HYM Consult Private Limited: Ratings reaffirmed

September 07, 2020

Summary of rated instruments

Instrument (Amounts in NPR Million)	Last Rated Amount	Current Rated Amount	Rating Action
Long-term loans, Fund based (I)*	900	832	[ICRANP] LB+; reaffirmed
Short-term loans, Non-fund based (within I above)	(400)	(600)	[ICRANP] A4; reaffirmed
Total	**900**	**832**	

** Bridge gap loans limit of NPR 180 million can be utilised within the term loans.*

Rating action

ICRA Nepal has reaffirmed the long-term rating of [ICRANP] LB+ (pronounced ICRA NP L B plus) to the reduced long-term loan limits of HYM Consult Private Limited (HCPL). ICRA Nepal has also reaffirmed the short-term rating of [ICRANP] A4 (pronounced ICRA NP A four) to the enhanced short-term loans of the company.

Rationale

The ratings continue to remain constrained by the significant execution risks of the 6-MW Rele Khola Hydroelectric Project (HEP) being developed by HCPL. The project's required commercial operation date (RCOD) was June 1, 2020 and the company has requested an extension of the same by two years, citing impact of the Covid-19 pandemic and other externalities. The uncertainties along the likely RCOD extension and the physical progress so far being limited to ~60% of road excavation, raise timeline concerns. The promoters' limited experience in hydropower project development is also worrisome. The rating action further considers the high evacuation risks for the project as the Kali Gandaki transmission corridor of the Nepal Electricity Authority (NEA) is still under construction, with likelihood of delays here as well. Any unexpected delays in project commissioning as well as corridor completion would increase the project costs. This in turn may lead to weakening of coverage and return indicators, given the fixed tariffs. The hydrological risks are also high for the project, given the lack of a deemed generation clause in the power purchase agreement (PPA). These risks are further heightened by the presence of stringent terms in the PPA, requiring a minimum of 30% dry energy. Failure to deliver this might impact the wet season (June to November) revenues as well.

Nonetheless, the rating action considers the lowered funding risks as the financial closure has now been achieved for the current cost estimates and equity injection is gradually increasing. Also, the project cost remains largely comparable to similar projects. The ratings also factor in the low regulatory and tariff risks, given the presence of the long-term PPA. Additionally, the relatively high share of dry energy (~32%) augurs well for the company's revenue prospects. Moreover, the supply-demand gap in Nepal's power sector is expected to result in a healthy offtake. However, the 10% conditional offtake clauses during the peak rainy months till FY2029 raises some concern. Going forward, the company's ability to commission the project within the budgeted cost and expected timelines and achieve the design operating parameters would remain the key rating sensitivities.

Key rating drivers

Credit strengths

Presence of long-term PPA lowers tariff risks - HCPL has entered into a PPA with the NEA (the sole purchaser and distributor of electricity in Nepal) for its entire project capacity for a period of 30 years from the commercial operation date (subject to validity of generation licence). The predefined tariff, as per the PPA, is NPR 4.80 per kWhr for the wet season, while that for the dry season[1] is NPR 8.40 per kWhr. For these rates, there is a 3% escalation per annum on the

[1] *As per PPA, period from December to May are considered as dry season; rest being considered as wet season.*

base tariff for eight consecutive years. With a firm PPA in place, the tariff risks for the project are low. However, the number of escalations could be lower, in case the project is significantly delayed compared to the revised RCOD. The project also remains exposed to counterparty credit risk, given the moderate financial profile of the NEA. However, it is offset by the sovereign support to the NEA and its past track record of timely payment to private HEP developers.

Healthy mix of dry energy to support return and debt coverage indicators – The contract plant load factor (PLF) for HCPL remains healthy at ~67%, given the six-month dry energy mix (commensurate to ~32% of the annual energy) against the four-month dry energy for most projects (commensurate to ~15–20% of annual energy). Since the dry energy tariff is much higher than the wet energy tariff, it would result in higher average tariff for the energy to be generated by the project . At the same time, the costs are largely comparable to most projects (~NPR 193 million per MW). Hence, the higher average tariff augurs well for the project's return and coverage indicators. However, these indicators could come under pressure in case the project is unable to achieve its design operating parameters.

Debt component tied up at current cost estimates, equity being gradually injected - The project's current cost estimates is NPR 1,155 million, which is to be funded in a debt-to-equity ratio of ~72:28. The financial closure has been achieved and debt drawdown is yet to begin. The promoters have already injected ~36% of the total equity requirements till mid-July 2020, which is being used towards initial project development activities. The equity stake is held by a few promoters with the largest promoter having committed ~44% of the total equity requirements. Hence, the timely infusion of equity could remain critical, given the short timeframe planned for the project execution.

Credit challenges

Project exposed to significant execution risks at preliminary stage of construction - Hydropower projects typically entail significant project execution risks as these projects are located in difficult terrains and are exposed to adverse climatic conditions during the construction period. Also, natural calamities/geological changes can result in time and cost overruns. Rele Khola HEP's RCOD as per the PPA is June 1, 2020, which is likely to be extended by the NEA in view of the pandemic and the likely delays in its transmission corridor. However, the extension remains uncertain and only ~60% of access road excavation has been completed so far, raising timeline concerns. The promoters also have limited experience in HEP development. HCPL has also shifted from the earlier EPC model of construction to multiple contract modality for various segments, wherein timelines may be impacted in case of inadequate cooperation among contractors. Any unanticipated delays could result in sharp cost escalations for the project, incremental interest capitalisation as well as project monitoring costs. This would have a negative impact on the project's return indicators and debt coverage indicators.

High evacuation risks, given possible delays in completion of NEA's transmission corridor - The power generated from the project is to be evacuated through the proposed Dana substation, which is a part of the NEA's Kali Gandaki transmission corridor (~150 km with three substations). Though the NEA had revised the target to complete the Dana substation by September 2020 (earlier March 2019), substantial works along the same remains pending. As of now, the NEA plans to complete the entire transmission corridor by December 2020. Given the possible delays in the NEA's transmission line corridor project, the evacuation risk remains high for the project. In case of any significant delays therein, the project operation is also to be pushed accordingly without any financial compensation.

High hydrological risks due to lack of deemed generation clause in PPA; stringent PPA terms - Like most of the small rivers in Nepal, Rele Khola is also not a gauged river. Hence, the lack of deemed generation clause in the PPA exposes the project to high hydrological risks as the loss in revenues in case of a fall in hydrology will not be compensated. Hydrological risks are further heightened because of the stringent PPA terms in case the project fails to supply a minimum of 30% energy in the dry months. Upon such an event, the supplied dry energy would be assumed to be 30% of the deemed annual energy and the additional energy in the wet months would not be paid. Additionally, the project has a relatively small catchment area of ~27 sq km, which raises concerns regarding the sustainability of flow. Since this is a low discharge and high head project[2], a slight fall in hydrology could impact the energy generation considerably and create pressure on the debt coverage metrics. The PPA also has conditional offtake clauses for 10% energy for five

[2] *Design discharge of 1.48 cusecs and gross head of 505 meters.*

months in the rainy season till FY2029, given the possible over-supply of energy in the country during the high generation season.

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

Incorporated in February 2007, HYM Consult Private Limited (HCPL) is the developer of the 6-MW Rele Khola Hydropower Project in Narchyang VDC, Myagdi District of Gandaki Pradesh, Nepal. The main promoters of the company include Mr. Tara Prasad Bhattarai (~46% stake currently), Ms. Shovana Pokharel (~16% stake) and Mr. Sujan Kumar Kafle (~11% stake), among others.

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About ICRA Nepal Limited:

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