Panchakanya Mai Hydropower Limited: [ICRANP] LBB-/A4 assigned

June 29, 2020

Summary of rated instruments

Instrument *	Rated Amount (NPR Million)	Rating Action
Long-term loan; Fund-based	1,705.14	[ICRANP] LBB-; assigned
Short-term loan; Fund-based	35	[ICRANP] A4; assigned
Total	**1,740.14**	

** Instrument details are provided in* *Annexure-1*

Rating action

ICRA Nepal has assigned a long-term rating of [ICRANP] LBB- (pronounced ICRA NP L double B minus) to Panchakanya Mai Hydropower Limited's (PMHL) long-term loan and a short-term rating of [ICRANP] A4 (pronounced ICRA NP A four) to its short-term loan.

Rationale

The assigned ratings remain constrained by the weak coverage and return indicators of the company that arise from the low levelized tariffs for its two operational projects *(12MW Upper Mai HEP and cascade 6.1MW Upper Mai 'C' HEP)* despite having moderate energy generations. The levelized tariff for the 12-MW project is on the lower side due to the fixed tariff structure of NPR 3.90/unit and 5.52/unit for 43% of the energy with no escalations and only five annual 3% tariff escalations for the rest of the energy to be generated by the 12-MW project. Similarly, the levelized tariff for the 6.1-MW project is on the lower side due to one tariff escalations loss (out of five annual tariff escalations), resulting from the delay in COD vis-à-vis the required commercial operation date (RCOD). The ratings also remain constrained by the tariff risk and the off-take risk for the excess 3.02MW installed capacities of these projects for which there is no power purchase agreements (PPAs). The PPA has been signed only for 15.08 MW *(9.98MW for Upper Mai and 5.1MW for Upper Mai "C")* out of a total installed capacity of 18.1 MW with the Nepal Electricity Authority (NEA), the sole purchaser and distributor of electricity in Nepal with pre-determined tariff rates and tariff escalations. The ratings also take note of the weak liquidity profile of the company due to high financial charges; at ~75% of OPBDITA (last 3-year average ending FY2019) and the increasing principal loan repayments. The liquidity profile remains supported by the director's loan. The ratings are also constrained by the short supply penalty and/or loss of revenue that the company might face for the differences in availability declaration (AD)[1] and the actual energy supplied as indicated in the PPA. Also, the ratings are constrained by the absence of a deemed generation clause in the PPA, which exposes the project to high hydrological risks in case of adverse flow in the river; this is further accentuated by the fluctuating hydrology record of the source. The ratings are also constrained by the counterparty credit exposure of the NEA, which has a moderate financial profile (with recent improvements). This is partly mitigated by the sovereign support of the Government of Nepal (GoN) to the NEA and its past track record of timely payments to independent power producers (IPPs).

Nonetheless, the assigned ratings consider the presence of the institutional promoter under the Panchakanya Group which, so far, has been providing financial and management support at times of need and is expected to do so going forward as well. The ratings also consider the good generation trend of the projects so far; ~86% average generation in the last three years ending FY2019 for the 12-MW project and 81% average generation since COD till 10M FY2020 for the cascade 6.1MW project. The rating remains further supported by a positive demand outlook for the energy sector, owing to the supply-demand gap in the power sector as well as the increasing energy consumption in the nation.

[1] Availability declaration cannot be lower than 60% and 90% of contracted energy for wet and dry season respectively. Supply of energy lower than 80% of AD attracts short supply penalty while excess generation more than AD is not eligible for any payments.

Going forward, PMHL's ability to execute the PPA for the excess 3.02 MW installed capacities and manage the liquidity profile with adequate hydrology of the rivers would be the key drivers for determining the project return metrics and other coverage indicators for the company.

Key rating drivers

Credit strengths

Strong institutional promoter support: The company has been promoted by the Panchakanya Group, which is an established business house with a proven track record of over 40 years. The strong promoter support has helped ease the stress in liquidity through injection of the promoter's loan (NPR 346 million as at mid-April 2020) in times of necessity. The institutional profile would remain an aid for the management and financial support of the company in times of need going forward as well.

Good energy generation from the projects: The 12-MW plant, commissioned in June 23, 2016 has operated for 46 months till mid-May-2020. The project operated at ~55% gross PLF (vs. contract PLF of 64%), generating ~91% of the contract energy for 10M FY2020 with an average PLF of ~55% and an average generation of ~86% for the last three fiscals ending FY2019. The transmission loss has been minimal with only 0.38% for 10M FY2020 and an average of ~0.3% for FY2017-FY2019. Similarly, the 6.1-MW plant was commissioned in July 24, 2017 and remains operated for 34 months till mid-May-2020. The project operated at ~57% gross PLF (vs. contract PLF of 68%), generating ~90% of the contract energy for 10M FY2020 vs. an average PLF of ~53% and an average gross generation of ~81% since operation. The transmission loss has been minimal with only 0.73% for 10M FY2020 and an average of ~0.4% for FY2018 and FY2019 with the energy being evacuated to the Godak Substation.

Credit challenges

High tariff and offtake risk for the excess 3.02-MW installed capacity: PMHL have installed capacities of 12MW for the upper project and 6.1MW for the cascade project. However, the PPA has been signed with the NEA for the project capacities of 9.98 MW and 5.1 MW, respectively. The tariff and offtake risks remain high for the excess installed capacities of 3.02 MW as there is no PPA for the excess installed capacities. The excess energy that the projects are generating is being off taken at 50% rates of the entered PPA rates amid a lack of PPA for the excess capacities.

