

Rating Rationale

Mathillo Mailun Khola Jalvidhyut Limited

Rating

Facility/ Instrument	Amount (Rs. In Million)	Rating ¹	Rating Action
Long Term Bank Facilities	1,875.00	CARE-NP BB- [Double B Minus]	Reaffirmed
Short Term Bank Facilities	90.00	CARE-NP A4 [A Four]	Reaffirmed
Total Facilities	1,965.00		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has reaffirmed rating of ‘CARE-NP BB-’ to the long-term bank facilities and ‘CARE-NP A4’ to the short-term bank facilities of Mathillo Mailun Khola Jalvidhyut Limited.

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of MMKJL is constrained by project implementation and stabilization risk including the power evacuation risk and MMKJL's exposure to regulatory risk. The rating is also constrained by MMKJL's exposure to volatile interest rates, hydrology risk associated with run of the river power generation and impact of COVID-19 on the project implementation. The rating, however, derives strength from board members and management having experience in hydro power sector, association with large group having multiple hydropower projects and presence of power purchase agreement (PPA) with sufficient period coverage. The ratings also factor in moderate counter party risk, achievement of financial closure for full project cost, power demand supply gap in Nepal coupled with increasing demand of power in the country and government support for the power sector. The ability of MMKJL 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 RCOD of the project was December 2019 and company is in process of further extension till July 2021. Till May 13, 2020, ~17.45% of the total project cost has been incurred. The project has 484.50m net head and includes 1830 m long headrace tunnel, and 770 m long penstock pipe. Two turbines (each having 7.5MW capacity), two generators and two transformers is proposed to be used in the project. As per progress report of May 2020, submitted by the company, there is no significant progress at headworks area. The tunnel excavation work and underground tunnel support works is in progress with excavation of 121m out of 1830m Headrace tunnel completed. Contract for Civil, Electro Mechanical Works and Hydro Mechanical is entered and Transmission line is under negotiation. As the project is in initial stages with

¹Complete definitions of the ratings assigned are available at www.careratingsnepal.com

expected COD of June 2021, the project is unlikely to meet the commercial operation date. Thus, 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.

Low power evacuation risk

The power generated from the project will be evacuated through 15Km long 132KV Transmission Line to the Trishuli 3B Hub Substation which is currently under construction by Nepal Electricity Authority (NEA). Power from Trishuli 3B substation will be further evacuated to an operational Matatirtha Substation in Kathmandu valley. Construction of transmission line from powerhouse to Trishuli 3B substation is within the scope of MMKJL. Bids are submitted for construction of Transmission line. Timely completion of the transmission lines and construction of substation by NEA will be key rating sensitivity.

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.

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 change by change in liquidity position which lead 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 is subject 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 river flows are high (Mid-April to Mid-December) and less during the winter season (Mid-Dec to Mid-April). MMKJP is proposed to utilize discharge from Mailung Khola which is a perennial river and having partly snow-fed and partly a rain fed catchment area of 72 sq kms. Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river/ khola.

Impact of Corona Virus on the Project Implementation

The outbreak of Coronavirus disease 2019 (COVID-19) which was recognized as Pandemic by World Health Organization. Government of Nepal (GoN) imposed travel restrictions and countrywide lockdown since March 24, 2020 closing most of the organizations which resulted in slowing down of the economic activities. GoN allowed construction works to continue around Nepal during lockdown period also with proper safety measures. Due to the pandemic there are several impacts in under-construction projects like unavailability of contract labor and construction material due to partial operations of manufacturing units across Nepal. MMKJL had initially issue in the manpower mobilization, however with majority of contractor's resources were available in project site during lockdown hence resource availability was not impacted. However, the company is in process of ascertaining any impact in time and cost caused by delay due to COVID-19.

