



Nepal Hydro Developer Limited

ICRA Nepal assigns [ICRANP] IPO Grade 4 to the proposed Initial Public Offering (IPO) of Nepal Hydro Developer Limited

Instrument/Facility	Issue Size	Grading Action (April 2016)
IPO (equity) Grading	NPR 65 million	[ICRANP] IPO Grade 4 (Assigned)

ICRA Nepal has assigned an “[ICRANP] IPO Grade 4”, indicating below average fundamentals to the proposed Initial Public Offering (IPO) of Nepal Hydro Developer Limited (NHDL). ICRA Nepal assigns IPO grading on a scale of IPO Grade 1 through IPO Grade 5, with Grade 1 indicating strong fundamentals and Grade 5 indicating poor fundamentals. For the Grading categories 2, 3 and 4, the sign of + (plus) appended to the Grading symbols indicate their relative better position within the Grading categories concerned. NHDL is proposing to come out with an Initial Public Offer of 650,000 numbers of equity shares of face value NPR 100 each at par. Of the total shares, 260,000 shares will be issued to project affected areas while remaining 390,000 shares will be issued to general public and staff.

The assigned grading factors in the weak financial profile of the company as reflected in high project costs, and weak profitability of the 3,520 KW Charnawati HEP developed by NHDL. High project costs (~NPR 198 million per MW) coupled with fixed tariff will result in lower profitability for the project. The grading is also constrained by moderate operational performance of the project (PLF¹ at net generation of ~55% in past 2 years ending FY15 as opposed to contract energy PLF of ~66%), which coupled with high financial leverage, has been affecting its financial profile. Unable to fulfil the contractual supply of energy will not only result in lower revenues but can also result in penalties if the shortfall is more than 80%. The project is also exposed to hydrology risk, interest rate volatility in the market and the counterparty credit risks arising out of exposure to loss-making NEA² for the energy supplied, although the same is partly mitigated by the fact that NEA is fully owned by the Government and has been making timely payments to NHDL so far which provides some comfort. Grading concerns further emanate from uncertainty about the revenue stream from 6,800 KW Lower Charnawati HEP along with project execution and hydrology risks where management planning to have investment from proposed IPO proceeds.

The assigned grade though takes into account the reputation of promoter group and their experience in hydropower development in Nepal. With a firm PPA³ in place and positive demand outlook, the tariff and off-take risks are reduced considerably for the project. NHDL has been operating 3,520 KW Charnawati HEP⁴ since June 2013 and has plans to invest into 6,800 kW Lower Charnawati HEP (which is planned to be developed at an estimated cost of NPR 1,121 million through a separate SPV⁵). Considering the limited developments in the planned cascade project, IPO proceeds are likely to be utilized towards downsizing bank loans as of now.

Charnawati HEP is the first hydropower project developed by NHDL, although its major promoters were have been actively involved in hydropower project development through various SPVs. NHDL has been operating 3,520 KW Charnawati HEP since June 2013 which was commissioned at a cost of NPR 696 million funded in a debt: equity mix of ~77:23. The tariff rates for contract energy as per PPA are NPR 4 and NPR 7 for wet and dry seasons respectively; subject to annual escalation after Commercial Operation Date (COD) @ 3% on base tariff for 9 years. Under the Government’s initiative of promoting private sector hydropower developers, the project has been availing promotional tariff rates of NPR 4.80 and NPR 8.40 per unit in wet and dry seasons; which shall remain effective for up to 6th year after COD with 5 times annual escalation of 3% on base tariff. The electricity sales revenue shall thereafter be based on the rates

¹ Plant Load Factor

² Nepal Electricity Authority

³ Power Purchase Agreement

⁴ Hydro-Electric Project

⁵ Establishment of separate SPV (Special Purpose Vehicle) pending.



as per PPA. The power generated by the project is evacuated via 7 km, 33KVA transmission line to Makaibari substation at Dolakha. The project has operated at an average annual PLF (at net generation) of ~55% in past two years; lower than design energy PLF of 66% and thus generated an average of ~82% of annual contract energy in past two years resulting in sizeable revenue loss to the company, in addition to occasional short supply penalty (albeit nominal).

