

Rating Rationale
KBNR Isuwa Power Limited

Rating

Particulars	Amount (Rs. in Million)	Rating ¹	Rating Action
Long Term Bank Facilities- Term Loan	8,500.00	CARE-NP BB [Double B]	Assigned
Long Term Bank Facilities- Term Loan (Proposed)	570.66	CARE-NP BB [Double B]	Assigned
Short Term Bank Facilities- Working Capital Loan	100.00	CARE-NP A4 [A Four]	Assigned
Short Term Bank Facilities- Fund based (Proposed)	329.34	CARE-NP A4 [A Four]	Assigned
Total Facilities	9,500.00		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned rating of ‘CARE-NP BB’ to the long term bank facilities and ‘CARE-NP A4’ to the short term bank facilities of KBNR Isuwa Power Limited (KBNR).

Detailed Rationale & Key Rating Drivers

The ratings assigned to KBNR are constrained by the early stage of construction of the project leading to high project implementation and stabilization risk associated with the project. The rating is also constrained by hydrology risk associated with run-of-the-river power generation, however minimized due to peaking reservoir, power evacuation risk and exposure to volatile interest rates. The ratings, however, derive strength from the experienced promoters and management team in hydropower sector, presence of power purchase agreement (PPA) with sufficient period coverage, moderate counter party risk, financial closure achieved for majority of the project cost and relatively low cost of power project. 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 timely execution of the project within Required Commercial Operation Date (RCOD) avoiding any time or cost overrun and the sufficient hydrology and timely receipt of the payment from the Nepal Electricity Authority (NEA) are the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Project implementation and stabilization risk

The project includes 6911.53m long headrace pipe, 2500m long steel penstock pipe, four turbines, four generators and four transformers. The contract for civil works, hydro-mechanical works, electro-mechanical works and transmission line works have been awarded. The project is at the preliminary stage

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

of construction. Till February 12, 2021, ~19.05% of the total project cost (i.e. Rs. 2,159.88 Mn) has been incurred which is being funded through equity share capital and bank loan. As per the progress report of February 2021, the access road up to powerhouse and to headwork is almost completed, the construction of permanent camp near powerhouse area is completed. The excavation along with the headrace pipe alignment has been started. As the major part of the project is yet to be initiated, 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.

Hydrology risk associated with run-of-the-river power generation, however minimized due to peaking reservoir

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-May to Mid –November) and less during the dry season (Mid-November to Mid-May). KBNR is proposed to utilize discharge from Ishuwa Khola having catchment area of 160.79 sq. kms based on snow fed perennial river. Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river/ khola. However, the risk is minimized to some extent in the project due to peaking reservoir of 6 hours for dry season which will be used during peak time of dry season.

Power Evacuation Risk

The Power generated from the project is proposed to be evacuated through ~22km long double circuit 230kV Transmission Line to Sitalpati Substation of Nepal Electricity Authority (NEA), in Sankhuwasabha district which is under construction and as per the management, it is expected to be completed within December 2021. The construction of transmission line from powerhouse to Sitalpati substation is within the scope of KBNR. Timely completion of the transmission lines and substation will be key rating sensitivity.

Key Rating Strengths:

Experienced Promoters and directors in hydropower sector

KBNR is promoted by single institutional promoter i.e. Himel Dolakha Hydropower Company Limited (HDHCL) and a group of individual promoters from different background and experience. KBNR has total 3 Board of Directors chaired by Mr. Birendra Bahadur Neupane who has more than 39 years of experience in civil construction including experience in hydropower sector. He is also the major promoter of the company. He has been associated in various operational hydropower projects under HDHCL and Joshi Hydropower Development Company Limited and under-constructed hydropower projects.

