

Rawa Energy Development Limited

Ratings

Facilities	Amount (Rs. Million)	Rating ¹	Rating Action
Issuer Rating	NA	CARE-NP BB (Is) [Double B (Issuer)]	Assigned

* The issuer rating is subject to overall gearing ratio of the company not exceeding 3.00x pre-Initial Public Offering (IPO) at the end of FY22.

Details of instruments/facilities in Annexure-1

CARE Ratings Nepal Limited (CRNL) has assigned the issuer rating assigned of 'CARE-NP BB (Is)' to Rawa Energy Development Limited (REDL). Issuers with this rating are considered to have moderate risk of default regarding timely servicing of financial obligations in Nepal.

Detailed Rationale & Key Rating Drivers

The issuer rating assigned to REDL factors in project stabilization risk, hydrology risk associated with run-of-the-river power generation, exposure to volatile interest rate risk and regulatory risk.

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

Going forward, the ability of the company to successful stabilization of the operations of hydro power project and generate energy equivalent to contracted are the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Weaknesses

Project stabilization risk

During FY21 (FY refers to 12 months ending in Mid-July), the company reported the total income of Rs. 4 Mn through the sale of electricity with the Plant Load Factor (PLF) of 20.53% and 43.30% during 7MFY22 (refer to 7 months period ending in Mid-February 2022). The project was shut down during Mid-November 2020 to Mid-August 2021 due to breakdown in the generator. The annual contracted PLF for the project is 63.99% of the installed capacity of the plant. For the year ended FY21, the company generated energy equivalent to 21.13% of contracted PLF and the same improved to 61.36% in 7MFY22.

The project came into an operation in September 20, 2020. However, the projected was impacted during FY21 due to the breakdown in generator as a result the plant was shut for the 8 months till Mid-August 2021. This led to delay in stabilization of the operations of hydro power project, resulting in stressed liquidity and cash flow mismatches. The same led to instances of delay in the repayment of term loan interest and installments in past.

The company has a relatively short track record of operations and faced challenges in the initial period of its operations. Therefore, post project implementation risk in the form of stabilization of its operations to achieve the envisaged scale of business remains crucial from rating perspective.

Relatively High project cost and leveraged capital structure

The total cost of the project was Rs. 686 Mn (i.e., Rs. 229 Mn per MW) which was funded through the debt amount of Rs. 470 Mn and remaining through equity. The company has taken the extended period from its creditors for making payments (creditors of project) and expected to make payment in next couple of months or through IPO proceeds. The high project cost was on

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

account of modification of the physical structure in powerhouse. Further due to the non-completion of the NEA transmission line, Interest during Construction (IDC) cost increased due to the increase in project period.

The overall gearing ratio of the company stood at 2.94x during FY21. The leveraged gearing ratio was on account of the high debt funded capital expenditure done by the company to set up the hydro power project and erosion of networth due to losses in the initial years of operations. The company also reported cash losses in FY21 and total debt to Gross Cash Accrual ratio stood negative for the said period.

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). The project utilizes discharge from Rawa Khola having catchment area of 68 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 rates

Nepalese banking sectors are fixing lending interest rate based on quarterly base rate and interest rate will be changed accordingly on quarterly basis. Due to tight liquidity in the market, the interest rate has been high and volatile during the last 12 months. Therefore, funding from Bank and Financial Institutions is exposed 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 Strength

Experienced board members and management team in hydropower sector

REDL is managed under the overall guidance of the company's Board of Directors (BoD), who possesses wide experience in the various sector including hydropower projects. Company has 7 directors in BOD, Chaired by Badri Prasad Gautam who has more than 30 years of experience in various sector. He is also a director at Mid-Solu Hydropower Company Limited (MSHCL) and Halesi Urja Private Limited. Mr. Rajendra Prasad Gautam, director, has more than 35 years of experience in various sectors. He is also director at MSHCL and Dolti Power Company Private Limited and he is supported by other experience team members.

Power purchase agreement with sufficient period coverage

REDL had entered into a PPA with NEA as on August 08, 2016 for sale of 2.8 MW power to be generated from the project and later amended to 3MW on August 29, 2018. The period of the PPA is 30 years from commercial operation date (COD) or till validity of Generation License whichever is earlier. 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 every year for 9 times after completion of 12 months from COD date. The contracted energy for the project is 16.82 million units (MU) at PLF of ~64%.

Favorable 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

Rawa Energy Development Ltd (REDL) is a public limited company, incorporated in August 16, 2009 as a private limited company and later converted to public limited company in June 28, 2019. It is promoted by business persons having long experience in the hydropower and other sectors for setting up Hydroelectric Project (HEP) in the territory of Nepal. REDL has 3 MW Upper Rawa Khola Small Hydropower Project (URKHP) at Khotang District which has been in commercial operation since September 20, 2020. The project is constructed under BOOT (Build, own, Operate and Transfer) mechanism.

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