Stable); Withdrawn	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)
2	Non Convertible Debentures	Long Term	**2000.0**	-	**[ICRA]AAA (stable) assigned**				
3	Term Loans	Long Term	**1,400.0**	350	**[ICRA]AAA (Stable)**	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)
4	Borrowing Programme	Long term	**2,000.0**	2000	**[ICRA]AAA (Stable)**	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	-

Complexity level of the rated instrument:

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the 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	Dec 2015	~8.45%*	Aug 2019	1,400.0	[ICRA]AAA (Stable)
NA	Borrowing Programme	Dec 2017	7%	June 2022	2,000.0	[ICRA]AAA (Stable)
NA^	NCDs^	-	-	-	2,000.0	[ICRA]AAA (Stable)

^proposed NCD and yet to be issued and company can raise upto Rs. 2,000.0 crore Source: NLC

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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.

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