

**STOCK IDEA**
Rating: BUY**NMDC Ltd**
Iron Ore Mining

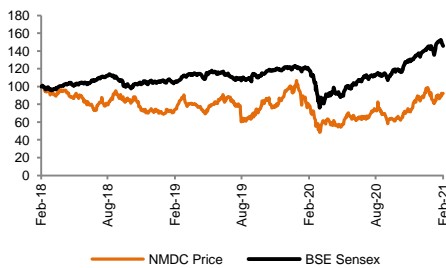
| | |
|------------------|---------------------|
| Date | Feb 26, 2021 |
| CMP (Rs) | 127.1 |
| Target Price | 161.0 |
| Potential Upside | 27.0% |
| BSE Sensex | 49,099 |
| NSE Nifty | 14,529 |

| | |
|-------------------|---------|
| Scrip Code | |
| Bloomberg | NMDC IN |
| Reuters | NMDC BO |
| BSE Group | A |
| BSE Code | 526371 |
| NSE Symbol | NMDC |

| | |
|--------------------|----------|
| Market Data | |
| Mar. cap(Rs Cr) | 37,233 |
| Eq. Cap.(Rs Cr) | 293 |
| 52 Wk High/Low | 131/62 |
| Avg.Qtly Volume | 12190293 |
| Face Value (Rs) | 1 |

Shareholding Pattern (%)

| Particulars (%) | Dec-20 | Sep-20 | June-20 |
|-----------------|--------|--------|---------|
| Promoters | 69.7 | 69.7 | 69.7 |
| FII | 4.5 | 4.5 | 5.4 |
| DII | 20.4 | 20.5 | 20.4 |
| Others | 5.4 | 5.4 | 4.6 |

Comparative Price Chart

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NMDC Ltd, incorporated in 1958 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. It is currently under the administrative control of the Ministry of Steel, Gol. The Gol has 69.7% ownership in NMDC as on Dec 31, 2020. It is one of the highest profit making 'Navaratna' public sector companies under the Ministry of Steel. The company is engaged in mining of iron ore which is a crucial raw material for the steel industry and hence the growth of the company is directly related to the growth of steel industry. NMDC is the largest iron ore producer in India with mining capacity of 43 mn tonnes. At an average of 64% Fe, NMDC sells one of the best grade iron ore globally. With iron ore production of around 31.9 million tonnes in FY20, NMDC contributed to around 18% of domestic production (excluding captive iron ore production). At present, it produces iron ore from Bailadila Deposit-14/11C, Bailadila Deposit-5, 10/11A (Chhattisgarh) and Kumarswamy Iron Ore Mines (Karnataka). Recent developments such as resumption of mining at Donimalai in Karnataka (18% of NMDC's production) with a capacity of 7 million tonnes per annum, after a waiting of almost 2 years bodes well for the company. Furthermore, the demerger of upcoming steel plant in Chattisgarh is expected to lead to value unlocking strengthening its liquidity. The increase in iron ore prices and strong demand in steel is expected to lead to better performance in the coming quarters.

INVESTMENT RATIONALE**Volumes expected to increase with resumption of Donimalai mine production**

NMDC resumed production of iron ore from Donimalai Mines in Karnataka on 18th Feb-21. The production remained halted since December 2018, when NMDC suspended mining in Donimalai due to a legal battle with the Karnataka government over the issue of imposition of premium on the sale price of the iron ore extracted from the mines. The Donimalai mine, with a capacity of 7 million tonnes per annum, contributes to nearly 18% of NMDC's production. Furthermore, Kumarasamy mines in Karnataka has also got environmental clearance to increase production from 7mt to 10mt. NMDC is also working on expanding production in Chattisgarh by the addition of screening lines and debottlenecking. Considering this, we estimate volumes FY22 to be ~42mt, respectively.

Strong performance expected to continue in the coming quarters

In Q3FY21, NMDC reported strong performance owing to improved realization and cost improvement. For Q3FY21, NMDC reported revenue from operations at Rs. 4,355 crore (up 45% YoY, 95% QoQ). Iron ore sales volume was at 9.3 MT (up 10% YoY and 41% QoQ) while Realizations increased 31%/Rs1,087/t YoY (+40%/Rs1,325 QoQ) at Rs4,645/t. EBITDA came in at Rs. 2,767 crore (up 74% YoY, 169% QoQ) & EBITDA/tonne came in at Rs. 2,982/tonne. (Rs. 1892/tonne in Q3FY20 and Rs. 1560/tonne in Q2FY21). For Jan-21, NMDC recorded iron ore production of 3.86 MT (vs 3.31 MT in Jan-20) a growth of 16.6% YoY while the iron ore sales rose 26.4% YoY to 3.74 million tonnes (vs 2.96 MT in Jan-20). As per World Steel Association, steel demand has picked up post pandemic across all sectors, and a revival from Auto & Construction sector will keep prices sustainable for some time domestically. These factors are indicative of continued strong performance.

