

Nifty Series

October 10, 2013

Key Triggers	3 month stock view vis-à-vis	
Expansion led volume growth to address higher demand	Nifty	Outperformer
Large reserves and resource base	BSE Metals Index	Performer
Forward integration to bring value add and diversify revenues	Expected price range – 3 months	Rs 114-137
Key Risks	Post Breakout Levels	
Regulatory/export policy changes could impact business	Support	Rs. 98
Mining Tax could negatively hurt profitability	Resistance	Rs. 150
Demand slowdown could impact volume growth		



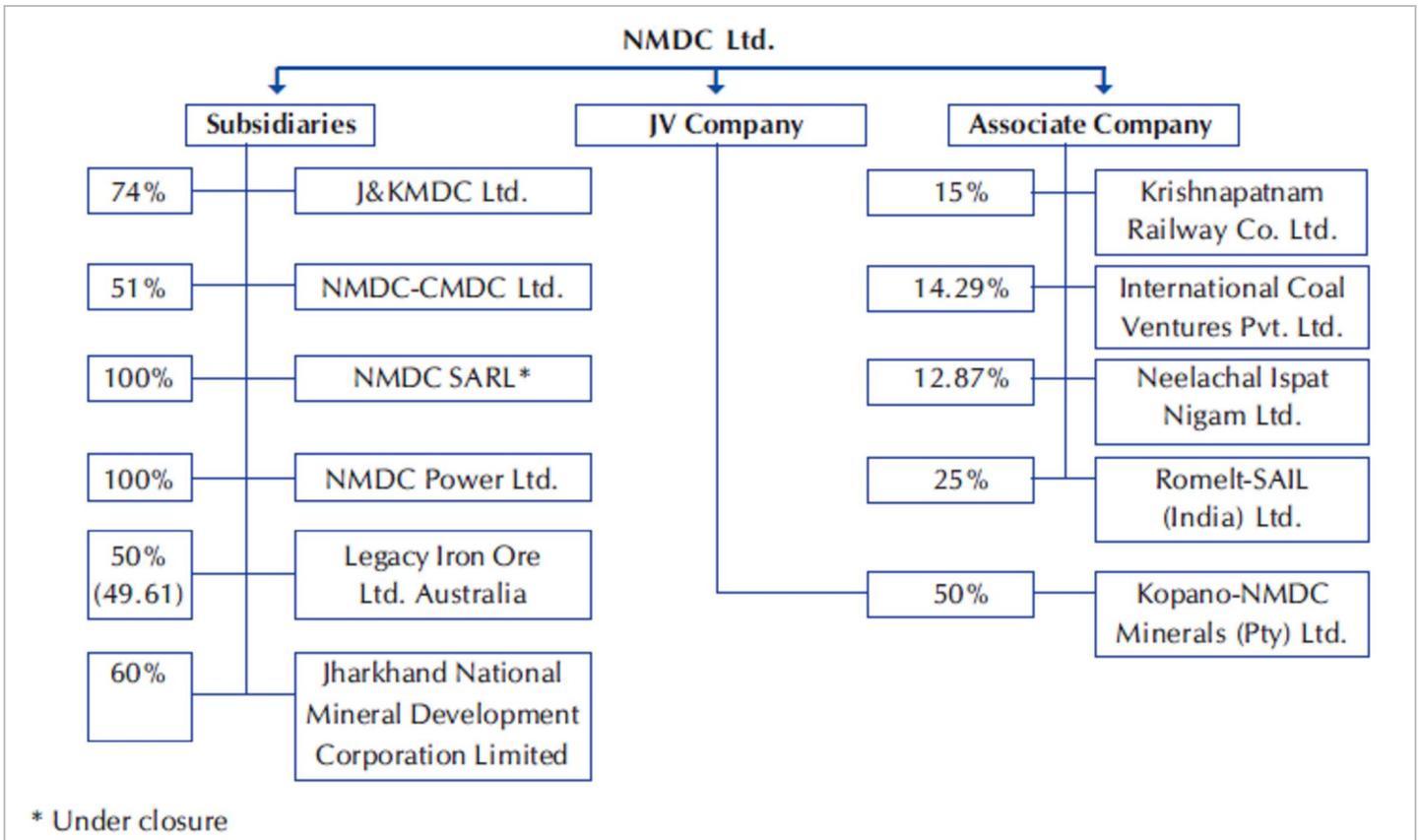
Stock Details	
BSE Code	526371
NSE Code	NMDC
Bloomberg	NMDC IN
Price (Rs) as on Oct. 10, 2013	130.95
Equity Capital (Rs Cr)	396.47
Face Value (Rs)	1.0
Eq. Shares O/s (cr)	396.47
Market Cap (Rs Cr.)	51917.7
Book Value (Rs)	69.39
Avg. Volume (52 Week)	386737
52 wk H/L	192.2/92.65

Shareholding Pattern	
(As on Jun 30, 2013)	% Holding
Promoters	80.0
Institutions	16.3
Non Institutions	3.7
Total	100.0

Company Background

Incorporated in 1958 as a Government of India fully owned public sector enterprise, NMDC is under the administrative control of the Ministry of Steel, Government of India. Since inception the company has been involved in the exploration of 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 India's single largest iron ore producer and exporter, presently producing about 30 million tons of iron ore from 3 fully mechanized mines viz., Bailadila Deposit-14/11C, Bailadila Deposit-5, 10/11A (Chhattisgarh State) and Donimalai Iron Ore Mines (Karnataka State) and also has the only mechanized diamond mine in the country. The company is currently producing 22 mt of iron ore from its Bailadila sector mines and 7 mt from Donimalai sector mines. It had developed many mines in the past like Kiriburu, Meghataburu iron ore mines in Bihar, Khetri Copper deposit in Rajasthan, Kudremukh Iron Ore Mine in Karnataka, Phosphate deposit in Mussorie. Some of these mines were handed over to companies in public sector while others became independent companies. NMDC is in process of securing some mining leases of iron ore mines: Sasangada Iron Ore Deposit and Ghatkuri Mine in Jharkhand, Ramandurg in Karnataka, Deposit – 13 and Deposit-4 in Bailadila, Chhattisgarh. For Value addition NMDC is in the process of developing a 3 mtpa steel plant at Jagdalpur and 2 pellet plants at Donimalai (1.2 mtpa) and at Bachelii (2 mtpa). The 12th plan capex for the company is Rs 30,000 cr.

