

## Eastern Hydropower Limited

### Ratings

Facility/Instrument	Amount (Rs. in Million)	Ratings <sup>1</sup>	Rating Action
<b>Issuer Rating</b>	<b>NA</b>	<b>CARE-NP BB (Is) [Double B (Issuer)]</b>	<b>Revised from CARE-NP B+(Is)</b>
<b>Long Term Bank Facilities</b>	<b>722.45</b>	<b>CARE-NP BB [Double B]</b>	<b>Revised from CARE-NP B+</b>
<b>Short Term Bank Facilities</b>	<b>5.00</b>	<b>CARE-NP A4 [A Four]</b>	<b>Reaffirmed</b>
<b>Total Facilities</b>	<b>727.45 (Seven Hundred Twenty Seven Million Four Hundred and Fifty Thousand Only)</b>		

*\*The issuer rating is subject to overall gearing not exceeding 1.50x at the end of FY23*

Details of instruments/facilities in Annexure-1

CARE Ratings Nepal Limited (CRNL) has revised Eastern Hydropower Limited's (EHL) issuer rating to 'CARE-NP BB (Is)' from 'CARE-NP B+ (Is)'. Issuers with this rating are considered to offer moderate risk of default regarding timely servicing of financial obligations in Nepal.

Also, CRNL has revised the rating assigned to the long term bank facilities of EHL to 'CARE-NP BB' from 'CARE-NP B+' and reaffirmed rating of 'CARE-NP A4' assigned to the short term bank facilities of EHL.

### Detailed Rationale & Key Rating Drivers

The revision in ratings assigned to the bank facilities and issuer rating of EHL considers improvement in its financial risk profile during FY22 (Unaudited; FY refers to the twelve-months period ended mid-July) marked by improvement in Plant Load Factor (PLF) leading to sustained revenue growth and gross cash accruals. The rating also takes cognizance of better hydrology and improvement in power evacuation setup resulting in lower tripping issues faced by the project since switching to Inaruwa sub-station during mid-July 2021. However, the ratings continue to be constrained by moderate debt service coverage indicators, hydrology risk associated with run-of-the-river power generation, exposure to volatile interest rates and exposure to regulatory risk.

The ratings continue to derive strengths from experienced promoters and management team in hydropower sector Power Purchase Agreement (PPA) with sufficient period coverage and government support for the power sector. The rating also takes cognizance of completion of the initial public offering of Rs. 67 Mn by the company in November 2022.

*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) will be the key rating sensitivities.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weaknesses

#### Below average financial risk profile, albeit improving trend during FY22

EHL has been operating a run-of-the-river 5 MW Pikhua Kholra Small Hydropower Project (PKSHP) at Bhojpur District of Nepal since June 10, 2019. During FY22, the company reported increase in Total Operating Income (TOI) by 22% to Rs. 122 Mn through sale of electricity from Rs. 100 Mn during FY21 (Audited) on account of improved hydrology coupled with lower tripping issues compared to previous years. PBILDT margin stood at 83.52% (PY: 84.73%). Despite

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

increased revenue, the company reported loss of Rs. 11 Mn in FY22 (PY: loss of Rs. 34 Mn) from operations on account of high interest cost and depreciation. For FY22, the company reported gross cash accruals (GCA) of Rs. 39 Mn. Furthermore, the capital structure of the company stood moderately leveraged with total gearing ratio of 1.79x as on mid-July 2022 (PY: 1.78x). Despite repayment of term loan gearing ratio stood similar on account of decline in tangible networth due to accumulated losses during the year. However, interest coverage ratio improved to 1.62x during FY22 from 1.21x in FY21. Furthermore, Total debt/GCA remains high at 20.16x during FY22, however improved from 50.66x during FY21 on account of improved GCA. Despite sequential improvement in the debt coverage indicators in FY22 over FY21, the company's overall financial risk profile remains below average. Improvement in hydrology leading to adequate cash flow generation from the project will be critical from credit perspective.

### **Hydrology risk associated with run-of-the-river power generation**

Run-of-the-river (ROR) 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). PKSHP utilizes discharge from Pikhuwa Khola having catchment area of 117 sq. 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 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.

