

September 25, 2017

NLC India Limited

Summary of rated instruments

Instrument	Amount Rs Crore	Rating Action
Long Term; Term Loans	1400.0	[ICRA]AAA (Stable); reaffirmed
Long Term, Non Convertible Debentures	600.0	[ICRA]AAA (Stable); reaffirmed

* Instrument Details are provided in Annexure I

Rating Action

ICRA has reaffirmed the [ICRA]AAA (pronounced as ICRA triple A) long-term rating on the Rs 600 crore¹ bond programme and Rs 1,400 crore term loans of Neyveli Lignite Corporation Limited (NLC)². The outlook on the long term rating is stable.

Rationale

While reaffirming 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 reaffirmation 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, comfortable capital structure & robust debt protection metrics. 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.

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 ~90% in NLC India Limited 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

¹ 100 lakh = 1 crore = 10 million

² For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications.

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 has resulted 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 implementing 630 MW of solar power projects in Tamil Nadu in addition to the 61 MW renewable (wind + solar) capacity that is already operational. The tariff levels for these renewable projects are relatively robust and the return on these projects could be healthy if execution risks are managed.
- **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. In FY 2017, with the upward revision of the lignite transfer prices and the final orders from CERC for various plants considering the revised costing, the company billed large arrears to its beneficiaries and this resulted in a sharp increase in the revenues and profitability. 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 Weakness

- **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 due to steady availability of fuel. 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 in the past two years. 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 still constitute a minor portion of the overall power generation and hence the impact is expected to be moderate.
- **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. Recent CERC regulations with regards to fixing of a technical minimum of 55% for operation of thermal power plants is also expected to set a floor for thermal power PLFs and further impact the sector till renewable and merchant power prices firm up.
- **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. Nevertheless, the recent financial restructuring undertaken by the various discoms especially

under the Ujwal Discom Assurance Yojna (UDAY) scheme have resulted in an improved financial profile and payment timelines. The long term financial health of the discoms would depend on frequent tariff revisions, reduced subsidy dependence from the respective State Governments and improved operational efficiencies.

- **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 past 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, NUPPL 1980 MW power plant, Mine I restructuring and the 130 & 500 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 TN/Odisha. ICRA notes that the funding mix and execution risks associated with these projects would be the key rating sensitivities. The company also intends to increase its operational thermal capacity through inorganic acquisitions and has identified the 1200 MW Raghunathpur plant of Damodar Valley Corporation as the first acquisition target. The final approval from the Government is still pending for the acquisition. Details with regards to project valuation and acquisition funding mix are not available as yet; ICRA would continuously monitor the same and assess the impact on the financial profile of NLC.
- **Liquidity weakened by large outgo towards dividend / share buyback and higher working capital intensity; albeit cash generation expected to be adequate to fund equity commitments** – 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. 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 March 2017. 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 recent sanction of working capital limits is also expected to provide a substantial liquidity buffer to the company.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria

[Corporate Credit Rating Methodology](#)

[Rating Methodology for Thermal Power Producers](#)

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 4295 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 ~90% 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)

Consolidated	FY2016	FY2017
Operating Income (Rs. crore)	7,899	11,591
OPBDIT (Rs. crore)	2,547	4,632
PAT (Rs. crore)	974	3,330
OPBDIT/ OI (%)	32.2%	40.0%
PAT/OI (%)	12.3%	28.7%
Total Debt/ TNW (times)	0.52	0.69
Total Debt/ OPBDIT (times)	3.31	2.48
Interest coverage (times)	5.45	7.87

Source: Audited IndAs financials of the company. OI: Operating Income; 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: Not applicable

Rating History for last three years:

Table: Rating History

S.No	Name of Instrument	Current Rating			Chronology of Rating History for the past 3 years		
		Type	Rated amount (Rs. Crores)	Month-year & Rating	Month-year & Rating in FY2017	Month-year & Rating in FY2016	Month-year & Rating in FY2015
				September 2017	April 2016	-	February 2015
1	Non Convertible Debentures	Long Term	600.0	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	[ICRA]AAA (Stable)
2	Term Loans	Long Term	1400.0	[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
Details of Instrument

ISIN	Name of the instrument	Date of issuance	Coupon rate	Maturity Date	Size of the issue (Rs. Cr)	Current Rating and Outlook
INE589A07029	NCDs	Jan 2009	8.83%	Jan 2019	600.0	[ICRA]AAA (Stable)
-	Term Loans	-	NA	Aug 2019	1400.0	[ICRA]AAA (Stable)



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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.

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