Following the survey license for Lower Charnawati HEP (6.8 MW), feasibility study was conducted in Nov-2015, while all other procedures including IEE (Initial Environment Examination), power generation license, detailed designing, grid connection and PPA with NEA and financial closure are to be carried out. The proposed cascade project would utilize the water from tailrace of the current project along with addition of another stream emanating downstream from headwork of current project. The project is planned to be commissioned at a cost of NPR 1,121 million (cost per 1 MW ~NPR 165 million) to be financed in a debt: equity of 70:30. Though the quantum of investment that NHDL is to make in the said project is yet to be finalized, preparatory works for the project has been concluded through NHDL managed funds as of now (~NPR 19.5 million has been incurred by Jul-15 for the same which has been financed partly through short term loans from bank amounting to ~14.3 million). With the project in its very initial stages, IPO proceeds are likely to be utilized towards downsizing bank loans as of now. Timely completion of the planned project within the budgeted time and cost estimates is a key sensitivity for determining the returns generated by the project. Typically, hydro-power projects entails significant project execution risks as they are located in difficult terrain and hence adverse climatic conditions during the construction period and also geological surprises can disrupt construction schedule of any project. Nevertheless, the promoters and management personnel have substantial experience in construction and operation of hydro power projects which mitigates this risk to some extent.

Since the revenues are entirely linked to unit sales from a single operational project, the project returns and also the financial health of the company is entirely dependent on the hydrology of the project stream. Owing to increment in PLF in FY15⁶, NHDL posted gross sales revenue of ~NPR 97 million in FY15 compared to ~NPR 86 million in FY14. PAT⁷ for FY15 was NPR 0.62 million over OPBDITA⁸ of ~NPR 68 million on year ending July 2015 compared to PAT of NPR 9.33 million in FY14. Reported profits of both these years were benefitted by non-operating income sources amounting to ~NPR 6 million for FY15⁹ and ~NPR 25 million for FY14¹⁰; disregarding which company would have been reporting losses till FY15. The company had ~NPR 455 million of outstanding term loan payable to the consortium banks as on July 2015 as per audited financials, corresponding to a gearing ratio of 3.06 times. NHDL's track record of debt servicing (which began from mid-April 2014) remains good so far; partly benefitted from the regime of low lending rates in banking system and ballooning instalment method of repayment which entails small portion of principal repayment in initial years.

Going forward, the ability of the project to achieve its design operating parameters will be the most important driver for the project returns.

Company Profile

Founded in the September 2006 by 10 promoters, NHDL was converted into a public company in July 2014 with the objective of facilitating public participation. Major promoters of the company include Er. Gyanendra Lal Pradhan (22.5% holding as of now), Mr. Kumud Kumar Dugar (12.5%), Mr. Pashupati Murarka (12.5%), Mr. Dev Kishan Mundara (12.5%), Mr. Ananda Prasad Pokharel (10%), among others. Promoter: public holding would be diluted to 75:25 post the proposed IPO, assuming full subscription.

⁶ Net PLF of 52% in FY14 increased to 57% in FY15, however still remaining lower than design PLF of 66%

⁷ Profit After Taxes

⁸ Operating profit before depreciation, interest, tax and amortization expense

⁹ Largely from insurance claims relating to repair expense to pipes booked as other income.

¹⁰ Includes discount received from electro-mechanical contractor (~10 million) and reversal of excess depreciation owing to change in depreciation method for selected assets (~15 million).



The company is at present operating 3,520 kW Charnawati HEP in Dolakha District of Central Nepal since June 2013 and it has plans to invest in 6,800 kW Lower Charnawati HEP that is in process of PPA and financial closure.

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