

September 30, 2021

NMDC Limited: Rating continues to remain under Watch with Negative Implications

Summary of rating action

Instrument [^]	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Proposed Non-Convertible Debenture (NCD) Programme	4,476.20	4,476.20	[ICRA]AAA@; Rating continues to remain under Watch with Negative Implications
NCD Programme	523.80	523.80	[ICRA]AAA@; Rating continues to remain under Watch with Negative Implications
Total	5,000.00	5,000.00	

[^]Instrument details are provided in Annexure-1; @ - rating watch with negative implications

Rationale

The rating Watch with Negative Implications on NMDC Limited's (NMDC) [ICRA]AAA rating reflects uncertainty over the debt servicing arrangement to be made by NMDC Iron & Steel Plant (NISP) in the initial period post its demerger. The demerger was approved by NMDC's board on August 27, 2020. While the debt servicing would be met by NMDC till the demerger, as per the demerger scheme, the obligation for the rated debt would shift to the new entity once the demerger is complete. This, in turn, would exert rating pressure as the credit profile of NISP would be much weaker than NMDC as it does not have any track record in the steel industry and would take some time in ramping up and stabilising its steel business. ICRA also notes that NISP would have a mirror shareholding of NMDC and the ~Rs. 18,000 crore invested by NMDC towards the steel plant till date would be transferred to NISP as equity, thereby weakening the net worth of NMDC. ICRA will continue to monitor these developments.

The rating derives comfort from NMDC's status as the largest iron ore miner in India, with its mines having adequate reserve of high-quality ore and its strong capital structure and debt coverage indicators. The total reserves of its mines stood at around 1,800 million tonnes (mt) with an average Fe content of 63-65%. The company has an approved environmental clearance (EC) for 51.8 million tonnes per annum (mtpa) and reported an average annual production of 33.5 mt during the past five fiscals. Following the ongoing upcycle in the steel sector, NMDC has been reporting strong sequential earnings growth since Q3 FY2021. In Q4 FY2021, the company reported its highest ever quarterly operating profits since its inception. Notwithstanding a moderation in domestic iron ore prices in Q2 FY2022 following the correction in seaborne ore prices, ICRA expects NMDC to report strong earnings growth in FY2022, supported by rising dispatches as well as higher average iron ore realisations compared to FY2021. The rating also draws comfort from the company's Navratna status under the Ministry of Steel, Government of India (GoI), with the latter holding a 68.3% stake in the company as on June 30, 2021. Sovereign ownership and superior liquidity profile supported by a healthy unencumbered cash balance of about Rs. 3,723.8 crore as on March 31, 2021, impart a high degree of financial flexibility. Nevertheless, ICRA notes that the company remains exposed to the cyclicality inherent in the steel industry and to regulatory risks associated with the mining operations.

Salient terms as specified in the term sheet for the rated NCD programme

- » Liability towards the proposed NCD proceeds shall be transferred to the demerged entity (NISP) without the need for any separate consent solicitation exercise from the debenture holders.
- » Post the demerger, in case the credit rating of the demerged entity is downgraded to AA+ or below anytime till the maturity of the NCDs, then the coupon rate shall be enhanced further by an additional 25 basis points for each notch of

rating downgrade below AAA, and such enhanced coupon shall be payable effective from the date of the rating downgrade.

- » In the event of a delay in payment of the interest amount and/or the principal amount on the due date(s), the company shall pay an additional interest of 2% per annum in addition to the respective coupon rate payable on the bonds, on such amounts due, for the defaulting period i.e. the period commencing from and including the date on which such amount becomes due and up to but excluding the date on which such amount is actually paid.

Key rating drivers and their description

Credit strengths

Status as the largest iron ore mining company in India – NMDC, incorporated in 1958, is the largest iron ore miner in India with its mines having adequate reserve of good quality ore. Its total reserves stand at around 1,800 mt. During the past five fiscals, the company reported an average annual production of 33.5 mt, which is around 16% of the total iron ore produced in India during that period. The company has seven iron ore mines in four different locations – Kirandul, Bacheli (in Chhattisgarh), Donimalai and Kumarswami (in Karnataka) with existing EC approved capacity of 51.8 mtpa.

Significant sovereign ownership and strategic importance to the GoI – NMDC is a flagship company under the Ministry of Steel, with a *Navratna* status. The GoI has a 68.3% ownership in NMDC as on June 30, 2021 and has strategic importance to the Government, given its status as the largest iron ore producer in India.

