

Peoples Power Limited

Ratings

Facilities	Amount (Rs. Million)	Rating ¹	Rating Action
Issuer Rating	NA	CARE-NP BB (Is) [Double B (Issuer)]	Reaffirmed

* The issuer rating is subject to overall gearing ratio of the company not exceeding 2.00x at the end of FY23.

Details of instruments/facilities in Annexure-1

CARE Ratings Nepal Limited (CRNL) has reaffirmed the rating of 'CARE-NP BB (Is)' assigned to Peoples Power Limited (PPL). Issuers with this rating are considered to have moderate risk of default regarding timely servicing of financial obligations in Nepal.

Detailed Rationale & Key Rating Drivers

The issuer rating assigned to PPL continues to be constrained by the residual project implementation risk and operation stabilization risk associated with its under-construction hydropower project. The rating also factors in hydrology risk associated with run-of-the river power generation, exposure to regulatory risk and volatile interest rates.

The rating, however, derives strength from PPL's experienced promoters and management team, presence of power purchase agreement (PPA) with sufficient period coverage, and lower power evacuation risk, moderate counter party risk and government support for the power sector.

Going forward, the ability of the company to successfully execute the project without further cost and time overrun and early stabilization thereafter will be the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Weaknesses

Residual Project implementation and stabilization risk

PPL is setting up a 4.96 MW Upper Puwa-II hydropower project in Ilam district of Nepal. The revised estimated cost of the project is Rs. 962.60 Mn (Rs 194 Mn per MW) which is proposed to be financed through debt of Rs. 640.00 Mn and remaining through equity. The total debt amount of Rs. 640 Mn has already been tied up. As on April 13, 2022, the company has achieved physical progress of 95%. Although nearing completion, the project is still exposed to the residual risks associated with the implementation of the project and satisfactory operations thereafter to achieve the envisaged revenue. Furthermore, the power generated from the project is proposed to be evacuated to the NEA's operational Upper Puwa I substation. Construction of transmission line from powerhouse to Upper Puwa I substation is within the scope of PPL. As on May 15, 2022, around 60% of transmission poles have been erected. Timely completion of the transmission line by PPL and smooth evacuation of the power remains crucial from revenue generation perspective.

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 (June to November) and less during the winter season (December to May). PPL is proposed to utilize discharge from Puwa Khola having catchment area of 63.90 sq. kms based on semi snow-fed river. Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river/ Khola.

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

Exposure to volatile interest rate risk

Nepalese banking sector has a floating interest rate regime, where a certain premium is added to the quarterly base rate and interest rate is changed accordingly on quarterly basis. The base rates of the banks and financial institutions (BFIs) in Nepal remain quite volatile as they are impacted by available liquidity in the system which leads to change in interest rates. The volatility in interest rate is more evident currently on account of the ongoing liquidity stress in the economy, with substantial upward pressure on interest rates in the last 2-3 quarters. Any further significant rate hikes could put increased interest burden on the company, squeezing its profitability and impacting its liquidity position. Therefore, funding taken by the company 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 hydropower companies in Nepal. ERC will regulate generation, transmission and distribution of electricity in Nepal among others. Policies and directives issued by ERC such as approval process for IPO issuance and 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 Strength**Experienced promoters and management team in hydropower sector**

PPL has four board of directors, chaired by Mr. Bharat Khatri who has more than 20 years of experience in practicing lawyer and also been associated with hydro power company in the capacity of public director. Mr. Santosh Raj Nepal, Director, has been associated with hydro power companies for more than 10 years and has extensive experience of handling the administrative operations of under construction and operational hydro power plants. Mr. Tanka Raj Aryal is an advocate by qualification and associated with the company as Director. He is looking after the legal affairs of the company. He is also associated at various capacities in several other hydropower companies.

Power purchase agreement with sufficient period coverage

PPL had entered into a long term PPA with NEA in 2017 for sale of power generated from 4.96 MW hydro power and the basis of arrangement is take or Pay basis. The contracted Plant Load Factor (PLF) is 64.40% with total contracted energy of 27.98 MU (dry season: 8.41 MU and wet season: 19.57 MU). PPA is for the period of 30 years from the COD or till validity of generation license (obtained on September 17, 2018 for 35 years) whichever is earlier. PPA period may be extended with mutual consensus during the last six months of validity. Tariff rate as per PPA is Rs 4.80 per kWh for wet season (June to November) and Rs 8.40 per kWh for dry season (December to May) with 3% annual escalation on base tariff for 8 years.

Required Commercial Operation Date (RCOD) of the project was March 24, 2022 and the company has applied for the extension of RCOD with NEA. If the project is not completed within the mentioned RCOD, then the delay penalty will be levied to the company which is 5% of total contracted energy for the delay periods at the applicable tariff rate as on COD. As per PPA, NEA will recover the penalty amount from monthly billing.

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.

About the company

Peoples Power Limited (PPL) was incorporated on January 26, 2017. It is promoted by individual promoters for setting up of a 4.96MW run-of-river Upper Puwa-II hydropower project. The project is being constructed under "BOOT" (Build, Own, Operate and transfer) model and is located in Sakhejung and Maipokhari VDC of Ilam district of Nepal. The expected COD of the project is June 30, 2022.

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