

Rating Rationale
Eastern Hydropower Limited

Rating

Particulars	Amount (Rs. In Million)	Rating ¹	Rating Action
Issuer Rating	NA	CARE-NP D (Is) [Single D (Issuer)]	Assigned
Long Term Bank Facilities	737.15	CARE-NP D [Single D]	Assigned
Short Term Bank Facilities	30.00	CARE-NP D [Single D]	Assigned
Total Facilities	767.15		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned Issuer rating of ‘CARE-NP D (Is)’ to Eastern Hydropower Limited. Issuers with this rating are considered to be in default or are expected to be in default soon. Also, CRNL has assigned the rating of ‘CARE-NP D’ for the long term and short term bank facilities of Eastern Hydropower Limited (EHL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to EHL is constrained by on-going delays in the repayment of bank loan obligations, high project cost along with the weak financial risk profile of the company during FY20 (Audited, refers to 12 months period ended Mid-July 2020) and power evacuation issue. The rating is also constrained by project currently being operated at lower Plant Load Factor (PLF), exposure to volatile interest rates and hydrology risk associated with run-of-the-river power generation. The ratings, however, derive strength from experienced promoters and management team in the various sectors, presence of power purchase agreement with sufficient period coverage and moderate counter party risk. The ratings also factor in current demand and supply gap of power generation in the country and government support for the power sector. The ability of company to reduce the gap between operational PLF and contracted PLF, timely repayment of the bank loan obligations and receipt of the payments from NEA are the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

On-going delays in the payment of bank debt obligations

EHL has delayed the payment of bank loan obligations during FY20 due to cash flow mismatches on account of multiple reasons (delays being more than 30 days) and still has ongoing delays for the Quarter ended October 16, 2020. The delay in repayment of the term debt during FY20 was on account of low cash accruals and low energy generation from project. Further, energy generation declined during the year on account of shutdown of the plant for more than one month due to landslide. The ability of EHL to

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

generate sufficient cash flow from operations, maintain liquidity and timely service its debt obligation is the key rating driver.

High Project Cost along with weak financial risk profile of the company during FY20

EHL was constructed at the total project cost of Rs. 1,306 Mn (i.e. Rs. 261 Mn per MW) which was financed through the debt amount of Rs. 770 Mn and remaining through equity and advances. The high project cost was majorly due to the high interest during construction (IDC) cost and increase in civil cost. EHL came into an operation in June 10, 2019. EHL reported total income of Rs. 89 Mn during FY20 through the sale of electricity. The total revenue from the project was low during FY20 on account of the low energy generation and shutdown of the plant for one month due to landslide. PBILDT of the company was Rs.76 Mn, however, the company reported loss of Rs. 69 Mn during FY20 majorly due to high interest expenses of Rs.100 Mn. The company reported negative cash profit during FY20. Overall gearing ratio and the interest coverage ratio of the company was 1.55x and 0.76x at the end of FY20.

Power Evacuation Issue

The power generated from Pikhua Khola Small Hydroelectric Project (PKSHP) is evacuated through 4 km long 33 KVA transmission Line from the project to Pani Tanki, Bhojpur sub-station of NEA which connects Bhojpur to Dubahi. The NEA line is 33KVA and is transmitting higher power than its carrying capacity. Due to the over load on transmission line, tripping was main problem for the project during FY20 leading to low transmission of power. Considering this problem NEA is constructing 33KVA transmission line from Bhojpur to Tumlingtar. After construction of new transmission line the tripping problem is expected to be addressed. The company expects that the transmission line will be completed by the end of FY21. Timely completion of the transmission lines and smooth evacuation of power without any tripping will be key rating driver.

Current project operated at lower PLF

The annual contracted PLF for PKSHP is 70.67% of the installed capacity of the plant. The project came into operation on June 10, 2019 and has been operated at a lower PLF. During FY20, first full year of operation, the PLF was low at 42.09% (over generation capacity). The power generation from the project as a %age to the contracted power was also low at 59.51% during FY20. The lower generation from the project was on account of initial year of operation coupled with the energy loss due to tripping on the NEA transmission line. Further, energy generation declined during FY20 due to non-operation of plant for more than one month due to landslide. The Company was liable to pay the short supply penalty of Rs. 2.35 Mn during FY20.

