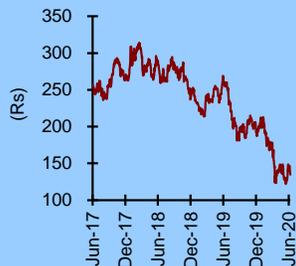


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## Sector update

## Coal India (BUY)



## INDIA

## Coal sector

## Coal mine auctions: A move towards self-reliance and efficiency

Government of India has announced start of the much-awaited auction of 41 mines with an estimated peak cumulative production capacity of 225mtpa by FY26. This is the first tranche of auctions after passing of the Mineral Laws (Amendment) Act in Mar'20, which had opened up commercial coal mining to the private sector and removed end-use restrictions. Coal demand in the country was 954mnte in FY20 and is expected to increase by 4-5% p.a., despite significant renewable capacity addition. The current auctions, along with investments by Coal India (CIL) to improve its efficiency and ramp up production, will significantly help reduce India's dependence on imports, which touched 247mnte in FY20 (up from 235mnte in FY19) with an estimated forex outgo of >US\$25bn. It may also make India a net exporter in the long term. This, we believe, will strengthen CIL and make it more competitive and efficient as we expect coal demand to increase to 1.3bnte p.a. by FY30 (of which CIL will produce 0.9-1bnte).

- ▶ **41 coal blocks up for auction:** In the first round, 41 coal blocks across five states are up for auction (including four coking coal blocks). The blocks have a cumulative reserve of 16,979mnte and peak mining capacity is estimated at 225mtpa by FY26. Rs330bn is the estimated investment over next 5-7 years. These are some of the better coal mines on offer after cancellation of coal blocks by Supreme Court in 2014, since which only 29 blocks have been auctioned. Some mines already have good infrastructure while some have a few clearances/leases in place. The mines are a mix of underground and open cast and fully/partially explored. Revenue sharing will be on ad-valorem basis instead of the earlier fixed price per tonne. Upfront amount has been reduced to only 0.25% of the value of estimated gross revenues (limited to a maximum of Rs5bn) while guarantee required is only up to 20% of upfront amount for fully explored and 25% of estimated expenditure for partially explored blocks. Gol estimates states to earn Rs200bn from these mines and create employment for ~0.3mn people.
- ▶ **Significant features and policy support to attract private/foreign investment:** The Mineral Laws (Amendment) Act passed by Parliament in Mar'20 aims to make coal mining an attractive business for private investors (both domestic and foreign). It allowed participation of private players while removing end-use restrictions for the mined coal. Further, it allows transferability of ownership and concessionary rights, freedom to manage production schedule (100% of planned production is also allowed now) and revise mine plan, right to exploit CBM and minerals, and incentivises early production. Features of the current auction also include option to relinquish partially explored blocks, no exit barrier and allowing mortgage of mines for financing. Coal ministry has facilitated sharing of responsibilities for getting statutory approvals (an agency has already been hired to liaise with states/regulatory bodies) for the auctioned mines, which will substantially help auction winners to start production as early as possible.
- ▶ **Private participation to co-exist with CIL:** In FY20, India's demand for coal was 954mnte. Of this, CIL accounted for 582mnte, SCCL 63mnte and captive production 63mnte, while the balance 247mnte coal was imported. Taking coal demand growth at 4% p.a., India's demand is expected to reach 1.3-1.4bnte by FY30 (we expect coal to remain the dominant source of power generation in the medium term despite expected 200GW installed renewable capacity). Even though this auction will result in peak production of 225mtpa by FY26, India's aim of import substitution combined with growing domestic demand augurs well for CIL to retain its status as the key coal supplier, and possibly become an exporter as well in the foreseeable future.

