State digs a hole for CIL

The state-owned monopoly is bleeding but the government keeps pressuring it to declare generous dividends

SUBHOMOY BHATTACHARJEE
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Coal India Limited (CIL) is bleeding its cash reserves. As the first ever auctions for coal mines without any restrictions on sale of coal began on November 2, it is a sobering thought. The haemorrhaging also has implications for whether CIL will end up practically defunct like another public sector behemoth, BHEL, or whether it would manage to retain its dominance, like Life Insurance Corporation. Perhaps the government feels the former is more likely and so is in a hurry to gobble up dividends and sell more tranches of its shares.

Since September 2018, CIL's cash reserves have fallen over 17 per cent to ₹28,446.83 crore. Although the Covid-19 pandemic has hurt coal movement, it is not the primary reason for CIL's ill health. As of March this year, the company's cash flow from its operations had dried up by three-fourths.

What is hurting the company is its old nemesis, first highlighted by the World Bank in the mid-nineties: Declining efficiency. BSE data shows CIL's operating profit margin (operating profit to sales ratio) for the June quarter at 16.51 per cent, the lowest in five quarters. It was 26.51 per cent in June 2019. A third of its income from operations disappears in its staff cost. No surprise, CIL has the costliest output per man shift among major mining companies globally.

CIL's efficiency is slipping despite operating in a protected market (so far) with a straightforward line of business. CIL has to just dig for coal and dump those besides the rail lines running past the mines. India, faced with a perennial shortage of coal, has enough buyers ready to arrange the transportation and pay for the entire cost.

This operation is simple in theory but proves massively difficult in practice, because the company routinely supplies coal of inferior quality than the buyers have contracted for, which raises the cost for companies because they often have to import better quality coal.

When the company was listed in 2010, this problem of efficiency was expected to be sorted out. Evidently it hasn't. Meanwhile, CIL has effected two successive revisions within the past five years in the price of coal it mines to bolster profits. As a result, a tonne of coal from Mahanadi Coalfields, the most efficient of CIL's seven subidiaries, costs ₹4,365 per when it reaches a power station in Tamil Nadu against the imported coal price of ₹3,779. Ironically, despite having the world's fifth largest coal reserves, India's coal imports have risen by a CAGR of nearly 10 per cent in the five years up to 2019-20, the third largest by value among imports.

In response, major coal customers such as public sector NTPC have created a backward linkage to develop their own coal mines. In the recent auctions, key power, aluminium and steel producers, such as Adani, Hindalco, Vedanta and JSW, have bid for mines that will substantially end their dependence on CIL.

In a decade since November 2010, when it reached ₹342.35 on listing, CIL has erased almost 67 per cent of its price to reach ₹114.2 as of October 30. In a year of stellar upward movement in the market, the CIL stock has underperformed the BSE Sensex by 43.5 per cent. No wonder brokerages have no buy recommendations on the stock. It is the reason CIL will possibly not opt for a share buyback "owing to its financially weak position," a *Business Standard* report notes.

The government, too, does not seem to have a strong plan to reverse this decline. Instead, it is milking the stock dry for its cash reserves. The government owns 66.13 per cent and this has paid handsome returns. In the past three years, the company's average dividend yield is at 10.9 per cent — compare this with a minus 60.47 per cent return on its stock price. In other words, the stock is in value more for the dividend it pays than for its performance in the market.

In March this year, CIL paid a 120 per cent dividend on each share. Even that is less than the 165 per cent it paid out in 2018. The government's attitude makes worse the already adverse international environment against coal. The result is foreign institutional investors (FIIs) are selling the stock. As of September 20, the number of FIIs holding the stock fell by 13 per cent. This is quite a climb-down for a stock that had listed on a massive premium a decade ago. It had made CIL India's fourth largest company by market cap.

The other path the government has used to benefit from CIL is share sales. In 2010, the sale of a 10 per cent stake in CIL had garnered ₹15,200 crore for the government. In this financial year, there are plans to sell another 15 per cent. Given the low share price, the government will possibly get much less — certainly nowhere near the ₹12,000 crore predicted by some media reports. Still, it is the dividend that is keeping the markets interested and erasing its cash reserves.

Yet this approach is strange. India needs more coal for at least another couple of decades, even with the target of producing 450 Mw from renewable energy. The balancing power for renewables has to be either gas or coal. Given that coal is available domestically. there is good reason to keep CIL in shape. As Rahul Tongia in his *Future of Coal* points out, there is an even greater reason. "CIL's average coal tonne [or rate of extraction] has been declining perhaps by about as much as 1 per cent per annum over multiple years." This means that India needs more production just to keep the same number of downstream plants running.

This shortfall cannot be made up by the auctions taking place now, even if those coal mines come up within the next few years. Copious quantities of coal will continue to be shipped to India from as far afield as Richards Bay in South Africa. But the shortage could get worse if CIL totters.

