

Mountain Energy Nepal Limited

Ratings

Facility/Instrument	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	3,978.52 (Decreased from 4,169.04)	CARE-NP BB+ [Double B Plus]	Reaffirmed
Short Term Bank Facilities	641.81 (Increased from 451.29)	CARE-NP A4+ [A Four Plus]	Reaffirmed
Total Facilities	4,620.33 (Four Thousand Six Hundred Twenty Million Three Hundred and Thirty Thousand Only)		

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 Mountain Energy Nepal Limited (MENL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of MENL continues to remain constrained by moderate operating performance of the power projects and power evacuation risk. The ratings also factor in hydrology risk associated with run-of-the-river power generation, risk of natural calamities and exposure to regulatory risk.

The ratings, however, derive strength from experienced promoters and management, power purchase agreement (PPA) with sufficient period coverage, improving financial risk profile in FY22 (Audited; FY refers to the twelve-month period ending mid-July) marked by growth in sales with improved cash accruals and government support for the power sector.

Going forward, the ability of the company to successfully reduce the gap between operational 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. Removal of the project from NEA's list of projects under contingency plan leading to lower power offtake risk will also remain a key rating sensitivity.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Moderate operating performance of power projects

The annual contracted PLF for Tadi Khola Hydro Electric Project (TKHEP) is 74.52% of the installed capacity of the plant and for Mistri Khola Hydroelectric Project (MKHEP) is 65.20% of the installed capacity of the plant. During FY22, the energy generated by TKHEP was 86.85% of contracted energy which increased from 71.52% of contracted energy during FY21. Furthermore, PLF was 79.75% of contracted capacity during 7MFY23 (Unaudited, refers to the seven-month period ended mid-February 2023).

For MKHEP, the energy generated increased to 71.22% of contracted capacity during FY22 (FY21: 23.07% operated for one month). The PLF has continued to 71.01% in 7MFY23 of total contracted energy. However, the power generation of MKHEP has moderated on account of the project currently falling under the 'Projects Under Contingency Evacuation Plan' list of NEA. Under the contingency plan, power generation of the project is dependent on the dispatch instructions from NEA. Projects under the contingency evacuation plan generally get lower priority in power evacuation from NEA, particularly during the high supply wet seasons, leading to low Plant Load Factor (PLF) levels. It is critical from analytical perspective for the company to reduce the gap between operational PLF and contracted PLF.

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

Power evacuation risk and stabilization risk

Power generated from MKHEP was proposed to be evacuated to Dana substation. The power from Dana substation will be further evacuated through operational NEA's Dana-Kushma transmission line (220KV - 38 Kms) and further transmitted through Kushma-New Butwal transmission line (220kV-88 kms) which is under construction by NEA. However, NEA and the company have entered into an agreement stating that until the completion of 220kV Dana-Kushma-New Butwal transmission line, the power generated by MKHEP is to be evacuated through 132kV Dana-Kushma-Pokhara transmission line with minimum agreed energy of around ~68% of contracted energy on take or pay basis from Mid-April to Mid-October and 100% of the contracted energy on take or pay basis for remaining months as per PPA. Until the Dana-Kushma-New Butwal transmission line is commissioned by NEA, MKHEP will evacuate power under the contingent plan. Thus, it has impacted the revenue generation of the company from Mid-April to Mid-October.

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 times when seasonal river flows are high and much less during the drier months. MENL is generating electricity from discharge of Tadi River at TKHEP and Mistri River at MKHEP, which are snow fed streams, comprising of mountainous terrain. Similarly, Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid rivers.

Risk of natural calamities

In Nepal, hydropower projects are usually located in terrains that are topographically challenging making their construction and operations vulnerable to adversities of nature. Floods and landslides that tend to occur in these areas pose threat to these power projects damaging their infrastructures, adversely affecting the smooth flow of power generation and distribution, which can impact financial returns of the projects. MENL is also exposed to such risks of natural calamities that might cause infrastructural, operational and financial damages to the project.

Exposure to regulatory risk

Government of Nepal (GoN) has 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**

MENL is managed under the overall guidance of the company's Board of Directors (BoD), who possesses wide experience in the different sectors. The company has seven members in its board, chaired by Mr. Suhrid Raj Ghimire, who has more than three decades of cross sector experience. Mr. Manohar Das Mool, Managing Director, is involved day to day operations of the company. He is also engaged in different businesses as insurance, pharmaceuticals and paper industry. BODs are further supported by experienced teams across various functions/ departments.

