

Shuvam Power Limited

ICRA Nepal assigns [ICRANP] IPO Grade 5 to the proposed Initial Public Offering (IPO) of Shuvam Power Limited

Instrument/Facility	Issue Size	Grading Action (June 2017)
IPO (equity) Grading	NPR 60 million	[ICRANP] IPO Grade 5 (Assigned)

ICRA Nepal has assigned “[ICRANP] IPO Grade 5”, indicating poor fundamentals to the proposed Initial Public Offering (IPO) of Shuvam Power Limited (SPL). 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. Thus, the grading of 2+, 3+ and 4+ are one notch higher than 2, 3, and 4, respectively. SPL is proposing to come out with an Initial Public Offer of 600,000 numbers of equity shares of face value NPR 100 each at par. Of the total shares, 200,000 shares will be issued to residents of project affected areas while remaining 400,000 shares will be issued to general public and staff. The proceeds from IPO are proposed to be used towards downsizing long term project loans of SPL.

The assigned grading is constrained by the poor financial profile of SPL, which owns and operates 990 KW Lower Piluwa Hydroelectric Project (HEP) in eastern Nepal. Weak operational performance of the HEP has resulted in accumulated loss of NPR 32 million as of mid-April 2017. The plant has operated with maximum recorded plant load factor (PLF) of ~50% during past 3-4 years, which is much lower than the contract energy PLF of 79%. Relatively low energy tariff rate has offset the benefits accruing from extended project life (the project is not to be transferred to Government of Nepal (GoN) after completion of 25 years) and exemption from income tax and royalty payments to the government. High equity capitalization post-IPO, and modest revenue stream from the project is likely to result in subdued return for the shareholders. Grading concerns also emanate from hydrological risks and interest rate volatility in the market which could impact the project earnings and returns. The project is also exposed to counterparty credit risks arising out of exposure to loss-making Nepal Electricity Authority (NEA) for the energy supplied, although partly mitigated by sovereign support of GoN to the NEA.

990 KW Lower Piluwa HEP was designed and developed at 50% exceedance flow model along Piluwa river in Sankhuwasabha district of eastern Nepal. The project started commercial operation from July 2011 with a delay of 30 months from required commercial operation date (COD). The tariff rates for the energy generated by the projects as per the Power Purchase Agreement (PPA) with NEA are NPR 3.90 and NPR 5.52 for wet and dry seasons respectively with no tariff escalations (as against NPR 4.80 for wet season and NPR 8.40 for dry season for hydro projects below 25 MW). Being a hydropower project with less than 1,000 KW installed capacity, Lower Piluwa HEP is entitled to certain regulatory benefits like indefinite project life with tax holiday, exemption from royalty payment to the government and exemption from energy short supply penalty. However, these benefits are diluted due to weak project performance and low energy tariff as compared to its peers.

Inadequate generation and penalty for delayed project commissioning and short supply of energy¹ in the initial years have impacted the company's financial profile. The project developers were unable to inject funds to service debt obligations or carry out necessary repairs for ensuring smooth plant operations, leading to sizeable project downtime. Project loans were restructured (with loan repayment period extended from earlier 8.5 years to 20 years) by the lender banks factoring in the weak revenue streams of the company. The project downtime has decreased after the company was taken over by new promoters in FY2015. This has relatively smoothed the earnings profile which coupled with extended loan repayment period and low interest rate charged by lender banks, has improved the debt servicing capacity of the company presently.

¹ Since then, the government has waived short supply penalty for projects less than 1,000 KW installed capacity. Lately, the waiver has been extended to projects less than 10 MW capacity if the short supply is due to hydrological reasons.

Since the revenues are linked to unit sales from a single operational project, the project returns and the financial health of the company is primarily dependent on the hydrology of the project. During FY2016, SPL reported gross sales revenue of ~NPR 18 million (corresponding to 65% of the contract energy) vs. NPR 9 million in FY2015 (corresponding to 33% of contract energy). The company reported net profit of NPR 3.50 million in FY2016 vs. net loss of NPR 12.5 million in FY2015. As on mid-April 2017, the company has ~NPR 110 million of outstanding long-term loan payable to banks, translating into a gearing ratio of 1.03 times. Gearing ratio improved (1.66 times in mid-July 2016 vs. >160 times in mid-July 2015) after the new promoter injected fresh equity (~NPR 60 million) into the company in FY2016. Gearing level and debt servicing capacity of the company is likely to be further comforted after the project loans are repaid from the IPO proceeds, as planned by the management. Going forward, the ability of the project to minimize the gap between actual generation and contractual energy will be the most important driver for the project returns.

Company Profile

Shuvam Power Limited (SPL) (erstwhile Baneshwor Hydro Private Limited) was incorporated on 6th July 2004 as a private limited company and subsequently converted into public limited company on 29th December 2015 to facilitate public participation. The name was changed following the acquisition of majority stake in Baneshwor Hydro by individuals and institutions related to Mr. Shailendra Guragain and his associates in FY2015. As on mid-April 2017, SPL has a total of 32 individual and institutional promoters. Major promoters of SPL include River Falls Power Limited (70.20%) and Ngadi Group Power Nepal (12.30%)-both entities with controlling interest of Mr. Guragain and associates. The current 100% promoter shareholding is expected to dilute to 70% after the proposed IPO. Subsequently, the shares of the company are proposed to be listed in the stock exchange. As a part of the IPO process, 10% of post IPO paid-up capital will be issued to project affected population and remaining 20% capital shall be offered to general public and staffs of SPL.

SPL owns and operates a 990 KW Lower Piluwa Khola Hydroelectric Project (SHEP) located in Sankhuwasabha district of eastern Nepal. The project began commercial operation from 17th July 2011 (30 months later than required commercial operation date of 13th January 2009).

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