Some of the customers include Rashtriya Ispat Nigam Ltd., (VSP), KIOCL Ltd., Essar Steels Ltd., JSW Steel Ltd., Ispat Industries Ltd., Chhattisgarh based Sponge Iron Units, Welspun Max Steel Ltd., Visveswaraya Iron & Steel Plant, Aparant Iron & Steel Co. Ltd., Tata Metalliks Ltd., Southern Iron & Steel Co. Ltd., MMTC Ltd., Vikram Sponge Iron Ltd.



A Joint Venture Company named Jharkhand National Mineral Development Corporation Limited (JNMDC) in Joint Venture with Jharkhand State Mineral Development Corporation Ltd. (JSMDC) was incorporated 06.08.2012 for exploration and exploitation of Iron Ore Deposits from Sasangoda Iron Ore lease, Jharkhand.

International Coal ventures (P) Limited (ICVL)

The Joint Venture company - International Coal Ventures (P) Limited (ICVL) has been incorporated between SAIL, NMDC, NTPC, Coal India and RINL. The objective of the joint venture is to primarily acquire coking and thermal coal assets abroad. Recently it has identified coal projects in Australia, New Zealand and Mongolia. These proposals will be taken forward jointly.

Strategic Alliances

Kopano-NMDC Minerals (Pty) Ltd.

A JV Company, Kopano-NMDC Minerals Pty Ltd. has been incorporated in Johannesburg, South Africa to acquire and develop mineral prospects of steel making and energy raw materials such as Iron Ore, coal and manganese ore. The JV with Kopano (Johannesburg, South Africa) has become functional and the first board meeting was held. Proposals related to coal assets are being reviewed by the JV.

ITMK3 Based Nugget Plant

The ITMK3 initiative proposes the production of high quality iron nuggets by utilizing iron ore fines and non-coking coal. NMDC has made significant progress in the ITMK3 initiative by testing the raw material i.e. domestic coal and NMDC iron ore. Feasibility study is kept in abeyance due to process stabilization issues.

NMDC-CMDC Limited

Minerals major, National Mineral Development Corporation (NMDC) had signed up a joint venture agreement (JV) with Chhattisgarh Mineral Development Corporation (CMDC) for the development of Bailadila Iron Ore, Chhattisgarh.

NMDC SARL Madagascar

Its main activity is prospecting, exploration and exploitation of high value mineral deposits in Madagascar. The company had suspended its operation from March 2002 due to disturbed political situation in the country and also due to poor exploration results.

In view of the above, NMDC took a decision to wind up NMDC SARM. The process of winding up is on hand. There have been no transactions after March 2002. On 1st January 2005, the Malagasy ariary (MGA) replaced the previous currency i.e. Malagasy franc (FMG) and one Malagasy franc was valued at 0.2 ariarys and accordingly the FMG monetary value are converted into MGA.

No transactions pertaining to the company have occurred during the financial year ended on 30th June 2012. Hence only the Balance Sheet has been reproduced without any change from the previous year's figures.

NMDC Power Ltd

J&K Mineral Development Corporation Limited

Jharkand National Mineral Development Corporation

Legacy Iron Ore, Australia

The principal activities of the company are exploration and evaluation of the company's iron ore and gold assets.

Subsidiaries	J&K Mineral Development Corporation Limited, Jammu	NMDC-CMDC Limited, Raipur	NMDC SARM Madagascar	NMDC Power Ltd	Jharkand National Mineral Development Corporation	Legacy Iron Ore Limited, Australia
Financial Year	Mar-13	Mar-13	Jun-12	Mar-13	Mar-13	Jun-12
Paid up Capital	Rs 4.74 cr	Rs 3.05 cr	MGA 209.28 cr	Rs 0.05 cr	Rs 0.01 cr	AUD 4.22 cr
Face Value	100	10	MGA 500	10	10	-
Extent of Interest	74	51	100	100	60	49.61
Reserves Rs	-124,945,334	-2,736,417	- MGA 1,597,284,704	-2,626,576	-88,263	15,672,539
Revenues	Nil	Nil	-	Nil	Nil	211,738*
Other income	47,955	10,74,964	-	Nil	Nil	-
Profit/Loss Rs	-9,572,865	-122,446	-	-2,626,576	-88,263	-11,371,5521*
Other shareholder	JKML and its nominee shareholders	CMDC Limited and its nominees	-	-	JSMDC	Le Hang Sharon Kia (7.8%) and others

*=currency in \$ and 2012 period

Shareholding Pattern

Particulars	30/06/2013	31/03/2013	31/12/2012	30/09/2012	30/06/2012
Indian (Promoter & Group)	80.0	80.0	80.0	90.0	90.0
Non Promoter (Institution)	16.3	16.2	16.3	9.1	9.1
Non Promoter (Non-Institution)	3.7	3.8	3.7	0.9	0.9
Custodians	0.0	0.0	0.0	0.0	0.0
Total	100.0	100.0	100.0	100.0	100.0

Department of Disinvestment, Government of India completed further disinvestment of 10% of the shareholding of President of India through Offer for sale (OFS) route. The floor price was fixed by Government of India at Rs.147 per share. The average sale price was Rs.150.8 per share. The realization netted by Government of India on account of the said divestment is Rs. 5,973.27 crore during the month of December 2012.

