

Eastern Hydropower Limited

ICRA Nepal assigns [ICRANP] IPO Grade 5 to the proposed IPO of Eastern Hydropower Limited

Instrument/Facility	Issue Size	Grading Action (November 2018)
IPO (equity) Grading	NPR 155 million	[ICRANP] IPO Grade 5 (Assigned)

ICRA Nepal has assigned an “[ICRANP] IPO Grade 5”, indicating poor fundamentals to the proposed initial public offering (IPO) of Eastern Hydropower Limited (EHL). ICRA Nepal assigns an 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. EHL is proposing to come out with an IPO of 1,550,000 equity shares with a face value NPR 100 each, at par. As a part of the IPO process, 620,000 shares would first be issued to the project-affected locals, and the rest would be issued to the general public and staff of EHL.

The assigned grading is constrained by the poor return potential of the 5-MW Pikhua Khola small hydropower project being developed by EHL, mainly owing to high project costs (~NPR 236 million per MW). The return indicators are also expected to be impacted by lower tariff for ~62% of contract energy that pertains to initial project capacity of 2.475 MW. Additionally, any loss in hydrology as well as the interest rate volatility in the market could further impact the project earnings. The company’s plans to invest in a few other projects are also in nascent stages, with no clarity regarding timeline and funding sources. Hence, these provide limited comfort in the expected return metrics at present. Going forward, the company’s ability to complete the project within the budgeted cost/time, achieve design operating parameters, efficacy of evacuation infrastructures and availability of sufficient hydrology will be the key parameters which can impact returns of the project.

Located in the Bhojpur district of eastern Nepal, the run-of-the-river project was initially planned as a 2.475-MW project to be built on 65% exceedance flow model. Later, the project capacity was increased to 5 MW by reducing the probability of exceedance to 45%. The project has a catchment area of ~117 sq. km, which is expected to support the design discharge of 5.6 m³/s. The project is being developed on build own operate transfer (BOOT) basis. The power generation license has been obtained from the Ministry of Energy on March 21, 2011 and is valid for 35 years, including the period of construction. Hence, the project would be operating for less than 30 years, i.e. the tenure of the power purchase agreement (PPA).

As per the PPA with the Nepal Electricity Authority (NEA), the tariff rates for the initial 2.475-MW capacity were fixed at NPR 4 per unit and NPR 7 per unit for the wet and dry seasons¹ respectively with 3% annual escalation on the base tariff for 9 times. For the balance 2.525 MW, the agreed tariff was NPR 4.8 per unit and NPR 8.4 per unit for the wet and dry seasons, respectively, with 3% annual escalation on the base tariff for 5 times. Thereafter, the escalated rates would be applicable till the life of the project. As per the contract, approximately 55% of wet energy and ~94% of dry energy would be billed at the initial low tariff which constrains the return potential. Furthermore, for the incremental 2.525 MW, there is a 10% reserve margin requirement during the five wet months (mid-June to mid-November) from FY2019 to FY2032. This would be subject to conditional offtake and hence remains an area of concern. The power generated by the project is to be evacuated via an approximately 4 km, 33-kVA transmission line to the NEA Bhojpur sub-station. The said sub-station has been charged recently and hence evacuation risks are low. The project is also entitled for capital subsidy of NPR 5 million per MW upon connection to the national grid.

Budgeted at a total cost of NPR 1,180 million (~NPR 236 million/MW), the project is being funded in debt: equity of 60:40 with sanctioned loan of NPR 685 million². The rest is to be financed from equity. The promoters have already infused equity of NPR 465 million, representing 75% of post IPO capital. After the proposed IPO, the total equity (NPR 620 million) would be in excess of project equity requirements (NPR

¹ Wet season corresponds to a period of eight months from mid-April to mid-December; rest being dry season.

² Debt tie-up as per earlier project estimate of NPR 1,142 million; to be enhanced for current cost estimates.



472 million). The balance would be utilised for investment in proposed projects. However, there have been no concrete developments so far to acquire stake in the respective companies developing those projects.

As of September 2018, the project is around 85% complete and hence, the execution risks are fairly low. Given the construction progress, the commercial operation of the project is expected within the required commercial operation date (RCOD) of July 15, 2019 as per the PPA. Of the NPR 1,156 million cost incurred till September 2018, NPR 638 million has been funded through external bank borrowings and NPR 428 million from equity (net of losses). The balance is contractor payables. Around 98% of the estimated project cost has already been incurred for the current level of physical progress. Hence, the project cost could witness some escalations towards project completion, mainly through incremental interest during construction (IDC budget has already exceeded by 3%), among other cost components.

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

Links to applicable criteria:

[IPO Grading Methodology](#)

About the company

Incorporated on December 2005 as a private limited company, Eastern Hydropower Limited (EHL) was converted to a public limited company in August 2017. The main promoters of EHL include Money Plant Investment Pvt. Ltd (~24% stake at present), Mr. Narhang Rai (~7%) and Mr. Mohan Kumar Rai (~5%), among others. Following the proposed IPO, EHL's paid-up capital is expected to reach NPR 620 million (assuming full subscription) with ~25% public shareholding.

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