Ru Ru Jalbidhyut Pariyojana Limited: Rating upgraded to [ICRANP-IR] BBB+

September 13, 2021

Facility/Instrument	Rated Amount (NPR Million)	Rating Action
Issuer Rating	NA	[ICRANP-IR] BBB+; upgraded from [ICRANP-IR] BBB

Rating action

ICRA Nepal has upgraded the issuer rating of Ru Ru Jalbidhyut Pariyojana Limited (RJPL) to [ICRANP-IR] BBB+ (pronounced ICRA NP issuer rating triple B plus) from [ICRANP-IR] BBB (pronounced ICRA NP issuer rating triple B). This rating indicates a moderate degree of safety regarding the timely servicing of financial obligations. Such issuers carry a moderate credit risk. The rating is only an opinion on the general creditworthiness of the rated entity and is not specific to any debt instrument.

Rationale

The rating upgradation mainly factors in the improved financial and operational risk profile of the 5-MW operational Upper Hudgi Hydropower Project (HPP) developed by RJPL. Sustained reduction in outage/transmission losses on account of strengthening of evacuation structures along with better hydrology, has resulted in increased generation in recent years. The project was also developed at a relatively lower cost of ~NPR 149 million per MW, which coupled with higher dry energy mix at ~19% of annual contract energy have supported the company's return and coverage indicators. The rating action also derives comfort RJPL's improved financial profile as characterised by low gearing after the recent partial loan prepayment (NPR 80 million prepaid from IPO proceeds in August 2021, which reduced the debt to net worth to 0.25 times) and comfortable debt service coverage indicators. Further, fixed interest rate of 7.10% for the remaining loan tenure (~2.5 years) will support its return indicators and coverage ratios. The rating also factors in the promoters' and management team's adequate experience in the sector, which remains a comfort for the project's operational and maintenance aspects. Similarly, the assigned rating also takes positive note of the low tariff and off-take risks amid already signed power purchase agreement (PPA) with the Nepal Electricity Authority (NEA), the sole purchaser and distributor of electricity in Nepal, with pre-determined tariff rates and escalations.

Nonetheless, the rating remains constrained by the absence of a deemed generation clause in the PPA, which accentuates the concern along hydrological risks. Given the fixed tariff structure, the company's ability to control the steadily rising operating costs will remain crucial. Since the project has been in operation for more than six years with just routine repairs, any major unexpected repair/overhaul requirements could also impact cash flows. The rating is also impacted by the company's increasing working capital intensity and counterparty credit exposure from the NEA, which has a moderate financial profile (albeit 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). Going forward, the project's ability to achieve its designed operating parameters along with its operating cost structure would be the key drivers for determining the company's return metrics and coverage indicators. Additionally, any funding support to the group's under-construction projects will be a key rating sensitivity.

Key rating drivers

Credit strengths

Improving generation trend – The operational 5-MW Upper Hudgi Khola HPP reported sustained improvement in power generation in the last two years at ~87-88% of annual contract energy in FY2020 and FY2021 (average generation was only ~77% for earlier three years ending mid-July 2019). The improvement in energy generation was aided by good hydrology support, along with a strengthened evacuation structure and, hence, reduced outage levels. In the first full year of operations (i.e., FY2016), the project faced ~2,346 outage hours (~6.5 hours per day), which gradually decreased to only ~732 outage hours (~2 hours per day) in FY2021. Furthermore, the net energy supplied to NEA also improved to ~84-85% of the contract energy in FY2020-FY2021 against ~73% in the earlier three fiscals ending mid-July 2019. The improvement in net energy supply was because of reduction in transmission losses to 2.37% for FY2021, which used to be in excess of 4% in earlier years. Going forward, the company's ability to control or further lower the outage levels along with hydrology support and, hence, the generation trend would determine the company's revenue profile.

Healthy capitalisation and coverage indicators; to be further aided by prepayment and interest rate fixation – RJPL's project was developed at a relatively low cost with a relatively low debt mix (~63%) in the project funding. With regular repayment and partial prepayment of NPR 10 million from IPO proceeds by mid-July 2021, RJPL's capitalisation remains healthy with low gearing of 0.42 time as of mid-July 2021; while total debt to OPBDITA also remains comfortable at 1.89 times. With further prepayment of the remaining IPO proceeds (NPR 80 million) in August 2021, the gearing further improved to 0.25 time. The company's interest cover and DSCR remained healthy in FY2021 at 4.78 times and 1.49 times, respectively. With the lowered loan volume and the recent fixation of interest rate at 7.10% for the remaining loan tenure (~2.5 years), these indicators are likely to improve further. Assuming energy generation remains similar to recent levels, ICRA Nepal expects the cumulative DSCR for the remaining loan tenure to remain at ~2.0 times.

