

Rating Rationale
Hotel Saffron C.K. Private Limited

Rating

Facility	Amount (Rs. In Million)	Rating ¹	Rating Action
Long Term Bank Facilities	790.41	CARE-NP BB- [Double B Minus]	Assigned
Total Facilities	790.41		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned rating of ‘CARE-NP BB-’ to the long term bank facilities of Hotel Saffron C.K. Private Limited (HSCK).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of HSCK are constrained by project implementation risk associated with the hotel project coupled with operational stabilization risk and long gestation period associated with hotel industry. The rating is also constrained by financial closure pending for the project; exposure to volatile interest rates; and susceptibility to cyclical, intense competition and geographic concentration in the hospitality sector. The ratings, however, derive strength from experience of directors of the company in other businesses and strategic locational advantage of the hotel. The ratings also factor in government initiative and support for tourism and increasing trend of tourists in Nepal. Timely execution of the hotel project without any cost overrun and financial closure of the debt component for funding of the hotel project will be key rating sensitivities.

Impact of Covid-19 on the travel & tourism industry

The outbreak of Coronavirus disease 2019 (Covid-19) which was recognized as Pandemic by World Health Organization, has affected Nepal as well. Government of Nepal (GoN) imposed travel restrictions and countrywide lockdown since March 24, 2020, halting operations of most of the organizations and slowing down economic activities. With lockdown imposed by the GoN, construction activities for the hotel project of the company were disrupted along with delay in finalization of bank funding which might result in extension of commercial operation date. Also, Visit Nepal Year 2020, an initiation by the GoN with a target to bring 2 million foreign tourists in the country, resulting in infrastructure development and huge public as well as private investments in the tourism and hotel sectors has been postponed in light of the Covid-19 outbreak. Considering the impact of Covid-19 in the economy of Nepal, GoN has introduced various packages to ease out the impact across different sectors including hotel sector. The company’s ability to achieve its projected revenue, maintain profitability margins and liquidity position will be key rating consideration.

¹Complete definitions of the ratings assigned are available at www.careratingsnepal.com

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Implementation risk associated with the hotel project

The hotel project is at the nascent stage of its construction phase with only land acquired for the proposed hotel project till mid- March, 2020. The construction of the hotel project had started pre-lockdown but was halted due to Covid-19 pandemic. Currently, mainly excavation work is ongoing at the hotel project site along with setup of labor camp, batching plant and lab testing etc. As major part of the project work is still pending, the project is exposed to the risks associated with project implementation without any time and cost overruns, and satisfactory operations thereafter. The hotel is expected to come into operations in July 2023.

Operational stabilization risk and long gestation period associated with hotel industry

The company is setting up a hotel with 107 rooms capacity which includes restaurants, swimming pool, conference and banquet hall, spa and other facilities with an aggregate project cost of Rs. 1,456 Mn which is proposed to be funded at a debt equity ratio of 54:46. Generally, hotels require longer gestation period to recover the fixed costs associated with it and become profitable. Hotel projects have long gestation period since construction of a premium hotel takes up to three to four years while stabilization of operations may take another two to three years. Going forward, the ability of the company to attract customers, maintain occupancy level, establish its brand and derive benefit from the hotel as envisaged will be crucial rating factor.

Financial closure pending for the project

The total cost of project is proposed to be financed with debt of Rs. 790 Mn and equity of Rs. 666 Mn. The financial closure for the debt portion is still under process with the bankers. Till July 16, 2019, Rs. 90 Mn has been incurred in the construction of the hotel project which has been funded by equity contribution by the promoters. The promoters of the company have infused total equity of Rs. 250 Mn for the hotel project. Financial closure for the entire debt component at the earliest and timely completion of the project would be key rating consideration.

Exposure to volatile interest rates

Nepalese banking sectors are fixing lending interest rate based on quarterly base rate and interest rate will be changed accordingly on quarterly basis. Due to tight liquidity in the market, the interest rate has been high and volatile during the last 12 months. Therefore, funding from Bank and Financial Institutions is exposed to volatile interest rate.

