

## Modi Energy Limited

### Ratings

Instrument / Facilities	Amount (Rs. In Million)	Rating <sup>[1]</sup>	Rating Action
Issuer Rating	NA	CARE-NP BB+ (Is) [Double B Plus (Issuer)]	Assigned
Long Term Bank Facilities	4,014.15	CARE-NP BB+ [Double B Plus]	Assigned
<b>Total Facilities</b>	<b>4,014.15 [ Four Thousand Fourteen Million One Hundred and Fifty Thousand Only]</b>		

\*The issuer rating is subject to the company maintaining overall gearing not exceeding 2.50x at the end of FY22.

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned Issuer rating of 'CARE-NP BB+ (Is) [Double B Plus (Issuer Rating)]' to Modi Energy Limited (MEL). Issuers with this rating are considered to have moderate degree of safety regarding timely servicing of financial obligations, in Nepal.

Also, CRNL has assigned the rating of 'CARE-NP BB+' for the long-term bank facilities of Modi Energy Limited (MEL).

### Detailed Rationale & Key Rating Drivers

The ratings assigned to Modi Energy Limited (MEL) is constrained by post implementation risk associated with its green field debt funded project, hydrology risk associated with run-of-the-river power generation and exposure to regulatory risk.

The ratings, however, derives strength experienced promoters' and management team, presence of power purchase agreement (PPA) with sufficient period coverage, government favourable policies for the sector and moderate counter party risk.

*Going forward, the ability of the company to achieve early stabilization of operations of the newly commissioned hydro power project and improvement in capital structure are the key rating sensitivities.*

### Detailed description of the key rating drivers

#### Key Rating Weaknesses

#### **Post implementation risk associated with its green field debt funded project**

As on June 14, 2021, MEL had incurred an expenditure of Rs. 5,509.84 Mn towards the project which has a total cost of Rs. 6,062.38 Mn. The expenditure incurred has been funded through term loan of Rs. 3,925.51 Mn and balance from the promoters' contribution in the form of equity capital. The plant is in the final stages of installation and trial runs of the plant has already been started. It is expected that the commercial production would commence in September 2021. Post project implementation, the project is exposed to risk in the form of stabilization and streamlining of the facilities and considering a new unit the same remains to be seen.

Furthermore, there has been in a significant delay in commencement of commercial operations which led to change in timelines of required commercial operation date (RCOD). The Required RCOD of the project was July 15, 2020 and the company has submitted the requisite documents to NEA for the revision of same. Due to change in scope of project and additional challenges (damage in headrace tunnel, leakages in tunnel etc) faced during implementation, the cost of

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

project revised from the initial envisaged estimates of Rs. 3,509.28 Mn which is relatively high per MW project cost. Considering the high project cost, to achieve the envisaged scale of business is crucial for the company.

***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 (Mid-April to Mid-December) and less during the winter season (Mid- December to Mid-April). The project is proposed to utilize discharge from Modi Khola and Pati Khola having catchment area of 552 sq kms based on snow fed Perennial River. The project has 26.52 m<sup>3</sup>/s design discharge at 40% exceedance flow. Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river/khola.

***Exposure to volatile interest rate***

Nepalese banking sectors are fixing floating 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 (BFIs) remains volatile to change in liquidity position which lead to change in interest rate. Interest rate has been changing frequently in Nepal market since last 2-3 years. Therefore, funding from BFIs is subject to volatile interest rate.

***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**

***Experienced promoters, directors and management in various sector***

MEL derives strength from its established promoters belonging to the Debenara group, Murarka organization, KL Dugar Group and Shanker Group. The groups are involved in diversified business interest viz. manufacturing, trading, power generation and other business. Company has five board members, chaired by Mr. Pashupati Murarka, who is also managing director of Muraraka group and has more than 35 years of work experience. Other directors of the company have also wide range of experience in various sector. Mr. Gyanendra Lal Pradhan, Director, has more 25 years of experience in different sector including Hydropower. He is also an executive Chairman of Hydro solutions Pvt Ltd. and Chairman at Nepal Hydro Developer Limited. He has been supported by other experience management team members.

***Power purchase agreement with sufficient period coverage and moderate counter party risk***

MEL had entered into a PPA with NEA as on September 06, 2011 for sale of 20 MW power to be generated from the project. The period of the PPA is 30 years from commercial operation date (COD) or till validity of Generation License (obtained on September 06, 2010 for 35 years), whichever is earlier. The contracted energy Plant load factor (PLF) for the project is 66.86% with total contracted energy of 117.14 million units (MU). The tariff for wet season (Mid-April to Mid-December) is Rs 4.80 per kWh and for dry season (Mid- December to Mid-April) is Rs 8.40 per kWh with 3% escalation on base tariff for 5 times in every year after completion of 12 months from COD date. 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.

The company has signed PPA with NEA is owned by Government of Nepal and hence counter party default risk is low; however, timely realization of critical for the company and from analytical perspective also.

***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. As per various directives from NRB whereby all the banks (type A, B C, D) have to allocate minimum share of their total advances to energy sector which argues well for the sector.

**About the Company**

Modi Energy Limited (MEL) was incorporated as Manang Trade Link Pvt Ltd in November 04, 1996. Later on, the name was changed into Modi Energy Pvt Ltd in May 2017. The company got converted into public limited in June 2018. The company was promoted with objective to setup hydroelectric Project (HEP) of 20 MW run-of-river, Tallo Modi Khola Hydropower Project (TMKHP). The project is being constructed under “BOOT” (Build, Own, Operate and transfer) model and is located in Parbat district of Nepal.

**Annexure 1: Details of Instrument / Facilities**

Name of the Instrument / Bank Facilities	Type of the Facility	Amount (Rs. in Million)	Rating assigned
Long Term Bank Facilities	Term Loan	4,014.15	CARE-NP BB+
<b>Total</b>		<b>4,014.15</b>	

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