Power purchase agreement with sufficient period coverage

MENL (through Aadhi Shakti Bidhyut Bikash Company Limited (ASBL) and Robust Energy Limited (REL) had entered into PPA with NEA in 2005 and 2011 for sale of entire power generated by the plants at TKHEP and MKHEP respectively. The PPA is signed for a period of 30 years from the date of COD or till validity of Generation License whichever is earlier. PPA period may be extended with mutual consensus through discussion from last six month of validity. TKHEP has two set of tariff rate which ranges from Rs. 3.90 per kWh to Rs. 8.40 per kWh with 3% annual escalation on base tariff rate for 5 times for 24.78 GWh energy. Tariff for MKHEP is Rs. 5.40 per kWh with 3% escalation on base tariff for next 10 years.

Improving financial risk profile in FY22 marked by growth in sales and cash accruals

MENL generates revenue from two hydroelectric projects i.e., 5 MW TKHEP operating since April 2013 and 42 MW MKHEP operating since June 17, 2021. During FY22, the company reported increase in total operating income (TOI) by ~634% to Rs. 1,234 Mn in FY22 compared to Rs. 168 Mn in FY21 on account of improved hydrology coupled with commencement of MKHEP project for full year in FY22 (operated for one month during FY21). With high revenue generation, PBILDT increased to Rs. 1,114 Mn in FY22 (FY21: Rs. 112 Mn). Consequently, PAT of the company increased to Rs. 610 Mn in FY22 from Rs. 112 Mn in FY21.

The capital structure of the company stood moderately leveraged with overall gearing ratio of 1.41x at the end of FY22; improved from 1.72x at the end of FY21 on account of accretion of profit coupled with repayment of term loan. Interest coverage ratio also stood moderate at 4.50x during FY22, declined slightly from 5.03x during FY21. Furthermore, total debt to Gross Cash Accruals (GCA) ratio of the company improved to 4.86x during FY22 which was high at 45.35x during FY21 on account of improvement in GCA to Rs. 859 Mn during FY22 from Rs. 89 Mn during FY21.

Favorable Government policies towards power sector

Government of Nepal (GoN) considers power generation as priority sector and intends to maximize private sector participation in generation of electricity by offering different exemptions and facilities on power sector. 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 2027. Also, with government focus more towards reservoir-based hydropower projects; Monetary Policy FY23 has provided full tax exemption for first 15 years and 50% tax exemption for next 6 years to reservoir and semi- reservoir projects whose capacity is higher than 40 MW, completing financial closure within mid-April 2029. As per various directives from NRB, 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. Also, increasing trend of cross-border energy trade and its prospect in upcoming days with bilateral agreements with the neighboring nations shows positive outlook on long- term demand for the power sector.

About the Company

Mountain Energy Nepal Limited (MENL) is a public limited company promoted by business persons having experience in the hydropower sector. Aadhi Shakti Bidhyut Bikash Company Limited (ASBL) and Robust Energy Limited (REL) were subsidiaries of MENL and merged into MENL in FY2019. ASBL was involved in the operation of 5MW run-of-the-river Tadi Khola Hydroelectric Project (TKHEP) and REL was involved in the construction of 42MW Mistri Khola Hydroelectric Project (MKHEP). The projects are constructed under BOOT (Build, own, Operate and Transfer) mechanism.

Financial Performance

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

For the Period	(Rs. In Million)		
	FY20 (A)	FY21 (A)	FY22 (A)
Income from Operations	144	168	1,234
PBILDT Margin (%)	64.87	66.79	90.27
Overall Gearing (times)	2.03	1.72	1.41
Interest Coverage (times)	2.45	5.03	4.50
Current Ratio (times)	9.01	1.29	12.12
Total Debt/Gross Cash Accruals(times)	67.97	45.35	4.86

A: Audited

Annexure 1: Details of the Facilities Rated

Nature of the Facility	Type of the Facility	Amount (Rs. in Million)	Rating
Long Term Bank Facilities	Term Loan	3,978.52	CARE-NP BB+ [Double B Plus]
Short Term Bank Facilities	Fund Based Limit	641.81	CARE-NP A4+ [A Four Plus]
Total		4,620.33	

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About CARE Ratings:

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