

Rating Rationale

Peoples Hydropower Company Limited

Rating

Facility/ Instrument	Amount (Rs. In Million)	Rating ¹	Rating Action
Issuer Rating	NA	CARE-NP BB (Is) [Double B (Issuer)]	Assigned
Long Term Bank Facilities	6,160.00	CARE-NP BB [Double B]	Reaffirmed
Short Term Bank Facilities	150.00	CARE-NP A4 [A Four]	Reaffirmed
Total Facilities	6,310.00		

* The issuer rating is subject to the company maintaining overall gearing not exceeding 2.10x at the end of FY22.

CARE Ratings Nepal Limited (CRNL) has assigned Issuer rating of ‘CARE-NP BB (Is)’ to Peoples Hydropower Company Limited (PHCL). Issuers with this rating are considered to have moderate risk of default regarding timely servicing of financial obligations, in Nepal. Also, CRNL has reaffirmed the rating of ‘CARE-NP BB’ assigned to the long-term bank facilities and ‘CARE-NP A4’ assigned to the short-term bank facilities of the company.

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of PHCL continue to be constrained by project implementation and stabilization risk including power evacuation risk where company is yet to revise its Required Commercial Operation Date (RCOD) in line with its expected COD of mid-October, 2021. The rating is also constrained by PHCL’s exposure to regulatory risk and volatile interest rates, geological risk and hydrology risk associated with run of the river power generation. The rating also factors in time overrun in the project; however, there is no change in the cost of the project. The rating, however, derives strength from board members and management having experience in hydro power sector and moderate counter party risk. The ratings also factors in achievement of financial closure for full project cost, relatively low cost of the project, presence of power purchase agreement (PPA) with sufficient period coverage, shortage of power in the country and government support for the power sector. The ability of PHCL to timely complete the project without any time or cost overrun, extension of RCOD to avoid late COD penalty and timely completion of transmission infrastructure are the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

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

Project implementation and stabilisation risk

On the basis of cost incurred till October 16, 2020, the company has achieved financial progress of ~49.5% of the total project cost. Company is expecting to complete the project by Mid-October, 2021 (however, expected COD was Mid-January, 2021 during last rating, which has been currently extended due to the impact of COVID 19) and is expected to revise RCOD with Nepal Electricity Authority (NEA). As per the progress report of December 2020 submitted by the company, overall tunnel works are completed by more than 90%. Hydro mechanical works are in progress and contract has been awarded for electro mechanical works, however delivery of equipment is pending. Though, there is major progress, the project is still exposed to the residual risks associated with project implementation and satisfactory operations thereafter. Timely completion of the project without cost overrun and satisfactory operations thereafter are the key rating sensitivities.

Power evacuation risk

The power generated from the project is proposed to be evacuated through 5.2Km long 132KV Transmission Line to Nepal Electricity Authority's (NEA) under construction Kirtipur Substation in Lamjung. Power from Kirtipur Substation will be further evacuated to Udipur Hub. Construction of transmission line from powerhouse to Kirtipur substation is within the scope of PHCL. The NEA kirtipur substation is expected to be completed within three/four months and transmission line from Kirtipur substation to Udipur Hub is expected to connect within next four/five months. Timely completion of the transmission lines and substations by both PHCL and NEA will be key rating sensitivity.

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). PHCL is proposed to utilize discharge from Dordi Khola having catchment area of 142.45 sq. kms based on snow-fed river. Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river/ Khola.

Geological Risk

The project area possesses significant geological risks as it is located in rough terrain and is likely to face adverse climatic condition during construction period. Access road is prone to landslides during monsoon.

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 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

PHCL has 7 Board of Directors, chaired by Mr. Udaya Nepali Shrestha, Masters, who has more than 40 years of experience including ~30 years of experience in different capacity in Government of Nepal. He has also served as Chairman of Nepal SBI Bank Ltd. and Nepal Investment Bank Ltd. in the past. Mr. Keshav Bahadur Rayamajhi, Managing Director, has more than 10 years of experience in hydropower sector apart from other management experience. He was Director of Global IME Bank Ltd. and was Chairman of Janata Bank Ltd. (now merged with Global IME Bank Ltd.). Management Team of PHCL is led by Mr. Rayamaji and he is supported by other experienced team members.

Financial closure achieved for the full project cost and relatively low cost of the project

The estimated cost of the project is Rs 8,800 Mn (i.e. Rs. 163 Mn per MW), which is relatively lower than the other hydropower projects in Nepal. The project cost is proposed to be funded in Debt equity ratio of 70:30 (i.e. Rs 6,160 Mn term loan and Rs 2,640 Mn equity). PHCL has achieved financial closure for the entire term loan requirement. Out of Rs 2,640 Mn of equity to be injected, till October 16, 2020, Rs. 1,869 Mn has been infused by shareholders. Out of the total project cost; PHCL has incurred Rs. 4,353 Mn till October 16, 2020.

Power purchase agreement with sufficient period coverage

PHCL had entered into a long term PPA with NEA as on February 25, 2015 for sale of 49.6 MW power to be generated from the project which was later amended on February 27, 2019 for additional 4.4 MW with total 54 MW power to be generated from the project. The contracted Plant Load Factor (PLF) for total 54 MW is 66.59%. Tariff rate as per PPA for 49.6 MW 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 8 years. In case of additional 4.4 MW, the definition of wet season is (June to November) and dry season is (December to May) with same tariff rate. Required Commercial Operation Date (RCOD) of the project was July 13, 2020 which has been extended till April 27, 2021.

Moderate counter party risk

PHCL 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 (Rs. 9,812 Mn during FY19) resulting the accumulated profit in its book. Further, during FY20, NEA achieved gross cash accrual of Rs 16,056 Mn (Rs 14,664 Mn in FY19). 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.

Shortage of power in the country

As per the NEA’s Annual Report for FY20, the current peak electricity demand is 1,408MW and the total domestic installed capacity stands at 1,328 MW. Overall, during FY20, total energy demand was 7,894 GWh which was met by import of 1,721 GWh 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 in wet season. This could put pressure on NEA’s payment capabilities which is sole counter party with majority of PPA signed 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

Peoples Hydropower Company Limited (PHCL) is a Public Limited company, incorporated as on October 9, 2007 as a Peoples Hydropower Company Private Limited and changed to public limited on February 27, 2019. The company has been set up to build, own and operate 54 MW run-of-river, Super Dordi Hydropower Project Kha (SDHPK) in Lamjung district of Nepal. The major shareholder of the company as on July 15, 2020 are Superdordi Investment Company Ltd. (holding 33.96%), Mr. Keshav Bahadur Rayamajhi (holding 5.26%) and Mr. Arjun Prasad Gautam (holding 5.23%).

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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	6,160.00	CARE-NP BB
Short Term Bank Facilities	Working Capital Loan	150.00	CARE-NP A4
Total		6,310.00	