

Eastern Hydropower Limited

Ratings

Facilities	Amount (Rs. Million)	Rating ¹	Rating Action
Issuer Rating	NA	CARE-NP B+ (Is) [Single B plus Issuer]	Revised from CARE-NP D
Long Term Bank Facilities	736.93 (Decreased from Rs. 737.15 Mn)	CARE-NP B+ [Single B Plus]	Revised from CARE-NP D
Short Term Bank Facilities	30.00	CARE-NP A4 [A Four]	Revised from CARE-NP D
Total facilities	766.93 (Seven Hundred Sixty Six Million and Nine Hundred Thirty Thousand only)		

**The issuer rating is subject to overall gearing ratio of the company being maintained at 1.75x at the end of FY22*

Details of instruments/facilities in Annexure-1

CARE Ratings Nepal Limited (CRNL) has revised Issuer rating to 'CARE-NP B+ (Is)' to Eastern Hydropower Limited (EHL). Issuers with this rating are considered to have high risk of default regarding timely servicing of financial obligations in Nepal.

Also, CRNL has revised the rating to 'CARE-NP B+' assigned to the long term bank facilities and to 'CARE-NP A4' assigned to the short term bank facilities of Eastern Hydropower Limited (EHL).

Detailed Rationale & Key Rating Drivers

The revision in ratings assigned to the bank facilities and Issuer rating of EHL considers improvement in debt servicing track record and improvement in financial risk profile during FY21 (Unaudited; refers to 12 months' period ended mid- July 2021). However, the ratings continue to be constrained by subdued operating performance, power evacuation risk, hydrology risk associated with run-of-the-river power generation and exposure to regulatory risk.

The ratings, however, derive strength from experienced board members and management team, presence of power purchase agreement with sufficient period coverage and moderate counter party risk. The ratings also factor in current demand & supply gap and government support for the power sector.

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) are the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Improvement in debt servicing track record

There were instances of delay in the repayment of interest and principal obligations during FY20 and FY21. This was mainly attributable to delay in commencement of operations coupled with post-project implementation risk in the form of stabilization of the power generation and its evacuation. The same led to low energy generation and availability of free cash accruals from the project to meet its debt obligations. During FY21, the liquidity of the company has improved due to avilment of short-term bank borrowings and infusion by the promoters in the form of unsecured loan. The improvement in liquidity has also been supported by improvement in the operational efficiency leading to higher revenue generation and company started honoring its installments timely from July 2021 onwards. There has been no delay in the interest and repayments of the term loan since Q4FY21. Furthermore, company's ability to improve its operating performance and realize its debtors in a timely manner would also be crucial for timely debt servicing.

¹Complete definition of the ratings assigned are available at www.careratingsnepal.com and other CARE publications

Subdued operating performance

The annual contracted PLF for Pikhwa Khola Small Hydroelectric Project (PKSHP) is 70.67% of the installed capacity of the plant; however, the project has been operated at a low PLF over the period. During FY21, PLF of the project was low at 47.81% (over generation capacity) which improved from 42.09% during FY20. Company has weak operating performance due to energy loss on account of evacuation issues. It is crucial for the company to reduce the gap between the operational and contracted plant load factor for having a stable revenue profile and cash flows.

Improvement in financial profile in FY21 though continued to remain modest

EHL is generating revenue by the selling of power generated through its 5 MW hydra power project. The company reported improvement in total operating income by around 11.80% to Rs. 100 Mn in FY21 (Unaudited; FY21 refer to 12 months ending on Mid-July 2021) from Rs. 89 Mn in FY20. Accordingly, PBILDT also increased to Rs. 84 Mn in FY21 (FY20: Rs. 76 Mn) on account of scaling up of operations. However, PBILDT margin remained almost stable at around 85%. The company reported net loss during FY21 majorly due to high depreciation and gross cash accruals stood at 16 Mn.

The capital structure of the company is leveraged with overall gearing ratio stood at 1.78x as on mid-July FY21. During FY21, the coverage indicators also stood weak as reflected from interest coverage ratio and total debt to Gross Cash Accruals (GCA) of 1.21x and 50.75x respectively.

