Rating Rationale

API Power Company Limited

Rating

Facility/ Instrument	Amount (Rs. In Million)	Rating[1]	Rating Action
Issuer Rating	NA	CARE-NP B+ (Is) [Single B Plus (Issuer)]	Assigned

**The issuer rating is subject to the company maintaining overall gearing not exceeding 1.5x at the end of FY21*

CARE Ratings Nepal Limited (CRNL) has assigned Issuer rating of 'CARE-NP B+ (Is)' to API Power Company Limited (APC). Issuers with this rating are considered to have high risk of default regarding timely servicing of financial obligations in Nepal.

Detailed Rationale & Key Rating Drivers

The ratings assigned to APC is constrained by delays in payment of bank's debt obligation due to stressed liquidity and cash flow mismatch during FY20 (refers to 12 months period ended mid-July 2020) and operational hydropower plant being operated at low Plant Load Factor (PLF). The rating is also constrained by project implementation risk and stabilization risk associated with the under-construction projects, exposure to volatile interest rates and regulatory risk coupled with hydrology risk associated with run-of-the-river power generation. The ratings, however, derive strength from experienced board member and management team, multiple hydropower projects being developed through associate companies, comfortable financial risk profile, financial closure achieved for under construction project and low power evacuation risk for the operational plants. The ratings also factor in presence of power purchase agreement with sufficient period coverage, moderate counter party risk, current demand and supply gap of power generation in the country and government support for the power sector. Sufficient hydrology to generate contracted energy, timely receipt of the payments from NEA and repayment of the bank loan obligations and the ability of company to reduce gap between operational PLF and contracted PLF are the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Delays in payment of bank's Obligation

The company has delayed the payment of bank's debt obligations on multiple times during FY20. The delay in repayment of the bank's debt obligations which was in the range of (5 days to 52 days) was mainly due to delay in releasing payment by the NEA amid the Covid-19 induced lockdowns and also due

to the weak generation in one of the projects being its first year of operations. There are no delays in meeting the bank's obligation for last 2 quarters due to better generation of power and improved cashflow. Also, during H1FY21, APC has increased the cash reserve by issuing the right share from Rs 33 Mn at the end of FY20 to Rs. 265 Mn at the end of H1FY21 which provide sufficient cushion to APC to meet the debt obligation on time in near future.

Project operated at low PLF till Mid -July 2020

The annual contracted PLF of the Naugarh Gad Hydropower project (NGHP) is 69.75% of the installed capacity of the plant. The project has been operated at low PLF of 47.07% (over generation capacity) during FY19 which improved to 53.23% during FY20, mainly on back of weak hydrology during the review period. The power generation from the project as a percentage to the contracted power as per the PPA was 67.30% in FY19 and 76.31% in FY20. The ability of the company to reduce the gap between operational PLF and contracted PLF and availability of sufficient hydrology is the key rating sensitivity.

The annual contracted PLF of the Upper Naugarh Small Hydroelectric Project (UNSHP) is 69.69% of the installed capacity of the plant. The project operated for only 9 months during FY20. During 9 months of operation, the PLF from the project was low at 35.81% (over generation capacity). The power generation from the project as a percentage to the contracted power as per the PPA was 67.38% in FY20.

Project implementation risk and stabilization risk

UCHP 40-MW project which is at initial stage of development, is exposed to inherent project execution risks. All major contracts across civil, hydromechanical, electromechanical and transmission line works are executed. Whereas in case of CSP 4 MW project RCOD date as June 09, 2019 but still project is not in operation. Project was postponed due to delay in funding the project from bank. However, its financial closure has already been achieved and APC expect that the project to come into operation from May 2021. The company's project completion track record in case of hydropower project prior to the RCOD in the earlier two operational projects provides comfort, though capacity remains to be tested for the bigger project. The project's ability to commission within the budgeted cost and expected timeline along with its ability to attain design operating parameters would remain critical.

