Arun Kabeli Power Limited

Ratings

Instrument/Facilities	Amount (Rs. Million)	Ratings[1]	Rating Action
Long Term Bank Facilities	**2,410.66**	**CARE-NP BBB- [Triple B Minus]**	**Reaffirmed**
Short Term Bank Facilities	**195.30**	**CARE-NP A3 [A Three]**	**Reaffirmed**
Total Facilities	**2,605.96**		

** Details of Facilities in Annexure 1*

CARE Ratings Nepal Limited (CRNL) has reaffirmed the rating of 'CARE-NP BBB-' assigned to the long-term bank facilities and 'CARE-NP A3' assigned to the short-term bank facilities of Arun Kabeli Power Limited (AKPL).

Detailed Rationale & Key Rating Drivers

The reaffirmation of the ratings assigned to the bank facilities of AKPL derive strength from the rebound in financial performance during Q1FY25 (Unaudited, refers to the three-month period ending mid-October, 2024) leading to net profitability with adequate gross cash accruals, following moderation during FY24 (refers to the twelve-month period ending mid-July 2024) as the plant was shut down from June 15, 2023 to January 24, 2024 owing to damages from flash floods of June 2023. The ratings also factor the moderate operational performance of the plant and moderate capital structure and debt coverage indicators of the company. The ratings, also, take into account experienced directors in powers sector, association with group having multiple hydropower projects, presence of power purchase agreement (PPA) with sufficient period coverage, moderate counter party risk and government support for the power sector.

The ratings, however, remain constrained by the equity commitments to an under-construction hydropower project and related project implementation and stabilization risk, risk of natural calamities inherent in operational hydropower project, hydrology risk associated with run-of-the-river power generation and exposure to volatile interest rate risk.

Going forward, the ability the company to reduce the gap between operational Plant Load Factor (PLF) and contracted PLF on sustained basis and availability of sufficient hydrology with timely receipt of payments from Nepal Electricity Authority (NEA) will be the key rating sensitivities. Furthermore, any substantial capital commitment that could lead to material deterioration in the company's capital structure from current levels will also be key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Strengths

Experienced directors/management team in power sector and part of Arun Valley Hydropower Group of Companies

AKPL is managed under the overall guidance of the company's Board of Directors (BoD), who possesses wide experience in the power sector. The board is chaired by Mr. Ramesh Prasad Neupane, who has more than two decades of experience in hydropower sector. He is also Managing Director of Arun Valley Hydropower Development Company Limited (AHPC) (CARE-NP BB+ (Is) and director of Ridi Power Company Limited (RIDI) (CARE-NP BB+(Is)). Mr. Jeevan Raj Shakya, Managing Director has more than one decade of experience in hydro power sector. He is supported by other experience management team members. Currently, Arun Valley group of companies have 148.74 MW operational power projects which include 25MW Kabeli B1 Hydropower Project (KBHP) operated by AKPL. Experienced background of BOD's and AKPL being a part of Arun Valley group could provide technical support and operational synergy to AKPL.

[1]Complete definition of the ratings assigned are available at https://www.careratingsnepal.com/ and other CARE publications

Average financial and operational performance during FY24; however, rebound in Q1FY25

Total operating income (TOI) of the company was Rs. 197 Mn during FY24, operated for around last 5.5 months during FY24 (FY23: Rs. 638 Mn) as the plant was shut down due to flood from June 15, 2023 to January 24, 2024 owing to damages of project assets caused by flood at plant site dated June 15, 2023. PBILDT margin was around 78% during FY24 which were around 87% during FY23 mainly on account of shut down of plant and owing to low energy generation that impacted the Gross Cash Accruals (GCA) of the company to negative during FY24 (FY23: Rs. 214 Mn). The energy generated and billed to NEA was ~61% of contracted energy during H1FY25 mainly due to disruption for around 40 days of NEA's 132 KV Kabeli transmission lines by flood (~65% of contracted energy for last 5.5 months during FY24).

The financial performance of the company was satisfactory during Q1FY25 with the TOI of Rs. 214 Mn and PBLIDT margin of 77%. The company GCA stood adequate at Rs. 101 Mn during Q1FY25 vis-à-vis scheduled term loan repayment of Rs. 102 Mn in FY25. The company's ability to reduce the gap between operational PLF and contracted PLF, on a sustained basis, will remain a key monitorable aspect.

Moderate capital structure and debt coverage indicators

The capital structure of the company was moderate with overall gearing ratio of 0.67x at the end of FY24 (FY23: 1.63x). The overall gearing ratio improved on account of prepayment of term loan coupled with the increase in tangible networth of the company post the right issue. Interest coverage ratios stood at 0.55x during FY24, which decreased from 1.59x during FY23 on account of decrease in overall TOI. Total Debt / GCA stood negative at the end of FY24 (FY23: 15.70x). Overall gearing ratio of the AKPL has improved to 0.62x with the moderate interest coverage ratio of 2.70x in Q1FY25. Also, the company has liquid investment in listed shares which provides the company with additional liquidity cushion. The ability of the company to sustain its net profitability over next couple of years while maintaining debt service coverage indicators at envisaged level is critical from credit perspective.