LIC of India holds 6.74% stake in the company as on June 2013.

Operational numbers across FY11-FY13

Sales	FY11	FY12	% Chg	FY13	% Chg
Domestic Iron Ore (lakh tonnes)	237.52	269.16	13.32	246.72	-8.34
Export Iron Ore (lakh tonnes)	25.63	3.85	-84.98	16.02	316.10
Total Iron Ore (lakh tonnes)	263.15	273.01	3.75	262.74	-3.76
Diamond (carats)	18421.22	8085.00	-56.11	17682.57	118.71
Sponge Iron (tonnes)	39775.00	33731.79	-15.19	37599.54	11.47
Domestic sales % share	90.26	98.59		93.90	
Export sales % share	9.74	1.41		6.10	

Total sales	100.00	100.00		100.00	
Production	FY11	FY12	% Chg	FY13	% Chg
Iron Ore (lakhs tonnes)	251.55	272.6	8.37	271.84	-0.28
Diamond (carats)	10865.93	18043.44	66.06	31533.39	74.76
Sponge Iron (tonnes)	38962	37260	-4.37	36289	-2.61
Sales Rs crore	FY11	FY12	% Chg	FY13	% Chg
Domestic Iron Ore	9753.85	10894.63	11.70	9602.72	-11.86
Export Iron Ore	1531.48	272.93	-82.18	955.99	250.27
Total Iron Ore	11285.33	11167.56	-1.04	10558.71	-5.45
Diamond	12.88	9.84	-23.60	28.51	189.74
Sponge Iron	63.12	65.93	4.45	73.5	11.48
Realization	FY11	FY12	% Chg	FY13	% Chg
Domestic Iron Ore (Rs per tonne)	4106.54	4047.64	-1.43	3892.15	-3.84
Export Iron Ore (Rs per tonne)	5975.34	7089.09	18.64	5967.48	-15.82
Total Iron Ore (Rs per tonne)	4288.55	4090.53	-4.62	4018.69	-1.76
Diamond (Rs per carat)	6991.94	12170.69	74.07	16123.22	32.48
Sponge Iron (Rs per tonne)	15869.26	19545.36	23.16	19548.11	0.01

Recent Developments and Key Takeaways

Expansion led volume growth to address higher demand

NMDC is India's largest iron ore producer with current capacity of 32 mtpa and current production of around 26-27 mtpa. It is the primary supplier of iron ore for most of the major domestic non-integrated steel producers. At present, the company has its operational mines in Chhattisgarh and Karnataka. While Chhattisgarh is the major contributor, Karnataka supplies one fifth of the total production.

Out of the total three operational mines, two are located in Bailadila range in Dantewada, Chhattisgarh. These are Bacheli and Kirandul. In Karnataka the mines are in Donimalai range. All the mines of NMDC are open cast and fully merchandise in nature. All these mines have environmental clearances with valid licenses in place for a substantially long period.

NMDC has drawn up a major expansion plan entailing expansion of iron mining and also forward integration through setting up of a steel mill and pellet plants.

In its primary business, the company is in the process of expanding its iron ore production capacity by developing its already owned assets in Chhattisgarh and Karnataka. This involves development of two new deposits and expansion of one existing deposit. It plans to expand its iron ore capacity to 48 mtpa by FY15.

Capacity of existing mines in Bailadila sector after expansion by 2014-15

Kirandul Complex		Bacheli Complex	
• Deposit – 14	: 5 MTPA	• Deposit – 5	: 10 MTPA
• Deposit – 11C	: 7 MTPA	• Deposit – 10&11A	: 7 MTPA
• Deposit – 11B	: 7 MTPA	Total	: 17 MTPA
• Total	: 19 MTPA		

Capacity of existing mines in Karnataka after expansion

Donimalai	: 7 mt
Kumaraswamy	: 7 mt

The company has been in the process of developing the Bailadila 11-B deposits located adjacent to its existing mines in South Baster district in Chhattisgarh. This would add a capacity of 7 mtpa for NMDC. The project cost stands at Rs 607 cr. The project has been progressing through seven packages, which have been ordered already. 90% of works at the mine is complete and trial runs have commenced for crusher, cranes, screens, etc. Balance work will be completed during FY14.

While the Donimalai iron ore mine is depleting, the company took up the construction of Kumaraswamy Iron Ore Mine with capacity of 7.0 MTPA and an estimated capital outlay of Rs 900 cr in a bid to achieve its 48 mtpa capacity target. Work orders have been placed for crushing plant package, downhill conveyor package, electrics and substation package and service centre facilities packages. Structural works and erection works are in progress. The project is scheduled to be completed by March 2014.

NMDC has seen minimal volume growth since FY07, as there was no significant addition by way of new projects during past 4-5 years. Timely starting of Bailadila 11-B and Kumaraswamy mines would further enhance NMDC's volume growth. Further better availability of railway rakes could improve evacuation capacity.

Large reserves and resource base

As per Behre Dolbear report dated January 29, 2010 the reserves and resources of NMDC put together stands at 1273.3 mt as on 21 Jan 2010. Out of this, proved and probable reserve stands at 1177.4 mt of high grade iron ore. This implies a mine life of 29 years at an annual mining capacity of 48 mt and ~43 years at the current production rate.

Robust demand expected for Iron ore

The demand for steel will continue to grow in the years to come and this in turn would call for increased demand for iron ore. NMDC is gearing itself to meet the expected increase in demand by enhancing production capabilities of existing mines and opening up new mines - Deposit -11B in Bailadila sector and Kumaraswamy in Donimalai sector. The production capability is expected increase to around 48 mtpa by FY15.

