

Rating Rationale
Pan Himalaya Energy Private Limited

Rating

Facility/ Instrument	Amount (Rs. In Million)	Rating ¹	Rating Action
Long Term Bank Facilities	6,961.00	CARE-NP BB [Double B]	Assigned
Total Facilities	6,961.00		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned rating of ‘CARE-NP BB’ to the long-term bank facilities of Pan Himalaya Energy Private Limited (PHEPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of PHEPL is constrained by project implementation and associated stabilization risk, power evacuation risk and PHEPL’s exposure to regulatory risk. The rating is also constrained by PHEPL’s exposure to volatile interest rates and hydrology risk associated with run of the river power generation. The rating, however, derives strength from strong promoters & experienced management team 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 at present coupled with increasing demand of power in the country and government support for the power sector. The ability of PHEPL 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 January 14, 2020, the company has achieved financial progress of ~31% of project. As per the progress report of December 2019, work is yet to be started in headworks whereas excavation work of adit tunnel is in progress. Excavation work of powerhouse is in progress with ~13% completion whereas hydromechanical works is yet to be started. As major part of the project work is yet to be completed and with expected commercial operation date as April 2021, the company continues to remain exposed to the 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.

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

Power evacuation risk

The power generated from the project is proposed to be evacuated through 7Km long 132KV Transmission Line to the under construction Likhu-2 hydropower project which would be further connected to Likhu-A hydropower project both of which is being developed by MV Dugar Group. Power will be further evacuated from Likhu-A to proposed New Khimti Substation through 30Km long transmission line and further to Dhalkebar substation. Construction of transmission line from powerhouse to Likhu-2 project is within the scope of PHEPL and from Likhu-A to New Khimti Substation will be constructed by three projects being developed by MV Dugar Group. Timely completion of the transmission lines and substations by both PHEPL 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). PHEPL is proposed to utilize discharge from Likhu Khola having catchment area of 253 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.

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 is the regulator under the GoN which will be responsible for regulating hydropower companies in Nepal. Policies and directives issued by ERC like approval process for IPO issuance, PPA approval through ERC poses a new challenge to hydropower companies. Hence, sector is prone to regulatory risk and changes in other policies by GoN.

Key Rating Strengths***Strong promoters and experienced management team***

PHEPL is part of MV Dugar Group which has business across different sectors along with Banks, Insurance, Automobiles, Construction etc. Mr. Motilal Dugar, Chairman of PHEPL and Executive Chairman of the group, is established businessman of Nepal and has more than 47 years of experience and

is Chairman of Sunrise Bank Limited [CARE-NP A-]. Mr. Vivek Dugar, Director is engaged in business of trading of Automobiles, Construction business etc. and has more than 22 years of experience. Company's management team is led by Mr. Vipin Arora, Chief Executive Officer of the company and has more than 42 years of experience in various organizations related to hydropower and energy sector. He is supported by other experienced management team.

Financial closure achieved for the full project cost

The estimated cost of the project is Rs 9281 Mn (i.e. Rs. ~181 Mn per MW) which is proposed to be funded in Debt equity ratio of 75:25 (i.e. Rs 6961 Mn term loan and Rs 2320 Mn equity). PHEPL has entered into consortium loan agreement on December 19, 2016 for the term loan. Out of Rs 2320 Mn of equity, till January 14, 2020 Rs. 1,086 Mn has been infused by shareholders.

Power purchase agreement with sufficient period coverage

PHEPL had entered into a long term PPA with NEA as on March 3, 2015 for sale of 51.4 MW power to be generated from the project. The contracted Plant Load Factor (PLF) of 62.82%. Tariff rate as per PPA 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. Required Commercial Operation Date (RCOD) of the project is July 16, 2020. However, project is expected to be delayed due to slow progress in the project work due to focus in Likhu-A project being developed by MV Dugar group in downstream of same river and landslides during construction of access roads. Project is expected to commercial start operation by April 2021. Company is yet to apply for extension of RCOD and if RCOD is not revised by NEA till COD, the company is required to pay late COD penalty. Further, if COD is delayed by 6 months to 18 months from RCOD, then the number of escalations in tariff rate will decrease to 8 times from 7 times. Further, PHEPL is in process of amending PPA with NEA to increase the capacity of the project to 77 MW. Terms of PPA, total cost for increasing the capacity and means of finance is yet to be ascertained by the company.

Moderate counter party risk

PHEPL 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 at present coupled with increasing demand of power in the country

As per the NEA’s Annual Report for FY19, the current peak electricity demand is 1,320 MW. The total domestic installed capacity stands at 1,178 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 balance was met by domestic generation. As per NEA, electricity demand is in increasing trend and is expected to increase in future with increase in electricity consumption through the promotion of electric vehicles by building charging station and replacing cooking gas with electricity, increase in access of population using electricity (78% in FY19) etc.

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. Income tax will be levied only 20% despite the normal tax rate for entity in Nepal is 25%. Also, GoN has declared to provide grant of amount equivalent to Rs. 5 Mn per MW installed capacity after receiving evidence of formal COD of power plant.

About the Company

Pan Himalaya Energy Private Limited (PHEPL) is a Private Limited company, incorporated as on December 27, 2005. It is promoted by individual promoters majorly related to MV Dugar group which has investments in other institutes which includes Banks, Construction company and Automobiles trading for setting up of a 51.4 MW run-of-river, Likhu 1 Hydropower Project (LIHP) in Solukhumbu and Ramechhap district of Nepal. MV Dugar Group is developing three hydropower projects including LIHP in Likhu river adjacently. The project is constructed under BOOT (Build, own, Operate and Transfer) mechanism. As per the Generation License, from Government of Nepal – Ministry of Energy, obtained as on October 9, 2015 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.

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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	6,961.00	CARE-NP BB
Total		6,961.00	