

Orchid Holdings Limited

Ratings

Facilities/ Instrument	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	950.00	CARE-NP B+ [Single B Plus]	Reaffirmed
Short Term Bank Facilities	50.00	CARE-NP A4 [A Four]	Reaffirmed
Total Facilities	1,000.00 (One Thousand Million Only)		

* Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has reaffirmed the ratings of 'CARE-NP B+' assigned to the long term bank facilities and 'CARE-NP A4' assigned to the short term bank facilities of Orchid Holdings Limited (OHL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of OHL continue to remain constrained by its weak financial risk profile marked by operational losses resulting in highly leveraged capital structure and weak debt service coverage indicators in FY22 (Audited, FY refers to the twelve-month period ending mid-July). The ratings also continue to factor in operations stabilization risk considering the long gestation period generally associated with hospitality industry, susceptibility to cyclical, intense competition and geographic concentration in the hospitality sector and exposure to volatile interest rates.

The ratings, however, derive strength from experienced directors and management team, strategic locational advantage of the hotel and government initiative and support for tourism sector. The ratings also take cognizance of the improving trend in both foreign and domestic tourist arrivals in the country in 2023 and likely growth trend expected over the medium-term, barring any setbacks, which augurs well for the overall hospitality sector.

Going forward, the ability of the company to improve occupancy level and average room rate (ARR) of the hotel on a sustained basis leading to growth in revenues and profitability resulting in improved solvency and debt service coverage indicators will be key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Weaknesses

Highly leveraged capital structure with weak debt service coverage indicators

The capital structure of OHL is highly leveraged with overall gearing of 5.62x at the end of FY22 which deteriorated from 3.06x at the end of FY21 majorly on account of net losses eroding net worth of the company. Interest coverage was also negative in FY22 amid operational losses. Although the company has earlier benefited from the relaxations provided by the Nepal Rastra Bank to the highly Covid19 impacted sectors such as tourism and hospitality, its ability to adequately service its debt obligations, now that these relaxations are over, will depend on its ability to generate sufficient income. With increased tourist inflow post pandemic, operational performance is likely to improve over the medium term. Furthermore, the company is in process of issuing right share of around Rs. 400 Mn. Post issuance, it is expected to provide assistance to reduce financial burden of the company to some extent. However, the ability of the company to profitably scale up the operations leading to improved debt service coverage indicators will remain crucial from analytical perspective.

¹Complete definitions of the ratings assigned are available at www.careratingsnepal.com and in other CRNL publications.

Weak financial performance marked by operating losses, albeit improving trend in 8MFY23

During FY22, Total operating income (TOI) of the company increased by 194% to Rs. 66 Mn from Rs. 23 Mn during FY21 majorly through higher sales from Meetings, incentives, conferences and exhibitions (MICE) (~72%) followed by slight uptick in room sales (~28%). Occupancy rate during FY22 stood low at around 8.53%. PBILDT stood negative Rs. 18 Mn during FY22. However, the financial performance of the hotel has been improving in FY23 and the company has already booked income of Rs. 137 Mn during 8MFY23 (Unaudited, refers to the eight-month period ended mid-March 2023). The average occupancy rate during 8MFY23 improved to 21% from 6% during 8MFY22 supported by increasing flow of tourists into the country. The company's ability to attract enough customers to run the hotel at an optimal occupancy level for a sustained period remains to be seen and will remain crucial from credit perspective.

Operational stabilization risk and long gestation period associated with hotel industry

The company has set up a hotel with 131 rooms capacity which includes all modern amenities, F&B service, swimming pool, conference and banquet hall, health facility, shopping arcade and other facilities has come into operations since August 2019. Generally, hotels generally require longer gestation period to recover the associated fixed costs and become profitable. The long gestation period of hotels is on account of the construction of a premium hotel taking up to three to four years while stabilization of operations may take another two to three years. Going forward, given limited operational record, 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.

Exposure to volatile interest rate

The company has substantial interest outgo lined up over the next couple of years amid high debt levels. The company's interest rates are based on a floating interest rate regime, where a certain premium is added to the quarterly base rate and interest rate is changed accordingly on quarterly basis. 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 rate.