As the domestic steel capacity is likely to go up from current ~84 mtpa to ~110 mtpa, we believe it will help iron ore demand to stay robust. Thus, NMDC's capacity expansion is very much timely as the higher production will find immediate buyers. Rise in steel capacity alone is expected to generate an incremental iron ore demand of ~47 mt within 2-3 years. Even after adjusting for the requirement of integrated producers the demand for iron ore would still be very strong, thereby ensuring off take of iron ore produced by NMDC.

Forward Integration to diversify revenues

NMDC along with increasing its iron ore capacity is also getting into forward integration by setting up steel plants, pellet plants and beneficiation plants. Barring the steel plant, other value additions are likely to help NMDC to maintain strong margins if not improve them.

NMDC has financial powers for investment in new projects as a Navaratna company.

The company plans to expand and establish its presence as an integrated producer of iron and steel through selective value addition projects. The company has signed an MOU with the state government of Chhattisgarh to develop a steel plant with a capacity of 3 MTPA at Jagdalpur, and also has plans to develop a steel plant in Karnataka. The company has initiated action for construction of 3 MTPA Integrated Steel Plant at Nagarnar. Furthermore, the company has already completed the acquisition of Sponge Iron India Limited, a company involved in the production of Sponge Iron. Through this acquisition the company has ventured for the first time into the manufacturing area. In addition, the company plans to develop pellet plants.

NMDC has been in the process of setting up a 3 mtpa integrated steel plant in Nagarnar, near Jagdalpur, Chhattisgarh. The total cost for this project is Rs 15,525 cr. NMDC has got all the major approvals and clearances including environmental and rail transport. All nine major technological packages viz., Sinter Plant, Blast furnace, Raw Material Handling system. Coke oven, By product, Steel Melting Shop, Thin slab caster & Hot strip mill, Oxygen plant and Lime & Dolomite packages have been ordered. With this, cumulative orders of Z13,478 crore have already been placed and an expenditure of Z3032 =re has been incurred. Civil and structural works for most of these packages are in full swing. Order has also been placed for one of the major auxiliary packages i.e. Power & Blowing Station while other auxiliary packages are in different stages of ordering. The plant is likely to be commissioned in 2015/2016. The plant will also be equipped with a 250 MW captive power plant. Among the nine major technological packages, for sinter plant, NMDC has signed a contract agreement with a consortium comprising of Siemens VAI, Austria, SVAI India and NCC Ltd for turnkey execution, while for blast furnace (4506 cubic meter, largest in India) NMDC has signed a contract with Tata Project Ltd, Danieli Corus, Netherlands and India. In total the company will be in possession of ~2120 acre of land for the plant, township and other facilities. The steel plant is expected to contribute from FY16 onwards. Though, the company has decided to get into steel business without prior experience and full raw material linkage like coking coal in this case, the value destruction (with low IRR) at the company level may not be very significant as simultaneously mining capacities would also increase.

Value addition to enhance margins

Because of its excellent chemical and metallurgical properties, the calibrated ore from Bailadila deposits has substituted the iron ore pellets in sponge iron making and hence became an important raw material for three major gas-based sponge iron steel producers like Essar Steel, Ispat industries and Vikram Ispat. In addition to these three, the entire requirement of the Visakhapatnam Steel Plant is also being met from Bailadila.

Value addition to iron ore through pelletization is on the cards for NMDC, as the company is in the process of setting up two pellet plants- one in Donimalai (1.2 mtpa), Karnataka and one in Nagarnar (2 mtpa), Chhattisgarh. While the later one would take time, the first plant in Donimalai is likely to be commissioned by December 2013, for which the total project cost is pegged at Rs 572 cr. The project execution is divided into six packages and NMDC has already placed orders for site leveling, miscellaneous building, MRSS, pelletization and beneficiation packages. Major civil works have been completed. Technological equipment has been received at site. Structural & erection works are in progress.

NMDC is also setting up a beneficiation plant at the Donimalai for treatment of low grade iron ore, Banded Hematite Jasper (BHJ). The plant is capable of processing 3.6 lakh tpa of low grade ore to produce 1.18 lakh tpa of BF grade pellet feed concentrate. The estimated cost of the project is Rs 134 cr.

Geographical Diversification

NMDC has expanded its international presence through the acquisition of Legacy Iron Ore Ltd.

To achieve its vision of making NMDC a Global Company, NMDC Global has acquired 50% equity in Legacy Iron ore Limited, an ASX listed entity based in Perth, Australia. Legacy has recently announced JORC inferred category resource of 1.59 billion tonnes with 30.2% Fe at its Flagship project, Mt. Bevan, where it will earn 60% interest as per the Farm In and Joint Venture agreement with Hawthorn Resources Ltd. The company is also developing an advanced gold exploration project at Mt. Celia and holds other prospective areas for iron and manganese and also gold at East Kimberley.

On 3 May 2012, the company had entered into a binding term sheet with three vendors to acquire six prospective coal tenements located in Queensland coal basins. A refundable deposit of \$200,000 was made during the year ended 30 June 2012. The remaining consideration will be payable in two tranches (i) \$3,100,000 upon granting of the EPCAs and completion of the due diligence; and (ii) \$2,500,000 deferred performance based cash payment payable upon the delineation of an inferred JORC standard resource of no less than 100Mt of thermal coal with a Calorific Value greater than 5,000 Kcal/kg calorific value on tenements EPCA 2303 and 2304. Completion of the acquisition must occur within 6 months from execution of the binding term sheet and includes re-imbursement of the first year tenement rents.

During the period, the company continued to undertake discussions with its Joint Venture partner, Hawthorn Resources Limited, to advance the Mt Bevan iron ore deposit in the most appropriate way. On 18 June 2012, the Company announced that it had incurred expenditure totalling \$3.5m satisfying the condition to earn 60% of the Mt Bevan iron ore project under its joint venture with Hawthorn Resources Limited. On 11 September 2012, Legacy is a 60% registered owner of the Mt Bevan iron ore project.