Power purchase agreement with sufficient period coverage

KBNR had entered into a long term PPA with NEA as on October 12, 2018 for sale of 97.2 MW power to be generated from the project. The contracted Plant Load Factor (PLF) for total 97.2 MW is 79.19% at probability of exceedance of 59% with total contracted energy of 674.30 MU (i.e. 262.54 MU for dry season and 411.76 MU for wet season). PPA has been entered for the period of 30 years from the COD or till validity of generation license (obtained on June 09, 2020 for 35 years) whichever is earlier. Tariff rate as per PPA is Rs 4.80 per KWh for wet season (Mid-May to Mid-November) and the tariff rate for peak dry season (Mid-November to Mid-May) is Rs 8.55 to 10.55 per KWh depending on the peak hours while the non-peak rate for the dry season (Mid-November to Mid-July) is 8.40 per Kwh, with 3% annual escalation on base tariff for 8 years. Required Commercial Operation (RCOD) of the project is July 17, 2023. However, as per the letter from the Ministry of Energy, Water Resources and Irrigation of Nepal dated March 24, 2021, the RCOD is to be extended for under constructed hydropower projects which are effected by COVID-19 restrictions on receiving the application for the same. If COD doesn't fall within RCOD, the company is bound to pay late COD penalty to NEA. Further, if COD is delayed by 6 months to 18 months from RCOD, then the number of escalations in tariff rate will decrease to 7 times from 8 times. As against PPA period of 30 years, the tenor of project debt is 12 years. The PPA is under the take-or-pay modality, which eliminates the risks related to tariff and offtake of the energy to be generated by the project.

Financial closure achieved for majority of project cost

The total cost of the project is envisaged at Rs. 11,338.33 Mn to be funded in debt equity ratio of 80:20 (debt of Rs. 9,070.66 Mn and equity of Rs. 2,267.67 Mn). KBNR has achieved the financial closure of Rs. 8,500 Mn till date, which is ~94% of total debt requirement for the project. The financial closure for the remaining term loan amount of Rs. 570.66 Mn is yet to be achieved. As per the consortium agreement, if the deficit funding of Rs. 570.66 Mn for full financial closure is not arranged fully or partly, the borrower shall manage the deficit funding through additional equity injection for timely completion of the project.

Moderate counter party risk

KBNR 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 in accumulated profit in its books. 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.

Current demand & supply gap coupled with increasing demand for power in the country

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. Further, no income source will be asked for investment made within mid-April 2020 in hydro-electricity project. Also, Unified Directive of 2020/21, has directed “Class-A” to allocate minimum 10% of credit to energy sector and “Class-B” and “Class-C” banks to allocate minimum 20% and 15% of total credit respectively to agriculture, energy, SMEs and tourism sector within mid-July 2024.

Relatively low cost of power project

The estimated project cost is Rs. 11,337.38 Mn including Interest During Construction (IDC) for setting up of a 97.2MW Isuwa Khola Hydropower Project (IKHP) in Makalu rural Municipality, Sankhuwasabha district of Nepal. The cost per MW of the project is Rs. 116.64 Mn, which is comparatively lower than other hydropower plants in Nepal.

About the Company

KBNR Isuwa Power Limited (KBNR) is a public limited company, incorporated on December 18, 2017. It is promoted by an institutional promoter and a group of individual promoters to develop Hydropower in Nepal under “BOOT” (Build, Own, Operate and Transfer) model. KBNR is setting up Isuwa Khola Hydropower Project (IKHP) in Sankhuwasabha district of Nepal. The project is proposed to utilize available head and flow from Isuwa Khola (river), which is a tributary of Arun river.

<p>Analyst Contact Mr. Rujan Bajracharya rujan.b@careratingsnepal.com Tel No.: +977-01-4012629</p>	<p>Group Head Mr. Shisir Pokharel shisir.pokharel@careratingsnepal.com Tel No.: +977-01-4012628</p>	<p>Relationship Contact Mr. Sajan Goyal sajan.goyal@careratingsnepal.com Tel No.: 9818832909/+977-01-4012628/29/30</p>
---	--	---

Disclaimer

CRNL's ratings are opinions on credit quality and are not recommendations to sanction, renew, disburse or recall the concerned bank facilities or to buy, sell or hold any security. CRNL has based its ratings on information obtained from sources believed by it to be accurate and reliable. CRNL does not, however, guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. Most entities whose bank facilities/instruments are rated by CRNL have paid a credit rating fee, based on the amount and type of bank facilities/instruments.

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	Term Loan	8,500.00	CARE-NP BB [Double B]
2	Long Term Bank Facilities (Proposed)	Term Loan	570.66	CARE-NP BB [Double B]
2	Short Term Bank Facilities	Working Capital Loan	100.00	CARE-NP A4 [A Four]
3	Short Term Bank Facilities (Proposed)	Fund based	329.34	CARE-NP A4 [A Four]
Total Bank Facilities			9,500.00	