Key Rating Strengths***Board members and management having experience in hydro power sector***

MMKJL has 3 Board of Directors, chaired by Mr. Rameshwor Rijal, who has more than ~37 years of experience in different organization. He has served as Department Chief for Public Works Department of Kathmandu Metropolitan City Office. Mr. Binaya Kumar Shrestha, Director, has more than 2 decades of experience. He is also a Chairman of Sanima Bank Ltd. Dr. Subarna Das Shrestha, Director, has ~27 years of experience including ~25 years in Hydropower sector. He was CEO in a promoter company; Sanima Mai Hydropower Ltd [CARE-NP BBB+/A3+] and is a Past President of Independent Power Producers Association of Nepal (IPPAN). Company management team is led by Mr Kangada Prasai, General Manager of the company and has over one decade of experience in different capacities. He is supported by other experience management team.

Associated with large group having multiple hydropower projects

MMKJL is part of Sanima Hydro Group which is promoted by group of Non-Resident Nepalese who are related to Sanima Group having business in Hydropower, Banking and insurance sector. Sanima Hydro has been developing a number of hydropower projects by setting up Special Purpose Vehicle (SPV) companies in Nepal.

Power purchase agreement with sufficient period coverage

MMKJP had entered into a long term PPA with NEA on September 09, 2011 for sale of 14.3 MW power to be generated from the project. The contracted Plant Load Factor (PLF) for total 14.3 MW is 63.60%. PPA has been entered for the period of 30 years from the COD or till validity of generation license whichever is earlier. Tariff rate as per PPA is Rs 4.80 per kWh for wet season (Mid-April to Mid-December) and Rs 8.40 per kWh for dry season (Mid-December to Mid-April) with 3% annual escalation on base tariff for 5 years. The Required Commercial Operation (RCOD) of the project was June 13, 2019 which was extended to December 2019. As per the company, the application for further extension of

RCOD till June 2021 is in-process with NEA and if RCOD is not revised by NEA, MMKJL is required to pay late COD penalty. Further, if COD is delayed by 6 months to 18 months from RCOD, then the number of escalations in tariff rate will decrease to 4 years from 5 years.

Moderate counter party risk

MMKJL 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. Further, during FY19, NEA achieved gross cash accrual of Rs 11,915 Mn. 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 generating positive gross cash accruals. Further, NEA has been making timely payment to independent power producers (IPPs) in the past.

Financial closure achieved for the full project cost

The total cost of the project is envisaged at Rs.2500 Mn to be funded in debt equity ratio of 75:25 (debt of Rs 1875 Mn and equity of Rs. 625 Mn). MMKJL achieved financial closure for the project on September 04, 2017. Till May 13, 2020, the company has incurred Rs.436 Mn and the shareholders infused Rs. 432 Mn for the project construction

Power demand & supply gap 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

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. Furthermore, GoN has declared to provide grant of amount equivalent to Rs. 5 Mn per MW installed capacity after receiving evidence of formal COD of complete power plant.

About the Company

Mathillo Mailun Khola Jalvidhyut Limited (MMKJL) is a Public Limited company, incorporated as on August 14, 2012. It is promoted by institutional investors majorly related to Sanima Hydro group and

other institutes which include Banks and Insurance companies also for setting up of a 14.3 MW run-of-river, Mathillo Mailun Khola Jalvidhyut Project (MMKJP) in Rasuwa district of Nepal. MMKJP has 9 institutional promoters who have contributed Rs 432.42 Mn equity share capital as on May 13, 2020. Sanima Mai Hydropower Ltd. [CARE-NP BBB+/A3+] (53.19%) and Molnia Power Limited (17.12%) are the major shareholders of the company. The project is constructed under BOOT (Build, own, Operate and Transfer) mechanism. 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 January 04, 2013 and renewed on March 20, 2017, the project shall be handed, on whatever conditions the project is, to the Government of Nepal after expiry of generation license.

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Annexure 1: Details of the Facilities rated

Facility/ Instrument	Type of the Facility	Amount (Rs. In Million)	Rating
Long Term Bank Facilities	Term Loan	1875.00	CARE-NP BB-
Short Term Bank Facilities	Working Capital Loan	90.00	CARE-NP A4
Total Facilities		1965.00	