Power evacuation risk

The power generated from PKSHP was evacuated through 4 km long 33 KVA transmission Line which was transmitting higher power than its carrying capacity. This resulted regular breakdowns and transmission losses during FY20 and FY21. Under temporary arrangement, NEA constructed 25 km long 33KVA transmission line from Bhojpur to Tumling Tar at the end of FY21 leading to diversion of line and reducing the load on the transmission line. Apart from the load reduction, NEA has constructed dedicated line from Bhojpur to Inaruwa which is expected to come into operation in next 2-3 months and accordingly, transmission line loss is expected to reduce. Timely operation of the new transmission lines and smooth evacuation of power without any significant tripping is crucial from analytical perspective and also for the company to improve its operating efficiencies.

Hydrology risk associated with run-of-the-river power generation

Run-of-the-river (ROR) 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). PKSHP utilizes discharge from Pikhwa Khola having catchment area of 117 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.

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 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 board members and management team

EHL has 7 Board of Directors, chaired by Mrs. Susan Karmacharya who has more than 26 years of experience in various sectors. Currently, she is chairperson in Money Plant Investment Company Pvt. Ltd and a vice chairperson at Laligurans Batika School and Namuna Hospital. Mr. Dhan Bahadur Shrestha, Managing Director, has ~36 years of experience in different sectors and worked as a Joint Secretary of Ministry of Federal Affairs and Local Development and Ministry of Labor and Employment. Apart from that, the day to day activities are run by experienced management team.

Power purchase agreement with sufficient period coverage

EHL entered into PPA with NEA for 5 MW on November 13, 2016 for sale of entire power generated by PKSHP. The PPA is valid for a period of 30 years from Commercial Operation date (COD). The tariff for wet season (Mid-April to Mid-December) is Rs 4 per kWh and for dry season (Mid-December to Mid-April) is Rs 7 per kWh with 3% escalation on base tariff for 9 years in case of 2.475 MW. Similarly, the tariff for wet season is Rs 4.80 per kWh and for dry season is Rs 8.40 per kWh with 3% escalation on base tariff for 5 years for additional capacity of 2.525 MW. The contracted energy for the project is 30.95 million units (MU).

Favourable Government policies towards 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

EHL is a Public Company, incorporated on August 4, 2017, promoted by institutional as well as individual promoters from different background. It is currently operating a 5 MW Pikhua Khola Small Hydropower Project (PKSHP) in run –of –river scheme located at Bhojpur district, Nepal. The project has been constructed under BOOT (Build, own, Operate and Transfer) mechanism.

Financial Performance

(Rs. In Million)

Particulars	FY20	FY21
	(A)	(UA)
Income from Operations	89	100
PBILDT Margin (%)	85.68	84.70
Overall Gearing (times)	1.65	1.78
Interest coverage (times)	0.76	1.21
Current Ratio (times)	0.75	0.92
Total Debt to Gross Cash Accruals(times)	-ve	50.75

A: Audited, UA: Unaudited

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	736.93	CARE-NP B+
Short Term Bank Facilities	Overdraft	30.00	CARE-NP A4
Total		766.93	

Contact us**Analyst**

Ms. Anjali Bhandari
Contact No.: 977-01-4012629
Email: anjali.bhandari@careratingsnepal.com

Senior Manager

Ms. Shalini Sanghai
Contact No.: +977-01-4012629
Email: shalini.sanghai@careratingsnepal.com

Relationship Contact

Name: Achin Nirwani
Contact No.: +977 9818832909
Email: achin.nirwani@careratingsnepal.com

About CARE Ratings:

CARE Ratings Nepal Limited (CRNL) is licensed by the Securities Board of Nepal w.e.f. November 16, 2017. CRNL is supported by CARE Ratings Limited through a technical services agreement to provide technical support in the areas such as rating systems and procedures, methodologies, etc. from CARE Ratings on an ongoing basis. The technical support shall ensure that CRNL has adequate resources to provide high quality credit opinions in Nepal.

Our parent company, CARE Ratings Limited commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI).

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. In case of partnership/proprietary concerns, the rating assigned by CARE is, inter-alia, based on the capital deployed by the partners/proprietor and the financial strength of the firm at present. The rating may undergo change in case of withdrawal of capital or the unsecured loans brought in by the partners/proprietor in addition to the financial performance and other relevant factors. CARE is not responsible for any errors and states that it has no financial liability whatsoever to the users of CARE's rating.