

Champawati Hydropower Limited

Rating

Facilities	Amount (Rs. Million)	Rating ¹	Rating Action
Long Term Bank Facilities	924.00	CARE-NP BB- [Double B Minus]	Reaffirmed
Total Facilities	924.00 (Nine Hundred and Twenty-Four Million Only)		

Details of instruments/facilities in Annexure-1

CARE Ratings Nepal Limited (CRNL) has reaffirmed the rating of 'CARE-NP BB-' assigned to the long-term bank facilities of Champawati Hydropower Limited (CHL).

Detailed Rationale & Key Rating Drivers

The rating assigned to CHL continues to remain constrained by project implementation and stabilization risk associated with its under-construction hydropower project. The rating also factors in hydrology risk associated with run-of-the-river power generation, risk of natural calamities, power evacuation risk, and the company's exposure to regulatory risk and volatile interest rate risk.

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

Going forward, the ability of the company to successfully execute the project within envisaged cost and time 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

CHL is setting up a 7 MW run-of-river Chepe A hydropower project (CAHP) in Gorkha and Lamjung district of Nepal. The total cost of the project is envisaged at Rs. 1,326 Mn (Rs. 189 Mn per MW) to be funded in debt-to-equity ratio of 70:30. The total debt amounting to Rs. 924 Mn has been fully tied up. Till Mid-November 2022, the company has incurred expenditure of Rs. 620.69 Mn (financial progress of around 46.81%) and the same was funded through debt of Rs. 315.14 Mn and remaining from equity. As on Mid-November 2022, promoters' contribution amounting to Rs. 336.82 Mn has been infused as against the required infusion of Rs 402 Mn. The company has awarded contracts for hydro-mechanical, and electro-mechanical works. In December 2022, the project's office was vandalized by some locals which had impacted the ongoing construction works for around two months. As per the management, the vandalization has not caused any damage to the project infrastructures and the issues have been sorted out. The construction works are currently being carried out smoothly.

Required Commercial Operation Date (RCOD) of the project has been extended to July 19, 2023 and the company is eligible to avail the extension of RCOD by one more year on account of the pandemic. If the project is not completed within the RCOD, the company will be liable to pay delay penalty. Furthermore, if COD is delayed by 6 months to 18 months from RCOD, there are restriction clauses in escalation of tariff rate. It is, therefore, critical for the company to complete the project within the timeline to avail the accelerated clauses of tariff. Any delay in the same would impact the project's expected returns and debt servicing capabilities which is critical from credit perspective.

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

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 (June to November) and less during the dry season (December to May).

Moreover, hydropower projects are also highly dependent on monsoon rains that determine the water flow in the river. Nepal receives 80% of its rain during monsoon which usually spans from June to November. However, incessant rains during this period can also adversely impact the power projects due to higher chances of floods and landslides. On the other hand, during other seasons, scanty rains or no rain can invite seasonal drought causing the flow in the river to reduce, which can also adversely impact these power projects.

CAHP is also proposed to utilize discharge from Chepe Khola (river) having catchment area of 212 sq. km 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.

Risk of Natural Calamities

In Nepal, hydropower projects are usually located in terrains that are topographically challenging making their construction and operations vulnerable to adversities of nature. Floods and landslides that tend to occur in these areas pose threat to these power projects damaging their infrastructures as well as impacting their timely completion. Moreover, disruption in their construction in turn could lead to time and/or cost overrun, negatively impacting the project's financial aspects. Moving forward also, these natural calamities can adversely affect the smooth flow of power generation and distribution, which can further impact financial returns of the projects. CHL is also exposed to such risks of natural calamities that might cause infrastructural, operational and financial damages to the project.

Power evacuation risk

The power generated from the project is expected to be evacuated via a 4 km long 33KV single circuit transmission line from its powerhouse to Parajuli Gaon's LILO substation which will eventually be connected with operational Palungtar Substation. The company is required to construct a switching station at the point nearby its powerhouse as per NEA standards. The connection / delivery point shall be a Loop In Loop Out (LILO) Connection at the Parajuli Gaon switching station, where NEA transmission line is available to connect. Timely completion of the power evacuation structures will be a key rating sensitivity.

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 half 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.

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

Key Rating Strengths

Experienced promoters and management team

CHL has nine board of directors having long experience in various sectors including hydropower projects. The board is chaired by Mr. Hari Ram Parajuli and he has more than two decades of work experience in various engineering projects. He is a civil engineer with expertise in feasibility study, tender design, construction supervision, structural design and risk management for infrastructure projects. He was associated with other hydropower projects in the capacity of Board Member. Mr. Tuk Prasad Neupane, Managing Director has more than two decades of work experience in various sectors. He is a mechanical engineer and has associated with other hydropower projects in the capacity of Board Member. The board is supported by other experienced management team.

Power purchase agreement with sufficient period coverage

CHL had entered into a long term PPA with NEA for sale of 7 MW power to be generated from the project on take or pay basis. The contracted Plant Load Factor (PLF) is 64.10% of total generation capacity. The PPA has been entered for a period of 30 years from COD or till the validity of generation license, whichever is earlier. PPA period may be extended with mutual consensus during the last six months of validity.

The project's PPA has been executed under the six-month dry season (December to May) and six-month wet season (June to November) modality. Tariff rate as per PPA is Rs. 4.80 per Kwh for wet season and Rs. 8.4 per Kwh for dry season with 3% annual escalation on base tariff for eight years. It is crucial for the company to start the commercial production within the RCOD to have the benefits of all the eight tariff escalations in the base tariff. The escalations would support the project's incremental revenue, return and debt service coverage indicators.

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 2027. Also, with government focus more toward reservoir-based hydropower projects; Monetary Policy FY23 has provided full tax exemption for first 15 years and 50% tax exemption for next 6 years to reservoir and semi-reservoir projects completing financial closure within mid-April 2029 with a capacity higher than 40 MW. 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

Champawati Hydropower Limited (CHL) is a public limited company, incorporated on June 10, 2010 having converted from Private Limited Company on February 15, 2022. It is promoted by institutional promoters and business persons having long experience in various sectors including hydropower for setting up Hydroelectric Project (HEP) in Nepal. It is developing 7 MW run-of river, Chepe A Hydropower Project (CAHP) in "BOOT" (Build, Own, Operate and Transfer) model and is located at Gorkha and Lamjung district of Nepal.

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Type of the Facility	Amount (Rs. Million)	Rating
Long Term Bank Facilities	Term Loan	924.00	CARE-NP BB- [Double B Minus]
Total Facilities		924.00	

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