

Rating Rationale
Peoples Hydropower Company Limited

Rating

Facility	Amount (Rs. In Million)	Rating ¹	Rating Action
Long Term Bank Facilities	6160.00	CARE-NP BB [Double B]	Assigned
Short Term Bank Facilities	150.00	CARE-NP A4 [A Four]	Assigned
Total Facilities	6310.00		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned rating of ‘CARE-NP BB’ to the long-term bank facilities and ‘CARE-NP A4’ to the short-term bank facilities of Peoples Hydropower Company Limited (PHCL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of PHCL is constrained by project implementation and stabilization risk including the power evacuation risk and PHCL’s exposure to regulatory risk. The rating is also constrained by PHCL’s exposure to volatile interest rates, geological risk and hydrology risk associated with run of the river power generation. The rating, however, derives strength from board members and management having experience in hydro power sector and moderate counter party risk. The ratings also factors in achievement of financial closure for full project cost, presence of power purchase agreement (PPA) with sufficient period coverage, shortage of power in the country and government support for the power sector. The ability of PHCL to timely complete the project without any time or cost overrun and timely completion of transmission infrastructure are the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Project implementation and stabilisation risk

On the basis of cost incurred till October 17, 2019, the company has achieved financial progress of ~34% of the total project cost. Contracts for Civil works, Hydro mechanical works, Electro-mechanical works and Transmission line has been awarded. Due to recent flood in the project area, design of headrace is proposed to be changed due to which, the company is expecting to incur additional cost of around Rs. 50 Mn. However, the overall project cost is not expected to increase as the company has set aside contingency of Rs. 464 Mn in the total project cost. Company is expecting to complete the project by Mid Jan 2021 and is expected to revise RCOD with NEA. As per the progress report of October 2019 submitted by the company, excavation works of headrace tunnel is in progress with ~61% completed whereas tailrace excavation works is completed. Hydromechanical works is in progress with fabrication of hydromechanical gates and stoplog works in progress. Though, there is major progress, the project is

¹Complete definitions of the ratings assigned are available at www.careratingsnepal.com

still exposed to the residual risks associated with project implementation and satisfactory operations thereafter. Timely completion of the project without cost overrun and satisfactory operations thereafter are the key rating sensitivities.

Power evacuation risk

The power generated from the project is proposed to be evacuated through 5.2Km long 132KV Transmission Line to Nepal Electricity Authority's (NEA) under construction Kirtipur Substation in Lamjung. Power from Kirtipur Substation will be further evacuated to Udipur Hub. Construction of transmission line from powerhouse to Kirtipur substation is within the scope of PHCL and the contract for construction of transmission line has already been awarded. Timely completion of the transmission lines and substations by both PHCL and NEA will be key rating sensitivity.

Exposure to volatile interest rate

Nepalese banking sectors are fixing interest rate on lending by adding certain percentage of premium on quarterly base rate and interest rate will be changed accordingly on quarterly basis. Base rate of the Bank and Financial Institutions will be changed by change in liquidity position which leads to change in interest rate. Interest rate has been changing frequently in Nepal market since last 1-2 year. Therefore, funding from Bank and Financial Institutions are exposed to volatile interest rate.

Hydrology risk associated with run-of-the-river power generation

Run-of-the-river power is considered an unsteady source of power, as a run-of-the-river project has little or no capacity for water storage and therefore is dependent on the flow of river water for power generation. It, thus, generates much more power during summer season when river flows are high (Mid-April to Mid-December) and less during the winter season (Mid-Dec to Mid-April). PHCL is proposed to utilize discharge from Dordi Khola having catchment area of 142.45 sq. kms based on snow-fed river. Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river/ Khola.

Geological Risk

The project area possesses significant geological risks as it is located in rough terrain and is likely to face adverse climatic condition during construction period. Access road is prone to landslides during monsoon. PHCL along with other projects in Dordi corridor were affected during the recent flooding that occurred in Dordi Khola in July 2019.

Exposure to regulatory risk

Government of Nepal (GON) has recently established Electricity Regulatory Commission (ERC) for regulating generation, transmission and distribution of electricity in Nepal. ERC has issued a directive to take approval before public issuance of share capital. It poses a new challenge to hydropower companies which has to go through an additional approval process before it can issue shares to public. Hence, the

hydropower companies planning for public issuance of share capital is exposed to risk associated with delay in approval process which may delay project funding and eventually delay the project.