Performance compared with Sensex (%)

One year	-45.13
Three year	-60.23
Five year	-63.75

Comparison with peer group (mining and minerals) (%)

Price\Earnings

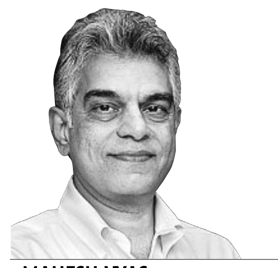
CIL	Industry average
4.98	6.26

Company metrics	June 2019	June 2020	(%)
Net Sales (₹ cr)	24,938.99	18,486.77	-25.87
PBT (₹ cr)	5,861.55	2,016.33	-65.6
Operating profit	6,612.4	3,051.68	-53.86
Operating profit to sales ratio	26.51	16.51	–
Earnings per share	7.51	3.37	
Cash & cash equivalents (₹ cr)	31,690.85	28,446.83	-11
Debtor Turnover ratio	13.23	6.2	

Source: CIL and BSE

ON THE JOB

Employment falls in October


MAHESH VYAS

By mid-October, fast-frequency indicators had signalled stagnation or a worsening of the labour markets in the month. We had reported on October 19 that the three key labour market ratios — labour force participation rate, unemployment rate and employment rate — had shown a slightly worsening trend until the third week ending in October. All the three ratios till then were a shade worse than their respective levels in September.

The fourth week that ended in October turned out to be better. Labour participation rate increased smartly and although the unemployment rate went up, it wasn't high enough to stop the most important indicator, the employment rate, from registering a gain. The week ended November 1 continued on similar lines — elevated labour participation rate and unemployment rate but still, a healthier employment rate. These improvements in the two most recent weeks moderated the impact of the initially declining trend on October's labour data. But, they did not change the overall results of the month too much.

Provisional estimates for the month of October released on November 1 confirm that the period of smart recovery of May, June and July has run its course. August, September and October do not show any significant further recovery. And, the rebound so far falls short of reclaiming levels that prevailed before the lockdown.

October was a festival month and a kharif-crop harvest month. It was also a month of much electioneering in Bihar, Madhya Pradesh and also Uttar Pradesh. None of this could help improve the demand for labour.

Labour participation rate at 40.66 per cent in October 2020 was exactly what it was in September 2020. It was much lower than the 42.9 per cent it was a year ago in October. For reference, the labour participation rate had never dropped below 42 per cent before the lockdown. So, the participation rate as of October 2020 continues to remain significantly lower than the levels seen till February 2020.

The labour participation rate had dropped by 7.08 percentage points in April. Between May and July, it recovered 5.04 percentage points. But, it has made negligible further recovery in the last three months. India, therefore, still suffers a loss of nearly two percentage points in labour participation rates compared to pre-lockdown levels.

> **Fatigue in the recovery is best reflected in the aggregate employment data. October 2020 is the first month, since the recovery began in May, that has recorded a fall in employment**

The unemployment rate had shot up from 7.6 per cent in 2019-20 to 23.5 per cent in April 2020. This was a sharp increase of 15.9 percentage points. This was reined in entirely during May, June and July. As a result, the unemployment rate in September and October has been lower than it was in any month since April 2019. The unemployment rate fell to 6.7 per cent in September 2020. However, it rose to 7 per cent in October. This is in line with the general worsening of labour market indicators in the month.

The employment rate also deteriorated in October. It fell from 38 per cent in September to 37.8 per cent in October. This is an outcome of a combination of a stagnant labour participation rate and an increase in the unemployment rate. The employment rate had shed a massive 12.2 percentage points in April. Much of this, 10.4 percentage points, was recovered during May, June and July. But, after that, the recovery has been negligible. The employment rate in October 2020 at 37.8 per cent was 1.56 percentage points lower than it was in 2019-20.

This fall of 1.56 percentage points is not entirely extraordinary as it is likely to reflect a trend of falling employment rates independent of the lockdown. The employment rate has been falling every year since 2016-17. It fell by 1.13 percentage points in 2017-18, then by 1.46 percentage points in 2018-19 and by 0.46 percentage points in 2019-20. If this trend were to continue, 2020-21 would see another fall of about one percentage point in the employment rate even if there was no lockdown. Implicitly, during the first seven months of the year, it could have seen a 55 basis points fall. The 156 basis points fall seen so far in the year is a much bigger fall than can be explained, prima facie, by the falling trend. The momentum to bridge this large gap seems to have been exhausted.