Demerger of Chattisgarh steel plant can lead to value unlocking and strengthening of liquidity

NMDC is in the process of constructing its 3 MTPA Integrated Steel Plant at Nagarnar in the State of Chattisgarh. Its board has approved the demerger of its upcoming steel plant in Chhattisgarh expected to be completed by September-21 and will create a separate listed company with shareholding similar to NMDC. The commissioning of steel plant is expected in Q1FY22. NMDC has incurred a capital expenditure of Rs. 17,000 crore and is likely to commence production next year. Once the sale/public listing after the de-merger of the plant is successfully, the funds will be used to unlock capex sitting as CWIP (Rs. 160 bn as on 30th Sept, 20), which will strengthen NMDC's liquidity.

Key Risks

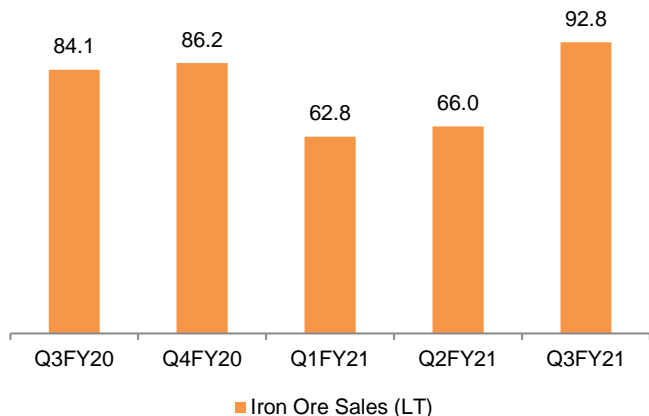
(1) The revision in royalty rates at Donimalai mines, wherein the rate will be decided by the committee and lead to a change in the MMDR Act is likely to have an impact on other mines of NMDC. (2) Sharp fall in iron ore prices. (3) Delay in steel plant demerger

Valuation and Outlook:

NMDC volume is expected to get a boost in FY22 from the restart of Donimalai mines. In addition the government impetus to the steel sector with growth envisaged in key sectors such as, infrastructure, housing, railways is expected to lead to strong demand of high grade ore, which should help NMDC in improving its performance in terms of volumes as well as EBITDA margins. For FY22, the revenue/EBITDA expected to grow at a CAGR of 16.7%/20.0% over FY20/22E. Compared to its global peers, such as Rio Tinto, Cleveland-Cliff, Ferrexpo and Vale, which trade at an FY21 EV/EBITDA of between 5 x to 7 x, NMDC has an FY21 EV/EBITDA of 4.6x. **Based on FY22E EBITDA, we apply EV/EBITDA multiple of 4.2x and arrive at a target price of INR 161/per share with an upside of ~27% from CMP and hence recommend a BUY on the shares of NMDC Ltd**

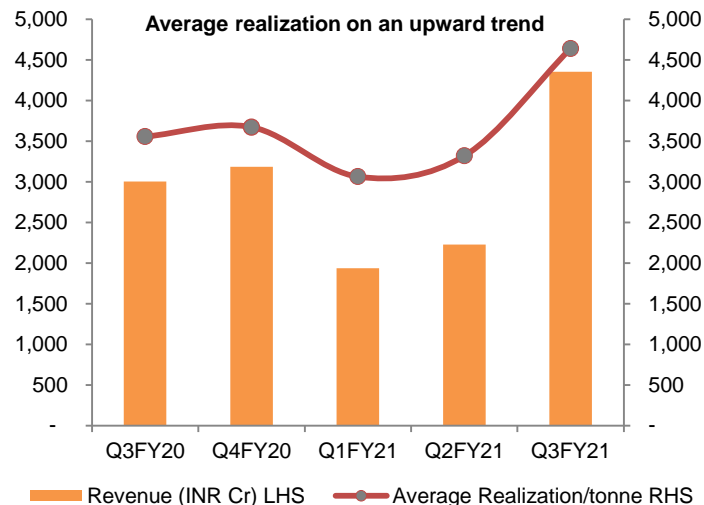
| Particulars | Revenue (Rs. Cr) | EBITDA (Rs. Cr) | EBITDAM (%) | PAT (Rs. Cr) | PATM (%) | EPS (Rs.Cr.) | P/E (x) |
|-------------|------------------|-----------------|-------------|--------------|----------|--------------|---------|
| FY18 | 11,615 | 5,803 | 50.0% | 3,808 | 32.8% | 12.0 | 9.9 |
| FY19 | 12,153 | 6,924 | 57.0% | 4,619 | 38.0% | 14.7 | 7.9 |
| FY20 | 11,699 | 6,002 | 51.3% | 3,574 | 30.5% | 11.7 | 10.3 |
| FY21E | 13,115 | 7,115 | 54.3% | 4,261 | 32.5% | 14.5 | 8.3 |
| FY22E | 15,940 | 8,647 | 54.3% | 5,179 | 32.5% | 17.7 | 6.8 |