Key Rating Strengths

Board members and management having experience in hydro power sector

PHCL has 7 Board of Directors, chaired by Mr. Udaya Nepali Shrestha, Masters, who has more than 40 years of experience including ~30 years of experience in different capacity in Government of Nepal. He has also served as Chairman of Nepal SBI Bank Ltd. and Nepal Investment Bank Ltd. in the past. Mr. Keshav Bahadur Rayamajhi, Managing Director, has more than 10 years of experience in hydropower sector apart from other management experience. He is currently a Director of Global IME Bank Ltd. and was Chairman of Janata Bank Ltd. (now merged with Global IME Bank Ltd.). Management Team of PHCL is led by Mr. Rayamajhi and he is supported by other experienced team members.

Financial closure achieved for the full project cost

The estimated cost of the project is Rs 8,800 Mn (i.e. Rs. 163 Mn per MW) which is proposed to be funded in Debt equity ratio of 70:30 (i.e. Rs 6,160 Mn term loan and Rs 2,640 Mn equity). PHCL has entered into consortium loan agreement on October 5, 2018 for Rs 6,160 Mn term loan. Out of Rs 2,640 Mn of equity, till October 17, 2019, Rs. 1,790 Mn has been infused by shareholders. Out of the total project cost; PHCL has incurred Rs. 3,027 Mn till October 17, 2019.

Power purchase agreement with sufficient period coverage

PHCL had entered into a long term PPA with NEA as on February 25, 2015 for sale of 49.6 MW power to be generated from the project which was later amended on February 27, 2019 for additional 4.4 MW with total 54 MW power to be generated from the project. The contracted Plant Load Factor (PLF) for total 54 MW is 66.59%. Tariff rate as per PPA for 49.6 MW is Rs 4.80 per kWh for wet season (Mid-April to Mid-December) and Rs 8.40 per kWh for dry season (Mid-December to Mid-April) with 3% annual escalation on base tariff for 8 years. In case of additional 4.4 MW, the definition of wet season is (June to November) and dry season is (December to May) with same tariff rate. Required Commercial Operation Date (RCOD) of the project is July 13, 2020.

Moderate counter party risk

PHCL is exposed to counter party payment risk pertaining to Nepal Electricity Authority (NEA), which has been making consecutive losses in past till FY16 and carry huge accumulated loss in its book. However, as per the annual report published by NEA, during FY19 (provisional), NEA earned profit of Rs 7,205 Mn (Rs 2,897 Mn during FY18). Further, during FY19, NEA achieved gross cash accrual of Rs 11,915 Mn (Rs 7,107 Mn in FY18). The counter party payment risk is moderated by the fact that, NEA is fully owned by government of Nepal, net loss is declining over the period and NEA is generating positive

gross cash accruals. Further, NEA has been making timely payment to independent power producer (IPPs) in past.

Shortage of power in the country

As per the NEA’s Annual Report for FY19, the current peak electricity demand is 1320 MW. The total domestic installed capacity stands 1178 MW which includes 617 MW owned by NEA and 561 MW by private sector IPPs. Overall, during FY19, total energy demand was 7,584 GWh which was met by import of 2,813 GWh from India whereas as balance was met by domestic generation.

Government support for the power sector

GoN considers hydropower generation as priority sector and intends to maximize private sector participation in generation of hydroelectricity by offering different exemptions and facilities. GoN has 5 December 2019 announced full tax exemption for first 10 years and 50% tax exemption for next 5 years to those who generate electricity within mid-April 2024. Also, GoN has declared to provide grant amounting to Rs. 5 Mn per MW installed capacity after formal.

About the Company

Peoples Hydropower Company Limited (PHCL) is a Public Limited company, incorporated as on October 9, 2007 as a Peoples Hydropower Company Private Limited and changed to public limited on February 27, 2019. It is promoted by individual promoters from different background and institutional investors for setting up of a 54 MW run-of-river, Super Dordi Hydropower Project Kha (SDHPK) in Lamjung district of Nepal. The project is constructed under BOOT (Build, own, Operate and Transfer) mechanism. As per the Generation License, the project shall be handed, on whatever conditions the project is, to the Government of Nepal after expiry of Generation License, which is 35 years.

<p>Analyst Contact Mr. Bidhan Ojha bidhan.ojha@careratingsnepal.com Tel No.: +977-01-4445474</p>	<p>Relationship Contact Mr. Sajan Goyal sajan.goyal@careratingsnepal.com Tel No.: 9818832909/+977-01-445472/3/4</p>
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Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. Million)	Rating
Long Term Bank Facilities	Term Loan	6,160.00	CARE-NP BB
Short Term Bank Facilities	Working Capital Loan	150.00	CARE-NP A4
Total		6,310.00	