

## Salmani Devi Hydropower Private Limited

### Ratings

Instrument	Amount (Rs. in Million)	Rating <sup>1</sup>	Rating Action
Long Term Bank Facilities	498.72	CARE-NP BB+ [Double B Plus]	Assigned
Short Term Bank Facilities	51.28	CARE-NP A4+ [A Four Plus]	Assigned
<b>Total Facilities</b>	<b>550.00</b>		

\*Details of instrument / facilities in Annexure-1

CARE Ratings Nepal Limited (CRNL) has assigned the ratings of 'CARE-NP BB+' to the long-term bank facilities and 'CARE-NP A4+' to the short-term bank facilities of Salmani Devi Hydropower Private Limited (SDHPL).

### Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of SDHPL are constrained by small scale and short track of operations, weak operating performance in the initial years of operations, its modest debt service coverage indicators and leveraged capital structure. Additionally, the rating also factors in hydrology risk with run-of-the-river power generation project and exposure to volatile interest rate.

The ratings, however, derive strength from the experienced directors and management team, presence of power purchase agreement (PPA) with sufficient period coverage, current demand & supply gap, government favourable policies for the sector and moderate counter party risk.

*Going forward, the ability of the company to reduce the gap between operational and contracted plant load factor (PLF) along with the timely receipt of payments from Nepal Electricity Authority (NEA), significant reduction in debt levels are the key rating sensitivities.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weakness

##### **Short track record and small scale of operations**

SDHPL started with its commercial production in June 2019 and has a relatively short track record of operations. The company achieved a turnover of Rs. 67 Mn in the first full year of business operations during FY20 (FY refers to 12 months' period ended in mid-July). Furthermore, post project implementation risk in the form of stabilization of the operations to achieve the envisaged scale of business remains crucial for achieving its contracted energy production.

With the small scale of operations, its operations are highly susceptible to any business shock arising due to unfavourable business parameters. Furthermore, it also results into increased vulnerability of its financial risk profile and limits the company's financial flexibility in times of stress and deprives it from scale benefits.

##### **Weak operating performance and stabilization risk associated with newly setup hydropower project**

SDHPL is the business of power generation through its 3.33 MW run-of-the-river project in Doti District, Nepal. The hydro power project has annual contracted PLF of 18.96 million units (MU) which is 65.01% of the installed capacity of the plant. The company has weak operating performance and the power generation from the project as a %age to the contracted power per annum (as per PPA) was 64.25% and 78.55% for FY20 & FY21 respectively. The total energy generated from the project was lower than the contracted energy mainly due to hydrology issues associated with run

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

of river project. Attributed to same, the company had paid short supply penalty of Rs. 4.85 Mn during FY20 and Rs. 0.14 Mn in FY21. In FY21 (based on provisional results), SDHPL has generated 14.90 MU of electricity and reported TOI of Rs. 85 Mn, a growth of ~19% over FY20.

SDHPL is currently evacuating its power through NEA's 33kV BP Nagar Substation in Doti district. The total length of transmission line from powerhouse to Substation is ~3 km. However, due to low voltage capacity of transmission line, the company is facing tripping problem during high peak hour period. The stabilisation of power evacuation is critical from stable revenue generation and crucial from analytical prospective.

#### ***Below averages financial risk profile***

In FY20, the company has comfortable PBILDT margin which stood at ~76%; however, SDHPL reported net loss of Rs. 45.45 Mn due to high interest cost and depreciation cost. Furthermore, the company has leveraged capital structure marked by overall gearing of 2.34 times as on mid-July 2020 and the same is expected to remain high in near future due to low repayments of loan initially coupled with low net worth base due to losses reported by the company. Also the debt service coverage indicators of the company remained stressed in the initial year of operations due to weak operating performance and the interest coverage ratio was below unity in 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). KKHP utilizes discharge from Kapadigad Khola having catchment area of 125.33 sq. kms based on Perennial River. 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.

#### **Key Rating Strengths**

##### ***Experienced directors and management in various sector***

SDHPL is managed under overall guidance of the company's Board of Directors (BoD), who possesses wide experience in various sectors including hydropower sector. SDHPL has three Board of directors, chaired by Ms. Uma Dahal, who has more than 25 years of experience. SDHPL's management team is led by Mr. Peras Dahal, who has more than 10 years of experience in different sectors.

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

SDHPL had entered into a PPA with NEA on March 25, 2013 for sale of 3.33 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 December 30, 2013 for 35 years), whichever is earlier. The tariff for wet season (Mid-April to Mid-December) is Rs.

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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.

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 prospective 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.

***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) has to allocate minimum share of their total advances to energy sector which argues well for the sector.

**About the Company**

Salmani Devi Hydropower (SDHPL) is a Private company, incorporated on August 2, 2009. The company was promoted with an objective to setup a run-of-river Hydroelectric Project (HEP) of 3.33 MW in Doti district of Nepal. The commercial operation of the same started in June 2019. The project is being constructed under "BOOT" (Build, Own, Operate and transfer) model.

**Financial Performance**

For the Period Ended / as at Mid-July,	(Rs. in Million)
	2020 (12m, A)
Total Operating Income	67.46
PBILDT Margin (%)	75.66
Overall Gearing Ratio (times)	2.34
Interest Coverage (times)	0.84
Current Ratio (times)	0.73

A: Audited

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

Name of the Instrument / Bank Facilities	Type of the Facility	Amount (Rs. In Million)	Ratings assigned
Long Term Bank Facilities	Term Loan	498.72	CARE-NP BB+
Short Term Bank Facilities	Fund Based Limits	25.00	CARE-NP A4+
Short Term Bank Facilities- Proposed	-	26.28	CARE-NP A4+
<b>Total</b>		<b>550.00</b>	

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