

Mathillo Mailun Khola Jalvidhyut Limited

Ratings

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

**The issuer rating is subject to the company maintaining overall gearing not exceeding 2.75x at the end of FY23.*

CARE Ratings Nepal Limited (CRNL) has assigned 'CARE-NP BB-' rating to Mathillo Mailun Khola Jalvidhyut Limited (MMKJL). 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 rating assigned to MMKJL is constrained by project implementation risk and operations stabilization risk thereafter associated with its under construction hydro project. The rating also factors in the hydrology risk associated with run-of-the-river power generation, power evacuation risk and exposure to volatile interest rate risk along with regulatory risk. The rating, however, derives strength from experienced board members and management team, presence of power purchase agreement (PPA) with sufficient period coverage, moderate counter party risk, and government support for the power sector. *Going forward, timely execution of the under construction project within the cost and time estimates along with swift stabilization of operations thereafter leading to generation of expected revenue will be the key rating sensitivities.*

Detailed description of the key rating drivers

Key Rating Weaknesses

Project implementation and operations stabilization risk

MMKJL is setting up a 14.3 MW Mathillo Mailun Khola Jalvidhyut Limited (MMKJP) in Rasuwa district of Nepal. The total estimated cost of project is Rs. 2,500 Mn, which is being funded in debt to equity in the ratio of 75:25 (debt of Rs 1,875 Mn and equity of Rs. 625 Mn). The total debt of Rs. 1,875 Mn has already been tied up. Till July 16, 2022, ~79.18% of the total project cost had been incurred. As per physical progress report of mid-July 2022 submitted by the company, 81.5% physical progress had been achieved. The RCOD of the project was July 15, 2022. The expected COD of the project is January 29, 2023 and the company has applied for extension of RCOD to NEA till January 29, 2023. This exposes the company towards residual project implementation in terms of completion of the project within the envisaged timelines and cost. Furthermore, if COD does not fall within RCOD, MMKJL is required to pay late COD penalty and if COD is delayed by 6 months to 18 months from RCOD, then the number of escalations in tariff rate will decrease to 4 years from 5 years. Extension of RCOD by NEA and commencement of operations within RCOD will remain a key monitorable aspect. Furthermore, the company also remains exposed to satisfactory operations of the project post COD leading to revenue generation at envisaged levels.

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 summer season when river flows are high (Mid-April to Mid-December) and less during the winter season (Mid-Dec to Mid-April). The project is proposed to utilize discharge from Mailung Khola which is a perennial river and having partly

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

snow-fed and partly a rain fed catchment area of 72 sq kms. Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river/ khola.

Power evacuation risk

The power generated from the project will be evacuated through 15Km long 132KV Transmission Line to the Trishuli 3B Hub Substation. Power from Trishuli 3B substation will be further evacuated to an operational Matatirtha Substation in Kathmandu valley by NEA through 220KV transmission line which has been already constructed by NEA. However, Trishuli 3B Hub is under construction. Construction of transmission line from powerhouse to Trishuli 3B substation is within the scope of MMKJL. Before commencement of commercial operations, it is critical for the company to construct of the transmission lines and completion of construction of substation by NEA for revenue generation prospective.

Exposure to volatile interest rate

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

Associated with large group having multiple hydropower projects and experienced board members and management team

MMKJL is part of Sanima Hydro Group which is promoted by group of Non-Resident Nepalese. In addition to the hydropower projects, the promoters of Sanima Group have made their investments in different other sectors.

MMKJL has 3 Board of Directors, chaired by Mr. Rameshwor Rijal, who has more than 37 years of experience in different organization. He has served as Department Chief for Public Works Department of Kathmandu Metropolitan City Office. Mr. Binaya Kumar Shrestha, Director, has more than 2 decades of experience. He is also a Chairman of Sanima Bank Ltd. Dr. Subarna Das Shrestha, Director, has ~27 years of experience including ~25 years in Hydropower sector.

Company management team is led by Mr. Kangada Prasai. He is associated with the company in the capacity of General Manager and has over one decade of experience in different capacities. He has served as Engineering Geologist in multiple Hydropower Companies in the past.

Power purchase agreement with sufficient period coverage

PPA for MMKJP was signed between NEA and Molnia Power Limited on September 09, 2011 for sale of 14.3 MW power to be generated from the project and the PPA was later transferred in the name of MMKJL on April 26, 2018. The contracted energy for 14.3MW is 79.67 Million Units (MU) annually. The contracted Plant Load Factor (PLF) for total 14.3 MW is 63.60%. PPA has been entered for the period of 30 years from the COD or till validity of generation license whichever is earlier. Tariff rate as per PPA is Rs 4.80 per kWh for wet season (Mid-April to Mid-December) and Rs 8.40 per kWh for dry season (Mid-December to Mid-April) with 3% annual escalation on base tariff for 5 years.

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

Mathillo Mailun Khola Jalvidhyut Limited (MMKJL) is a Public Limited company, incorporated as on August 14, 2012. It is promoted by institutional investors majorly related to Sanima Hydro group and other institutes which include Banks and Insurance companies also for setting up of a 14.3 MW run-of-river, Mathillo Mailun Khola Jalvidhyut Project (MMKJP) in BOOT (Build, own, Operate and Transfer) mechanism and located at Rasuwa district of Nepal.

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