

## Hydroelectricity Investment & Development Company Limited

### ICRA Nepal assigns [ICRANP] IPO Grade 4+ to proposed rights issue (equity shares) of Hydroelectricity Investment & Development Company Limited

Facility/Instrument	Amount	Grading Action (July 2019)
Rights Issue (equity shares)	NPR 11,000 Million	[ICRANP] IPO Grade 4+; Assigned

ICRA Nepal has assigned a grade of **[ICRANP] IPO Grade 4+**, indicating below average fundamentals, to the proposed rights issue (equity shares) of Hydroelectricity Investment & Development Company Limited (HIDCL). ICRA Nepal assigns IPO gradings on a scale of 1 through 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 symbol indicates their relative position within the grading category concerned. Thus, the gradings of 2+, 3+ and 4+ are a notch higher than 2, 3, and 4, respectively. HIDCL proposes to come up with a 100% rights issue of 110,000,000 equity shares, with a face value of NPR 100, to be issued at par to the existing shareholders.

The grading factors in the HIDCL's strong ownership profile (entire promoter share held by the Government either directly or indirectly), its strategically important role as an implementing agency for the power sector development agendas of the Government of Nepal (GoN) and its commitment towards development of the hydroelectricity sector, as demonstrated by providing subsidies, grants etc. for the hydropower units. Further, the grading also factors in the robust energy demand outlook within the country, limited use of the potential hydropower resources of Nepal (installed capacity close to only 1021<sup>1</sup> MW) and the possibility of power export to neighbouring countries, given the power trading agreement signed between the Governments of Nepal and India in October 2014, which is expected to provide adequate growth opportunities to the company.

Nonetheless, the grading remains constrained by HIDCL's limited track record (established in July 2011), sluggish growth in approval and disbursement of fund and moderate financial performance so far despite high importance given in the power financing sector by the GoN. The grading is further constrained by lack of clarity in the source of lending funds apart from equity, resulting in a limited return potential to equity holders. Going forward, HIDCL's ability to build a balanced and diversified portfolio, raise funds at competitive rates, manage the liquidity mismatch inherent in infrastructure financing (lending for relatively longer tenure while limited availability of long-term funds), further strengthen its project appraising and monitoring capabilities. Its ability to manage collections from the borrowers would have a bearing on HIDCL's operational and financial risk profile.

Added to which is the lack of regulatory framework (HIDCL being the first company of its kind in Nepal), concentrated portfolio towards the greenfield power generation projects, inherent risks in the hydropower and related infrastructure financing, including execution risks and evacuation risks. Their limited experience in commissioning power projects results in the possibility of time and cost overruns thus impairing the projects' ability to service their debt obligations within time.

HIDCL invests either through debt or through equity into a range of power sector activities, including generation, distribution and transmission. The company typically invests in hydroelectric projects with a capacity of 15 MW and above. Each proposal is assessed by a Risk Assessment Cell formed on a case-to-case basis for each project. This cell generally comprises higher officials and experts from the Government agencies and ministries along with some external experts. The cell does technical and financial assessment as per the investment appraisal template of the company. Also, management teams involving in-house experts prepare a management report based on which the board level risk management committee further analyses the proposal and if found reasonable, forwards the same to the Board for approval.

<sup>1</sup> As per annual report of FY 2018, Nepal Electricity Authority.

HIDCL is licensed to operate limited banking from the Central Bank of Nepal. As per the approval, HIDCL can only lend through a consortium, hence it also takes comfort from the assessment made by the lead bank of the consortium as well. As of now, HIDCL has approved 15 run-of-the-river type projects, 12 for-debt financing with a combined capacity of approximately 442 MW (financing commitment of approximately NPR 6,686 million) and three projects for equity financing with a combined capacity of approximately 551 MW (financing commitment of approximately NPR 4,711 million). Out of the 15 approved projects, all three equity-financed projects as well as three of the debt-financed projects are in nascent stages of development, while the other three projects are approaching completion, another one has come into operation and the rest have achieved physical progress of 40-80%. Disbursement, however, has remained on the lower side (~20% of the commitments, both equity and debt), mainly due to the slow project progress. Cost overruns due to these delays could affect the power project's viability and hence impact HIDCL's asset quality profile going forward. Delays in the construction of transmission lines have also been witnessed in Nepal's power sector, exposing HIDCL's borrowers to power evacuation risks, which in turn could pose asset quality risk for HIDCL.

Apart from investment in the hydro-electric projects, HIDCL has made investments in hydroelectricity related companies as well viz; NEA Engineering Company Ltd., Power Transmission Company Nepal Ltd. (construction of 400 KV cross border transmission line between India and Nepal), Nepal Power Trading Company Ltd. and Vidhyut Utpadan Company Ltd. (VUCL, invests in various HEP). Total investment commitment in these companies is NPR 869 million, out of which, NPR 349 million has been invested so far. Further, the company plans to invest in the hydropower projects proposed to be developed by VUCL and other Government HEPs. The aggregate commitment so far is around NPR 12 billion vs. the company's net worth base of NPR 17 billion as of now.

With regard to HIDCL's funding profile, it has no borrowing so far due to existing surplus in the equity base (total disbursement/ net-worth of ~15% as of mid-April-2019). HIDCL plans to raise debt funds from various Government agencies, foreign multilateral/bilateral agencies and through certificates of deposits, needed in future. However, the borrowing mechanism for any of the proposed borrowing has not been finalised yet. As HIDCL has already made a total commitment (incl. debt and equity investment in HEPs, and hydroelectricity related companies) of NPR 12,266 million as of now, the company would remain short of fund for further larger commitments, which may necessitate a fund crunch.

The company's profitability has been largely supported by income from investment (~90% of total income) in fixed and call deposits in commercial banks. The operational income is gradually increasing, starting from FY2016. However, all the interest income from loan and advances so far has been capitalised in the loan book as none of the projects have started the repayment. Profitability indicators of the company are improving with the increasing yield in assets amid an increasing interest rate scenario in market. Overall, HIDCL's profitability indicators are improving over the years with the RoE and the RoA of ~7% each in 9M FY2019 from ~3% each in FY2016. The company's future financial profile remains dependent upon its ability to efficiently mobilise the lendable fund, gaining leverage benefits for financing its loans and managing the asset quality risks.

**Analytical approach:** For arriving at the grading, ICRA Nepal has applied its grading methodology as indicated below.

**Links to applicable criteria:**

[IPO Grading Methodology](#)

[Credit Rating Methodology for Non-banking Finance Companies](#)

**Company Profile**

Hydroelectricity Investment and Development Company Ltd. (HIDCL) was established on July 11, 2011 as a specialised development financial institution to mobilise resources and cater to the needs of investments in hydroelectricity generation (15 MW and above), transmission and distribution projects. HIDCL is registered as a public limited company, with 80% stake of the Government of Nepal as on mid-April-2019 (50% direct holding and 30% holding equally distributed among three state-owned companies viz.



Employees Provident Fund, Citizen Investment Trust and Rastriya Beema Sansthan). The rest 20% is distributed largely among the general public.

HIDCL reported a profit after tax (PAT) of ~NPR 812 million during FY2018 over an asset base of ~NPR 16,558 million as of mid-Jul-2018 as against a PAT of ~NPR 498 million in FY2017 over an asset base of ~NPR 11,125 million as of mid-Jul-2017. During 9M FY2019, HIDCL reported a PAT of ~NPR 837 million over an asset base of ~NPR 17,414 million as of mid-April-2019.

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