

## Rating Rationale

### Taksar Pikhuwa Khola Hydropower Private Limited

#### Rating

Facility/ Instrument	Amount (Rs. In Million)	Rating <sup>1</sup>	Rating Action
Long Term Bank Facilities	1,200.00	CARE-NP BB [Double B]	Reaffirmed
<b>Total Facilities</b>	<b>1,200.00</b>		

*Details of Facilities in Annexure 1*

CARE Ratings Nepal Limited (CRNL) has reaffirmed rating of ‘CARE-NP BB’ to the long-term bank facilities of Taksar Pikhuwa Khola Hydropower Private Limited (TPKH).

#### Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of TPKH is constrained by project implementation and associated stabilization risk, high estimated project cost coupled with time overrun and TPKH’s exposure to regulatory risk. The rating is also constrained by TPKH’s exposure to volatile interest rates and hydrology risk associated with run of the river power generation. The rating, however, derives strength from experienced board members and management, moderate counter party risk and government support for the power sector and low power evacuation risk. The ratings also factors in achievement of financial closure for full project cost, presence of power purchase agreement (PPA) with sufficient period coverage, shortage of power at present coupled with increasing demand of power in the country. The ability of TPKH to timely complete the project without any time or cost overrun and timely completion of transmission infrastructure are the key rating sensitivities.

#### Detailed Description of the Key Rating Drivers

##### Key Rating Weaknesses

##### *Project implementation and stabilisation risk*

The project has achieved ~57% financial progress on the basis of cost incurred till February 12, 2020 with ~49% financial progress in civil works, ~80% in Hydromechanical (HM) work. As per the progress report of February 2020, work related to headworks is in progress with more than 50% completion, 3600m (out of 5800m) headrace pipe has been erected and ~60% of all powerhouse work is completed.

However, it seems challenging for the company to complete the remaining work including dry test and wet test within expected commercial operation date of Mid-July, 2020. Hence, the company continues to remain exposed to the risks associated with project implementation and satisfactory operations thereafter. Timely completion of the project within the estimated cost and time and satisfactory operations thereafter are the key rating sensitivities.

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

***High estimated project cost coupled with time overrun***

The total estimated cost of project is Rs 1,720 Mn (i.e. 215 Mn per MW) which is relatively higher. Further, the company was not able to complete the project within initial Required Commercial Operation Date (RCOD) of February 6, 2020 as the project work was disturbed for ~3 months during FY19 due to landslide and flood. The expected COD of the company is Mid July, 2020. The company has requested to NEA for extension of RCOD to April end, 2020 and if RCOD is not revised by NEA till COD, the company is required to pay late COD penalty. Further, if COD is delayed by 6 months to 18 months from RCOD, then the number of escalation in tariff rate will decrease to 4 times from 5 times.

***Exposure to volatile interest rate***

Nepalese banking sectors are fixing interest rate on lending by adding certain percentage of premium on quarterly base rate and interest rate will be changed accordingly on quarterly basis. Base rate of the Bank and Financial Institutions will be changed by change in liquidity position which leads to change in interest rate. Interest rate has been changing frequently in Nepal market since last 1-2 year. Therefore, funding from Bank and Financial Institutions are exposed to volatile interest rate.

***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-Dec to Mid-April). TPKH is proposed to utilize discharge from Pikhuwa Khola having catchment area of 253 sq kms based on rain fed 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 is 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*****Board members and management having experience in hydro power sector***

TPKH has 3 Board of Directors chaired by Mr. Narayan Ballav Pant, who has ~4 decades of experience in legal, banking and finance sector. He has served as director in United Modi Hydro Power Ltd., (UMHPL) in the past. Company's management team is led by Mr. Narendra Ballav Pant, Chief Executive Officer of the company who has more than decade of working experience and is chairperson of UMHPL

and director of Singati Hydro Energy Ltd. having 25MW under construction hydropower project [CARE NP IPO Grade 4].

***Financial closure achieved for estimated project cost***

The total cost of the project is envisaged at Rs. 1,720 Mn to be funded in debt equity ratio of 70:30. TPKH has entered into consortium loan agreement for Rs 1,200 Mn term loan on January 21, 2018. Till February 12, 2020, Rs 390 Mn equity share capital has been infused by promoter shareholder.

