

## Hotel Mystic Mountain Private Limited: Ratings downgraded to [ICRANP] LBB-/A4; remains on watch with negative implications

October 5, 2020

### Summary of rated instruments

Instrument*	Rated Amount (NPR Million)	Rating Action
Fund-based - Long-term loans	505.00	[ICRANP] LBB-@ <sup>1</sup> ; downgraded from [ICRANP] LBB
Fund-based - Short-term loans	35.00	[ICRANP] A4@; downgraded from [ICRANP] A4+
Non-Fund based - Short term loans	(1.50)	
<b>Total</b>	<b>540.00</b>	

\* Instrument details are provided in [Annexure-1](#)

### Rating action

ICRA Nepal has downgraded the long-term rating of Hotel Mystic Mountain Private Limited (MMH) to [ICRANP] LBB-@ (pronounced ICRA NP L double B minus from [ICRANP] LBB@ (pronounced ICRA NP L double B). ICRA Nepal has also downgraded MMH's short-term ratings to [ICRANP] A4@ (pronounced ICRA NP A Four) from [ICRANP] A4+@ (pronounced ICRA NP A Four Plus). The ratings continue to remain under watch with negative implications.

### Rationale

The downward revision in ratings factors in the expected weakening in MMH's credit profile in FY2021, owing to the sharp decline in demand caused by the prevalent Covid-19 pandemic. MMH's operations were adversely impacted after the Covid-induced lockdowns in March 2020, which caused occupancy levels to plummet, leading to sharp contraction in revenues. Even after easing of the lockdowns, the hotel operations are likely to remain muted in the near term, until the pandemic situation is resolved. The disruption in hotel operations is likely to result in subdued cash flows, leading to diminished liquidity and debt servicing ability vis-à-vis earlier estimates.

The continuation of the rating 'Watch with Negative Implications' factors in both the evolving economic impact of the pandemic and the impact of travel/movement restrictions on the hospitality sectors for the near to medium term. Furthermore, the financial profile and debt coverage indicators of the company will also depend on the restructuring of the current credit facilities by the lender bank, in line with the directions given by the central bank, which is expected to be completed by January 2021. Given the liquidity crunch created by the recent events, the business will require additional funding support, in addition to the restructuring of its current facilities. The promoters' ability to raise the requisite funding will remain a key monitorable.

The rating action also factors in the decline in MMH's revenue by 34% in FY2020 vs 52% growth in FY2019, due to the hotel closure during the last ~4 months of FY2020. For FY2021, the impact is expected to be higher, assuming the continuation of the pandemic impact over the next 6-12 months. MMH's gearing ratios are on the higher side, given its small capital base and debt financing for the hotel construction (TD/TNW of ~6 times in FY2019 and FY2020). With the expectation of operating losses leading to erosion in capital base, MMH's gearing level is likely to witness a concomitant rise. This, coupled with liquidity stress, is likely to subdue its financial profile. MMH's debt coverage indicators (interest cover of 1.4 times and DSCR of 0.96 times during FY2020) are also likely to weaken sharply in FY2021 as the low revenues and high operating leverage results in a sharp decline in profits. The promoters' ability to secure the restructuring and/or additional funding support will be essential to prevent the default risk.

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<sup>1</sup> Denotes rating on watch with negative implications

Nonetheless, the ratings continue to factor in the favourable location of the property, low reliance on foreign tourists and good support from corporate clients (~25% of total revenue in FY2019 & FY2020). The hotel managed a healthy occupancy level of 65% and 56% in FY2019 and FY2020, despite the Covid-induced lockdown, which reflects on its good reputation. It also continues to draw support from the owner's experience in the hotel business, knowledge of the local market and customer relations. ICRA Nepal also takes note of the financial flexibility accorded by the Central Bank to alleviate the liquidity stress on industries highly impacted by the pandemic.

## Key rating drivers

### Credit strengths

#### Strategic location and experienced promoter

MMH is strategically located at Nagarkot, which is one of the popular travel destinations close to Kathmandu, the capital city. The hotel's owner, Mr. Dhoju has more than 15 years of experience in the hotel industry on account of his association in the past as a General Manager of his family-owned 3-star hotel business. Mr. Dhoju has developed a good traction amongst the industry stakeholders, local corporates, and other potential customer base for supporting the hotel's business, going forward.

#### Well diversified customer base; support from corporate clients

The customer profile of MMH is primarily made up of corporate clients and local travel agents, followed by direct customers and online booking (mainly foreigners). During FY2019 and FY2020, its revenue was supported by corporates and local travel agents to the extent of 46% and 48% respectively. Also, MMH receives most of its corporate clients during the traditionally off-season periods offsetting the business seasonality to some extent.