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 (Mid-April

to Mid-December) and less during the dry season (Mid-December to Mid-April). PKSHP utilizes discharge from Pikhwa Khola, Perennial River, having catchment area of 117 sq. kms. 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 will be the regulator under the GoN which will be responsible for regulating hydropower companies in Nepal. Policies and the directives issued by ERC like approval process for Initial Public Offering (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

Experienced promoters and management team in the various sectors

EHL is managed under the overall guidance of the company's Board of Directors (BoD), who possesses wide experience in the different sectors. EHL has 7 Board of directors and is chaired by Mrs. Susan Karmacharya who has ~ 26 years of experience in different sector. Mr. Dhan Bahadur Shrestha, Managing Director, has ~36 years of experience in different sectors and worked as a Joint Secretary of Ministry of Federal Affairs and Local Development and Ministry of Labor and Employment

Power purchase agreement with sufficient period coverage

EHL entered into PPA with NEA for 5 MW on November 13, 2016 for sale of entire power generated by PKSHP .The PPA is valid for a period of 30 years from Commercial Operation date (COD). The tariff for wet season (Mid-April to Mid-December) is Rs 4 per kWh and for dry season (Mid-December to Mid-April) is Rs 7 per kWh with 3% escalation on base tariff for 9 years in case of 2.475 MW. Similarly, the tariff for wet season is Rs 4.80 per kWh and for dry season is Rs 8.40 per kWh with 3% escalation on base tariff for 5 years for additional power of 2.525 MW. The contracted energy for the project is 30.95 million units (MU).

Moderate counter party risk

EHL is exposed to counter party payment risk pertaining to Nepal Electricity Authority (NEA), which has been making consecutive losses in past till FY16. However, as per the annual report published by NEA, during FY20 (provisional), NEA earned profit of Rs 11,056 Mn and gross cash accrual of Rs 16,056 Mn. The counter party payment risk is moderated by the fact that, NEA is fully owned by government of Nepal, and generating positive gross cash accruals. Further, NEA has been making timely payment to independent power producers (IPPs) in past. During FY20, the company has received payment from NEA for supply of power generated within 30 to 64 days.

Current demand & supply gap however expected increase in supply in future

As per the NEA’s Annual Report for FY20, the current peak electricity demand is 1,408MW. The total domestic installed capacity stands at 1,328 MW which includes 632 MW owned by NEA and 696 MW by private sector IPPs. Overall, during FY20, total energy demand was 7,894 GWh which was met by import of 1,720 GWh (~22% of total demand) from India whereas balance was met by domestic generation.

However, considering under construction projects which are expected to generate electricity in next 2-3 years and electricity demand which has not increased substantially in past few years could create a situation of oversupply in near future. This could put pressure in NEA’s payment capabilities which is sole counter party with majority of PPA signed by NEA are on take or pay basis.

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.

About the Company

Eastern Hydropower Limited (EHL) is a public limited company, incorporated in August 24, 2017 as a private limited company and later converted to public limited company in August 02, 2017. It is promoted by institutional investors and individual promoters having experience in different sectors for setting up Hydroelectric Project (HEP) in Nepal. EHL is involved in the operation of 5 MW run-of-the-river Pikhua Khola Small Hydropower Project (PKSHP) at Bhojpur District which has been in commercial operation since June 10, 2019. As per the Generation License, from Government of Nepal – Ministry of Energy, obtained on March 21, 2011 for PKSHP, 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 respectively. As on December 6, 2020, major shareholder of the company are M/S Smart Investment Company Pvt. Ltd (holds 8.06%), Mr. Narhang Rai (holds 7.94%), and Mr. Mohan Kumar Rai (holds 4.23%).

Brief Financial Performance during FY20 is as follows:

(Rs. In Million)

Particulars	FY20 (A)*
Income from Operations	89
PBILDIT	76
PAT	(69)
Interest Coverage Ratio (times)	0.76
Overall Gearing (times)	1.65

*Audited

Analyst Contact Ms. Elisha Lamichhane elisha.lamichhane@careratingsnepal.com Tel No.: +977-01-4012629	Group Head Ms. Shalini Sanghai shalini.sanghai@careratingsnepal.com Tel No.: +977-01-4012628	Relationship Contact Mr. Sajan Goyal sajan.goyal@careratingsnepal.com Tel No.: 9818832909/+977-01-4012628/29/30
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Annexure 1: Details of the Facilities rated

S. N.	Name of Bank	Type of the Facility	Amount (Rs. in Million)	Rating
1	Long Term Bank Facilities	Long Term Loan	737.15	CARE-NP D
2	Short Term Bank Facilities	Fund based Limits	30.00	CARE-NP D
	Total		767.15	