

Singati Hydro Energy Limited

Ratings

Facilities	Amount (Rs. Million)	Rating ¹	Rating Action
Issuer Rating	NA	CARE-NP BB (Is) (Double B [Issuer Rating])	Reaffirmed
Long Term Bank Facilities	4,493.41	CARE-NP BB [Double B]	Reaffirmed
Short Term Bank Facilities	250.00	CARE-NP A4 [A Four]	Reaffirmed
Total Facilities	4,743.41 (Four Billion Seven Hundred Forty Three Million and Four Hundred Ten Thousand Only)		

**The issuer rating is subject to overall gearing ratio of the company not exceeding 3.50x at the end of FY23.*

Details of instruments/facilities in Annexure-1

CARE Ratings Nepal Limited (CRNL) has reaffirmed the issuer rating of 'CARE-NP BB (Is)' assigned to Singati Hydro Energy Limited (SHEL). Issuers with this rating are considered to offer moderate risk of default regarding timely servicing of financial obligations, in Nepal.

Also, CRNL has reaffirmed the rating of 'CARE-NP BB' assigned to the long term bank facilities and 'CARE-NP A4' assigned to the short term bank facilities of SHEL.

Detailed Rationale & Key Rating Drivers

The ratings assigned to SHEL are constrained by the relative high cost of project leading to leveraged capital structure coupled with increased financial burden towards debt servicing in the initial years of commercial operations owing to high interest expense considering the project is heavily debt funded. In addition, the ratings remain constrained by hydrology risk associated with run-of-the-river power generation and exposure to volatile interest rate risk.

The ratings, however, derive strengths from experienced board members and management team, presence of power purchase agreement (PPA) with sufficient period coverage and moderate counter party risk, and favorable government policy towards power sector. The ratings also take cognizance of SHEL's satisfactory operational performance in the early years of operations, sustenance of which remains imperative from credit perspective in coming years.

Going forward, the ability the company to profitably operate at contracted PLF levels leading to cash accruals as envisaged, availability of sufficient hydrology during both dry and wet seasons and 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

High debt service burden in initial years of operations owing to high cost of project

During the development of Singati Khola Hydropower Project (SKHP), SHEL had undergone multiple revisions in the project cost resulting in the final cost of Rs. 6,131 Mn which was financed in the debt equity mix of around 3:1. The project cost had increased multiple times due to delay in execution of project leading to increase in interest during construction (IDC) coupled with increase in other management expenses on account of the delay. Considering the project is highly debt funded, the project cost of around Rs. 245 Mn per Megawatt (MW) is relatively high compared to similar projects, which is likely to lead to a longer payback period coupled with elevated debt servicing requirements in the initial years of operations owing to higher interest outgo, exacerbated further by the relatively higher interest rates currently prevailed in the market. The company's ability to adequately service its debt obligations will therefore hinge on its ability to generate sufficient cash flow from operations.

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

As on July 16, 2022, SHEL's overall gearing stood high at 3.37 times, majorly due to net losses transferred to reserves which eroded the company's tangible net worth. Despite satisfactory operational performance, the company incurred net loss of Rs. 55 in FY22 (FY refers to the twelve-month period ending mid-July) on account of high interest outgo. Interest coverage ratio stood low at 1.40 times and total debt to gross cash accruals stood high at 30.12 times. The ability of the company to improve its net profitability with better debt service coverage indicators thereby lowering its gearing levels is critical from credit 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 seasonal river flows are high (Mid-April to Mid-December) and less during the winter season (Mid-December to Mid-April). SHEL is proposed to utilize discharge from Singati Khola which is a perennial river having catchment area of 195 sq km with the design discharge of 10.88 M³/S at Q40 exceedance flow and available gross head of 268m. Hence, any variation in discharge of water might impact the energy generation of project which is of key importance for the company from the revenue generation perspective.

Exposure to volatile interest rate

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 few quarters. A contractionary monetary policy for FY23 coupled with increasing inflation has only added to the upward pressure on interest rates, resulting in the rate hikes taken by BFIs in the first quarter of FY23. 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.

Key Rating Strengths

Experienced board members and management team in hydropower sector

SHEL has seven members in its Board of Directors chaired by Mr. Batu Lamichhane, who is involved in hydropower sector and construction sector for more than 20 years. Mr. Ganesh Karki, executive chairperson, is involved in hydropower sector for more than 20 years and is director in multiple under construction and operational hydropower projects. The board is aptly supported by an experienced management team across various functions.

Satisfactory operational performance

SHEL started commercial production in July 2021. FY22 was the first year of operations and the plant was operational for 11.5 months at 59.20% of its generation capacity. The total energy generated against the contracted PLF during the period was 100.12%. Similarly, during 5MFY23 (refer to five-months period ended mid-December 2022), the plant operated at 89.47% of its generation capacity and the total energy generated against the contracted PLF during the period was 96.55%. Ability of the company to sustain its operational Plant Load Factor (PLF) close to the contracted levels is critical from revenue generation perspective and will remain a key monitorable aspect.

Power purchase agreement with sufficient period coverage

Initially, SHEL had signed PPA with NEA on November 13, 2013 for sale of power generated from 16MW capacity. Later, the project capacity was increased to 25MW and PPA has been amended on December 14, 2017 for additional capacity. The contracted Plant Load Factor (PLF) for 25 MW is 60.55% with the contracted energy of 132.61 Million Units (MU) annually. PPA has been

entered for the period of 30 years from the COD or till validity of generation license whichever is earlier. The differential tariff rate ranges from Rs 4.80 per to Rs 8.40 per kWh with 3% annual escalation on base tariff for 5 years in case of 16MW and 8 years in additional 9MW. The company has signed PPA with NEA is owned by Government of Nepal and hence counter party default risk is low; however, timely realization of the same is critical for the company and from analytical perspective also.

Favorable Government policies towards power sector

Government of Nepal (GoN) considers hydropower generation as a 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 the 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 2026. 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 augurs well for the sector.

About the Company

SHEL was initially incorporated as a private limited company on May 19, 2010, and later converted to a public limited company on June 20, 2018. It is promoted by various institutional and individual promoters from different backgrounds for setting up of a 25 MW run-of-river, Singati Khola Hydropower Project (SKHP) in Dolakha district of Nepal. The project is one of the 'super six' hydro power projects of Nepal. This project is constructed under BOOT (Build, Own, Operate and Transfer) mechanism.

Brief financial performance of SHEL during FY22 is shown as follows:

Particulars	FY22 (Unaudited)
Income from Operations	658
PBILDT Margin (%)	86.13
Overall Gearing (times)	3.37
Interest coverage (times)	1.40
Current Ratio (times)	0.96
Total Debt/Gross Cash Accruals (times)	30.12

Annexure-1: Details of Instruments/Facilities

Name of the instrument	Type of the Facility	Amount (Rs. Million)	Rating
Long Term Bank Facilities	Fixed Term Loan	4,493.41	CARE-NP BB
Short Term Bank Facilities	Overdraft	250.00	CARE-NP A4
Total Facilities		4,743.41	

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