

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 the bank facilities of CHL continues to remain constrained by project implementation risk and operations stabilization risk thereafter 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 operations stabilization risk thereafter

CHL is setting up a 7 MW run-of-river Chepe A hydropower project (CAHP) situated in Nepal's Gorkha and Lamjung districts. With an estimated total cost of Rs. 1,326 Mn, equivalent to Rs. 189 Mn per MW, the project's funding structure follows a debt-to-equity ratio of 70:30. The company has successfully secured total debt amounting to Rs. 924 Mn. As of December 21, 2023, financial progress stands at 83.81%, with funding from equity totaling Rs. 376 Mn and bank debt amounting to Rs. 707 Mn.

In terms of physically progress, the project has achieved approximately 90% completion as of mid-January 2024. However, CHL faces residual project implementation risks regarding meeting the project's estimated cost within the Required Commercial Operation Date (RCOD). The RCOD has been extended to April 14, 2024 and if the project will not be completed by this date will result in delay penalties. Moreover, exceeding a 6-month delay beyond the RCOD will trigger restriction clauses on tariff rate escalation. Timely project completion is imperative for CHL to benefit from accelerated tariff clauses. Any delay in the same would impact the project's expected returns and debt servicing capabilities which is critical from credit perspective.

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

Run-of-the-river power generation, such as the Chepe A hydropower project undertaken by CHL, relies heavily on the natural flow of rivers for electricity production. Unlike traditional hydroelectric dams with reservoirs, run-of-the-river projects lack significant water storage capacity. This characteristic makes them inherently dependent on seasonal variations in river flow. In the case of CHL's project, it plans to harness the discharge from Chepe Khola, with a catchment area of 212 sq km, based on a semi-snow-fed perennial river system which highlights its vulnerability to fluctuations in water discharge.

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

The project's reliance on natural water flow exposes it to risks associated with variations in river discharge, particularly during different seasons. Typically, run-of-the-river projects generate more power during the wet season (June to November) when river flows are high and less during the dry season (December to May). The variability in water discharge poses a significant risk to the project's energy generation capacity, which is crucial for revenue generation. Any material deviation from expected water flow patterns could directly impact the project's ability to generate electricity and, consequently, its revenue streams.

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

CHL is required to construct a switching station near its powerhouse for the Chepe A Hydropower project and the switching station has to be in line with Nepal Electricity Authority (NEA) standards. This station will facilitate the connection and delivery of power via a Loop in Loop Out (LILO) Connection at the Parajuli Gaon switching station. The evacuation of power generated by the project will occur through a 4 km long 33KV Single Circuit Transmission Line from the Chepe A Hydropower's powerhouse to the Parajuli Gaon LILO substation, eventually linking up with the Palungtar Substation.

The timely completion of the switching station's construction holds critical importance for CHL's income prospects. Without this essential infrastructure in place, the project's ability to evacuate power to the grid and crucial from the generate revenue prospective.

Exposure to volatile interest rate

CHL's interest rates are based on floating interest rate regime, where a certain premium is added to the monthly base rate and interest rate is changed accordingly on monthly 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 changes in interest rates. Being high debt funded project, higher interest rates than envisaged could result in squeezed margins of the company, impacting its liquidity profile.

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 Dr. Hari Ram Parajuli who has more than two decades of 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.

Low offtake risk and moderate counterparty risk

CHL had entered into a PPA with NEA as on February 19, 2019 for sale of 7 MW power to be generated from the project. The period of the PPA is 30 years from commercial operation date (COD) or till validity of Generation License (obtained on May 28, 2020 for 35 years), whichever is earlier. PPA period may be extended with mutual consensus during the last six months of validity. The tariff for wet season (June to November) is Rs 4.80 per kWh and for dry season (December to May) is Rs 8.40 per kWh with 3% escalation on base tariff for 8 times in every year after completion of 12 months from COD date. The contracted energy for the project is 39.31 million units (MU) (i.e., 11.80 MU for dry season and 27.51MU for wet season), at PLF of 64.10%. Additionally, the counterparty payment risk associated with NEA is deemed moderate, given its full ownership by the Government of Nepal. Such arrangements are expected to provide revenue stability and sustainability to the company.

Favorable government policies towards power sector

The Government of Nepal (GoN) has prioritized hydropower generation as a crucial sector for economic development and aims to enhance private sector involvement by offering a range of incentives and facilities. In line with this objective, GoN has introduced a comprehensive tax incentive package, providing full tax exemption for the initial 10 years and a 50% tax exemption for the subsequent five years to individuals or entities engaged in the commercial operation, transmission, and distribution of electricity until mid-April 2027. These incentives are designed to encourage investment and promote growth in the hydropower sector. Additionally, directives from the Nepal Rastra Bank (NRB) mandate that all banks to allocate a minimum share of their total advances to the energy sector. This directive further reinforces the government's commitment to supporting and facilitating investment in the energy sector, including hydropower projects.

Furthermore, the long-term demand outlook for the Nepalese power sector is promising, with new bilateral agreements facilitating additional exports of power to India. These agreements underscore the potential for Nepal to capitalize on its hydropower resources and leverage them for economic growth and 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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