

Hotel Shangrila Village Private Limited: [ICRANP] LB+/A4 assigned

March 04, 2024

Summary of rating action

Instrument (Amounts in NPR Million) *	Rated Amount	Rating Action
Long-term loan limits	949	[ICRANP] LB+; assigned
Fund based; Short-term loan limits	(100)	[ICRANP] A4; assigned
Total Loan Limits	949	

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

Rating action

ICRA Nepal has assigned a long-term rating of [ICRANP] LB+ (pronounced ICRA NP L B plus) to the long-term loan limits of Hotel Shangrila Village Private Limited (HSV or the company) and a short-term rating of [ICRANP] A4 (pronounced ICRA NP A Four) to its short-term loan limits.

Rationale

The ratings are mainly constrained by the execution and funding risks for the company's proposed five-star hotel property in Gharipatan, Pokhara, and the offtake risks during the stabilisation period once operational. As of mid-January 2024, the project achieved ~9% financial progress, while the targeted commercial operations date is March 2025. Moreover, ~19% of the project's equity requirements still need to be infused and hence, the timely infusion of requisite funds (for current cost estimates and to cover for overrun, if any) will have a bearing on the project's timeline. The ratings are also impacted by the relatively higher debt financing proportion (~80%) for the project and its modest per key cost of ~NPR 12 million, despite most of the rooms being upgrades of existing properties. Furthermore, the ratings are also constrained by the stiff competition in Pokhara, characterised by intense fragmentation and an increasing number of premium properties. The ratings are also impacted by the company's weak financial profile with accumulated losses¹ from pre-Covid operations, leading to weak capitalisation and a stretched liquidity profile.

However, the ratings are comforted by the company's association with the InterContinental Hotels Group (one of the major European hotel groups) through a hotel management agreement, enabling HSV to operate the project under the brand name Hotel Indigo Pokhara Gharipatan. The franchise association is expected to enhance the initial revenue trajectory along with the expected benefit from the project's long operational track record (over two decades), which was earlier a four-star hotel property. Further, the ratings derive comfort from the project's favourable location in Pokhara, which is among the most popular destinations among domestic as well as foreign tourists visiting Nepal. ICRA Nepal also favourably factors in the Government of Nepal's (GoN) initiatives to provide support and boost the demand prospects of the Nepalese tourism industry. Going forward, the company's ability to complete the project within the anticipated cost/timeline and thereafter, maintain adequate occupancy/margins would remain the key rating sensitivities.

Key rating drivers

Credit strengths

Established brand presence of IHG, favourable location and past industry traction – The company is constructing a five-star hotel in Pokhara, a major tourist destination in the country. This, coupled with the company's established presence in the region with Hotel Shangrila Village for over two decades (from 1996 to 2020 i.e. until the start of Covid-19) augurs well for the demand prospects. Moreover, HSV has entered into a hotel management agreement with InterContinental Hotel Group (one of the leading European hotel groups) to operate the property under the brand name Hotel Indigo. This could enhance the property's visibility, especially during the early years of operations, in addition to the expected

¹ NPR 216 million in accumulated losses as of mid-July 2023, leading to negative net worth base of NPR 83 million. While this has been supported by revaluation reserves of NPR 3,792 million, ICRA Nepal's analysis excludes the impact of the same.

benefit from the long hospitality industry experience of the promoter group, the Shangri-La Hospitality Group (which also operated a five-star property in Kathmandu from 1979 to 2019).

Government support for the tourism sector – The GoN has been taking multiple positive steps to develop the country’s tourism sector, which remains its key priority. These include prescribing a lending floor for banks and financial institutions (BFIs) for tourism-related projects, interest capitalisation options during construction, the recent announcement of the Visit Nepal decade, and extended support to recover from the pandemic impact, among others. The long-term outlook also remains positive for the sector, considering the presence of two large populous nations as neighbours.

