



## Hydroelectricity Investment & Development Company Limited

### ICRA Nepal assigns [ICRANP] IPO Grade 3 to the proposed Initial Public Offering of Hydroelectricity Investment & Development Company Limited

Instrument/Facility	Issue Size	Grading Action (September 2015)
IPO Grading	NPR 2,000 Million	[ICRANP] IPO Grade 3 (Assigned)

ICRA Nepal has assigned an “[ICRANP] IPO Grade 3”, indicating average fundamentals to the proposed IPO amounting NPR 2,000 Million of Hydroelectricity Investment & Development Company Limited (HIDCL). 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 position within the Grading categories concerned. Thus, the Grading of 2+, 3+ and 4+ are one notch higher than 2, 3, and 4, respectively. HIDCL is proposing to come out with its IPO of 20,000,000 numbers of equity shares of face value NPR 100/- each to be issued to general public at par.

The grading factors in HIDCL’s strong ownership (entirely owned by Government of Nepal either directly or indirectly), its strategically important role as an implementing agency for the power sector development agendas of Government of Nepal (GoN) and GoN’s commitment towards development of hydroelectricity sector as demonstrated by providing subsidies, grants etc. for Hydro power units. However, the grading is constrained due to HIDCL’s concentrated portfolio towards greenfield power generation projects, lack of regulatory framework considering HIDCL is the first company of its kind in Nepal, inherent risks in infrastructure financing including development risks (risk of hydrological and geological surprises during construction as approved projects are in very initial phases of construction), evacuation risks (possible delays in construction of transmission line by Nepal Electricity Authority) and developer risks owing to the limited experience in commissioning power projects resulting in possibility of time and cost overruns and hence impairing the ability of the projects to timely service their debt obligations. HIDCL has a limited track record (established in July 2011) and ICRA Nepal notes the evolving nature of its systems and processes, which would need to be further strengthened. The capability of HIDCL’s team is adequate for the current scale of operations, but in ICRA Nepal’s opinion, expansion in the management team and infusion of sector expertise is essential for scalability. ICRA Nepal favourably takes note of the robust energy demand outlook within the country, limited use of potential hydropower resources of Nepal so far (installed capacity close to only 800 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 provides HIDCL with more financing avenues in the sector. 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), strengthen its project appraising and monitoring capabilities and manage collections from the borrowers would have a bearing on HIDCL’s operational and financial risk profile.

HIDCL currently lends as a consortium member with other commercial banks. The projects are assessed by HIDCL’s Risk assessment cell (comprising external members from the industry). However, these assessments are limited in scope and ICRA Nepal notes the initiatives taken by HIDCL to strengthen the appraisal process, going forward. So far, HIDCL has approved 8 Run of River type projects with a combined capacity of close to 271 Mw with financing commitment of NPR 3,236.1 million. None of the projects sanctioned by HIDCL are operational as on date and are expected to be commissioned over the next four years. However, the projects are expected to witness significant delays considering limited construction (6 out of 8 projects have not commenced construction), which is further aggravated by the promoter’s limited experience in commissioning such large projects. So far, HIDCL has witnessed marginal disbursements (less than 1% of the commitments have been disbursed so far), however cost overruns due to these delays could affect the power projects viability and hence impact HIDCL’s asset quality profile going forward. Delays in the construction of transmission lines have also been witnessed in the Nepal’s power sector, exposing HIDCL’s borrowers to power evacuation risks. Although the projects



have the power purchase agreements in place, weak financial health of NEA exposes HIDCL approved projects to counter party risks. However, ICRA Nepal draws comfort from NEA being a state owned entity and no history of default in payments to IPPs.

As for impact of earthquake in the approved projects, 5 out of 8 projects were outside the regions affected by earthquake. Further the impact of the quake in affected projects remain minimal due to the fact that most of the projects were either in initial stages of construction or were yet to begin construction.

Since FY12, HIDCL income largely comprised interest on the term deposits made out of equity infused by GoN. However, with disbursements to power projects commencing from FY16, the income profile is expected to improve. Although, on an overall basis the company's return indicators are expected to remain weak due to slow pace of disbursements in the short term leading to sub optimal utilisation of HIDCL's large capital base. In the near term, HIDCL does not plan to raise debt, however various sources are being evaluated (including loan from GoN and/or bilateral/multilateral agencies, bond/debentures etc). Efficient utilisation of capital and managing the asset quality risks would have a strong bearing on HIDCL's financial profile going forward.

### **Company Profile**

Hydroelectricity Investment and Development Company Ltd. (HIDCL) was established on 11<sup>th</sup> July 2011 as a specialized development financial institution to mobilize 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 entire shareholding with the Government of Nepal as on mid-Jul-15 (62.5% direct holding and 37.5% holding equally distributed among three state owned companies viz. Employees Provident Fund, Citizen Investment Trust and Rastriya Beema Sansthan). However 20% stake would be diluted post the proposed IPO.

HIDCL is strategically important for the GoN given the latter's objective of augmenting power capacities across the country. The company would either extend debt or invest through equity route in the potential projects. So far, HIDCL has provided financing commitments to 8 hydropower projects with 7 other projects being in various stages of appraisals. It also has a wholly owned subsidiary - Remit Hydro Limited, which further plans to invest in hydropower projects and HDICL has also holds 14% equity in Power Transmission Company Nepal for the construction of cross border transmission line between Nepal and India. However, HIDCL does not intend to increase its investment in these two companies.

HIDCL reported a profit after tax (PAT) of NPR 434 million during 2013-14 over an asset base of NPR 8,812 million as against a PAT of NPR 418 million on an asset base of NPR 8,793 million in the previous financial year. Based on provisional figures of FY15, HIDCL reported PAT of NPR 339 million over an asset base of NPR 8,749 million.

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