

**Rating Rationale**

**Barun Hydropower Company Limited**

**Rating**

| Particulars   | Amount (Rs. in Million) | Rating <sup>1</sup>                          | Rating Action |
|---------------|-------------------------|--|---------------|
| Issuer Rating | NA                      | CARE-NP BB+ (Is)<br>[Double B Plus (Issuer)] | Assigned      |

\* The issuer rating is subject to the company maintaining overall gearing not exceeding 1.0x at the end of FY21.

CARE Ratings Nepal Limited (CRNL) has assigned Issuer rating of ‘CARE-NP BB+ (Is)’ to Barun Hydropower Company Limited. Issuers with this rating are considered to offer moderate risk of default regarding timely servicing of financial obligations in Nepal.

**Detailed Rationale & Key Rating Drivers**

The issuer rating assigned to Barun Hydropower Company Limited (BHCL) is constrained by modest operating performance of hydro power project being operated at low plant load factor (PLF), hydrology risk associated with run-of-the-river power generation, moderate power evacuation risk and exposure to regulatory risk and volatile interest rates.

The rating, however, derives strength from the experienced promoters and management team, presence of Power Purchase Agreement (PPA) with sufficient period coverage, and moderate financial risk profile with comfortable gearing levels. The rating also factors in current demand & supply gap however possible oversupply in future, moderate counter party risk and government support for the power sector.

*Going forward, the ability the company to successfully reduce the gap between operational PLF and contracted PLF and availability of sufficient hydrology with timely receipt of payments from Nepal Electricity Authority (NEA) are the key rating sensitivities.*

**Detailed Description of the Key Rating Drivers**

**Key Rating Weaknesses**

***Modest operating performance of power project***

BHCL has commissioned run-of-the-river small hydropower project of 4.5 MW in Shankhuwasava district of Nepal. The commercial operations started in August 2011. In the last two financial years (FY19 & FY20; FY refer to 12 months’ period ending in mid-July), the project was operated at PLF of ~52% and ~46% respectively. Also, plant load factor (PLF) was low in 10 months’ performance of FY21 at ~35%. The operating performance in terms of power generation is low due to insufficient hydrology and disturbances in transmission due to transmission line issues. For the year ended in FY20, PLF stood at 52.49% against

<sup>1</sup>Complete definitions of the ratings assigned are available at [www.careratingsnepal.com](http://www.careratingsnepal.com)

contracted PLF of 66.74%, thereby generating ~79% of the contracted energy. It is crucial from the analytical prospective for the company to reduce the gap between operational PLF and contracted PLF.

***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 seasonal river flows are high (mid-April to mid-December) and less during the winter season (mid-December to mid-April). Hewa Khola Small Hydropower Project (HKHP) utilizes available head and flow from Hewa Khola having catchment area of 81.03 sq.km based on perennial river. Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river.

***Exposure to regulatory risk***

Government of Nepal (GON) has recently established Nepal Electricity Regulatory Commission (NERC) for regulating generation, transmission and distribution of electricity in Nepal. NERC 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.

***Exposure to volatile interest rate***

Nepalese banking sectors are fixing floating 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 (BFIs) remains volatile to change in liquidity position which lead to change in interest rate. Interest rate has been changing frequently in Nepal market since last 2-3 years. Therefore, funding from BFIs is subject to volatile interest rate.

**Key Rating Strengths**

***Experienced Promoters and Management team***

BHCL is managed under the overall guidance of the company's Board of Directors (BoD) having wide experience in the power sector. BHCL has six board of directors, chaired by Dr. Bhushan Guragain who has more than 10 years of experience in hydropower and health sector.

The management team is led by Mr. Shailendra Guragain, Chief Executive Officer of the company, who has more than 20 years of experience in hydropower sector and banking sector. He is also a director in Ngadi Group Power Limited (CARE-NP BBB- (Is) assigned on June 2021).

***Power purchase agreement with sufficient period coverage***

BHCL had entered into a long term PPA with Nepal Electricity Authority (NEA) for 2.4 MW as on September 19, 2007 and amended thereafter on August 26, 2009 for additional 2.1 MW. Thus, the PPA covers 4.5 MW energy generated by the power project. The period of the PPA is 30 years from the date of

COD or till validity of Generation License, whichever is earlier. PPA period may be extended with mutual consensus during the last six months of validity. The tariff for wet season (mid-April to mid-December) is Rs 3.90 and Rs. 4.80 per kWh and for dry season (mid-December to mid-April) is Rs 5.52 and Rs. 8.40 per kWh for 2.4 MW and 2.1 MW respectively and 3% escalation on base tariff for 9 years is available only for 2.1 MW.

***Moderate counter party risk***

BHCL is exposed to counter party payment risk pertaining to NEA, which has been making consecutive losses in past till FY16. However, as per the annual report published by NEA, during FY20 (provisional), NEA earned profit of Rs 11,056 Mn (Rs. 9,812 Mn during FY19) resulting in accumulated profit in its book. Further, during FY20, NEA achieved gross cash accrual of Rs 16,056 Mn (Rs 14,664 Mn in FY19). The counter party payment risk is moderated by the fact that, NEA is fully owned by government of Nepal, and generating positive gross cash accruals. Further, NEA has been making timely payment to independent power producers (IPPs) in past.

***Current demand & supply gap however possible oversupply in future***

As per the NEA's Annual Report for FY20, the current peak electricity demand is 1,408MW. The total domestic installed capacity stands at 1,328 MW which includes 632 MW owned by NEA and 696 MW by private sector IPPs. Overall, during FY20, total energy demand was 7,894 GWh which was met by import of 1,721 GWh from India whereas balance was met by domestic generation.

However, considering under construction projects which are expected to generate electricity in next 2-3 years and electricity demand which has not increased substantially in past few years could create a situation of oversupply in near future in wet season. This could put pressure on NEA's payment capabilities which is sole counter party with majority of PPA signed on take or pay basis.

***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. Also, Unified Directive of 2020/21, has directed "Class-A" to allocate minimum 10% of credit to energy sector and "Class-B" and "Class-C" banks to allocate minimum 20% and 15% of total credit respectively to agriculture, energy, SMEs and tourism sector within mid-July 2024.

***About the Company***

Barun Hydropower Company Limited (BHCL) was incorporated as on January 20, 2004 as a private limited company and later converted to public limited company in July 15, 2009. The company was listed with Nepal Stock Exchange (NSE) in October 2015. It is promoted by individual promoters having long experience in the hydropower and other sectors for setting up of a 4.5 MW run-of-river Hewa Khola Small

Hydropower Project. The project is being constructed under “BOOT” (Build, Own, Operate and transfer) model and is located in Jaljala VDC of Sankhuwasava district.

**Brief Financial Performance of BHCL during last 3 years ending FY20 is given below:**

(Rs. In Million)

| For the year ended Mid July             | FY18      | FY19      | FY20      |
|---|-----------|-----------|-----------|
|   | (Audited) |           |           |
| Period of operation                     | 12 months | 12 months | 12 months |
| Income from power sales                 | 86        | 78        | 85        |
| PBILDT Margin (%)                       | 84.08     | 62.90     | 65.28     |
| Overall Gearing (times)                 | 1.17      | 1.06      | 0.90      |
| Interest coverage (times)               | 1.91      | 1.48      | 1.84      |
| Current Ratio (times)                   | 2.91      | 1.81      | 2.80      |
| Total Debt/ Gross Cash Accruals (times) | 9.10      | 16.97     | 9.72      |

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