### Credit challenges

#### Stressed liquidity caused by business disruption; Central bank's support for alleviating pandemic-induced stress provides some comfort

MMH's operations were shut down during the four-month period between mid-March and mid-July 2020 after the start of the Covid-19 lockdowns. This led to a ~34% revenue decline during FY2020. The resulting decline in cash flows has affected business liquidity. Working capital intensity of the business has risen due to the rise in debtor days and MMH's creditor days has also spiked, partly due to the liquidity issues. The liquidity profile of the company is expected to be further tightened, impacting the cash flows and debt-servicing ability of the hotel until the impact of the pandemic persists. Although the extension of ad hoc loan by the lender bank is expected to alleviate the near-term liquidity stress, the long-term liquidity will depend on the promoter's ability to secure favourable restructuring of credit facilities and the ability of the business to resume regular operations without major delays.

The Central bank has introduced the provisions for allowing restructuring/rescheduling of loans, including deferral of principal and interest repayment for a maximum of two years for industries most hit by the pandemic, including the hospitality sector. This facility is expected to benefit hotels to a certain extent in managing their liquidity requirements for the short-medium term.

#### High leverage and weak coverage indicators

Given the small capital base and debt-funded capex for hotel construction, MMH's gearing level has remained high (~6 times for FY2019 and FY2020 end). The same is likely to remain elevated over the medium term, given the expected erosion in the net worth due to operating losses expected in FY2021. High gearing and moderation in operating revenues resulted in deterioration of debt coverage indicators in FY2020 (interest cover of 1.4 times and DSCR of 0.96 times during FY2020). The debt coverage indicators are likely to remain weak over the next 6-12 months in the expectation of the continued impact of the Covid-19 pandemic on the hotel sector.

### Limited geographical/ segment diversification and competitive intensity

Hotel Mystic Mountain is a single-property hotel in Nagarkot and is, therefore, exposed to geographical concentration risk. At the same time, a major portion of the hotel revenue comes from a relatively small customer segment. The Nagarkot area has a plethora of hotels across different segments, which increases the competitive intensity for MMH. Older and established hotels in the region with lower debt burden could exert pricing pressure on MMH, which could affect the financial profile of the company further.

**Analytical approach:** For arriving at the ratings, ICRA Nepal has applied its rating methodology as indicated below:

#### Links to applicable criteria:

[Corporate Credit Rating Methodology](#)

### About the company

Hotel Mystic Mountain Private Limited (MMH) was incorporated in May 2013. Its registered office is located at Mandan Deupur, Kavrepalanchowk. MMH owns and operates a four-star resort-type 72-room hotel. It commenced operations with 33 rooms on July 28, 2017. The hotel property is located ~30 kilometres east of Kathmandu, in Nagarkot, a small town in the hills surrounding the Kathmandu valley. The property is developed over ~3.5 acres and consists of two blocks housing 72 rooms (including 71 rentable rooms). The hotel is under the sole ownership of Mr. Bal Krishna Dhoju, a second-generation hotelier.

MMH is an independent hotel without any affiliation to foreign or domestic hotel chains. The hotel has been certified as a four-star property by the Department of Tourism, Nepal on March 20, 2018 which is valid for a five-year period.

### Key financial indicators of MMH

	FY2018 (Audited)	FY2019 (Audited)	FY2020 (Provisional)
Operating Income-OI (Sales; in NPR Million)	145.76	222.0	147.26
OPBDITA <sup>2</sup> /OI (%)	35.89%	41.3%	40.24%
Total debt/Tangible Net Worth-TNW (times)	4.32	6.01	6.25
Total Outside Liabilities/ TNW (times)	5.94	7.86	7.77
Total Debt/OPBDITA2 (times)	7.67	5.40	8.70
Interest Coverage (times)	2.90	1.88	1.41
DSCR (times)	2.96	1.33	0.96
NWC/OI (%)	51.80%	6.47%	12.16%
Current Ratio	0.66	0.62	0.67

Source: Company data

### Annexure-1: Instrument Details

Instrument	Rated amount (NPR Million)	Rating assigned
Fund-based -Long-term Loans (Project loan)	475.00	[ICRANP] LBB-@
Fund-based -Long-term Loans (Banquet construction)	25.00	(Downgraded)
Fund-based -Long-term Loans (Vehicle Loan)	5.00	
Fund-based -Short-term Loans (Overdraft)	35.00	[ICRANP] A4@
Non-fund based Short-term Loans (Bank Guarantee)	(1.50)	(Downgraded)
<b>Total</b>	<b>540.00</b>	

<sup>2</sup> Operating profit before depreciation, interest, tax and amortization

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### **About ICRA Nepal Limited:**

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