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

The hotel industry of Nepal is fragmented in nature with presence of large number of organized and unorganized players spread across various regions. The number of hotels operating in the city of Kathmandu remains high which will ultimately result in intense competition that might lead to competitive pricing leading to subdued ARR's despite surge in tourists. Also, occupancy levels and revenue in the hotel industry are susceptible to macroeconomic trends, both in the domestic and global markets. Furthermore, the company's hotel has a single establishment located at Kathmandu, thus exposing operations to geographic concentration risk.

Key Rating Strengths**Experienced directors and management team**

OHL is managed under the overall guidance of the company's board of directors (BOD) who possess wide industry experience. Mr. Sudhir Man Maskey, Managing Director, has work experience of over 27 years in various industries including hospitality sector. Similarly, other directors of the company have experience in diversified industries such as manufacturing, banking and financial institutions, education sector, 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 Ravi Bhawan, Kathmandu with Tribhuvan International Airport at around 9 km. The influx of tourists is high in Kathmandu as it is an entry point for international tourists in the country via flight and being one of the most attractive tourist destinations of Nepal which is visited by large number of tourists every year. Also, it is being built in Kathmandu, the capital city of Nepal with 7 UNESCO world heritage sites; known as city of temples and living goddess; close to the three durbar squares famous for its rich architecture; good infrastructure and approximately 28 kms away from Nagarkot which has a reputation as top spot for enjoying Himalayas view.

Government initiative and support for tourism industry

Tourism sector remains a prioritized sector of Nepal. In Budget Announcement for FY23 by Ministry of Finance, the government has allocated Rs. 9.38 Bn for tourism infrastructure development. Also, as per the Unified Directives of 2022/23, whereby the banks (type B and C) have to allocate minimum share of their total advances to hospitality sector which augurs well for the sector. Similarly, Monetary Policy of 2022/23 had amended refinance procedure to covid-19 impacted industries. With the government prioritizing development of travel and tourism in the country, the prospect of this sector looks encouraging over the medium-term.

Industry Outlook

Tourism sector which was hardly hit by the covid-19 pandemic started to bounce back slowly. The number of tourist arrivals, which had been nearly zero since April 2020, started picking up to reach nearly 17,000 in January 2022. The revival can be largely attributed to pent-up demand for leisure and business travel, supported by increased bookings on account of weddings and significant uptick in MICE. As per report of Nepal Tourism Board (NTB), the growth in tourist arrival reach to over 600,000 tourists in CY22 against 1,49,833 in CY21 (CY20: 230,085 tourists). Furthermore, 3,26,528 foreign tourists visit Nepal in the first four month of 2023. All key performance indicators such as revenue per available room, average room rate, and occupancy rate are expected to reach to pre-pandemic levels by the end of FY23. However, series of events hit the world economy in 2022 contributing to inflationary pressure triggering a global cost-of-living crisis. Recession in the world economy could limit the prospects of recovery in 2023 as expected.

About the Company

Orchid Holdings Limited (OHL) is operating a four-star hotel located in Kathmandu, Nepal. The company was incorporated as a private limited company in November 13, 2007 under Company Act, 2063 and later converted into a public limited company in July 11, 2022. The hotel property spread over 9,136 sq. mt. of land with a total of 131 room keys. The hotel is operating under the commercial name of 'Hotel Crowne Imperial' located in Ward No-14, Ravi Bhawan, Kathmandu, Nepal.

Financial Performance

(Rs. in Million)

Particulars	FY20 (A)	FY21 (A)	FY22 (A)
Income from Operations	82	23	66
PBILDT Margin	Negative	Negative	Negative
Overall Gearing (times)	1.70	3.06	5.62
Interest coverage (times)	Negative	Negative	Negative
Current Ratio (times)	1.18	3.76	1.34
Total Debt/Gross Cash Accruals (times)	Negative	Negative	Negative

A: Audited

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	950.00	CARE-NP B+ [Single B Plus]
Short Term Bank Facilities	Fund Based Limit	50.00	CARE-NP A4 [A Four]
Total		1,000.00	

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