

## Unique Hydrel Company Limited

### Rating

Facility/Instrument	Amount (Rs. in Million)	Ratings <sup>1</sup>	Rating Action
Issuer Rating	NA	<b>CARE-NP B (Is) [Single B (Issuer)]</b>	Reaffirmed

*\*The issuer rating is subject to total debt of the company not exceeding Rs. 400 Mn at the end of FY23*

CARE Ratings Nepal Limited (CRNL) has reaffirmed the issuer rating of 'CARE-NP B (Is)' assigned to Unique Hydrel Company Limited (UHCL). Issuers with this rating are considered to have high risk of default regarding timely servicing of financial obligations in Nepal.

### Detailed Rationale & Key Rating Drivers

The reaffirmation of the rating assigned to UHCL continues to factor in its weak financial risk profile characterized by sustained muted operating performance amid hydrology related challenges, highly leveraged capital structure, and modest debt service coverage indicators. The rating continues to be constrained by the inadequate cash generation from the project amid lower than expected power generation leading to dependence of the company on financial support from the promoters to meet its financial obligations. The rating also factors in hydrology risk associated with run-of-the river power generation, exposure to regulatory risk and volatile interest rates.

The rating, however, continues to derive strengths from experienced promoters and management team in hydropower sector, Power Purchase Agreement (PPA) with sufficient period coverage, low power evacuation risk and government support for the power sector. While the rating takes cognizance of the measures taken by the company to mitigate the hydrology related challenges, the project's ability to materially improve its operating performance for a sustained period remains to be seen.

*Going forward, the ability of the company to successfully reduce the gap between operational Plant Load Factor (PLF) and contracted PLF and availability of sufficient hydrology with timely receipt of payments from Nepal Electricity Authority (NEA) will be the key rating sensitivities.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weaknesses

#### Weak financial risk profile and continued dependence on promoters for meeting financial obligations

UHCL has been operating a run-of-the-river 4.2 MW Baramchi Hydropower Project (BHP) in Sindhupalchowk district of Nepal since November 2010. The contracted PLF of the projects is 61.31% of the installed capacity, however the project has been operating at low PLF over the period due to actual hydrology levels being substantially lower than earlier expectations. During FY22 (Unaudited; refers to the twelve-month period ended mid-July 2022), the PLF from the project remained low, albeit improved year on year, to 34.79% of total capacity (PY: 32.18%). Consequently, UHCL reported increase in Total Operating Income (TOI) by 13.14% to Rs. 62 Mn through sale of power during FY22 aided by improved hydrology. This also led to improvement in PBILDT margin to 70.36% during FY22 against 57.25% during FY21. Despite increased revenue, the company reported loss of Rs. 18 Mn from operations on account of high interest cost and depreciation. For FY22, the company reported gross cash accruals of Rs. 37 Mn.

The capital structure of the company stood leveraged with total gearing ratio of 9.28x as on mid-July 2022 which improved from 10.16x as on mid-July 2021 due to decline in term liabilities with scheduled repayment of loans. The interest coverage

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

ratio improved to 1.69x during FY22 from below unity in FY21. Furthermore, Total debt/GCA increased to 10.19x during FY22 from negative total debt/GCA during FY21. Despite sequential improvement in the debt coverage indicators in FY22 over FY21, the company's overall financial risk profile remains weak. The company continues to depend on financial support from promoters to meet cash flow mismatches. Since the power plant is still facing issues related to hydrology, timely infusion by the promoters to support the cash flow of the company when required remains critical for timely payment of the debt obligations. Improvement in hydrology leading to adequate cash flow generation from the project will be critical from credit perspective.

### **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. UHCL utilizes discharge from Baramchi Khola (tributary of Balephi river), a perennial river, having catchment area of 14.75 sq kms. The company is in the process to add water diversion from the Majhe Khola for dry season which is expected to improve the power generation and revenue for the company. However, the project is still exposed to risk associated with variation in discharge of water from the aforesaid river.

### **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, with substantial upward pressure on interest rates in the last few quarters. A contractionary Monetary Policy for FY23 coupled with increasing inflation has only added to the upward pressure on interest rates, resulting in the rate hikes taken by BFIs in the first quarter of FY23. Any further 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.

### **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 promoters and management team in hydropower sector**

UHCL has three members in its Board of Directors, chaired by Mr. Prakash Kumar Shrestha who has more than 30 years of experience in various sectors including banking sector. Mr. Gyanendra Lal Pradhan, director, has more than 25 years of experience in power generation through his association with different companies. He is also Executive Chairman at Hydro Solutions and National Council Member at Confederation of Nepalese Industries (CNI). Ms. Swasti Shrestha, director, has over 15 years of experience in Hydropower sector with major specialization in Hydropower. The BOD is further supported by other experienced management team members.

### Power purchase agreement with sufficient period coverage

UHCL entered into PPA with NEA as on November 18, 2009 for 4.2 MW for sale of power generated by the plant. The period of PPA is 30 years from date of the commercial operation date (COD). The tariff for wet season (Mid-April to Mid-December) is Rs 3.9 per kWh and for dry season (Mid-December to Mid-April) is Rs 5.52 per kWh and for additional contract energy it is Rs 4 & Rs 7 per kWh for wet & dry season respectively with 3% escalation every year on base tariff for 9 times after completion of 12 months from COD date.

### Low power evacuation risk

The power generated from the project is evacuated through 33KV Transmission Line to NEA Laamo Sangho Substation. A single transmission line connects to NEA sub-station. In overall aspect, there is lower power evacuation risk with no tripping problem. However, smooth power evacuation for a reasonable period remains to be seen and will remain a key monitorable.

### 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

UHCL is Public Company, incorporated on July 14, 2000, promoted by institutional as well as individual promoters from different background. It is currently operating 4.2 MW Baramchi Hydropower project in run-of-river scheme located at Sindhupalchowk district, Nepal. The project is constructed under BOOT (Build, own, Operate and Transfer) mechanism. The project started commercial operation on November 14, 2010.

### Financial Performance

Brief financial performance of UHCL during last 3 years is given below:

For the Period	(Rs. In Million)		
	FY20 (A)	FY21 (A)	FY22 (UA)
Income from Operations	53	55	62
PBILDT Margin (%)	48.70	57.25	70.36
Overall Gearing (times)	5.02	10.16	9.28
Interest Coverage (times)	0.64	0.78	1.69
Current Ratio (times)	0.29	0.22	0.22
Total Debt/Gross Cash Accruals(times)	Negative	Negative	10.19

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