### **Key Rating Strengths**

#### **Experienced promoters and management team**

EHL is managed under the overall guidance of the company's Board of Directors (BoD), who possesses wide experience in the different sectors. The company has six members in its board, chaired by Mr. Dhan Bahadur Shrestha, Managing Director, who has over four decades of experience in different sectors including hydropower sector and worked as a Joint Secretary of Ministry of Federal Affairs and Local Development and Ministry of Labor and Employment. Similarly, other directors of the company also have work experience in related sector. The BOD are further supported by a team of experienced management team members.

#### **Improvement in power evacuation risk**

The company's power evacuation risk has improved substantially after switching to NEA's 33KVA Inaruwa Substation. Prior to this, the power generated from PKSHP was evacuated through 4 km long 33 KVA transmission Line from the project to Pani Tanki, Bhojpur sub-station of NEA which was transmitting higher power than its carrying capacity. This resulted regular breakdowns and transmission losses during FY20 and FY21. Under temporary arrangement, NEA constructed 25 km long 33KVA transmission line from Bhojpur to Tumling Tar at the end of FY21 leading to diversion of line and reducing the load on the transmission line. After switching to NEA dedicated line from Bhojpur to Inaruwa, the issues related to tripping has been reduced significantly and company billing units has increased. Thus, power evacuation risk of the hydropower project is likely to be moderate going forward.

### Continued reduction in gap between contracted PLF and operational PLF

The annual contracted PLF of the project is 70.67% of the installed capacity of the plant. During FY22, the PLF from the project improved to 56.29% of total capacity (PY: 47.81%). The PLF improving trend continued in 4MFY23 (Unaudited, refers to the four-month period ended mid-May 2022) and stood at 89.47% of total capacity. Although first quarter of the financial year, being mostly wet season, leads to higher generation, however, on a year-on-year basis, the company's PLF levels have shown steady improvement, benefitting from an improved hydrology coupled with efficient power evacuation. The PLF as a percentage of contracted energy has also been on an improving trend (4MFY23: 95.39%, FY22: 79.65%, FY21: 67.65%). The ability of the company to continue to reduce the gap between operational PLF and contracted PLF and availability of sufficient hydrology remains a key monitorable aspect.

### Power purchase agreement with sufficient period coverage

EHL entered into PPA with NEA for 5 MW on November 13, 2016 for sale of entire power generated by PKSHP. The PPA is valid for a period of 30 years from Commercial Operation date (COD). The tariff for wet season (Mid-April to Mid-December) is Rs 4 per kWh and for dry season (Mid-December to Mid-April) is Rs 7 per kWh with 3% escalation on base tariff for 9 years in case of 2.475 MW. Similarly, the tariff for wet season is Rs 4.80 per kWh and for dry season is Rs 8.40 per kWh with 3% escalation on base tariff for 5 years for additional capacity of 2.525 MW. The contracted energy for the project is 30.95 million units (MU).

### 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

EHL is a Public Company, incorporated on August 4, 2017, promoted by institutional as well as individual promoters from different background. It is currently operating a 5 MW Pikhua Khola Small Hydropower Project (PKSHP) in run –of – river scheme located at Bhojpur district, Nepal. The project has been constructed under BOOT (Build, own, Operate and Transfer) mechanism.

### Financial Performance

Brief financial performance of EHL during last 3 years is given below:

For the Period	(Rs. In Million)		
	FY20 (A)	FY21 (A)	FY22 (UA)
Income from Operations	89	100	122
PBILDT Margin (%)	85.68	84.73	83.52
Overall Gearing (times)	1.65	1.78	1.79
Interest Coverage (times)	0.76	1.21	1.62
Current Ratio (times)	0.75	0.92	1.26
Total Debt/Gross Cash Accruals(times)	Negative	50.66	20.16

A: Audited, UA: Unaudited

**Annexure 1: Details of the Facilities Rated**

Nature of the Facility	Type of the Facility	Amount (Rs. in Million)	Rating
Long Term Bank Facilities	Term Loan	722.45	CARE-NP BB [Double B]
Short Term Bank Facilities	Fund Based Limit	5.00	CARE-NP A4 [A Four]
<b>Total</b>		<b>727.45</b>	

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