

PRESS RELEASE

SOLU HYDROPOWER LIMITED

August 2024

Ratings

Instrument/Facilities	Amount (NPR Mn)	Rating	Rating Action
Issuer Rating	NA	IRN BB (Is)	Reaffirmed
Total	NA		

Infomerics Credit Rating Nepal Limited (Infomerics Nepal) has reaffirmed the issuer rating of IRN BB (Is) [IRN Double B (Issuer)]. Issuers with such rating are considered to have the moderate risk of default regarding timely servicing of financial obligations.

Detailed Rationale

The reaffirmation of ratings assigned to Solu Hydropower Limited (SHL) continues to derive strength from the robust and experienced group of promoters & a proficient management team, low tariff and offtake risk with the presence of a long term PPA alongside low evacuation risk. The rating also factors in the resiliency of management to overcome a major setback through a strategic redesign of penstock pipes alongside restructuring its debt, thereby avoiding significant increase in overall project cost. Additionally, the ratings also factor in the moderate counter party risk, improving electricity demand, tie up of project cost and GoN¹ support for the power sector.

However, the rating continues to be mainly constrained by the execution and stabilization risk associated with SHL's under construction 82 MW hydropower project given its significant cost and time overruns. The rating is also constrained by significant delays in originally envisaged timelines due to realignment of penstock pipes resulting in potential tariff escalation losses and any further delays may result in reduction of project life further and ultimately adversely impact the initially estimated financial benefits from the project. Also, the project is exposed to the hydrology risk connected with run-of-river (ROR) power generation arrangement and vulnerability to natural calamities.

Going forward, the ability of the company to manage the timely completion of the project without any additional time or cost overrun alongside ability to raise IPO proceeds at par without significant delay will be key rating sensitivities.

Detailed Description of Key Rating Drivers

Key Rating Strengths

Project secures funding

The total estimated project cost for 82 MW amounts to NPR 16,644 Mn (NPR 203 per MW) to be funded in debt to equity ratio of 40:60. The company entered in to a loan agreement with both international and local lenders on December 31, 2014. As on mid-July 2024, of the NPR 10,000 Mn of equity required for project, the promoter shareholders have already infused 80% of the equity. The remaining 20% equity is projected to be raised from an IPO at par value which is suffering from regulatory delays prompting management to rely on local additional borrowings. Delays in meeting this equity injection target could impact the project cost on account of increased IDC. Issuance and receipt of such IPO proceeds at par within reasonable time will remain key monitorable.

Strong and experienced promoters/group and management team

SHL is governed by a five-member board of directors chaired by Mr. Subhash Chandra Sanghai, with 45 years of business experience, including a significant portion of his career focused on the tea industry. Mr. Vishal Agrawal, Director, brings over 23 years of experience and holds directorship positions in various companies. Similarly, Mr. Vijay Singh Baidya, Director, have more than 35 years of experience in trading and industry. Mr. Trilokachand Agrawal and Mr. Aaditya Sanghai, directors, bring in decades of experience and holds directorship of various financial institutions. Furthermore, SHL derives strengths from the financial flexibility of its promoter groups namely Triveni Group, Vishal

¹ Government of Nepal

Group, Goyal Group, Rathi Group, Baidya Group, and Jain Group. These groups have been operational across various sectors for decades, instilling confidence in their market presence and knowledge. Moreover, the board is aptly supported by experienced and well diverse management team.

Low offtake and evacuation risk with presence of a long-term PPA including predetermined tariffs

SHL had entered into a long term PPA of 30 years from commercial operation date (COD) or till validity of Generation License, whichever is earlier, for sale of power to be generated from the 82 MW project. Furthermore, the tariff for wet/ dry season (8-4 months) is NPR 4.80/ 8.40 per kWh with 3% escalation on base tariff for 5 times in every year after completion of 12 months from COD date. Additionally, the project has a moderate PLF of ~63%. Furthermore, the company successfully established a PPA agreement with NEA in USD, which accounts for 55% of the total bill amount, and this arrangement extends for ten years from the COD. The USD rate is fixed at NPR 98.68 per USD assisting SHL in receiving required foreign exchange for repayment of loans. Regarding evacuation, the power expected to be generated by the project will be evacuated through 4.123km long 132kV transmission line to NEA's operational Lamane substation, thereby removing the evacuation bottleneck from NEA's end.