The company will continue its mineral exploration activity its exploration projects with the object of identifying commercial resources. The main area of focus will be the ongoing development of the Mt Bevan iron ore project and the recently acquired Queensland coal project. The company also seeks to acquire other exploration and mining projects.

Diversification into coal and other minerals

Besides iron ore, NMDC also plans to go for other minerals like Coal, Diamond, gold etc for which NMDC is looking forward for leases / buy properties from foreign countries directly / under Special Purpose Vehicle / Joint Ventures.

The company is in the process of diversifying into coal mining. NMDC was allotted 2 coal blocks by Ministry of Coal in July 2007. The blocks are located in Shahpur East and West blocks in Shahdol, Madhya Pradesh. These blocks have resources of 63.6 mt and 52.7 mt respectively. While the mine plan has been approved for Shahpur West block, the detailed project feasibility report is under preparation. The company has applied for 9 coal blocks for captive use and commercial mining and is also in discussion to acquire coal blocks in Mozambique, Russia and US. NMDC is also developing Magnesite mine in Jammu and Arki Lime Stone Project in Himachal Pradesh.

For continuing the exploration activities NMDC has set a Global Exploration Centre at Raipur, Chhattisgarh. NMDC is taking up diversification activities through its intensive R&D efforts for production of High-Tech and High Value added products from Blue Dust like Carbon free sponge iron powder, Nano crystalline powder. Besides, study is also being conducted for setting up a demonstration plant to beneficiate BHJ/BHQ material for upgradation to +64% Fe iron ore concentrate.

Infrastructure augmentation to enhance evacuation capacities

NMDC is in process to setting-up the infrastructure for better evacuation capacity. For this purpose, the company has taken various projects. NMDC plans to augment resources, improve infrastructure and enhance technology through joint ventures and commercial tie-ups - the company seeks to augment its resources and reserves, improve its infrastructure and enhance its technology through joint ventures and commercial tie-ups.

NMDC is also considering Slurry beneficiation & transportation from Bailadila to Vizag. The transportation system is intended to transport pellet feed concentrate from Bailadila to Vizag via Jagdalpur along with a provision of partial offtake at Nagarnar. For part of this project, NMDC board has approved an investment proposal involving 2 MTPA ore processing plant at Bachel, Slurry pipeline from

Bacheli to Nagarnar and 2 MTPA pellet plant at Nagarnar. Gazette Notification for 'Right of Use' for a corridor of land to lay the Slurry Pipeline has been issued by Govt. of India in August 2012.

To allow round-trip movement of rakes, East Coast Railways has been assigned the work of constructing Uniflow Dispatch Line at Bacheli and an amount of Rs 30.9 cr has been deposited with East Coast Railways towards the estimated cost of work. The work is completed on 31.03.2012 and the system is in operation.

The company has reportedly signed an MoU with the Indian Railways to double the 150 km long Jagdalpur- Kottavalsa section of 472 km long Kirandul- Kottavalsa line (KK Line). The KK line is under the East Coast Railway. The cost of the project is pegged at Rs 827 cr. While, NMDC would fund the cost of laying of the rail track, the Railways will contribute wagons, locomotives, other maintenance facilities. The cost of this would be recovered by way of a rebate offered by railways in future. The doubling of the KK line is likely to add an additional 12 million tonne per annum to the traffic from Bailadila.

Higher grade, Lower cost of production and pricing power

NMDC continues to be a low cost, efficient and environmentally friendly mining company. NMDC has a perfect blend of the ingredients required to ensure sustainable profits – High grade Fe, low cost of production and emergence of pricing power. Value unlocking from High grade Fe and low cost of production and the likely emergence of pricing power due to shift from export parity to domestic market driven pricing are likely to ensure sustainable profits thus making it an attractive play.

The average Fe content in NMDC's existing mines has been 66%, which can be considered as the best quality ore in the world. This normally ensures higher premium. As a thumb rule, every 1% change in Fe content changes the premium/ discount changes by ~US\$5/tonne. This is also important, as reserves adjusted for the metal content stand higher at ~767 mt. Also, out of the total reserves of 1159.6 mt, 977.4 mt of ore i.e. 84% is under proved category and 182.2 mt i.e. 16% is under probable category. This can be considered as a very good case, as probability of actual availability of ore is very high.

When compared to its peers too, NMDC's grade stands superior. This is evident as Sesa Goa's average Fe content stands at ~58% while for BHP Billiton, Rio Tinto, Vale, Fortescue, Kumba and Atlas, the Fe content is in the range of 56% to 62%.

With all mines being open cast and highly mechanized in nature along with the high grade of ore, NMDC's cost of production has been at the lowest quartile of the cost curve due to least overburden removal. Despite being a PSU and compared to SAIL, the employee cost management indicates NMDC's operational efficiency. Proximity of the current expansion projects to the existing operations further ensures containment of costs due to usage of the existing infrastructure and equipments. A close look at the overall cost of production reveals that rise in costs over the years has been mainly due to rise in royalty, as without royalty the costs remained almost stable over the years.

In comparison to its peers also, NMDC stands significantly ahead, as is evident from its strong margins compared to peers. In FY13 NMDC's EBITDA margin stood at 69%, which is one of the highest in the industry.

Pricing of products has been an overhang for all PSU companies. Till 2010 NMDC was not an exception, selling their goods at a discount to the global prices despite having better grade. Till Q4FY12, NMDC used to fix prices on export parity basis i.e. based on the FoB prices and adjusting for export duty and freight charges. However, after the union government increased the export duty to 30% and as freight costs kept rising periodically, the company chose to shift to a pricing policy, which apparently is based on domestic demand supply situation. This gave NMDC opportunity to hike prices during Q1 and Q2 of FY13. However NMDC had to cut prices for October and November months but that was primarily due to sharp fall in international prices. For December, the prices were kept unchanged and there are little chances of any reduction in prices in near future.

