Mewa Developers Limited

Ratings

Facilities	Amount (Rs. Million)	Ratings[1]	Rating Action
Long Term Bank Facilities	13,906.85 (Increased from 6,948.45)	CARE-NP BB [Double B]	Reaffirmed
Total Facilities	13,906.85 (Thirteen Billion Nine Hundred Six Million and Eight Hundred Fifty Thousand Only)		
Issuer Rating	NA	CARE-NP BB (Is) [Double B (Issuer Rating)]	Assigned

**The issuer rating is subject to overall gearing ratio of the company not exceeding 3.25x at the end of FY24 (FY refers to the twelve-month period ending mid-July).*

***Details of Facilities in Annexure 1*

CARE Ratings Nepal Limited (CRNL) has assigned issuer rating of `CARE-NP BB (Is)' to Mewa Developers Limited (MDL). Issuers with this rating are considered to offer moderate risk of default regarding timely servicing of financial obligations, in Nepal.

Also, CRNL has reaffirmed the rating of 'CARE-NP BB' assigned to the long term bank facilities of MDL.

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of MDL continue to remain constrained by the project implementation risk associated with its under-construction hydropower projects amid change in scope. With amendment of Middle Mewa Hydropower Project (MMHP) to 73.5 and setting up another 9.3 MW peaking run-of-river, Siwa Khola Hydropower Project (SKHP), the risk is accentuated by possibility of geological surprises during construction exposing the company towards execution risk in terms of completion of the projects within the envisaged time and cost. The ratings continue to factor in exposure to power evacuation risk, risk of natural calamities, and exposure to regulatory risk and volatile interest rate risk of the company. The ratings also take cognizance of the relatively high estimated cost of the project leading to likelihood of increased debt servicing requirements in the initial years of operations. However, this is mitigated, to some extent, by relatively high contracted Plant Load Factor coupled with high dry season energy mix with better peaking tariff rate which augurs well for revenue profile prospect of the company. Furthermore, hydrology risk normally associated with run-of-the-river power generation is also mitigated, to an extent, with change in scope of project. The ratings continue to derive strength from MDL's experienced promoters and management team, presence of power purchase agreement (PPA) with sufficient period coverage, full financial closure achieved for the revised estimated debt component of the projects, and government support for the power sector.

Going forward, the ability of the company to successfully execute the projects within the envisaged cost and time and early stabilization thereafter will be the key rating sensitivities.

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

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Project implementation risk

MDL is setting up a 73.5 MW (amended from 49 MW) peaking run-of-river Middle Mewa Hydropower Project (MMHP) and another 9.3 MW peaking run-of-river Siwa Khola Hydropower Project (SKHP). Both the projects are in Mikhuwa Khola Rural Municipality, Taplejung district of Nepal. The estimated cost of the two projects (82.8 MW) is Rs 18,543 Mn (i.e., ~Rs 224 Mn per MW) which is proposed to be financed in Debt equity ratio of 75: 25 (i.e., Rs. 13,907 Mn term loan and Rs. 4,636 Mn equity). The estimated cost is relatively higher compared to other similar sized projects and could impact the project returns and debt servicing during the initial years of operations.

The company had achieved financial progress of ~36% on the basis of financial verification as on January 01, 2023. As per the progress report as on April 2023, MMHP has achieved the overall physical progress of 51.86% (for 73.5 MW). SKHP is in middle stages of development with pre-construction and infrastructure works completed. Contrary to expectations of speedy construction works at the site (before amendment to 73.5 MW), the project experienced geographical surprises and both timelines as well as cost estimations had to be revised. Sand layer was discovered during excavation leading to sinking risk. The landscape was grouted to solidify the base to eliminate the risk. This led to change in construction design and increasing the project cost. Furthermore, under-ground powerhouse instead of above-ground powerhouse was constructed after change in design. As majority of the works is yet to be completed for both the projects, any major setback impacting the pace of construction would remain critical from analytical perspective.

RCOD of 49 MW was September 23, 2023, which is extended till March 19, 2024 on account of COVID-19 and RCOD of 24.5 MW is June 02, 2024. The company is likely to apply for extension for one year. The extension, if applied and approved, is expected to provide some cushion to complete the project in revised timelines, barring any major setback. Similarly, RCOD of 9.3 MW is June 09, 2025. If COD doesn't fall within RCOD, the company is bound to pay late COD penalty to Nepal Electricity Authority (NEA). Further, if COD is delayed by 6 months to 18 months from RCOD, then the number of escalations in tariff rate will decrease to 7 times from 8 times. It is crucial for the company to complete the project within the timelines to have the accelerated clauses of tariff. Any delay in the same would lead to impact on project returns and debt servicing capabilities which is critical from analytical perspective.

