

Salmani Devi Hydropower Private Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	517.80 (increased from 498.72)	CARE-NP BB+ [Double B Plus]	Reaffirmed
Short Term Bank Facilities	25.00 (decreased from 51.28)	CARE-NP A4+ [A Four Plus]	Reaffirmed
Total Facilities	542.80		

Details of instruments/facilities in Annexure 1

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

Detailed Rationale & Key Rating Drivers

The reaffirmation of the ratings assigned to the bank facilities of SDHPL factor in its modest scale and limited track record of operations, weak operating performance in the initial years of operations albeit on an improving trend year on year, modest debt service coverage indicators coupled with leveraged capital structure. The ratings also factor in hydrology risk associated with run-of-the river power generation and exposure to regulatory risk and volatile interest rates.

The ratings, however, continue to derive strengths from experienced directors and management in various sectors and continued reduction in gap between contracted Plant Load Factor (PLF) and operational PLF. The ratings also factor in presence of Power Purchase Agreement (PPA) with sufficient period coverage and government support for the power sector.

Going forward, the ability of the company to continue to reduce the gap between operational PLF and contracted PLF and improvement in overall financial risk profile are the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Short track record and weak financial performance in initial years of operations

The scale of operations remained small marked by total operating income (TOI) of Rs. 84 Mn in FY21 (Audited, refers to the twelve-month period ended mid-July 2021). 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. SDHPL reported increase in total operating income by 25% to Rs. 84 Mn through sale of electricity during FY21 from Rs. 67 Mn in FY20 aided by improved hydrology. This also led to improvement in PBILDT margin to 91.49% during FY21 against 75.66% in FY20. However, SDHPL reported net loss of Rs. 23.14 Mn (FY20: Rs. 45.45 Mn) due to high interest cost and depreciation cost. Gross Cash Accruals (GCA) increased to Rs. 16 Mn during FY21 from negative GCA of Rs. 10 Mn during FY20.

Furthermore, the company's capital structure stood leveraged with Debt-Equity ratio of 2.41x at the end of FY21 (PY:2.23x) and overall gearing ratio deteriorated to 2.53x at the end of FY21 from 2.34x at the end of FY20. The project was completed with high project cost of Rs 226 Mn per MW and the leverage position of the company was also impacted by net losses till FY21. It is expected that with stabilization of the operations in the coming years, the profitability would increase and hence, the tangible networth of the company; thereby would lead to improvement in overall financial risk profile. Interest coverage ratio was moderate at 1.26x during FY21, substantial improvement from 0.84x in FY20.

¹Complete definitions of the ratings assigned are available at www.careratingsnepal.com and in other CRNL publications

Attributed to high project cost, the debt service coverage indicators expected to remain weak in the initial operations of operations.

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 risk

Nepalese banking sector has a floating interest rate regime, where a certain premium is added to the quarterly base rate and interest rate is changed accordingly on quarterly basis. The base rates of the banks and financial institutions (BFIs) in Nepal remain quite volatile as they are impacted by available liquidity in the system which leads to change in interest rates. The volatility in interest rate is more evident currently on account of the ongoing liquidity stress in the economy. Furthermore, increased bank rates announced in the Monetary Policy for FY23 is likely to add to the upward pressure on interest rates going forward. Any significant rate hikes could put increased interest burden on the company, squeezing its profitability and impacting its liquidity position. Therefore, funding taken by the company 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 power sector as well as other industries. SDHPL has three Board of directors, chaired by Ms. Uma Dahal, who has more than 25 years of experience in hydropower, health, education and finance sector. The company's management team is led by Mr. Peras Dahal, who has more than 10 years of experience in different sectors. The BOD is further supported by other experienced management team members.

Continued reduction in gap between contracted PLF and operational PLF

The annual contracted PLF of the project is 65.01% of the installed capacity of the plant. During FY21, the PLF from the project improved to 51.08% of total capacity (FY20: 41.79%). The PLF improving trend continued in 10MFY22 (Unaudited, refers to the ten-month period ended mid-May 2022) and stood at 56.72% of total capacity aided by improved hydrology. Although first half of the financial year, being mostly wet season, leads to higher generation, however, on a year-on-year basis, the company's PLF levels have shown steady improvement, benefitting from an improved hydrology coupled with efficient power evacuation. The power generation from the project as a percentage of the contracted power as per the PPA has also been on an improving trend (10MFY22: 91.21%, FY21: 78.59%, FY20: 64.26%). The ability of the company to continue to reduce the gap between operational PLF and contracted PLF and availability of sufficient hydrology remains a key rating sensitivity.

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

SDHPL entered into PPA with NEA on March 25, 2013 for sale of 3.33 MW power generated by the plant. 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. 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. NEA is owned by Government of Nepal and hence counter party default risk is low; however, timely realization of receivables is critical for the company and remains a key monitorable.

Government support for the power sector

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

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.

Brief financials of SDHPL for last two years for period ending FY21 are as under:

Financial Performance

For the Period	(Rs. Million)	
	FY20 (A)	FY21 (A)
Income from Operations	67	84
PBILDT Margin (%)	75.66	91.49
Overall Gearing (times)	2.34	2.53
Interest Coverage (times)	0.84	1.26
Current Ratio (times)	0.73	1.00

Annexure 1: Details of the Facilities Rated

Name of the Bank Facilities	Type of the Facility	Amount (Rs. In Million)	Ratings
Long Term Bank Facilities	Term Loan	517.80	CARE-NP BB+ [Double B Plus]
Short Term Bank Facilities	Fund Based Limits	25.00	CARE-NP A4+ [A Four Plus]
Total		542.80	

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