Power purchase agreement with sufficient period coverage

AKPL had entered into PPA with NEA as on July 13, 2012 for sale of 25 MW power to be generated from the project. The period of the PPA is 30 years from Commercial Operation Date (COD) or till validity of Generation License (received on July 12, 2013 for 35 years), whichever is earlier. PPA period may be extended with mutual consensus during the last six months of validity. The tariff for wet season (Mid-April to Mid-December) is Rs 4.80 per kWh and for dry season (Mid-December to Mid-April) is Rs 8.40 per kWh with 3% escalation on base tariff for 5 times on annual basis. KBHP utilizes discharge from snow fed Kabeli River with higher catchment area of 710 sq kms, which supported the project to generate satisfactory energy levels in dry as well as wet seasons since commissioning of plant. The annual contracted energy for the project is 141.74 million units (MU) (i.e., 22.89 MU for dry season and 118.86 MU for wet season) at contracted PLF of 64.72%. AKPL commenced it commercial operations from November 09, 2019 and was eligible for all five tariff escalations on tariff rate.

Favourable Government policies towards power sector

Government of Nepal (GoN) considers power generation as priority sector and intends to maximize private sector participation in generation of electricity by offering different exemptions and facilities on power sector. GoN has announced full tax exemption for first 10 years and 50% tax exemption for next 5 years for such person/entity who starts commercial operation, transmission and distribution of electricity up to mid-April 2027. This approach is aimed at promoting investment and growth in the energy sector. Furthermore, directives from the Nepal Rastra Bank (NRB) mandate financial institutions regulated by NRB to allocate a minimum share of their total advances to the energy sector. This strategic initiative is expected to contribute to the financial support and development of projects within the energy sector which argues well for the sector. The increasing trend of cross-border energy trade, coupled with the growing prospects stemming from new

bilateral agreements between Nepal and India for additional power export from Nepal to India, further boosts the long-term demand outlook for the power sector in Nepal.

Key Rating Weaknesses

Associated project implementation and stabilization risk related to investment in under construction hydropower project

Kabeli Energy Limited (KEL) has been setting up 37.60 MW Kabeli A Hydropower Project in Pachthar and Taplejung district. The estimated total cost of the project is Rs. 7,520 Mn proposed to be financed in debt equity mix of 60:40. AKPL has committed to invest 40% of equity amount i.e. 1,200 Mn in KEL. Rs. 733 Mn (61% of AKPL equity commitment) has already been invested by AKPL as mid-October 2024 and balance equity will be infused on gradual basis as per the requirement of project. Substantial fund flow requirement for such investments as a result of current commitments and any potential cost overrun, which is not uncommon for hydro projects in Nepal given the challenging geology, could have adverse impact on future liquidity prospects and financial risk profile of the company. Thus, additional required investments will continue to be key monitorable. Furthermore, any major regulatory changes related to investment companies which may impact the financial risk profile of the company will remain concern from analytical perspective.

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 summer season when river flows are high (Mid-April to Mid-December) and less during the winter season (Mid-Dec to Mid-April). Hence, the project is exposed to risk associated with variation in discharge of water from the aforesaid river.

Risk of natural calamities

In Nepal, hydropower projects are usually located in terrains that are topographically challenging making their operations vulnerable to adversities of nature. Floods and landslides that tend to occur in these areas pose threat to these power projects damaging their infrastructures. These natural calamities can adversely affect the smooth flow of power generation and distribution, which can impact financial returns of the projects. AKPL is also exposed to such risks of natural calamities that might cause infrastructural, operational, and financial damages to the project. Revenue loss from shut down of the plant till January 24, 2024 (around 6.5 months in FY24) has resulted into material revenue loss during FY24.

Exposure to volatile interest rate risk

AKPL's interest rates are based on a fixed rate interest for three years beginning from October 2024 and after 3 years the interest rate will be Base rate plus 1% premium, so interest rate is changed accordingly on a monthly basis after 3 years. The base rates of the banks and financial institutions (BFIs) in Nepal remain quite volatile as they are impacted by available liquidity in the system which leads to change in interest rates. Higher interest rates than envisaged could result in squeezed margins of the company. Hence, funding taken by the company is exposed to volatile interest rates.

About the Company

Arun Kabeli Power Limited (AKPL) is a public limited company incorporated in January 07, 2011, is promoted by business persons having long experience in the hydropower and other sectors for setting up Hydroelectric Project in the territory of Nepal. It is part of Arun Valley Hydropower group. AKPL has one operational 25 MW run of the river Kabeli B1 Hydropower Project at Panchthar & Taplejung District which has been in commercial operation since November 09, 2019. The project is constructed under BOOT (Build, own, Operate and Transfer) mechanism.

Financial performance

(Rs. Million)

Particulars	FY22 (A)	FY23 (A)	FY24 (A)	Q1FY25 (UA)
Income from operations	721	638	197	214
PBILDT Margin (%)	91.36	87.39	77.55	76.83
Overall Gearing (times)	1.66	1.63	0.67	0.62
Interest Coverage (times)	2.67	1.59	0.55	2.70
Total Debt/ Gross Cash Accruals (times)	9.29	15.70	Negative	5.83

A: Audited, UA: Unaudited

Annexure 1: Details of the Facilities Rated

Nature of the Facility	Type of the Facility	Amount (Rs. Million)	Ratings
Long Term Bank Facilities	Term Loan	2,410.66	CARE-NP BBB-
Short Term Bank Facilities	Working Capital Loan	195.30	CARE-NP A3
Total		**2,605.96**	

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