Focus on domestic markets increasing

Along with change in the pricing mechanism, NMDC has also started focusing more on the domestic markets. In FY13 NMDC sold 94% of its products in the domestic markets. In the international markets NMDC normally sells on long term contract basis to Japan and Korea and on spot basis to China. In the domestic markets the company predominantly sells through long term contracts to its customers. Domestic contracts are done normally for 5 years with quantity allocation being done on an annual basis. Till October 2012, the pricing used to be fixed on quarterly basis. However, since Q3FY13 the prices were fixed on a monthly basis.

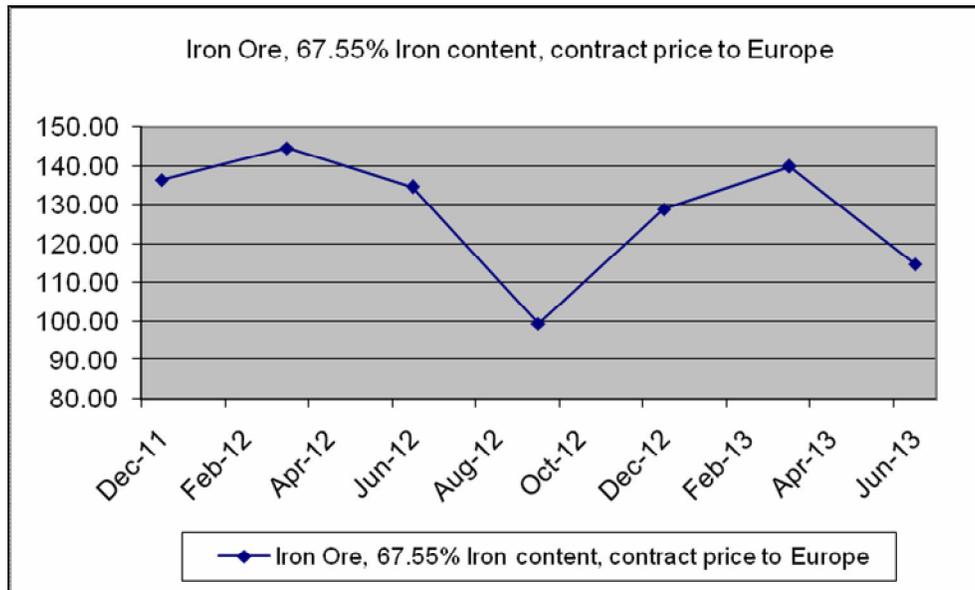
Post the hike in export duty and differential freight rates for exports, focusing on domestic markets definitely seems more remunerative.

Sales Iron Ore Rs crore	FY11	FY12	% Chg	FY13	% Chg
Domestic	9753.85	10894.63	11.70	9602.72	-11.86
Export	1531.48	272.93	-82.18	955.99	250.27
Total	11285.33	11167.56	-1.04	10558.71	-5.45
Domestic value % share	86.43	97.56		90.95	
Export value % share	13.57	2.44		9.05	

Total Value	100.00	100.00	100.00
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Global Iron ore prices

Iron ore prices globally have seen wide swings during past few years. Like coking coal, iron ore prices also used to be settled in yearly contracts. However, since Q1FY11, contract pricing shifted to quarterly intervals. Off late more and more iron ore players have been trying to make the contract pricing even closer to the spot prices. Recently, after the sharp fall in iron ore prices from the peak of ~US\$190/ tonne to ~US\$90/ tonne iron ore (62% Fe) prices quickly bounced back again to US\$135/ tonne. Iron ore prices are expected to remain well supported in the range of US\$110- 120/ tonne, which is the cost of production for Chinese marginal cost producers. This in turn would act as a support for NMDC's domestic pricing.



Healthy Return ratios, high cash per share and good dividend yield

NMDC has reported book value of Rs 69.39 in FY13 as compared to Rs 61.56 in FY12 and is expected to be Rs 76.14 in FY14. While its RoE has declined from 29.8% in FY12, it is still healthy at 23% in FY13.

Cash per share stood at Rs 53 as at March 2013 as compared to Rs 51.1 as at March 2012. It is expected to be Rs 58.1 in FY14. NMDC paid dividend of Rs 7 in FY13 which leads to a dividend yield of 5.3% based on CMP of Rs 130.95.

INDUSTRY

The total worldwide production of iron ore during 2012 was about 1.9 billion T out of which India's contribution were to the extent of about 144 million T. Total World crude steel production reached 1,547 million T for the year 2012, up by 0.7% compared to 2011. India's crude steel production during 2012 was 77.6 million T registering a growth of about 5.6%. India continues to be the 4th largest steel producer in the world.

The demand of iron ore in 2012-13 remained encouraging primarily due to higher domestic demand and also favorable demand from China. Iron ore demand both in export as well as in domestic market is likely to remain conducive during current year 2013-14.

The growth in global steel production in 2012 at 0.7% was considerably lower as compared to 7.3% in 2011 and 15.6% in 2010, with capacity utilization hovering around 80% implying overcapacity in the steel industry. As a result, iron ore prices remained subdued during the year 2012-13 and, due to overcapacity, it is expected that there will be pressure on steel prices in future, which in turn will put pressure on raw material prices including iron ore as well.

Risks and Concerns

Mining Tax

The Mines and Minerals Development Regulation (MMDR) Act 2010 has been undergoing modifications since 2009 and some proposals were already made and discussed by the concerned ministries and the GoM. The cabinet committee on 30th September, 2011 had approved the bill, which needs to be presented before the parliament for the final nod.