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## Highlights of today's briefing

### Details of auction of blocks on offer today:

- **41 blocks** are on offer, including small (0.15mtpa) to large (40mtpa) mines.
- Cumulative reserves of these mines are 16,979mnte and **estimated peak cumulative production capacity is 225mtpa** by FY26 (will therefore contribute ~15% of total estimated domestic production).
- **Rs330bn** is estimated to be invested over next 5-7 years.
- **Status of offered mines:**
  - Seven mines already have environmental clearance
  - Seven mines already have forest clearance
  - Six already have mining leases in place
  - Twelve have completed land acquisition
  - Five schedule-II mines are on offer.
- Current round of auctions have **some of the best mines on offer** post cancellation of coal blocks by the Supreme Court. Several already have good infrastructure in place.
- 26 mines will be open cast while seven are UG. 23 mines are fully explored while three are partially explored. Four coking coal mines are on offer.
- **Location:**
  - Chhattisgarh: 9 mines, 44mtpa
  - Jharkhand: 9 mines; 36mtpa
  - Madhya Pradesh: 11 mines, 17mtpa
  - Maharashtra: 3 mines, 4mtpa
  - Odisha: 9 mines, 124mtpa
- **Ad-valorem revenue share instead of fixed (Rs/te) introduced:** Auction quote will be in multiples of 0.5% up to 10% of total revenue and in multiples of 0.25% thereafter. Revenue calculation has been changed from fixed basis to a method based on the National Coal Index (derived from imported price, notified price of CIL and auction price of CIL).
- Minimum number of bidders for qualification has been reduced to two.
- **Upfront amount has been reduced to 0.25% of value of estimated gross revenues:** Limited to a maximum of Rs1bn up to 200te and maximum of Rs5bn over 200te. Entire upfront amount is adjustable against revenues paid to the state government.
- **Guarantee:** 20% of upfront amount for fully explored mines and 25% of estimated expenditure for partially explored.

- **Features and advantages:**
  - No restriction on end-use
  - Right to exploit CBM and minerals
  - Flexibility in coal production: 100% of coal can be produced
  - Option to relinquish partially explored blocks
  - No exit barrier
  - Mortgage of mines allowed for financing
  - Incentives for early production
  - Ministry to share responsibilities for getting statutory approvals (agency has already been hired to liaise with states/regulatory bodies)
  - Huge employment opportunity: Over 200,000 directly and over 80,000 in associated infrastructure
  - Contribution of Rs200bn annually to state governments is estimated

### **Coal sector reforms aimed at making India self-reliant**

- While energy demand in India is rising at 5% p.a., coal imports grew higher at 5.5% p.a.
- Coal is still a major fuel and caters to over 50% of total energy requirements. Coal sector contributes ~Rs1trn to India's GDP.
- Mining sector's contribution to GDP is <2%. It can easily contribute >5%.
- Recent structural reforms and policies are aimed at providing support to Coal India's endeavor as India aims to become a net exporter.
- "Importing crude is understandable, but importing coal is a sin": Coal Minister
- India imported 247mnte of coal in FY20. Total domestic production was 730mnte.
- Only 8% of coal is produced through U/G mining.
- Policies have been brought to simplify mine plan approval process.
- Aim is to make India self-reliant (*Atma Nirbhar Bharat*) in coal:
  - Instead of import, which is the current reality, India has the potential to become the largest coal exporter in the coming years. Coal import substitution opportunity is worth US\$10bn.
  - Policy to allow commercial mining by private players without end-use restrictions will help support CIL as it aims to achieve 1bnte production by FY24.
  - Self-reliance is not possible without support from the mining industry. Coal reforms will unlock the sector's potential and become a model for mining of other minerals.
  - Associated infrastructure is being developed for improving evacuation. Special focus is on developing railway lines and port infrastructure.

- Coal reforms will have a positive impact on other sectors too, particularly power, steel and aluminum.
- There will be a huge positive impact on employment.

**Commercial coal mining policy overhauled:**

- 100% FDI is now allowed. Participation of private players too is allowed.
- Transferability of ownership and concessionary rights is allowed.
- Complete freedom has been given to decide:
  - Sale
  - Pricing
  - Captive utilisation
  - Export
  - Manage production schedule
  - Mine plan revision
- Incentives for early production
- Right to exploit CBM and minerals
- Welfare provision for workers to be similar to that in public sector.

**Coal gasification and liquefaction to be incentivised:**

- Aim is to achieve gasification of 100mnte of coal by FY30.
- Investment of Rs200bn has currently been envisaged and four projects have already been identified.

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