

**Rating Rationale**  
**Peoples Power Limited**

**Rating**

Particulars	Amount (Rs. in Million)	Rating <sup>1</sup>	Rating Action
Issuer Rating	NA	CARE-NP BB (Is) [Double B (Issuer)]	Assigned

\* The issuer rating is subject to the company maintaining overall gearing not exceeding 2.0x at the end of FY22.

CARE Ratings Nepal Limited (CRNL) has assigned Issuer rating of ‘CARE-NP BB (Is)’ to Peoples Power Limited. Issuers with this rating are considered to offer moderate risk of default regarding timely servicing of financial obligations in Nepal.

**Detailed Rationale & Key Rating Drivers**

The issuer rating assigned to **Peoples Power Limited** (PPL) is constrained by residual project implementation and stabilization risk, hydrology risk associated with run-of-the-river power generation, exposure to regulatory risk and volatile interest rates.

The rating, however, derives strength from the experienced promoters and management team, presence of power purchase agreement (PPA) with sufficient period coverage, and low power evacuation risk. The rating also factors in current demand & supply gap however possible oversupply in future, moderate counter party risk and government support for the power sector.

*Going forward, the ability the company to successful execute the project within cost and time estimates and early stabilization thereafter are the key rating sensitivities.*

**Detailed Description of the Key Rating Drivers**

**Key Rating Weaknesses**

***Residual Project implementation and stabilization risk***

PPL is setting up a 4.96 MW Upper Puwa-II hydropower project in Ilam district of Nepal. The total cost of the green-field project is estimated at Rs. 928.99 Mn which will be funded by term loan of Rs. 600.00 Mn, and remaining from the promoter’s contribution. The debt of the same has been tied up and the commercial operation is expected in September 2021. Out of the total capex planned, as on March 25, 2021, the company has incurred a total expenditure of Rs. 719.17 Mn and the same is funded through bank loan of Rs. 500.83 Mn and remaining through promoters’ contribution. Though the plant is in the advance stages of installation and any delays in the implementation may impact adversely on the company’s financial risk profile and is also crucial from credit perspective.

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

***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 (June to November) and less during the winter season (December to May). PPL is proposed to utilize discharge from Puwa Khola having catchment area of 63.90 sq kms with 2.72 m<sup>3</sup>/s design discharge at 40% exceedance flow, based on perennial river. Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river.

***Exposure to regulatory risk***

Government of Nepal (GON) has recently established Nepal Electricity Regulatory Commission (NERC) for regulating generation, transmission and distribution of electricity in Nepal. NERC has issued a directive to take approval before public issuance of share capital. It poses a new challenge to hydropower companies which has to go through an additional approval process before it can issue shares to public. Hence, the hydropower companies planning for public issuance of share capital is exposed to risk associated with delay in approval process which may delay project funding and eventually delay the project.

***Exposure to volatile interest rate***

Interest rate is determined by adding certain percentage of premium (risk premium) on quarterly base rate and interest rate will be changed accordingly on quarterly basis. Base rate of the Bank and Financial Institutions is changed 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 are exposed to volatile interest rate.

**Key Rating Strengths*****Experienced Promoters and Management team***

PPL has four board of directors, chaired by Mr. Bharat Khatri who has more than 20 years of experience in legal sector and has worked as Public director of Api Power Company Limited [CARE-NP B+ (Is)] for a tenor of four years. He is also working as a legal consultant in different business houses in Nepal, especially airways, stock exchange, insurance companies and hydro companies.

Mr. Birendra Bahadur Neupane is the previous chairperson of the company and is also one of the major promoters of PPL. He has more than 39 years of experience in civil construction including 15 years of experience in hydropower sector.

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

PPL had entered into a long term PPA with Nepal Electricity Authority (NEA) as on August 21, 2017 for sale of 4.96MW power to be generated from the project. The period of the PPA is 30 years from the date of COD or till validity of Generation License, whichever is earlier. PPA period may be extended with

mutual consensus during the last six months of validity. The tariff for wet season (June to November) is Rs 4.80 per kWh and for dry season (December to May) is Rs 8.40 per kWh with 3% escalation on base tariff for 8 years.

If COD doesn't fall within RCOD, the company is bound to pay penalty to NEA as per the PPA. Further, number of escalations in tariff rate will be reduced if there is delay in COD of the project than RCOD by more than 6 months. As per the letter from the Ministry of Energy, Water Resources and Irrigation of Nepal dt. 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.

***Low Power evacuation risk***

The power generated from the project is proposed to be evacuated through ~6 km 33 kV distribution line to the Upper Puwa I substation, which is then connected to the Nepal Electricity Authority (NEA's) power grid line passing through Puwa Khola Bazar. Construction of transmission line from powerhouse to Upper Puwa I substation is within the scope of PPL and the contract for transmission line has been awarded. There is a low power evacuation risk as the Upper Puwa I substation is already operational which is being connected to the NEA's power grid. However, the timely completion of the transmission line by PPL will be critical for the revenue generation.

***Moderate counter party risk***

PPL 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.

***Current demand & supply gap however possible oversupply 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 1,721 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. 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. Also, GoN has waived off the under-supply penalty charges for hydropower having installed capacity less than 10 MW.

**About the Company**

Peoples Power Limited (PPL) was incorporated as on January 26, 2017. It is promoted by individual promoters from different backgrounds for setting up of a 4.96MW run-of-river Upper Puwa-II. The project is being constructed under “BOOT” (Build, Own, Operate and transfer) model and is located in Sakhejung and Maipokhari VDC of Ilam district of Nepal.

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