The proposals of this bill include - In case of major minerals (except coal and lignite) payment of compensation (mining tax) of an amount equivalent to the royalty paid during the financial year should be made; In case of coal and lignite, an "profit sharing" amount equal to 26% of the profit (after deduction of tax paid) of the immediately preceding financial year from mining related operations in respect of the lease should be paid. In case of minor minerals, such amount as may be prescribed by the State Government with the concurrence of the National Mining Regulatory Authority

Cess, at such rate not exceeding 2.5% of the duty as may be specified in the notification by the Central Government. Further the State Government may, by notification specify, that there shall be levied and collected a cess on major minerals and minor minerals extracted at a rate not exceeding 10.0% of the royalty in such manner as Levy and collection of cess by State Government.

The Bill is however yet to be presented before the Parliament and a lot of discussion and deliberation on this has already taken place.

If the Bill gets passed in the Parliament in the same form and fashion, it would be a deterrent for all the mining companies in India, as it would directly hit the earnings of these companies. NMDC being a pure iron ore mining company would also be impacted due to this. As per our estimates a 100% increase or doubling of the royalty rate would reduce the EPS by 10% in FY14. We have however, not factored in the same in our estimates as of now, as we believe there could be further changes in the bill.

While all prices quoted by NMDC are ex works and hence theoretically the royalty amount is to be borne by the customer, any abnormal increase could be resisted by customers.

Regulatory Risk

The serious concern for NMDC in expanding its activities is the hurdle the company is encountering in getting mining leases. Delay in forest and environmental and other clearances affecting time schedules for opening and commissioning of new mines and affecting the investment plans. Further, regulatory issues arising due to judicial verdicts may also affect mining.

The case pertaining to mining in Bellary in Supreme court could hurt operations in case of any adverse judgement.

Demand slowdown due to industry/economy

The industry being cyclic in nature, NMDC is exposed to sharp fluctuations in demand for its products. The company also faces risks in respect of high inventory of stocks and its disposal.

Competition Risk

NMDC could face intense competition from private sector in securing fresh mining leases, resulting in denial of leases in many cases and litigation delaying actions. Inability to secure additional reserves of iron ore that can be mined at competitive costs or cannot mine existing reserves at competitive costs, profitability and operating margins may be affected. Entry of MNCs and other Indian private companies into iron ore mining could also increase competition and hurt margins.

High Capex

The company is in the process of setting up an integrated steel plant in Nagarnar, near Jagdalpur, Chhattisgarh. The total cost for this project stands at Rs 15525 cr. If the raw material prices move adversely going forward, the project may prove to be value destructive for the company. Also, the IRR of the project is very low and would be an overhang for the company going forward. This could also impact the leverage ratios for the company.

However NMDC feels that putting up a steel plant is justifiable as it has surplus funds, the state Govt insists on value addition in the state, it provides logistical benefits in the use of rail infrastructure, NMDC would have a monopoly in Chhattisgarh and NMDC has got allocation of lucrative iron ore mines in Chhattisgarh (in JV with the state Govt entity). Further it feels that the steel industry is cyclical and whenever the cycle turns up, it will benefit out of setting up this plant.

Revision in Royalty rates

Under the National Mineral Policy, the royalty rates get revised once in every three years. Considering the recent regulatory environment, there is high possibility of revision of royalty rate on iron ore mining, which currently stands at 10%. An upward revision of the same will directly impact the EBITDA margin as well as bottomline of NMDC.

High cash leading to declining return ratios

In a bid to keeping cash for investment purposes, NMDC maintains high amount of cash in its books. Continuing to hold huge cash may result in missing out on higher return assets and may affect return ratios adversely. RoE for NMDC declined from 33.8% in FY11 to 23.1% in FY13 and would decline further if the company continues to hold huge cash.

Naxalites/Maoists attacks

The major risk NMDC is facing is the Maoists' attacks on and around its project at Bailadila on and off. Such attacks have made some impact on production and at other times has affected the movement of ore from the Bailadila sector. The company is in contact with the Government agencies for support and protection of its people and installations. The initiatives taken by the Government of Chhattisgarh and the Central Government are expected to find a solution to the risk.

Quarterly Performance - Consolidated

NMDC reported 1.1% growth in sales to RS 2869.1 cr. Operating margins were down from 81% to 66.4% due to increase in employee costs, selling expenses including freight as well as consumption of stores and spares. EBITDA de-grew 17.2% to Rs 1905.2 cr. Net Profit de-grew 17.5% to Rs 1572.2 cr.

Iron ore production grew 1% y-o-y to 69.21 LT while sales grew 6% y-o-y to 72.52 LT. Domestic sales were down 1% to 67.6 LT while exports were 4.92 LT versus nil y-o-y. Lump: fines ratio stood same y-o-y at 37:63.

NMDC incurred capital expenditure of Rs 525.55 cr upto June 2013 as compared to target of Rs 450 cr. Ministry has set a target of Rs 2720 for 2013-14.

Particulars (Rs cr)	Q1 FY14	Q1 FY13	% YoY	Q1 FY13	% QoQ
Net Sales	2869.1	2837.9	1.1	3202.1	-10.4
Total Income	3391.5	3392.5	0.0	3751.6	-9.6
Operating Expense	965.4	538.3	79.3	1454.5	-33.6
EBITDA (Inc OI)	2426.1	2854.2	-15.0	2297.2	5.6
EBITDA (Excl OI)	1905.2	2302.0	-17.2	1749.8	8.9
Depreciation	36.4	32.8	10.9	38.7	-6.0
Interest	0.0	0.0		13.2	-100.0
Exceptional Item	0.0	0.0		0.0	
PBT	2389.7	2821.4	-15.3	2245.3	6.4
Tax	817.6	915.4	-10.7	780.4	4.8
PAT	1572.2	1906.0	-17.5	1465.0	7.3
EPS	4.0	4.8	-17.5	3.7	7.3
OPM (%)	66.4%	81.0%		54.6%	
NPM (%)	54.8%	67.2%		45.7%	
Equity	396.47	396.47		396.47	
FV	1	1		1	

Annual review

Turnover for the year under review was down 5% to Rs 10,704 crore. Profit before Tax (PBT) was down 12% to Rs 9,465.1 crore. Profit after Tax (PAT) was down 12.7% to Rs 6,342 crore.

