

## KBNR Isuwa Power Limited

### Ratings

Facilities	Amount (Rs. Million)	Rating <sup>1</sup>	Rating Action
Long Term Bank Facilities	9,069.00 (Decreased from 9,070.66)	<b>CARE-NP BB</b> [ Double B]	<b>Reaffirmed</b>
Short Term Bank Facilities- Fund based and non-fund based limits	100.00 (Decreased from 429.34)	<b>CARE-NP A4</b> [A Four]	<b>Reaffirmed</b>
<b>Total</b>	<b>9,169.00</b>		

*Annexure-1 Details of Facilities/Instruments to be rated*

CARE Ratings Nepal Limited (CRNL) has reaffirmed ratings of 'CARE-NP BB' assigned to the long term bank facilities and 'CARE-NP A4' assigned to the short term bank facilities of KBNR Isuwa Power Limited (KBNR).

### Detailed Rationale & Key Rating Drivers

The reaffirmation of ratings assigned to KBNR factor in the early stage of construction of the project leading to a high project implementation and stabilization risk associated with the project. The ratings are also constrained by hydrology risk associated with run-of-the-river power generation, however mitigated to an extent due to peaking reservoir, power evacuation risk, exposure to regulatory risk and volatile interest rates.

The ratings, however, continues to derive strength from the experienced promoters and management team in hydropower sector, presence of power purchase agreement (PPA) with sufficient period coverage, moderate counter party risk and full financial closure achieved for the project. The ratings also factor in current government support for the power sector and relatively low cost power project.

*Going forward, the ability of company to timely execute the project within Required Commercial Operation Date (RCOD) avoiding any time or cost overrun and early stabilization thereafter will be the key rating sensitivities.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weaknesses

#### Project implementation and stabilization risk having relatively lower project cost

KBNR is setting up a 97.2 MW peaking run-of-river Isuwa Khola Hydropower Project in Sankhuwasabha district of Nepal. The estimated total cost of the project is Rs. 11,338.33 Mn (cost per MW is Rs. 116.64 Million) to be funded in debt equity ratio of 80:20 (debt of Rs. 9,070.66 Mn and equity of Rs. 2,267.67 Mn). Entire debt component has been tied up. The contract for civil works, hydro-mechanical works, electromechanical works and transmission line works have been awarded. The project is at the preliminary stage of construction. Till May 14, 2022, ~27.37% of the total project cost (i.e. Rs. 3,103.18 Mn) had been incurred. As per the progress report of May 30, 2022, physical progress was around 25%. This exposes the company towards project execution risk in terms and of completion of the project with-in the envisaged time and cost.

Required Commercial Operation Date (RCOD) of the project is July 17, 2023. The company has applied for extension of RCOD for one year. If COD doesn't fall within RCOD, the company is bound to pay late COD penalty to Nepal Electricity Authority (NEA). Further, if COD is delayed by 6 months to 18 months from RCOD, then the number of escalations in tariff rate will decrease to 7 times from 8 times. It is crucial for the company to complete the project within the timelines to have the accelerated clauses of tariff. Any delay in the same would lead to impact on project returns and debt servicing capabilities which is critical from analytical perspective.

<sup>1</sup>Complete definition of the ratings assigned are available at [www.careratingsnepal.com](http://www.careratingsnepal.com) and other CARE publications

The projected cost of under construction hydropower is relatively lower at NPR 116.63 million per MW. Attributed to the low project cost, the project's return indicators are expected to remain better on account of fixed tariff and escalation structure attached to it.

### **Hydrology risk associated with run-of-the-river power generation, however minimized due to peaking reservoir**

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-May to Mid-November) and less during the dry season (Mid-November to Mid-May). KBNR is proposed to utilize discharge from Ishuwa Khola having catchment area of 160.79 sq. kms based on snow fed Perennial River. Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river/ khola. However, the risk is minimized to some extent in the project due to peaking reservoir of 6 hours for dry season which will be used during peak time of dry season.

### **Power Evacuation Risk**

The Power generated from the project is proposed to be evacuated through ~22km long Double circuit 230kV Transmission Line to NEA's Tumlingtar sub-station. The construction of transmission line from powerhouse to substation is within the scope of the company. Timely completion of the transmission lines and substation will be crucial for the company from revenue generation prospective.

### **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, the hydropower sector is prone to regulatory risk and changes in other policies by GoN.

### **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. Furthermore, increased bank rates announced in the Monetary Policy for FY23 is likely to add to the upward pressure on interest rates going forward. Any 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.

### **Key Rating Strengths**

#### **Experienced Promoters and directors in hydropower sector**

KBNR is managed by 3 Board of Directors and board is chaired by Mr. Birendra Bahadur Neupane who has around 4 decades of experience in civil construction including experience in hydropower sector. He has been associated in various operational hydropower projects under Himal Dolakha Hydropower Company Limited (HDHCL) and Joshi Hydropower Development Company Limited and under-constructed hydropower projects.

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

KBNR had entered into a long term PPA with NEA as on October 12, 2018 for sale of 97.2 MW power to be generated from the project. The contracted Plant Load Factor (PLF) for total 97.2 MW is 79.19% at probability of exceedance of 59% with total

contracted energy of 674.30 MU (i.e. 262.54 MU for dry season and 411.76 MU for wet season). PPA has been entered for the period of 30 years from the COD or till validity of generation license (obtained on June 09, 2020 for 35 years) whichever is earlier. Tariff rate as per PPA is Rs 4.80 per KWh for wet season (Mid-May to Mid-November) and the tariff rate for peak dry season (Mid-November to Mid-May) is Rs 8.55 to 10.55 per KWh depending on the peak hours while the non-peak rate for the dry season (Mid-November to Mid-July) is 8.40 per Kwh, with 3% annual escalation on base tariff for 8 years. The PPA is under the take or-pay modality, which eliminates the risks related to tariff and offtake of the energy to be generated by the project.

### **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**

KBNR Isuwa Power Limited (KBNR) is a public limited company, incorporated on December 18, 2017. It is promoted by an institutional promoter and a group of individual promoters to develop Hydropower in Nepal under "BOOT" (Build, Own, Operate and Transfer) model. KBNR is setting up Isuwa Khola Hydropower Project (IKHP) in Sankhuwasabha district of Nepal. The project is proposed to utilize available head and flow from Isuwa Khola (river), which is a tributary of Arun River.

### **Annexure-1 Details of Facilities/Instruments to be rated**

<b>Name of Instrument</b>	<b>Type of Facility</b>	<b>Amount(Rs in Million)</b>	<b>Rating</b>
Long Term Bank Facilities	Term Loan	9,069.00	CARE-NP BB
Short Term Bank Facilities	Working Capital Loans	100.00	CARE-NP A4
Total		<b>9,169.00</b>	

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