Superior liquidity profile – NMDC's financial risk profile has remained comfortable over the years, as reflected by its comfortable capital structure (with a gearing of 0.1 times as on March 31, 2021) and superior liquidity profile. Despite regular dividend payouts, NMDC's unencumbered cash balance remained healthy at Rs. 3,723.8 crore as on March 31, 2021.

Healthy profitability owing to high-margin iron ore mining business – NMDC's operating profitability remained strong in the range of 50-60% during the last four fiscals mainly on account of its low-cost mining operations (mining cost excluding taxes of about Rs. 770 per metric tonnes) and high grade of its iron ore deposits. The average Fe grade of NMDC's Bailadila mines stood at 65% and that of Donimalai mines stood at 63%. In addition, NMDC's recent lease extensions have been made at significantly lower revenue shares¹ with the state governments compared to the levels discovered in mine auctions, which further give NMDC a strong competitive advantage. Despite disruption in production in Q1 FY2021 due to the Covid-19 pandemic, the company reported iron ore sales of 33.3 mt in FY2021. The rally in iron ore prices from H2 FY2022 resulted in a healthy operating margin of 64.1% in Q1 FY2022 and 57.2% in FY2021 against 51.3% in FY2020. While ICRA expects the company's profitability to witness some moderation in FY2022 owing to the recent correction in iron ore prices and an increase in revenue share to the state governments, the margins would remain above 50% in the medium term and the company is likely to report strong earnings growth in FY2022.

Credit challenges

Transfer of debt servicing liability to NISP, which would have a weaker credit profile – NMDC is in the process of setting up a 3-mtpa steel plant at Nagarnar (i.e. NISP). Out of total project cost of Rs. 21,940 crore, the company has incurred capex of Rs. 18,536 crore till March 31, 2021. The commissioning is expected in Q4 FY2022. Its timely commissioning within the budgeted time and costs would remain a key monitorable from the credit perspective. While a major part of the capex has been funded by equity, the company is proposing debt funding of Rs. 5,000 crore (including the rated NCD). Post the demerger, the entire debt servicing obligation would be transferred from NMDC to NISP, which would have a weaker credit profile compared to NMDC. The new entity would be listed on the stock exchanges to achieve a mirror shareholding same as NMDC.

¹As per the amended Mines and Mineral Regulation (Development) Act, 22.5% additional premium is being levied by the state governments of Chhattisgarh and Karnataka for NMDC's Kirandul, Bacheli and Donimalai mines. This is w.e.f. Q4 FY2021. As against the same, average auction premiums in Odisha have generally remained above 100%

While the detailed demerger scheme is yet to be finalised, future debt servicing by NISP from its own cash flows and the overall transaction structure would remain a key credit monitorable.

Exposure to cyclical risk in steel sector – Iron ore is used as an input in the steel manufacturing process. NMDC, like other iron ore miners, remain exposed to the cyclical risk inherent in the steel sector. A prolonged downturn in the steel industry might put pressure on NMDC's production levels and impact its cash flows. ICRA also notes that the major part of the company's iron ore output is sold to three customers viz. ArcelorMittal Nippon Steel India, Rastriya Ispat Nigam Limited and JSW Steel Limited, exposing it to high sales concentration risk.

Exposure to regulatory risks related to mining business – NMDC remains exposed to the regulatory risks associated with the mining business. ICRA notes that the Donimalai iron ore mine was non-operational between November 2018 and February 2021 post the expiry of its mining lease. While the lease was renewed in February 2021, the company lost production of ~15 mt between November 2018 and February 2021. Going forward, the risk of timely renewal of other mining leases is minimal given the amendment of the Mines and Mineral Regulation (Development) Act by the Central Government to make it mandatory for all the state governments to renew the mining leases of public sector companies for 20 years on the expiry of the current lease.

ICRA also notes that as per the Supreme Court (SC) guidelines, the company's entire sales in Karnataka are currently routed through a monitoring committee (MC) set up by the apex court. The MC retains 10% of the sales proceeds towards reclamation and rehabilitation plan (R&R plan). The retention amount stood at Rs. 2,344 crore as on March 31, 2021, which corresponds to the period from October 4, 2011 to March 31, 2021. The R&R plan has been approved by the Central Empowered Committee (CEC) and the matter is pending with the SC for the release of 10% amount.