Iron ore sales volumes expected to surge on opening of Donamalia mines



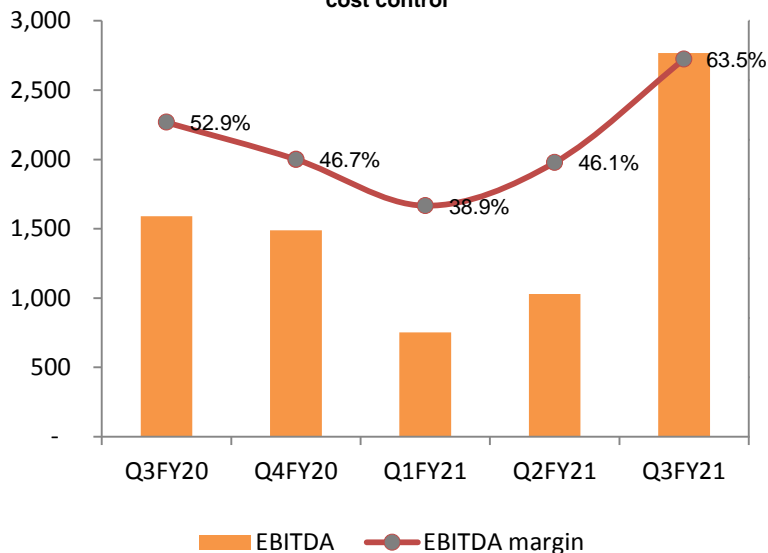
Source: Company filings, SystematixResearch

Average realization on an upward trend



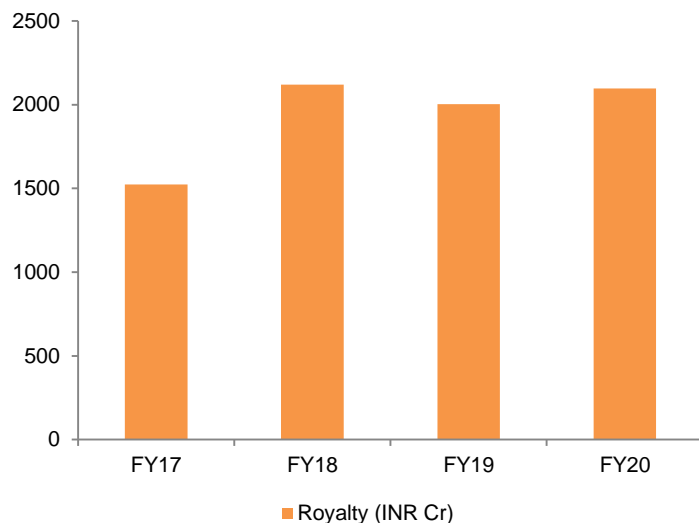
Source: Company filings, SystematixResearch