Credit challenges

High execution and funding risks – At present, the project execution risks remain high, given the financial progress was ~9% as of mid-January 2024, while the management plans to commence the hotel operations by March 2025. Additionally, timely injection of the balance ~19% equity would also remain critical in achieving the expected project commissioning timeline. Any unexpected delays/cost overruns towards project completion could have an adverse impact.

Sizeable debt burden could constrain liquidity and debt servicing ability – The latest project cost estimate of ~NPR 1,192 million is proposed to be financed through ~80% debt, which is likely to impact the debt coverage metrics during the initial years of operations. Additionally, the modest project commissioning cost (per key cost of ~NPR 12 million, despite largely being a reconstruction project for majority of the rooms) and moderate scale of operations/revenue expectations in the initial years are likely to exert pressure on the company’s liquidity and debt servicing capacity during these years. ICRA Nepal expects timely and adequate funding support from the promoters in case of exigencies, which would remain a key rating sensitivity.

Project offtake risk – The hotel industry in Pokhara is highly competitive, given the presence of multiple existing and proposed properties in the region, including other five-star projects. Pricing pressure could be exerted by older and established properties with low debt burden, thus accentuating the offtake risk. However, the upgraded property will have a higher banquet capacity compared to earlier, which is expected to provide segmental diversification avenues.

Cyclical industry, vulnerable to general economic slowdown and exogenous factors – Given the dependence of the hospitality industry on discretionary spending (especially leisure travel), the tourism industry remains highly susceptible to exogenous shocks like political instability, economic downturns, and pandemics such as Covid-19. Further, the tourism industry in Nepal is seasonal, which could add volatility to the company’s cash flows. Its ability to consistently maintain an adequate liquidity buffer to counterbalance the seasonality will be monitorable.

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

Link to the applicable criteria:

[Corporate Credit Rating Methodology](#)

About the company

HSV, incorporated in September 1993, commenced operations of its four-star resort with 60+1 keys in Gharipatan, Pokhara, in 1996. The company started renovations and re-constructions of its project in July 2023, with the new property proposed to have 100 keys and be categorised as a 5-star hotel (along with the plan of an additional casino facility). The hotel management agreement with M/s. InterContinental Hotels Group was signed on December 20, 2022, to operate this property under the brand name Hotel Indigo. As of mid-January 2024, the company’s shares were held by Mr. Prabin Bahadur Panday (48%), Mr. Prasadha Bahadur Panday (30%), M/s Mayur International Private Limited (18%), Ms. Darpana Panday (2%), Ms. Sumita Panday (2%) and Ms. Merry Panday (1%).

Key Financial Indicators

(Amounts in NPR Million) *	Audited				
	FY2016	FY2017	FY2018	FY2019	FY2020

Operating Income-OI (Sales; NPR million)	61	87	122	130	82
OPBDITA/OI (%)	-22%	-5%	24%	11%	1%
Total Debt/ Tangible Net Worth (TNW; times)	-3.9	-6.1	2.6	1.3	1.8
Total Outside Liabilities/TNW (times)	-8.4	-14.7	6.1	3.8	4.8
Total Debt/OPBDITA (times)	-4.0	-9.8	1.3	1.9	28.2
OPBDITA/Interest (Interest coverage; times)	-3.1	-1.1	7.4	4.5	0.3
DSCR (times)	-3.1	-1.1	7.4	4.0	0.3
Net Working Capital/OI (%)	-47%	-36%	-15%	-20%	-32%

*Key financial indicators are for operational period only.

Annexure-1: Instrument details

Instrument (Amounts in NPR Million)	Rated Amount	Rating Action
Long-term loan Limits (A)	949	[ICRANP] LB+; assigned
Fixed Term Loan – I	104	
Fixed Term Loan – II	843	
Hire Purchase Loan	2	
Short-term loan limits (B)	-	[ICRANP] A4; assigned
Fund based; Bridge Gap Loan (within Fixed Term Loan - II)	(100)	
Total Loan Limits (A+B)	949	

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About ICRA Nepal Limited

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