

Bhagawati Hydropower Development Company Limited

Ratings

Facilities	Amount (Rs. Million)	Rating ¹	Rating Action
Issuer Rating	NA	CARE-NP BBB-(Is) (Triple B Minus [Issuer Rating])	Assigned

**The issuer rating is subject to overall gearing ratio of the company not exceeding 0.30x at the end of FY22.*

Details of instruments/facilities in Annexure-1

Care Ratings Nepal Limited (CRNL) has assigned the issuer rating of 'CARE-NP BBB- (Is) to Bhagawati Hydropower Development Company Limited (BHCL). Issuers with this rating is considered to have moderate degree of safety regarding timely servicing of financial obligations, in Nepal.

Detailed Rationale & Key Rating Drivers

The ratings assigned to the BHCL derives strength from experienced board members and management team, satisfactory operating performance of power project, moderate financial risk profile and presence of power purchase agreement (PPA) with sufficient period coverage. The rating also factors moderate counter party risk, current demand & supply gap; however, possible oversupply in future and government support for the power sector.

However, these rating strengths are partially offset by declining operating revenue and profitability margins on y-o-y basis in last 3 financial years (FY19-FY21), hydrology risk associated with run-of-the-river power generation, exposure to volatile interest rate risk and regulatory risk.

Going forward, the ability of 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. Any significant increase in debt levels would also be key monitorable.

Detailed description of the key rating drivers

Key Rating Strength

Experienced board members and management team in hydropower sector

BHCL has 7 Board of Directors, chaired by Mr. Hari Prasad Pandey, who holds 9.09% of the total share capital, has more than 4 decades of experience in different sectors which includes power, manufacturing, trading etc. He is also associated with hydro power companies in different capacities. Mr. Roshan KC, Director, who holds 10.62% of the total share capital, has more than 15 years of experience in various sector including hydropower projects. The other Directors of the company have also long experience in different sectors. Further, the day-to-day operations are supported by experience management team.

Power purchase agreement with sufficient period coverage

BHCL had entered into PPA with Nepal Electricity Authority (NEA) for 4.41 MW as on July 14, 2009 for sale of entire power generated by the plant. The PPA is signed for a period of 30 years for from the date of COD. PPA period may be extended with mutual consensus through discussion from last six month of validity. The tariff rate as per PPA is Rs. 5.08 per kWh for wet season (Mid-April to Mid-December) and Rs 8.89 per kWh for dry season (Mid-December to Mid-April) including escalations.

Moderate operating performance

BHCL has commissioned run-of-the-river 4.41 MW Bijayapur Small Hydroelectric Project (BSHP) at Kaski District which has been in commercial operation since August 21, 2012. In the last 2 financial years (FY19-FY20) on y-o-y basis, the PLF has declined

¹Complete definition of the ratings assigned are available at www.careratingsnepal.com and other CARE publications

from 63.20 % in FY19 to 51.36% FY21. The decline in PLF was on account of the plant operated at half capacity for around six months (mid-June 2020 to mid-December 2020) due to breakdown in one of its generators. After the subdued operating performance in last 2 financial years, the operating performance has shown recovery in the current financial year. As against the annual contracted PLF for the company is 74.52% of the installed capacity of the plant, BSHP reported PLF of 77.08% against the generation capacity and 95.03% against contracted energy during 9MFY22 ending in Mid-April 2022. The improvement was boosted by improved hydrology during the period coupled with smooth operations of the project.

The company's ability to consistently reduce the gap between contracted PLF and generated PLF coupled with swift turnaround of any similar stoppages in future so as to maintain generated PLF at least above 80% of contracted PLF would be critical from analytical perspective.

Moderate Financial risk profile

The total operating income in last 3 financial years (FY19-FY21) declined on y-o-y basis on account of low generation of power attributed to above mentioned reasons. The decline in revenue also resulted to decline in profitability. The company mainly expenses are fixed in nature and decline in capacity utilization resulted in increase in cost due to high proportion of fixed cost which deprived it of its scale benefits which led to decline in PBIDLT and PAT. Though the revenue and probability decline in past few years, the company has improved the operating performance in current financial years during 9MFY22, the company report total operating income of 141 Mn.

In 9MFY22, the company reported revenue of Rs 44 million per MW which was slightly better vis-à-vis revenue/MW of industry average. The main reason for higher-than-average industry revenue generation per MW is because of relatively better hydrology (water diverted to the project from the now defunct local irrigation canals) during the dry season leading to higher energy generation.

Capital structure remains comfortable with overall gearing ratio of 0.39x at the end of FY21 (FY20: 0.60x). The lower gearing ratio was on account of reduced debt levels over time and improvement in company's tangible networth due to accretion of profit. Apart from overall gearing, interest coverage ratio and total debt to GCA ratio stood comfortable at 4.43x and 2.80x during FY21 (FY20: 3.53x & 3.58x). Going forward, the debt coverage indicators of the company are likely to remain at comfortable levels owing to lower interest outgo amid decreasing debt levels. The same is due to company plans to increase its networth base by issuing new share through initial public offerings which is proposed to be utilized for the prepayment of the term loan.

Favorable Government policies towards 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. As per various directives from NRB whereby all the banks (type A, B C, D) have to allocate minimum share of their total advances to energy sector which argues well for the sector.

Key Rating Weaknesses

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 wet season when river flows are high (Mid-April to Mid-December) and less during the dry season (Mid-December to Mid-April). The project utilizes discharge from Bijayapur Khola having catchment area of 63.5sq. kms based on Perennial River. Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river/ Khola.

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.

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.

About the Company

Bhagawati Hydropower Company Limited (BHCL) is a public limited company, incorporated in December 18, 2000 as a private limited company and later converted to public limited company in April 19, 2018. BHCL is involved in the operation of 4.41 MW run-of-the-river Bijayapur 1 Small Hydroelectric Project (BSHP) at Kaski District which has been in commercial operation since August 21, 2012. The project is constructed under BOOT (Build, own, Operate and Transfer) mechanism.

Financial Performance

(Rs. in Mn)

Particulars	FY19	FY20	FY21
	Audited	Audited	Audited
Income from Operations	164	141	123
PBILD Margin (%)	75.22	75.13	66.82
Overall Gearing (times)	0.63	0.60	0.39
Interest coverage (times)	3.52	3.53	4.43
Current Ratio (times)	NA	1.11	1.06
Total Debt/Gross Cash Accruals (times)	3.64	3.58	2.80

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