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

Run-of-the-river power is considered an unsteady source of power, as a run-of-the-river project has little or no capacity for water storage and therefore is dependent on the flow of river water for power generation. It, thus, generates much more power during wet season when river flows are high (Mid-April to Mid-December) and less during the dry season (Mid-December to Mid- April). The energy generated by operational projects are hampered due to the fluctuation in river hydrology. First project, NGHP was able to generate only 76% of contacted energy during FY20 due to which penalty of Rs. 0.4 Mn was

charged by NEA. Similarly, for second project, UNSHP was able to generate only 67% of contracted energy during FY20 due to which penalty of Rs. 16 Mn was charged. NGHP utilized discharge from Naugarh Gad, UNSHP utilize discharge from Naugarh Gad & Gaddi Gad and UCHP utilizes discharge from Chameliya Khola having catchment area of 192 sq. kms, 148 sq. kms and 656.3sq. kms respectively based on Perennial River. Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river/ Khola.

Exposure to regulatory risk

Government of Nepal (GON) has recently established Nepal Electricity Regulatory Commission (NERC) for regulating generation, transmission and distribution of electricity in Nepal. NERC has issued a directive to take approval before public issuance of share capital. It poses a new challenge to hydropower companies which has to go through an additional approval process before it can issue shares to public. Hence, the hydropower companies planning for public issuance of share capital is exposed to risk associated with delay in approval process which may delay project funding and eventually delay the project.

Key Rating Strengths

Board members and management having experience in hydro power sector

APC is managed under the overall guidance of the company's Board of Directors (BoD), who possesses wide experience in the Power sector. Mr. Satish Neupane is the Chairperson of the company, he is also founder director of Arun Valley Hydropower Development Company Limited [AVHDCL, CARE-NP BB+ (Is)], Managing Director of API Hydro Mechanical Pvt. Ltd. Mr. Neupane has more than a decade of experience in hydro power sector. Mr. Sanjeev Neupane is the Managing Director who looks after day-to-day operation of APC since 2012. He was also director of Arun Kabeli Power Limited. Currently he is also one of the directors of AVHDCL.

Multiple hydropower projects being developed through associate companies

APC has been involved in operation and construction of hydropower projects by itself and through associate companies under Arun Valley Hydropower Group of companies. Currently, the group has 57.30 MW hydropower projects which are operational and 49.94 MW hydropower projects are under construction. Also, there are 22 MW of solar power projects which are under initial stage of construction/ pipeline to be developed by the group and its associate companies.

Track record in operating hydro power projects

APC has two operational projects. NGHP with operational capacity of 8.5 MW is located at Darchula district of Nepal. The project came into operation since August 2015. Another operational project is UNSHP of 8 MW capacity located at Darchula district of Nepal. This project came into operation since October 30, 2019.

Power purchase agreement with sufficient period coverage

APC had entered into a long term PPA with NEA for sale of power to be generated from different projects. The period of the PPA is 30 years from the date of COD (25 years in case of solar project) or till validity of Generation License, whichever is earlier. In case of NGHP the tariff for wet season is Rs 4.00 per kWh and for dry season is Rs 7.00 per kWh whereas for UNSHP and UCHP tariff for wet season is Rs 4.80 per kWh and for dry season is Rs 8.40 per kWh and for CSP tariff rate is Rs. 7.30 per KWh with clause of escalation in the base tariff over the period. The Required Commercial Operation Date (RCOD) for UCHP is February 25, 2023 and for CSP was June 9, 2019 (expected to be in operation from May 2021). The achievement of the RCOD would remain critical in determining the number of tariff escalations that the project would avail as well as implications of any late COD penalty.