Improvement in EBITDA margin due to high realization and cost control



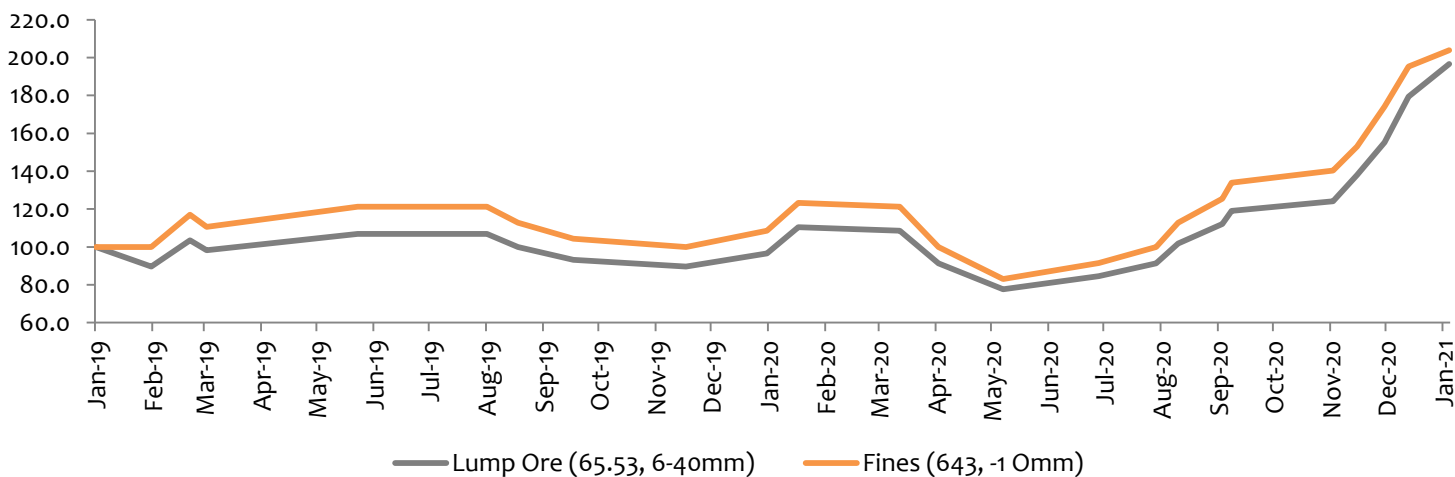
Source: Company filings, SystematixResearch

High volumes to mitigate the expected increase in premium



Source: Company filings, SystematixResearch

Domestic iron ore prices surge due to iron ore shortage and demand revival



Source: Company filings, SystematixResearch

Exhibit 1: Income Statement

| INR Cr | FY 18 | FY 19 | FY 20 | FY 21E | FY 22E |
|-----------------------------|---------------|---------------|---------------|---------------|---------------|
| Revenues | 11,615 | 12,153 | 11,699 | 13,115 | 15,940 |
| COGS | 249 | 238 | 226 | 253 | 308 |
| Gross profit | 11,366 | 11,915 | 11,473 | 12,862 | 15,632 |
| Employee cost | 1,049 | 1,039 | 1,049 | 1,167 | 1,419 |
| Other expenses | 4,514 | 3,951 | 4,422 | 4,579 | 5,566 |
| EBITDA | 5,803 | 6,924 | 6,002 | 7,115 | 8,647 |
| EBITDA Margin | 50.0% | 57.0% | 51.3% | 54.3% | 54.3% |
| Depreciation & amortization | 257 | 279 | 295 | 236 | 319 |
| EBIT | 5,546 | 6,645 | 5,707 | 6,879 | 8,329 |
| Interest expense | 37 | 40 | 10 | 11 | 11 |
| Other income | 523 | 589 | 514 | 365 | 314 |
| PBT | 6,177 | 7,194 | 6,115 | 7,232 | 8,631 |
| Tax | 2,373 | 2,557 | 2,513 | 2,972 | 3,453 |
| Minority interest | -1 | -1 | 0 | 0 | 0 |
| PAT | 3,808 | 4,619 | 3,574 | 4,261 | 5,179 |
| Adj. PAT | 3,664 | 4,619 | 3,478 | 4,261 | 5,179 |
| EPS (INR) | 12.0 | 14.7 | 11.7 | 14.5 | 17.7 |
| Adj. EPS | 11.6 | 15.1 | 11.4 | 14.5 | 17.7 |

Source: Company filings, SystematixResearch

Exhibit 2- Cash Flow Statement

| INR Cr | FY18 | FY19 | FY20 | FY21E | FY22E |
|---|---------|---------|---------|---------|---------|
| Net Cash Generated From Operations | 3,376 | 4,002 | 2,126 | 5,419 | 5,186 |
| Net Cash Flow from/(used in) Investing Activities | (1,865) | (788) | (313) | (1,451) | (2,548) |
| Net Cash Flow from Financing Activities | (1,557) | (3,201) | (1,753) | (3,706) | (2,829) |
| Net Inc/Dec in cash equivalents | (46) | 11 | 60 | 262 | (191) |
| Opening Balance | 80 | 34 | 46 | 106 | 367 |
| Closing Balance Cash and Cash Equivalents | 34 | 46 | 106 | 367 | 176 |

