

United Mewa Khola Hydropower Private Limited

Ratings

Facilities	Amount (Rs. Million)	Rating ¹	Rating Action
Long Term Bank Facilities	6,750.00	CARE-NP BB [Double B]	Reaffirmed
Short Term Bank Facilities	250.00	CARE-NP A4 [A Four]	Reaffirmed
Total Facilities	7,000.00 (Seven Billion Only)		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has reaffirmed the rating of 'CARE-NP BB' assigned to the long-term bank facilities and the rating of 'CARE-NP A4' assigned to the short-term bank facilities of United Mewa Khola Hydropower Private Limited (UMHPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of UMHPL continue to remain constrained by the project implementation risk associated with its under-construction hydropower project. The ratings also factor in risk of natural calamities, exposure to power evacuation risk, hydrology risk associated with run-of-the-river power generation and exposure to regulatory risk and volatile interest rate risk.

The ratings, however, continue to derive strength from UMHPL's experienced promoters and management in diversified sector, presence of power purchase agreement (PPA) with sufficient period coverage, moderate counter party risk, and government support for the power sector.

Going forward, the ability of the company to successfully execute the project without further cost and time overrun and early stabilization thereafter are the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Project implementation risk

UMHPL is setting up a 50 MW Mewa Khola Hydroelectric Project (MKHP) with an estimated cost of Rs. 9,000 Mn (Rs. 180 Mn per MW), which is proposed to be funded through debt to equity in the ratio of 75:25 (debt of Rs. 6,750 Mn and equity of Rs. 2,250 Mn). The debt component required for the project has been fully tied up. As per the progress report submitted by the company, as on April 2023, the overall physical progress of the project was ~45%. Financial progress was ~29% as on mid-May, 2023. Since majority of the works is still pending, the company continues to remain exposed to the risks associated with project implementation within envisaged cost and timelines.

The Required Commercial Operation Date (RCOD) of the project was July 13, 2023. However, the company has applied for extension of the RCOD by two more years, citing delays in construction amid the pandemic. If approved, the extended RCOD is likely to provide additional cushion to complete the project within the required timeframes to avoid late COD penalty and to avail the accelerated clauses of tariff. If COD doesn't fall within RCOD, the company is bound to pay penalty to NEA as per the PPA. The number of escalations in tariff rate will also be reduced if COD of the project is delayed by more than 6 months.. Any material delays in commissioning of the project could impact the project's expected returns and debt servicing capabilities which is critical from credit perspective.

Power evacuation risk

The power generated from the project is proposed to be evacuated through 7 km long 132KV transmission line to NEA's Dhungesanghu Substation at Taplejung district which is under construction. Power from Dhungesangu substation will be

further evacuated to Basantapur Substation, which is also currently under construction. Construction of transmission line from powerhouse to the substation is within the scope of UMHPL, while construction of the substations is within the scope of NEA. Timely completion of the transmission line and the substations will be crucial for the company in terms of revenue generation aspects as envisaged.

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 seasonal river flows are high (June to November) and less during the winter season (December to May). The project is proposed to utilize discharge from Mewa Khola having catchment area of 527 sq km based on Perennial River. The project has 33 m³/s design discharge at 40% exceedance flow. Hence, the expected power generation is exposed to risk associated with variation in discharge of water from the aforesaid river/khola.

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 as well as impacting their timely completion. Moreover, disruption in their construction in turn could lead to time and/or cost overrun, negatively impacting the project's financial aspects. Moving forward also, these natural calamities can adversely affect the smooth flow of power generation and distribution, which can further impact financial returns of the projects. MKHPL is also exposed to such risks of natural calamities that might cause infrastructural, operational and financial damages to the project.

Exposure to volatile interest rate

The company's interest rates are based on 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. Higher interest rates than envisaged could result in squeezed margins of the company. Hence, funding taken by the company is exposed to volatile interest rate.

Exposure to regulatory risk

Government of Nepal (GoN) has established Electricity Regulatory Commission (ERC) for regulating hydropower companies in Nepal. ERC will regulate generation, transmission and distribution of electricity in Nepal among others. Policies and directives issued by ERC such as approval process for IPO issuance and 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

UMHPL has three board of directors with experience in diversified sectors including hydropower. The board is chaired by Er. Aashish Thapa who is involved in various hydropower related companies in the capacity of investor as well as board member. Er. Thapa is also a director in United Modi Hydropower Limited (Lower Modi I Hydropower Project-10 MW), and is involved in Suryakunda Hydroelectric Private Limited (Tadi Khola Hydropower Project-11 MW). Furthermore, he is the Executive Chairman in Kist Medical College Private Limited. Other directors of the company also have experience of more than 20 years in various sectors including hydropower projects. The board is aptly supported by an experienced management team.

Power purchase agreement with sufficient period coverage

UMHPL had entered into PPA with NEA as on June 04, 2017 for sale of 50 MW power to be generated from the project. The period of PPA is 30 years from commercial operation date (COD) or till validity of Generation License, whichever is earlier. The tariff for wet season (June to November) is Rs. 4.80 per kWh and for dry season (December to May) is Rs 8.40 per kWh with 3% escalation every year after completion of 12 months from COD date on base tariff for 8 times. The contracted energy for the project is 303.01 million units at PLF of 69.18%.

Favorable Government policies towards power sector

Government of Nepal (GoN) considers hydropower generation as a 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 the 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

United Mewa Khola Hydropower Private Limited (UMHPL) is a private company, incorporated on June 01, 2010. The company has been promoted by individual promoters for setting up a 50 MW run-of-river Mewa Khola Hydroelectric Project (MKHP) in Taplejung district. The project is constructed under BOOT (Build, Own, Operate and Transfer) mechanism.

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	6,750.00	CARE-NP BB
Short Term Bank Facilities	Fund Based Working Capital Loan	250.00	CARE-NP A4
Total		7,000.00	

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