Susceptibility to cyclical, intense competition and geographic concentration risk in the hospitality sector

The hotel industry of Nepal is fragmented in nature with the presence of large number of organized and unorganized players spread across various regions. Occupancy levels and revenue in the hotel industry are

susceptible to macroeconomic trends, both in the domestic and global markets. The company's hotel has a single establishment located at Butwal, thus exposing operations to geographic concentration risk. Furthermore, by catering largely to the hotel segment, revenue and profitability remain susceptible to business growth and the dynamics of the hotel industry. Any slowdown in industry may impact HSCK's operations.

Key Rating Strengths

Experienced directors of the company in other businesses

HSCK is managed under the overall guidance of the company's board of directors (BOD) who possess wide industry experience. Mr. Chunna Prasad Sharma is the Chairman of the company who has wide work experience of 35 years and holds position as Chairman and Director in various other businesses. Similarly, other directors of the company have work experience in various businesses such as manufacturing, packaging, spices, real estate etc. BODs are further supported by an experienced team across various functions/ departments.

Strategic locational advantage of the hotel

The hotel is centrally located in Butwal with Bhairahawa Airport at a distance of ~24 kms and Sonauli (Indian Border) at a distance of ~26 km. The influx of tourists is high in Butwal which is closely located to UNESCO's World Heritage Site Lumbini at a distance of ~38 kms. Lumbini is one of the most popular tourist destinations of Nepal in terms of frequency of visits and has religious and historical significance which is visited by large number of tourists every year. In 2019, 1.78 Mn tourists visited Lumbini (vis-à-vis 1.52 Mn tourists in 2018). Also, the hotel site is located opposite of proposed Butwal Mandap, i.e. International Convention and Exhibition Centre having capacity of 10,000 visitors, which is expected to provide additional mileage for the hotel business.

Government initiative and support for tourism

Tourism sector remains the prioritized sector of Nepal and income from tourism sector in ratio with gross domestic product was 2.2% in FY19. Also, Monetary Policy of 2019/20, has directed commercial banks to allocate minimum 25% of total credit to priority sector of which 15% should be allocated to energy and tourism sector only. GoN also provided 20% exemption in tax rate for hotel industry with transaction more than Rs. 10 Mn. The government also provides tax holiday for large hotel projects established with capital investment of more than Rs. 1 Bn and providing direct employment to more than 500 individuals. With the government prioritizing development of travel and tourism in the country, the future prospect of this sector looks encouraging post Covid-19.

Increasing trend of tourists in Nepal before Covid-19 Pandemic

Inflow of tourist in Nepal has seen continuous growth in last few years with 0.54 Mn tourist visiting Nepal in CY15 which increased to 0.75 Mn in CY16 registering ~40% growth. Further, it recorded a growth of ~25% in CY17 with 0.94 Mn tourist inflows and ~25% in CY 18 with 1.17 Mn tourist inflows. In CY19, 1.18 Mn tourists

visited the country with majority of tourists. With ~79% (CY19) of tourist as Non-Indian tourist and ~17% (CY19) of total tourist arriving for trekking and mountaineering, Nepal has become one of the preferred destination of tourists for trekking and mountaineering beside being a holiday destination. However, with the recent outbreak of Corona Virus that led to World Health Organization declaring global health emergency, it is expected that travel and tourism industry in Nepal as well as around the world will be adversely impacted in CY20.

About the Company

Hotel Saffron C.K. Private Limited was incorporated on November 21, 2018 and is constructing a hotel in Butwal, Rupandehi with a total of 107 room keys and is proposed to be categorized as a 5-star hotel property. The hotel is expected to come into commercial operation from July 2023 onwards. HSKK is being promoted by total number of 6 individual shareholders.

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Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. In Million)	Rating
Long Term Bank Facilities	Term Loan (Proposed)	790.41	CARE-NP BB-
Total		790.41	