Source: Company filings, SystematixResearch

Exhibit 3- Key Ratios

| Key Ratio | FY18 | FY19 | FY20 | FY21E | FY22E |
|-----------------------|-------|-------|-------|-------|-------|
| EBITDA Margin (%) | 50.0% | 57.0% | 51.3% | 54.3% | 54.3% |
| Net Profit Margin (%) | 31.5% | 38.0% | 29.7% | 32.5% | 32.5% |
| RoE (%) | 15.0% | 17.7% | 12.6% | 15.1% | 16.9% |
| RoCE (%) | 24.3% | 27.4% | 22.0% | 25.2% | 27.7% |
| EPS (INR) | 12.0 | 14.7 | 11.7 | 14.5 | 17.7 |

Source: Company filings, Systematix Research

Exhibit 4- Balance Sheet

| INR Cr | FY18 | FY19 | FY20 | FY21E | FY22E |
|--|---------------|---------------|---------------|---------------|---------------|
| Non-current assets | | | | | |
| Property, plant and equipment | 3,150 | 3,199 | 3,254 | 3,334 | 3,331 |
| Capital work-in-progress | 12,545 | 13,819 | 15,500 | 17,467 | 19,699 |
| Intangible assets under development | 0 | 94 | 94 | 30 | 30 |
| Other intangible assets | 214 | 220 | 455 | 455 | 455 |
| Right of use of assets | 0 | 0 | 7 | 7 | 7 |
| Financial assets | | | | | |
| Investments | 673 | 859 | 910 | 902 | 638 |
| Loans | 140 | 155 | 224 | 192 | 159 |
| Deferred tax assets (Net) | 386 | 583 | 397 | 397 | 397 |
| Other non-current assets | 2,626 | 2,986 | 3,075 | 3,212 | 4,004 |
| Total non-current assets | 19,827 | 21,914 | 23,946 | 26,090 | 28,813 |
| Current assets | | | | | |
| Inventories | 572 | 666 | 724 | 647 | 830 |
| Financial assets | | | | | |
| Trade receivables | 1,473 | 1,425 | 2,224 | 1,797 | 2,361 |
| Cash and cash equivalents | 34 | 46 | 106 | 367 | 176 |
| Bank balances other than above | 5,427 | 4,574 | 2,332 | 1,500 | 1,500 |
| Other financial assets | 443 | 398 | 365 | 447 | 319 |
| Other current assets | 313 | 417 | 1,168 | 704 | 262 |
| Total current assets | 8,864 | 7,977 | 7,348 | 5,892 | 5,878 |
| TOTAL ASSETS | 28,691 | 29,891 | 31,294 | 31,982 | 34,691 |
| EQUITY AND LIABILITIES | | | | | |
| Equity | | | | | |
| Equity share capital | 316 | 306 | 306 | 293 | 293 |
| Other equity | 24,101 | 25,738 | 27,367 | 27,935 | 30,285 |
| Equity attributable to the equity shareholders | 24,417 | 26,044 | 27,673 | 28,228 | 30,578 |
| Non-controlling interests | 15 | 14 | 8 | 8 | 8 |
| Total equity | 24,432 | 26,058 | 27,681 | 28,236 | 30,586 |
| Liabilities | | | | | |
| Non-current liabilities | | | | | |
| Borrowings | 0 | 0 | 0 | 0 | 0 |
| Provisions | 714 | 769 | 828 | 828 | 828 |
| Financial liabilities | 0 | 0 | 6 | 6 | 6 |
| Total non-current liabilities | 714 | 769 | 834 | 834 | 834 |
| Current liabilities | | | | | |
| Financial liabilities | | | | | |
| Borrowings | 500 | 364 | 566 | 566 | 566 |
| Trade payables | 160 | 203 | 226 | 210 | 275 |
| Other financial liabilities | 1,889 | 1,668 | 1,220 | 1,368 | 1,662 |
| Other current liabilities | 968 | 788 | 545 | 545 | 545 |
| Provisions | 28 | 41 | 223 | 223 | 223 |
| Total current liabilities | 3,545 | 3,065 | 2,780 | 2,912 | 3,271 |
| Total liabilities | 4,259 | 3,833 | 3,613 | 3,746 | 4,105 |
| TOTAL EQUITY AND LIABILITIES | 28,691 | 29,891 | 31,295 | 31,982 | 34,691 |

Source: Company filings, Systematix Research

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| Disclosure of Interest Statement | Update |
|--|--------|
| Analyst holding in the stock (%) | |
| Served as an officer, director or employee | |

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EXPLANATION TO RATINGS: BUY: TP>15%; ACCUMULATE: 5%<TP<15%; HOLD: -5%<TP<5%; REDUCE: -15%<TP<-5%; SELL: TP<-15%

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