Power Evacuation Risk

The Power generated from the project is proposed to be evacuated through 11km long 132KV double circuit Transmission Line to NEA's under construction Hangpang Substation at Taplejung district. Power from under construction Hangpang/ Dhungesangu Substation is further evacuated to NEA's under construction Basantapur Substation. Construction of transmission line from powerhouse to Hangpang substation has started and is within the scope of MDL. Timely completion of the transmission lines and substations will be crucial for the company from revenue generation perspective.

Hydrology risk associated with run-of-the-river power generation, however mitigated to some extent due to peaking reservoir

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 (June to November) and less during the dry season (December to May). The 73.5 MW project has 333 km^2 (Mewa) plus 25.5 MW project has 131.56 km^2 (Siwa) catchment area and is proposed to utilize discharge from Mewa Khola and Siwa Khola based on perennial river. SKHP has 131.56 km^2 catchment area and is proposed to utilize available head and flow from Siwa Khola. Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river/ Khola. However, the risk is mitigated to some extent in the project due to peaking reservoir of six hours for dry season which will be used during peak time of dry season.

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. MDL 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

MDL is part of Urja Developers Group which has multiple hydropower projects under its portfolio through Special Purpose Vehicles (SPV) companies. The flagship company of the group is Urja Developers Private Limited, promoted by CE Construction Private Limited (CECPL) which started business operations in early 1990's. The group has presence in construction, consultancy, manufacturing, education, finance, hospitality and power generation etc. CECPL was awarded "Construction Company of the Year 2017" by Frost & Sullivan.

Hydroelectricity Investment and Development Company Limited (HIDCL) also known as Jalvidhyut Lagani Tatha Bikas Company Limited (CARE-NP A- (Is)), also holds equity stake in MDL and provides financial strength and professional expertise. MDL has five board of directors chaired by Mr. Bijay Bahadur Rajbhandary who has more than 30 years of experience in the diversified industry. Mr. Mohan Das Manandhar, Director, has more than 30 years of experience in various fields across different sectors in Nepal, South Asia and South East Asia. Mr. Bhanu Bhakta Pokharel, Managing Director of the company possesses more than 30 years of experience. The BOD is further supported by other experienced management team members.

Power Purchase Agreement (PPA) having sufficient period of coverage and high dry energy mix

MDL had entered into a long term PPA with NEA as on August 20, 2018 for sale of 49 MW power and amended to 73.5 MW on December 05, 2022 for sale of power to be generated from the project. The contracted Plant Load Factor (PLF) for total

73.5 MW is 67.73% with total contracted energy of 436.09 Million Units (MU). MDL entered another long term PPA with NEA as on September 05, 2022 for sale of 9.3 MW power to be generated from the project. The contracted PLF for total 9.3 MW is 67.07% with total contracted energy of 54.64 MU. PPA for both projects has been entered for the period of 30 years from the COD or till validity of generation license whichever is earlier. PPA period may be extended with mutual consensus during the last six months of validity.

PPA for MMHP is entered for peaking run of the river with high tariff rate for peak dry season with 6 months of dry season. Tariff rate as per PPA is Rs 4.80 per Kwh for wet season (June to November) and the tariff rate for peak dry season (December to May) is Rs 10.55 per Kwh while the non-peak rate for the dry season (December to May) is Rs. 8.40 per Kwh, with 3% annual escalation on base tariff for 8 years. Similarly, PPA for SKHP is entered for peaking run of the river with high tariff rate for peak dry season with 6 months of dry season. Tariff rate as per PPA is Rs 4.80 per Kwh for wet season (June to November) and the tariff rate for peak dry season (December to May) is Rs 8.50 per Kwh while the non-peak rate for the dry season (December to May) is Rs. 8.40 per Kwh, with 3% annual escalation on base tariff for 8 years.

Following six-month wet and six-month dry season, the total contracted energy of the project is 436.09 MU (MMHP) and 54.64 MU (SKHP) with relatively higher dry energy mix of ~31% of the total contracted energy for both the projects, which augurs well for the company’s income profile.

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 2027. Also, with government focus more toward reservoir-based hydropower projects; Monetary Policy FY24 has provided full tax exemption for first 15 years and 50% tax exemption for next 6 years to reservoir and semi-reservoir projects completing financial closure within mid-April 2029 with a capacity higher than 40 MW. 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.

About the Company

Mewa Developers Limited (MDL), incorporated as a private limited company on July 8, 2016 was converted to a public limited company on June 23, 2021. It is promoted by individual promoters from different background and institutional investors. MDL has two hydropower projects namely, 73.5 MW (Amended from 49 MW), Middle Mewa Hydropower Project (MMHP) and 9.3 MW, Siwa Khola Hydropower Project (SKHP), both peaking run-of-river projects in Mikhuwa Khola Rural Municipality, Taplejung district of Nepal. 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	13,906.85	CARE-NP BB
Total		13,906.85	

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About CARE Ratings Nepal Limited:

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Our parent company, CARE Ratings Limited commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI).