Aashutosh Energy Private Limited: [ICRANP] LBB-/A4 assigned

April 27, 2020

Summary of rated instruments

Instrument *	Rated Amount (NPR Million)	Rating Action
Long-term loans; Fund based	1,125	[ICRANP] LBB-; Assigned
Short-term loans; Fund based	40	[ICRANP] A4; Assigned
Short-term loans; Fund based (proposed)	10	[ICRANP] A4; Assigned
Total	**1,175**	

** 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 Aashutosh Energy Private Limited's (AEPL) long-term loan and a short-term rating of [ICRANP] A4 (pronounced ICRA NP A four) to its short-term loans.

Rationale

The assigned ratings are constrained by the nascent stage[1] of development of the 8.63-MW Chepe Khola Small HPP and the inherent project execution risks associated with it. This coupled with the hindering of further works amid the Covid-19 lockdown further accentuates the project execution risk. This may expose the company towards failure in meeting the required commercial operation date (RCOD)[2], resulting in the loss of tariff escalations as well as late COD penalty. Regarding the funding arrangements, although the entire portion of debt has been tied up, the timely infusion of equity (~34% infused so far) from the promoters remains critical. The assigned ratings also remain constrained by the monthly short supply penalty as well as the 30% dry energy short supply penalty as indicated in the PPA, which can impact the revenue profile of the company in case of fluctuations in hydrology. The ratings also consider the timely completion of the under-construction evacuation structure (Kirtipur substation and transmission line connecting Kirtipur substation and Udipur substation) by the Nepal Electricity Authority (NEA), which remains a key monitorable in evacuating power generated from the project; however, the evacuation risk remains low as of now since the project is at a nascent stage of development. Similarly, the ratings concern also emanates from hydrological risks, given the absence of a deemed generation clause in the power purchase agreement (PPA) for which no compensation is payable to the company by the NEA in case of an adverse flow in the river. 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 ratings consider the relatively lower budgeted cost of the project (NPR 1,500 million; per MW cost of ~NPR 174 million) and the presence of experienced promoters and key managerial personnel which is expected to aid the constructional aspect and operational aspects of the project once operational. Likewise, the ratings consider the availability of access roads up to the powerhouse as well as no tunnelling structures in the civil works component which reduces the risk of geological surprises to some extent. The ratings also factor in the high dry energy mix of ~31% in PPA under the six months dry: wet energy mix modality as well as the eight tariff escalations on the base rate, which are expected to support the revenue profile and other indicators amid the fixed tariff regime. Further, the ratings take comfort from the firm long-term PPA for the entire project capacity, which eliminates tariff risk and offtake risk for the energy to be generated by the project.

Going forward, AEPL's ability to swiftly execute the works contract and start site mobilisation soon after the lift-up of the Covid-19 lockdown, timely infusion of the balance ~66% equity, commissioning the project within the estimated cost and timeline remain critical. The extension of the RCOD by the NEA to address the slackness in work amid the Covid-19 pandemic, availability of the NEA's evacuation structures[3] before the project becomes operational, and achieving its designed operating

[1] *Financial progress is around ~7% as of mid-March 2020*

[2] *RCOD is February 21, 2022.*

[3] *The evacuation structures consist of Kirtipur substation and ~10km transmission line connecting Kirtipur-Udipur substations*

parameters as well as interest rate volatility in the market are considered the key drivers for determining the project return metrics and coverage indicators for the company.

Key rating drivers

Credit strengths

Prior experiences of promoters and management team in hydropower sector: AEPL's major promoters and key management team have prior experiences of project development and operations of hydropower projects such as 7.8MW Super Mai HPP(rated at LBB+/A4+) and Ru Ru Jalbidhyut Pariyojana Limited (graded at IPO4+) which are expected to aid the constructional aspect and the operational aspect of the 8.63-MW Chepe Khola Small HPP, once operational. Similarly, the chairperson of the company, Mr. Mohan Bikram Karki, has also been involved in other under-construction hydropower projects. Their past track record of timely execution of project within the budgeted cost remains a comfort in terms of project execution to some extent.

Moderate return and coverage indicators: The project has been appraised to be developed at a total cost of NPR 1,500 million (NPR 174 million per MW) at a D:E ratio of 75:25; which remains on a relatively lower side. This, coupled with the entire energy of the project contracted under the six-months dry energy and six-months wet energy modality with a mix of ~31% dry energy in the overall energy mix are expected to support the revenue profile of the company. Also, the high tariffed (base rate of NPR 8.4/unit) high dry energy mix, coupled with the eight-times tariff escalation would support the revenue profile of the company amid the fixed tariff and fixed escalations regime resulting in moderate return and coverage indicators. However, for the company to be able to avail of all the eight tariff escalations, the project should be in commercial operation latest within six months of the current RCOD (February 21, 2022). Also, any extension of the RCOD by the NEA to address the slackness in work brought by the Covid-19 pandemic would remain critical in determining the tariff escalation for the company.

Low tariff risk given long-term PPA at predetermined tariffs and escalations: The tariff risk for the project remains low as the company has a 30-year PPA with the NEA (the sole purchaser and distributor of electricity in Nepal) for its entire project capacity of 8.63 MW. The dry energy mix for the project is ~31%, with pre-defined base tariffs of NPR 8.4 per kWh for the dry season (December- May) and NPR 4.8 per kWh for the wet season with 3% annual escalation for eight times on the base tariffs.

Credit challenges

Inherent project execution risks amid nascent stage of project development: The 8.63-MW project is in nascent stage of development (7% financial progress as of mid-March 2020). which exposes it to inherent project execution risks. Similarly, the company has not awarded any of its major construction works contract of civil works, hydro-mechanical works, electro-mechanical works and transmission line works, which further pressurises the project execution timeline amid the fixed RCOD structures; failure in meeting which would result in late COD penalty and loss of tariff escalations. Nonetheless, already available access roads up to the powerhouse of the project and lower complexity of civil works with no tunnelling structures remain a comfort in this front.

Timely infusion of balance equity is critical: The project has been planned to be completed within the budgeted cost of NPR 1,500 million at a D:E ratio of 75:25. The management has already tied up a loan agreement with NMB Bank Limited (Rated LA- by ICRA Nepal) for the loan limit of NPR 1,125 million. The first loan disbursement is expected after the infusion of 70% of the overall equity requirement of NPR 375 million; equity infused is ~NPR 126 million (~34%) as of mid-March 2020. The management plans to infuse the additional equity as on a need basis as the work progresses. Hence, the timely infusion of the balance equity would remain critical in a proper and timely loan disbursement from the bank as well as a smooth project execution.

Power to be evacuated through NEA's under-construction evacuation structures: The energy to be generated from the project has been planned to be evacuated through the NEA's proposed substation at Kirtipur, which is in the construction phase. The completion of all proposed NEA's Kirtipur substation and ~10km 132kV transmission line connecting Kirtipur substation and operational Udipur substation remains critical for evacuation of the project's energy. Any delays in the completion of these integrated structures, before the project comes into operation, would have a bearing on the company's revenue profile. However, the required evacuation structures are expected to be in place before the project becomes operational since other projects in the vicinity (including 25 MW Liberty Energy Private Limited rated BB-), having the same evacuation structures and delivery points, are nearing completion and pressurising the NEA for the early completion of the sub-station.

Short supply penalty clauses in case the project is unable to deliver 30% dry energy and required monthly energy supply: The company shall be liable for short supply penalties in case the project is unable to deliver the required 30% dry energy as well as required monthly energy supply to the NEA - resulting in fluctuating revenue profile of the company under such a scenario.

Low offtake risk, however, provision of 10% reserve margin clause in the PPA: The offtake risk for the project is low, given the presence of the take-or-pay PPA for the entire 8.63-MW project capacity. However, a provision of 10% reserve margin clause in the PPA for the specified period empowers the NEA to offtake such 10% energy based on the dispatch instruction of the load dispatch centre without paying any compensation to AEPL. The revenue of the company would be impacted for such specified period if such a scenario prevails.

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 hydrology risk in case of adverse river flow scenarios without receiving any compensation for such losses.

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

Aashutosh Energy Private Limited (AEPL), incorporated on January 5, 2018 as a private limited company, is developing an 8.63-MW Chepe Khola Small HPP in Lamjung district, Gandaki Province of Nepal. It is a run-of-the-river (RoR) type project and has been proposed to be developed at 45% probability of exceedance (Q45) with a total cost of NPR 1,500 million to be funded in a D:E ratio of 75:25. The project is at a nascent stage of development with around 7% financial progress as of mid-March 2020. The paid-up capital of the company as of mid-March 2020 is ~NPR 126 million which is 100% promoter held. Equity infused so far is ~34% of the overall equity requirement. As on the same date, the major promoters include M/s Suruchi Investment Pvt. Ltd. (~28%), Mr. Mohan Bikram Karki (~14%) and M/s Aashutosh Energy Pvt. Ltd. (~13%) and other 27 individual shareholders aggregately holding ~46% of the share of the company.

Annexure-1: Instrument details

Instrument *	Rated Amount (NPR Million)	Rating Action
Fund-based facilities; Long-term loan (A)	**1,125**	
Term Loan	1,125	[ICRANP] LBB-; Assigned
Fund-based facilities; Short-term loans (B)	**40**	
Bridge gap loan (within term loan)	(100)	[ICRANP] A4; Assigned
Overdraft	40	[ICRANP] A4; Assigned
Non-fund based facilities; Short-term loans (within term loan) (C)	-	
Letter of Credit (within term loan)	(700)	[ICRANP] A4; Assigned
Bank Guarantee (within term loan)	(5.478)	[ICRANP] A4; Assigned
Fund-based facilities; Short-term loans (proposed) (D)	**10**	[ICRANP] A4; Assigned
Total (A+B+C+D)	**1,175**	

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About ICRA Nepal Limited

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