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

TPKH had entered into a long term PPA with Nepal Electricity Authority (NEA) as on December 16, 2016 for sale of 8 MW power to be generated from the project. The contracted Plant Load Factor (PLF) for 8 MW is 64.94%. The tariff for wet season (Mid-April to Mid-December) is Rs 4.80 per kWh and for dry season (Mid-December to Mid-April) is Rs 8.40 per kWh with 3% escalation on base tariff for 5 years. The period of the PPA is 30 years from the date of COD or till validity of Generation License (received on June 17, 2016 for 35 years), whichever is earlier. PPA period may be extended with mutual consensus during the last six month of validity. The expected COD of the company is Mid July, 2020 against Initial Required Commercial Operation Date (RCOD) of February 6, 2020. The company has requested to NEA for extension of RCOD to April end, 2020.

***Low power evacuation risk***

The power generated from the project will be evacuated through ~7.5Km long 33KV Transmission Line to the operational Bhojpur Substation. Construction of ~7.5Km long 33KV transmission line from powerhouse to Bhojpur substation is within the scope of TPKH. The power evacuation risk of the project is low, as major part of the transmission line work within the scope of the company has been completed along with operational substation of NEA.

***Moderate counter party risk***

TPKH is exposed to counter party payment risk pertaining to Nepal Electricity Authority (NEA), which has been making consecutive losses in past till FY16 and carry huge accumulated loss in its book. However, as per the annual report published by NEA, during FY19 (provisional), NEA earned profit of Rs 7,205 Mn (Rs 2,897 Mn during FY18). Further, during FY19, NEA achieved gross cash accrual of Rs 11,915 Mn (Rs 7,107 Mn in FY18). The counter party payment risk is moderated by the fact that, NEA is fully owned by government of Nepal, net loss is declining over the period and NEA is generating positive gross cash accruals. Further, NEA has been making timely payment to independent power producer (IPPs) in past.

***Shortage of power at present coupled with increasing demand of power in the country***

As per the NEA's Annual Report for FY19, the current peak electricity demand is 1,320 MW. The total domestic installed capacity stands at 1,178 MW which includes 617 MW owned by NEA and 561 MW by private sector IPPs. Overall, during FY19, total energy demand was 7,584 GWh which was met by import

of 2,813 GWh from India whereas balance was met by domestic generation. As per NEA, electricity demand is in increasing trend and is expected to increase in future with increase in electricity consumption through the promotion of electric vehicles by building charging station and replacing cooking gas with electricity, increase in access of population using electricity (78% in FY19) etc.

**Government support for the power sector**

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 5 December 2019 announced full tax exemption for first 10 years and 50% tax exemption for next 5 years to those who generate electricity within mid-April 2024. Income tax will be levied only 20% despite the normal tax rate for entity in Nepal is 25%. Also, GoN has declared to provide grant of amount equivalent to Rs. 5 Mn per MW installed capacity after receiving evidence of formal COD of power plant.

**About the Company**

Taksar Pikhuwa Khola Hydro Power Pvt. Ltd (TPKH) is a Private company, incorporated as on April 23, 2014. It is promoted by individual promoters from different background for setting up of an 8 MW run-of-river, Taksar Pikhuwa Khola Hydropower Project (TPKHP) in Bhojpur district of Nepal. The major shareholders of the company as on February 12, 2020 are Mr. Narayan Ballav Pant (24.41%) and Mrs. Anju Pant (16.36%). The project is constructed under BOOT (Build, own, Operate and Transfer) mechanism. As per the Generation License, from Government of Nepal – Ministry of Energy, obtained as on June 17, 2016, the project shall be handed, on whatever conditions the project is, to the Government of Nepal after expiry of Generation License, which is 35 years.

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

Nature of the Facility	Type of the Facility	Amount (Rs. Million)	Rating
Long Term Bank Facilities	Term Loan	1,200.00	<b>CARE-NP BB</b>
<b>Total</b>		<b>1,200.00</b>	