

Rating Rationale

Swet Ganga Hydropower & Construction Limited

Rating

Facility/ Instrument	Amount (Rs. In Million)	Rating ¹	Rating Action
Long Term Bank Facilities	4192.88	CARE-NP BB [Double B]	Reaffirmed
Short Term Bank Facilities	120.00	CARE-NP A4 [A Four]	Reaffirmed
Total Facilities	4,312.88		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has reaffirmed rating of ‘CARE-NP BB’ to the long-term bank facilities and ‘CARE-NP A4’ to the short-term bank facilities of Swet Ganga Hydropower & Construction Limited (SGHCL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of SGHCL is constrained by project implementation and stabilization risk including the power evacuation risk and SGHCL's exposure to regulatory risk. The rating is also constrained by SGHCL's exposure to volatile interest rates, hydrology risk associated with run of the river power generation and impact of COVID-19 on the project implementation. The rating, however, derives strength from board members and management having experience in hydro power sector, strong institutional promoter group and presence of power purchase agreement (PPA) with sufficient period coverage. The ratings also factor in moderate counter party risk, achievement of financial closure for full project cost, power demand supply gap in Nepal coupled with increasing demand of power in the country and government support for the power sector. The ability of SGHCL 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

The RCOD of the project is December 01, 2021. Till February 12, 2020, the company has achieved financial progress of 38.72% of the project. Contracts for Civil works, Hydro mechanical and Electro-mechanical has already been awarded whereas contract for transmission line is under negotiation. The project has 114.71 m net head and includes 4797 m long headrace tunnel, and 223 m long penstock pipe. Two turbines (each having 14.05MW capacity), two generators and two transformers are proposed to be used in the project. As per the progress report of April 2020 submitted by the company, ~50% of the civil works, ~35% of the hydro mechanical work, ~15% of the electromechanical work have been completed. Tunnel evacuation work is in progress with ~83.61% of the tunnel excavation work has been completed.

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

Though, there is progress in project, the company continues to remain exposed to the risks associated with project implementation of hydropower project 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 27Km long 132KV Transmission Line to the proposed New Khimti Substation. Power from New Khimti Sub Station will be further evacuated to Dhalkebar substation which is operational and is connected to national grid. Construction of transmission line from powerhouse to New Khimti substation is within the scope of SGHCL. Timely completion of the transmission lines and substations by both SGHCL and NEA will be key rating sensitivity.

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 will be 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.

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 change by change in liquidity position which lead 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 is subject 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). SGHCL is proposed to utilize discharge from Likhu Khola having catchment area of 755 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.

Impact of Corona Virus on the Project Implementation

The outbreak of Coronavirus disease 2019 (COVID-19) which was recognized as Pandemic by World Health Organization has affected Nepal as well. Government of Nepal (GoN) imposed travel restrictions and countrywide lockdown since March 24, 2020 closing most of the organizations which resulted in

slowing down of the economic activities. GoN allowed construction works to continue around Nepal during lockdown period also with proper safety measures. Due to the pandemic there are several impacts in under-construction projects like unavailability of contract labor and construction material due to partial operations of manufacturing units across Nepal. SGHCL had initially issues in the manpower mobilization. With respect to supply of construction material and the labor mobilization, SGHCL coordinated with local government to issue travel approvals to ease the supply. However, company is in process of ascertaining any impact in time and cost caused by COVID-19.

Key Rating Strengths

Board members and management having experience in hydro power sector

SGHCL has 4 Board of Directors, chaired by Mr. Manik Lal Shrestha, who has ~30 years of experience including 20 years of working experience in International Monetary Fund (IMF). Dr. Subarna Das Shrestha, Executive Director, has ~27 years of experience with 25 years in Hydropower sector. He has served as CEO in a promoter company in the past; Sanima Mai Hydropower Ltd [CARE-NP BBB+/A3+] and is a Past President of Independent Power Producers Association of Nepal (IPPAN). Company management team is led by Bhoj Raj Poudel, General Manager of the company and has more than ~29 years of experience. He has been supported by other experience management team members.

Strong institutional promoter group

SGHCL is part of Sanima Hydro Group which is promoted by group of Non-Resident Nepalese who are related to Sanima Group, having business interest in Hydropower, Banking and Insurance sector. Sanima Hydro has been developing a number of hydropower projects by setting up Special Purpose Vehicle (SPV) companies in Nepal. Dolma Impact Fund (DIF) which has invested Rs. 320.74 Mn equity (holds 31.48% as on June 06, 2020) in SGHCL is an institutional investor and is the first commercial impact fund setup in Nepal for providing growth capital to Small and Medium Enterprises (SMEs) with strong entrepreneurial and management capacities.

Power purchase agreement with sufficient period coverage

SGHCL had entered into a long term PPA with NEA as on December 29, 2016 for sale of 28.10 MW power to be generated from the project. The contracted Plant Load Factor (PLF) for total 28.10 MW is 69.40% with total contracted energy of 170.84 MU. The period of PPA is 30 years from the date of COD or till validity of generation license. Tariff rate as per 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 December 1, 2021.

Moderate counter party risk

SGHCL 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. Further, during FY19, NEA achieved gross cash accrual of Rs 11,915 Mn. 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 generating positive gross cash accruals. Further, NEA has been making timely payment to independent power producers (IPPs) in the past.

Financial closure achieved for the full project cost

The total cost of the project was envisaged at Rs 5590 Mn to be funded in debt equity ratio of 75:25 (i.e. Rs 4193 Mn term loan and Rs 1397 Mn equity) which has further increased by Rs. 649 Mn to Rs. 6239 Mn. The increased cost is proposed to be funded through equity, however company has requested the consortium bank to fund the same. Till June 06, 2020 Rs. 1,019.03 Mn has been infused by shareholders. As on May 13, 2020 SGHCL has incurred Rs. 2,416.19 Mn project cost.

Power demand & supply gap 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

Government of Nepal (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 announced full tax exemption for first 10 years and 50% tax exemption for next 5 years for such person/entity who starts commercial operation, transmission and distribution of electricity up to mid-April 2024. Further, no income source will be asked for investment made within mid-April 2020 in hydro-electricity project. GoN has declared to provide grant of amount equivalent to Rs. 5 Mn per MW installed capacity after receiving evidence of formal COD of complete power plant.

About the Company

Swet Ganga Hydropower & Construction Limited (SGHCL) is a Public Limited company, incorporated as on February 18, 2005 as a Swet Ganga Hydropower & Construction Private Limited and changed to Public limited on September 28, 2016. It is promoted by individual promoters from different background, institutional investors majorly related to Sanima Hydro group and other institutes which includes Banks

and Investment companies for setting up of a 28.1 MW run-of-river, Lower Likhu Hydropower Project (LLHP) in Ramechhap district of Nepal. The major shareholder of the company as on July 24, 2020 are Sanima Mai Hydropower Ltd. [CARE-NP BBB+/A3+] (44.16%) and Dolma Impact Fund-I (31.48%). 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 April 10, 2016, 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

Facility/ Instrument	Type of the Facility	Amount (Rs. In Million)	Rating
Long Term Bank Facilities	Term Loan	4192.88	CARE-NP BB [Double B]
Total Short Term Facilities	Working Capital Loan	120.00	CARE-NP A4 [A Four]
Total Facilities		4,312.88	