Successfully withstanding the challenging economic and market conditions, the company has been able to maintain its robust performance to a large extent during the year 2012-13. Iron ore production during the year under review was 271.84 lakh tonnes, which was more or less at the same level of previous year's production of 272.60 lakh tonnes. This was accomplished inspite of the fact that the slurry pipeline of Essar was not available at all during the year for evacuation. Iron ore sales during the year was 262.74 lakh tonnes showing a small fall of 4% over previous year sales of 273.01 lakh tonnes mainly due to incessant rainfall as well as low off-take by customers and evacuation problems in the Bailadila region during the second and third quarter of the year. Exports during the year was 16.02 lakh tones vis-a-vis 3.85 lakh tonnes in the previous financial year recording a sharp increase of 316%.

Sale of Iron Ore to domestic industries was 246.72 lakh tonnes as against the previous year supply of 269.16 lakh tonnes. Sponge Iron Production for the year under review was 36,289 tonnes as against 37,260 tonnes in the previous financial year. Diamond production for the year under review was 31,533 carats vis-a-vis 18,043 carats in the previous financial year, recording a sharp increase of around 75%.

Conclusion

NMDC proposes to augment its production of iron ore from the present level of about 30 million to 48 mtpa by 2015. It also has chalked out plans for value addition by setting up pelletization plants by utilizing the slimes and 3.0 MTPA integrated steel plant in Chhattisgarh. NMDC is also planning to venture into coal mining and other minerals. The world economy is recovering from the recession and the company anticipates strong growth in all parameters. However, weak European economy continues to be a matter of concern.

In its quest to achieve growth by opening new mining projects in India in iron ore as well as other minerals, NMDC has applied for more than 50 Prospecting Licenses (PLs) and more than 40 Mining Leases (MIs) for various minerals viz. Iron ore, Gold, Bauxite, Diamond, Coal, Dolomite, Platinum group of elements etc. in different states of the country. The company has also, as another mode of

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acquisition of mineral properties, embarked upon opening of new mines through joint ventures with State Governments, through PSUs and private sector subject to registration of JV and all statutory clearances. Notable developments are:

Ministry of Coal, Government of India, had allotted two coal blocks viz., Shahpur East & Shahpur West in Shandol District, Madhya Pradesh to NtviDC. While prior approval for Shahpur West ML area has been obtained from the Central Govt., the same is awaited for Shahpur East ML area. Mine plans and mine closure plans for both coal blocks have already been approved. Work is in progress for finalisation of DPR and as per the approved mine plan, coal production will start in 2014/2015.

Govt. of Jharkhand has granted PL for iron ore in favour of NMDC under JV with Jharkhand State Mineral Development Corporation (JSMDC) for exploration and exploitation of Sasangada North- East block.

The company believes diversification and expansion of its mining activities and products fits well with its strategy of becoming an integrated producer of iron and steel and will enable it to better balance cyclical change in mineral prices and economic change as well as to grow its business. The company has applied for and has been granted mining leases for diamonds, limestone and magnesite. The company also has acquired two coal blocks and is looking to diversify into other minerals including minerals used in fertilizer.

NMDC's financial strength is characterized by high net worth, zero debt and good credit rating.

NMDC expects to exceed the Govt's target of 28 mn tones for FY14 (compared to 27.2 mn tones in FY13). NMDC reduced the price of iron ore fines by Rs.100 a tonne in July and has left this unchanged at Rs.2,510 a tonne for the past two months. The price of iron ore lump has fallen by Rs.1,100 per tonne since January. NMDC raised iron ore prices in October 2013 by Rs.100/ton each for fines and lumps. The increase follows similar increases by other miners in Odisha in September. We believe the price increases were driven by an improved steel pricing scenario; steel mills have taken a Rs.1,500-2,000/ton price increase. The depreciation of the Rupee against the US Dollar also provided a floor to iron ore prices.

The stock is a long term buy and is available at steep discount to its inherent value. Value unlocking can help if and when

1. Global growth resumes uptrend resulting in an uptrend in iron ore prices
2. Mining tax provisions are either shelved or changed to be more friendly for miners
3. Mining clearances process becomes faster and NMDC is allotted more mines for iron ore, coal etc
4. Litigation over mining is either reduced or taken to a logical conclusion soon.
5. Forward integration plans actually result in better margins and return ratios instead of using up cash and impacting margins and return ratios.
6. PSUs as a sector are back in favour due to stand taken by the current or new Govt that PSUs will be given more autonomy and be more accountable to all shareholders (and not just the Govt) and that Govt stake in PSUs will not be sold in a panic
7. Rupee depreciation, cut in export duty and iron ore mining in other states being hit due to policy or judiciary action are some other triggers that could play out.

If however the above takes time or does not happen then the process of rerating could get delayed or may never happen.

Quick Estimates – Consolidated Financials

Particulars (Rs. Cr.)	FY11	FY12	FY13	FY14(E)*
Net Sales	11,368.9	11,260.5	10,698.7	11,019.6
PBIDT	8,644.0	8,924.6	7,372.4	7,228.9
PBIDTM (%)	76.03	79.26	68.91	65.60
Profit After Tax	6,499.2	7,265.4	6,342.4	6,385.7
PATM (%)	57.17	64.52	59.28	57.95
EPS	16.4	18.3	16.0	16.1
PE	7.99	7.15	8.19	8.13

* = Quick Estimates

(Source: Annual Report, HDFC sec Estimates)

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