Financial Closure achieved for under construction project

The total cost of UCHP is Rs. 7,400 Mn which is proposed to be financed in debt equity ratio of 70:30 (i.e., Rs. 5,180 Mn debt and Rs. 2,220 Mn equity). APC has achieved the financial closure for the entire debt of UCHP on September 27, 2020. Similarly, for CSP, total cost of the project is Rs. 330 Mn which is proposed to be financed in debt equity ratio of 75:25 (i.e., Rs. 247.5 Mn debt and Rs. 82.5 Mn equity). APC has already achieved the financial closure on January 04, 2021.

Comfortable financial risk profile

APC reported Rs. 324 Mn through the sale of electricity during FY20 as compared to Rs. 179 Mn in FY19. The increase in revenue during FY20 was due to operation of UNSHP which contributed 36% (i.e. Rs. 116 Mn) of total sales as in FY20. PBILDT of the company increased by 77% to Rs. 288 Mn in FY20 from Rs. 163 Mn in FY19. Due to which the PBILDT margin of the company marginally increased to 87.01% during FY20 as compared to 86.95% in FY19. PAT of the company during FY20 was Rs. 109 Mn with the PAT margin of 32.80%.

Company reported overall gearing ratio of 1.44x at the end of FY20 as compared to 1.52x at the end of FY19. Gearing ratio improved marginally due to increase in profit during FY20 which resulted increased in reserve and net worth and also repayment of term loan has further strengthened the gearing ratio. Total debt to Gross Cash Accrual (GCA) ratio improved to 14.65x during FY20 as compared to 21.70x in FY19 due to decrease in long term debt of the company. Likewise, interest coverage ratio has been improved from 2.25 in FY19 to 1.91 in FY20. Current ratio of APC increased marginally to 0.73X in FY20 from 0.42x in FY19. As on H1FY21, APC reported revenue from sales of energy of Rs. 242 Mn which is increased by 79.19% over H1FY20 with PBILDT margin of 92.23%. PAT of the APC was reported Rs. 143 Mn during H1FY21 from Rs. 41 Mn from H1FY20.

Low Power evacuation risk for all projects

The Power generated from the under-construction project CSP is proposed to be evacuated through 3km long 33kV Transmission Line to NEA's Chandranigahapur substation at Rautahat District, likewise for UCHP was proposed to be evacuated through 16km long 132kV transmission line to NEA's Balanch substation at Darchula District. The power evacuation risk is low given that both substations are already in operation. In case of operational project NGHP and UNSHP energy totaling 16.5 MW is being evacuated through 132kV transmission line to NEA's operational Balancha substation.

About the Company

API Power Company Limited (APC) is a public limited company promoted by business persons having long experience in the hydropower and other sectors for setting up Hydroelectric Project (HEP) in the territory of Nepal. The company was established as on June 19, 2003 as a private limited company and later converted to public limited company by reorganizing the shareholding pattern of the company as on July 21 2013. APC have two operational projects of 8.5 MW run-of-the-river (RoR) HEP at Naugarh river (Naugarh Gad HEP) in Darchula district (came into operation in August 2015) and 8 MW Upper Naugarh Gad HEP lies upstream of the first project (came into operation in October 30, 2019). There are two under construction project of 40 MW Upper Chameliya HEP whose RCOD is February 2023 and Chandranigapur 4 MW Solar PV Project, its expected RCOD is May 2021.

Brief Financial Performance of last two years and H1FY21 is as follows:

Particulars	FY19 (A)	FY20 (A)	H1FY21* (UA)
Income from Operation	179	324	242
PBILDT	163	288	280
Overall Gearing (times)	1.52	1.44	0.86
Interest coverage (times)	2.25	1.91	2.90
Total Debt to GCA (times)	21.70	14.65	11.27

* refers to 6 months period ended mid-January 2021

Analyst Contact	**Relationship Contact**
Mr. Shisir Pokharel	Mr. Sajan Goyal
shisir.pokharel@careratingsnepal.com	sajan.goyal@careratingsnepal.com
Tel No.: +977-01-4012628	Tel No.: 9818832909/+977-01-4012628/29/30