Liquidity position: Superior

NMDC's liquidity position remains superior, supported by its healthy cash generation from the mining business. While the company has NCDs of Rs. 523.8 crore on its books, the repayment would be due in August 2025. ICRA expects the company's liquidity profile to remain comfortable given the large unencumbered cash balances of Rs. 3,723.8 crore as on March 31, 2021, unutilised fund-based facilities of Rs. 635 crore with adequate drawing power, and healthy cash generation from the mining business.

Rating sensitivities

Positive factors – Not applicable

Negative factors – Pressure on the rating would emerge post the demerger event due to a significantly weak standalone credit profile of NISP. The rating could also be downgraded in case of a sustained deterioration in profitability due to a sharp correction in iron ore prices.

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	For arriving at the ratings, ICRA has considered the consolidated financial risk profile of NMDC Limited. As on March 31, 2021, NMDC Limited had 8 subsidiaries, 5 joint venture companies and 5 associate companies. These have been enlisted in Annexure-2.

About the company

NMDC, incorporated in 1958, is under the administrative control of the Ministry of Steel, GoI. Mr. Sumit Deb is the Chairman and Managing Director of the company. NMDC is involved in the exploration of a wide range of minerals including iron ore, copper, rock phosphate, lime stone, dolomite, gypsum, bentonite, magnesite, diamond, tin, tungsten, graphite, beach sands etc. and is also the largest iron ore producer in India. At present, it produces more than 30 million tonnes (mt) of iron ore from Bailadila Deposit-14/11C, Bailadila Deposit-5, 10/11A (Chhattisgarh) and Kumarswamy Iron Ore Mines (Karnataka).

Key financial indicators

Consolidated financials (Ind AS)	FY2020 (Audited)	FY2021 (Audited)	Q1 FY2022 (Audited)
Operating Income (Rs. crore)	11699.2	15370.1	6512.2
PAT (Rs. crore)	3602.3	6247.1	3191.5
OPBDIT/OI (%)	51.3%	57.2%	64.1%
PAT/OI (%)	30.8%	40.6%	49.0%
Total Outside Liabilities/Tangible Net Worth (times)	0.1	0.2	
Total Debt/OPBDIT (times)	0.1	0.2	
Interest Coverage (times)	607.5	522.9	1392.1

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

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	
						Oct 1, 2020	Sep 7, 2020			
					Sep 30, 2021			Mar 23, 2020	-	
1	Proposed NCD	LT	4,476.20	-	[ICRA]AAA@; Rating Watch with Negative Implications	[ICRA]AAA@; Rating Watch with Negative Implications	[ICRA]AAA&; Rating Watch with Developing Implications	[ICRA]AAA (Stable)	-	
2	NCD	LT	523.80	523.80	[ICRA]AAA@; Rating Watch with Negative Implications	[ICRA]AAA@; Rating Watch with Negative Implications	-	-	-	

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

Complexity level of the rated instrument

Instrument	Complexity Indicator
NCD	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	Proposed NCD	-	-	-	4,476.20	[ICRA]AAA@; Rating Watch with Negative Implications
INE584A08010	NCD	August 28, 2020	7.3%	August 28, 2025	523.80	[ICRA]AAA@; Rating Watch with Negative Implications

Source: Company

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Legacy Iron Ore Limited	90.05%	Full consolidation
J & K Mineral Development Corporation Limited	95.86%	Full consolidation
NMDC Power Limited (*)	100%	Full consolidation
Karnataka Vijaynagar Steel Limited	100%	Full consolidation
NMDC Steel Limited	100%	Full consolidation
Jharkhand Kolhan Steel Limited (*)	100%	Full consolidation
NMDC-SARL, Madagaskar (Under closure)	100%	Full consolidation
NMDC-CSR Foundation	100%	Full consolidation
Kopano-NMDC Minerals(Proprietary) Limited	50%	Equity method
Jharkhand National Mineral Development	60%	Equity method
NMDC-CMDC Ltd., Raipur	51%	Equity method
NMDC-SAIL Ltd. (**)	51%	Equity method
Bastar Railway Pvt. Ltd	52%	Equity method
Romelt-Sail(India) Limited(*)	25%	Equity method
International Coal Ventures (Pvt.) Ltd	25.94%	Equity method
Krishnapatnam Railway Company Ltd.	6.40%	Equity method
Neelachallspat Nigam Ltd	10.10%	Equity method
Chhattisgarh Mega Steel Ltd.	26%	Equity method

Source: NMDC; (*) Under closure; (**) Under the process of striking off

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