Weak coverage and return metrices: The operational Upper Mai HEP project was developed at the total project cost of ~ NPR 2,273 million (i.e. ~NPR 189 million per MW) against the budgeted cost of ~NPR 2,040 million i.e. with ~11% cost escalation. Similarly, the cascade project was developed at a total cost of NPR 1,201 million (~NPR 197 million per MW) as against its budgeted cost of NPR 1,050 million i.e. with a cost overrun of ~14%. The return and the coverage indices are on a weaker side owing to the relatively higher project cost (NPR 192 million/MW for aggregate capacities) and higher financial charges (75% of OPBDITA). Fixed tariff rates of NPR 3.90/unit and PPA rates for 43% of the energy and only five times the tariff escalation for the rest of the energy from the 12-MW project, with only four escalations for the cascade project and lack of a PPA for the excess installed capacities has weakened the revenue profile of the company, despite having fair energy generations. Based on our assumption, the return indicators remain weak with project IRR of 9.25%, a cumulative DSCR of 1.09x and a levelized tariff of NPR 5.33/unit for the aggregate project capacity.

Exposure to short supply penalty and/or loss of revenue: The projects remain exposed to short supply penalty and/or loss of revenue for failure to produce an availability declaration which could constrain its revenue profile. The projects are exposed to short supply penalty in case of supply of energy lower than 80% of the AD. Similarly, the project would be losing the revenue for energy supplied above the AD as the NEA is liable to pay for the energy supplied up to the AD declared by the project. Going forward, the prudent declaration of the AD to avoid short supply penalty and/or loss of revenue could impact the profitability and coverage ratios of the company.

High hydrology risk, given lack of deemed generation clause in PPA: The lack of a deemed generation clause in the PPA exposes the project to the hydrology risk in case of an adverse river flow scenario without receiving any compensation for such losses. Additionally, a rain-fed perennial source could affect the hydrology of the river with fluctuations in rainfall in the basin. Such fluctuations were reported in FY2019 when net generation reduced to 77% for 12 MW and to 73% for 6.1 MW projects from the respective generations of 89% and 84% in FY2018.

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

Links to applicable criteria:
Corporate Credit Rating Methodology

About the company

Panchakanya Mai Hydropower Limited (PMHL), incorporated on May 21, 2016 as a public limited company, has a paid-up capital of ~NPR 1,100 million as of mid-April 2020, which is 80% promoter held and 20% publicly held. As on the same date, the major promoters include M/s Panchakanya Power Development Pvt. Ltd. (~39%), Mr. Prem Bahadur Shrestha (~25%), Mr. Dhurba Kumar Shrestha (~6%), Mr. Pradeep Kumar Shrestha (~6%), Mr. Santosh Kumar Pradhan (2%), eight other individuals (2%) and the public (20%).

The company is operating two hydropower projects viz. 12-MW Upper Mai HEP and the cascade 6.1-MW Upper Mai C HEP in Ilam district, Province 1 of Nepal. The 12-MW Upper Mai HEP project is in operation since June 23, 2016 and was developed at a cost of ~ NPR 2,273 (NPR 189 million per MW) at a D:E ratio of 67:33. The cascade 6.1-MW Upper Mai 'C' HEP is in operation since July 24, 2017 and was developed at a total cost of NPR 1,201 million (NPR 197 million per MW) at a D:E ratio of 71:29. Both are run-of-the-river (R-o-R) type projects and have been respectively developed at 38% and 35% of probability of exceedance. Though the installed capacities of these projects are 12MW and 6.1MW respectively for the Upper Mai HEP and the Upper Mai 'C' HEP; the PPA has been signed for the respective capacities of 9.98 MW and 5.1 MW only

The 12-MW Upper Mai project generated ~91% of the contract energy for 10M FY2020 (average generation of ~86%.in the last three ending FY2019) while the cascade 6.1-MW Upper Mai 'C' project has generated ~90% contract energy for 10M FY2020 (average generation of ~79% ending FY2019). Both the projects have been financed by a consortium of banks in lead of Nabil Bank Limited [ICRA-IR] AA-. The company was also graded for its IPO issue back in June 2017 for which it was assigned an [ICRANP] IPO Grade 4.

Key Financial Indicators

Amount in NPR million	Audited			Provisional
	FY2017	FY2018	FY2019	9MFY2020
Operating Income	223	365	322	289
OPBDIT/OI (%)	89%	84%	82%	88%
PAT/OI (%)	8%	-27%	-17%	-7%
Gearing (times) (Total debt/TNW)	2.42	2.45	2.27	2.26
OPBDITA/Interest (times)	1.54	1.33	1.18	1.54
DSCR (times)	1.75	0.74	0.74	0.82
NWC/OI (%)	43%	4%	-3%	4%
Total Outside Liabilities/TNW (times)	2.50	2.55	2.38	2.36
Total Debt/OPBDITA (times)	11.01	7.24	8.24	6.22

Annexure-1: Instrument details

Instrument *	Rated Amount (NPR Million)	Rating Action
Term Loan (long-term; fund based)	1,705.14	[ICRANP] LBB-; Assigned
Working Capital loan (Short-term; fund based)	30	[ICRANP] A4; Assigned
Total	**1,740.14**	

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About ICRA Nepal Limited

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Our parent company, ICRA Limited, was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency. Today, ICRA and its subsidiaries together form the ICRA Group of Companies.

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