Strategic penstock redesign and debt restructuring propel project past financial setback

The project encountered significant financial losses due to an unstable penstock caused by unfavorable geological conditions. This necessitated a complete redesign of the penstock, resulting in considerable cost and time overruns. However, strategic measures and contract execution led to written off of 40% of the total USD Debt. Moreover, 19.75% of the total USD Debt will be written off at the end of the loan term, considering potential adjustments to the Required Commercial Operation Date (RCOD), PPA penalties, and generation license term. Furthermore, the project benefited from the waiver of Interest During Construction (IDC) for both senior and subordinated loans, due from January 2020 till COD. The project is now progressing with the construction of a new penstock tunnel along a different alignment and the project is at ~93% overall completion as on June 2024 with expected date of completion being September 2025.

Key Rating Weaknesses

Project implementation risk and stabilization risks with possibility of tariff escalation loss

The company is constructing Lower Solu Hydroelectric Project (LSHEP), which suffered from significant cost overruns and time extensions as a result of unstable penstock pipes resulting in complete redesign of such. The total estimated cost of the project is NPR 16,644 Mn (equivalent to NPR 203 Mn per MW) which increased from NPR 15,811 Mn (NPR 193 Mn per MW) after considering concession provided by foreign lenders, which is proposed to be financed in the debt: equity mix of 40:60. The increase in cost is attributable to increase in IDC as result of delays in IPO and construction of additional adit tunnel to expedite the work. As per the management, the project has achieved ~93% overall physical progress with expected completion date being September 2025 in contrast to RCOD of February 14, 2022 set in PPA. Since, the number of allowable escalations is contingent upon the actual COD, in the event of a delay in commissioning by more than six months from the RCOD, the company could potentially lose one tariff escalation. Additionally, each subsequent year of delay in COD might result in further tariff escalation losses. Furthermore, an extended COD could potentially limit the project's economic lifespan, given that its generation license remains valid only until March 2050. The ability of the management to secure extension of the generation license till PPA period and completion of the project without incurring further cost overruns will be key monitorable.

Hydrology risk associated with run-of-the-river power generation

ROR projects face direct exposure to the risks linked to fluctuations in water discharge from rivers, given that they lack the capacity for water storage. LSHEP is intended to utilize discharge from Solu river having catchment area of 411 sq. with design discharge of the project is 19.85m³/s at exceedance flow of 40%. Insufficient water flow may lead to reduced energy output, affecting project performance and financial viability. Therefore, the project is exposed to risks linked with fluctuations in river water discharge. Furthermore, the lack of a deemed generation clause in the PPA leaves the project vulnerable to revenue losses during adverse conditions without compensation, which may have an impact on company's financial health.

Risk of natural calamities

Hydropower projects are prone to risk from natural disasters, such as floods, landslides and earthquakes, as the projects are generally located in challenging terrains with uncertain geology. These occurrences can significantly disrupt infrastructure, leading to construction delays and inflated costs. Moreover, they may disrupt power generation and evacuation, consequently affecting the financial performance of the projects. Hydropower projects like LSHEP are inherently exposed to risk of these natural calamities, which may affect the project's execution, functioning and financial performance.

Analytical Approach: Standalone

Applicable Criteria:

[Power Projects Rating Methodology](#)

Link to past rating rationale:

[Solu Hydropower Limited: Issuer Rating Assigned](#)

About the Company:

Incorporated on June 09, 2010, as a Private Limited, the company was subsequently converted into Solu Hydropower Limited (SHL) on July 13, 2022. Initially, Essel Infraprojects Ltd, India held the majority stake, which was later transferred to individual Nepalese Shareholders. Currently, the company is promoted by stakeholders belonging to Triveni Group, Vishal Group, Goyal Group, Rathi Group, Baidya Group, and Jain Group. The 82 MW LSHEP is located in the Solukhumbu district of Nepal and have catchment area of 411Km², with a design discharge of 19.85m³/s at 40% PoE and a gross head of 493m. As of mid-February, 2024, the major shareholders include Mr. Govind Lal Sanghai (8.16%), Mr. Nitesh Agrawal (7.09%) and Mr. Ram Chandra Sanghai (4.93%).

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About Infomerics Credit Rating Nepal Limited:

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