Stable operating profitability and dividend policy – The project has been in operation since March 2015 and was developed at a relatively low cost of NPR 745 million (~NPR 149 million per MW), funded in an initial debt-to-equity ratio of ~63:37. This has supported the company's profitability profile in the fixed tariff regime. While the improved operational performance has supported profitability, this was offset by increased operating expenses leading to a largely stable operating profitability. However, the lowering debt levels and interest rate fixation at 7.10% for the remaining loan tenure led to improved net profitability metrics. RJPL maintained a stable dividend policy and provided ~10% returns to shareholders on an average from FY2017 to FY2019 and further proposed 10% returns for FY2020 and FY2021 as well.

Low tariff risk, given long-term PPA at predetermined tariffs and escalations – The tariff and off-take risks remain low for the project amid the presence of a firm PPA with the NEA. The tariff for the wet season (mid-April to mid-December) is NPR 4 per kWh while that for the dry season is NPR 7 per kWh. For the PPA rates, there is a 3% annual escalation on the base tariff for nine times. The project is eligible for all its escalation clauses. By the Government's initiative to promote hydropower development, the company has also entered into a promotional tariff rate agreement of NPR 4.80 and NPR 8.40 (for wet and dry seasons, respectively) with 3% annual escalation for 5.0 times on the base tariff. This would be applicable till the completion of seven years from the commercial operation (i.e., till March 2022). Thereafter, the rates will be as per the original PPA. Though the original tariff rates are 20% lower than recent projects, this is compensated by the lower project cost structure. Incrementally, the Government has also waived the short supply penalty for projects up to 10MW, which remains a positive factor.

Experienced promoters and management team – The company's promoters/ board and the senior management have adequate experience and technical expertise in the hydropower/ engineering sector. The promoters' extensive association with other hydropower projects and the management team's experience provide comfort in terms of the project's operational aspects. The company has developed in-house maintenance capabilities for routine issues, which remain a positive.

Credit challenges

Increased working capital intensity – The company has witnessed gradual build-up in debtor levels in the last two fiscals (debtor days of 205 in FY2021 against 105 in FY2019), on account of the increasing promotional tariff receivables. The timeline of receipt of these remains uncertain and in the past too, the recovery of such receivables was lumpy. Hence, the working capital intensity (net working capital to operating income) is likely to remain high over the near term (57% for FY2021), impacting the company's liquidity profile. However, the company is not reliant on short-term debts to finance the working capital requirements, which provides comfort.

Rising operating costs amid fixed tariff structure – Since the revenues are fixed, rising operating cost could have impact company's profitability and coverage ratios. The company has reported a steady increment in operating costs at CAGR of ~10% in the last four fiscals. Hence, its ability to control the operating cost structure would also remain critical.

High hydrology risk, amid lack of deemed generation clause in the 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. This concern is further accentuated by the fact that the river flow is dependent on the rain-fed, perennial source, which could affect the available hydrology based on rainfall fluctuations in the basin.

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

Links to applicable criteria:
Issuer Rating Methodology

About the company

Incorporated on March 22, 2006, as private limited company, RJPL was converted into a public limited company on July 23, 2015, to facilitate public participation. As on mid-July 2021, the company's paid-up capital stood at ~NPR 408 million with its major promoters being Mr. Bharat Prasad Nepal (12%), M/S. Subhakarma Investment Company (10%) and M/S. Samuchit Investment Company (9%).

RJPL has one operational hydropower project, the 5-MW Upper Hugdi Khola Hydropower Project in the Gulmi District of Province-5 of Nepal. A run-of-the-river (R-o-R) type project, it has been developed at 43% probability of exceedance (Q43). The project came into commercial operation from March 23, 2015, against a required COD of March 28, 2014, and was developed at a total cost of NPR 745 million, which was funded by an initial debt-to-equity ratio of ~63:37.

Key Financial Indicators

Amount in NPR million	Audited				
	FY2017	FY2018	FY2019	FY2020	FY2021
Operating Income (OI)	121	122	124	147	150
Profit after tax (PAT)	39	34	36	58	71
OPBDITA/OI (%)	84%	81%	80%	80%	80%
PAT/OI	32%	28%	29%	40%	48%
ROCE (%)	11%	11%	11%	13%	13%
Total debt/Tangible net worth (TNW; times)	1.34	1.09	0.95	0.79	0.42
Total Outside Liability/TNW (times)	1.35	1.11	0.97	0.80	0.43
Total Debt/OPBDITA (times)	4.29	3.95	3.47	2.60	1.89
Interest coverage (times)	2.39	2.23	2.30	3.22	4.78
DSCR (times)	1.43	1.13	1.09	1.28	1.49
NWC/OI (%)	41%	58%	37%	44%	57%

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