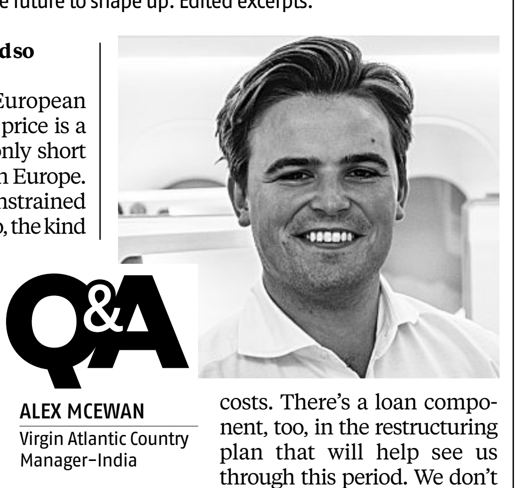
Fatigue in the recovery is best reflected in the aggregate employment data. October 2020 is the first month, since the recovery began in May, that has recorded a fall in employment. The fall is relatively small at 0.55 million. Yet, what is significant is that the process of recovery of jobs that was robust during May, June and July and which slowed down in August and September now has reversed into a fall in employment in October. Of the 121 million jobs lost in April, 110 million jobs came back during May, June and July. Then, August and September saw the addition of only 5 million jobs. Now, October recorded the first fall since the recovery began.

This fall in employment came when demand for employment was rising. The count of the unemployed who were willing to work increased by 12 million in October.

The writer is MD and CEO, CMIE P Ltd

A confident Virgin Atlantic to double down on India

India, where Virgin Atlantic started operating in 2000, is the airline's third largest market, with decent load, revenue and brand recall. The airline, which had stopped flights from India because of the pandemic, has recently resumed operations and intends to return with more vigour than ever. In an interview with **Anjuli Bhargava**, Virgin Atlantic Country Manager–India **ALEX MCEWAN** speaks about the impact of the pandemic on global aviation and on Virgin Atlantic, and how he anticipates the future to shape up. Edited excerpts.



ALEX MCEWAN
Virgin Atlantic Country Manager–India

Why has Virgin Atlantic remained so niche for so many years?

Two reasons. The short-haul European market is very competitive and price is a key factor. Many airlines with only short haul have gone out of business in Europe. Second, Heathrow is a very constrained airport and slots are expensive. So, the kind of expansions you see here are simply not possible. This has put a cap on our own growth. As a result, we have partnerships and code shares with other airlines to offer our passengers a wider network within Europe without taking the risk of operating the flights directly. When Heathrow has a third runway and more capacity, this may change.

So far, we are a purely full service, long-haul airline that focuses on the quality of service while running a profitable business. We have very new and efficient airplanes. This has worked well as a strategy for us so far. We are not the largest airline in the world, but we fly to the most significant destinations across.

How is Virgin Atlantic coping with this crisis?

We have come up with a £1.2 billion restructuring plan, which has various components. One of the biggest has been cost reduction and that has been done by cutting staff numbers in two phases, from almost 10,000 pre-pandemic to around 5,500 now. We have downsized in keeping with our current operations.

In addition, we are retiring some of our older, less efficient aircraft. Some aircraft orders are being delayed. The new planes will be more fuel efficient and help lower costs. There's a loan component, too, in the restructuring plan that will help see us through this period. We don't have new shareholders. The pandemic has forced us to think about sustainability more comprehensively.

Crisis in the past have changed the way people travel completely. We expect India to have a quicker V-shaped recovery. We also see far more demand for flexibility — making changes in tickets and plans, free of charge, something we offer already. All airlines will focus on sustainability, and four-engine aircraft will be replaced by two-engine planes, which allow for lower fuel bills. Passengers may choose to avoid connections and prefer direct flights, particularly in the next 12 months.

Since all flights stopped, how has Virgin fared in India?

Before the pandemic, India was our third largest market, accounting for 5-10 per cent of our total revenue. We've also had pretty high load factors, typically over 85-90 per cent, especially after Jet shut down. But India load factors have always been higher than average for our network. We've also seen a greater willingness and ability to pay from India in the last two years in particular, so fares have been robust. The propensity to travel amongst Indians is going up as is their willingness to pay.

Pre-pandemic, we had daily flights from Delhi and Mumbai to London, which, of course, stopped. But, like others during the pandemic, we restarted flights from Delhi and Mumbai to London under the air bubble in September, although load factors are much lower. We are now starting flights to Manchester. Global supply chains have been impacted severely so the average price charged for cargo has gone up. Prior to the pandemic, we barely carried any cargo: Our revenue was 90 per cent from passengers and just 10 per cent from cargo. But currently, almost 50 per cent of our revenue is from cargo.

What do you think of the increased competition that you and others will face from the Indian players? Many in India's aviation sector feel Vistara and SpiceJet's move — adding London to their destination list in the midst of the pandemic — is suicidal.

Both Vistara and SpiceJet have talked about operating to London for some time now. This may have been a good time for them to get a foothold and access to London. A flight to London, although expensive, may form a small part of their overall costs, since these are large and growing airlines. It may be a risk worth taking.

Competition is part of Virgin's fabric: We came into existence to compete with British Airways! So, we are always happy with more of it. But as I see it, we have a few advantages: We have a vast network of further connectivity to our fliers from India, be it to Europe, the US or even Latin America. The new entrants don't have this as of now. We are also known in the Indian market since we have been here almost 20 years; so we have a committed clientele already.