Tara Air Private Limited: Ratings reaffirmed with removed from 'Issuer not cooperating' category

June 03, 2024

Summary of rating action:

Instrument* (Amounts in million)	Currency	Previous Rated Amount	Current Rated Amount	Rating Action
Long-Term Loan Limits				
Fund-based (Term loans and hire purchase loans)	NPR	377.91	394.01	**[ICRANP] LB-**; reaffirmed and removed from 'Issuer not cooperating' category
Fund-based (Term loans)	USD	3.99	6.68	
Short-Term Loan Limits				
Fund-based Working capital loans	NPR	497.65	248.43	**[ICRANP] A4**; reaffirmed and removed from 'Issuer not cooperating' category
Non-fund-based limits (Bank Guarantee - BG)	NPR	107.50	145.41	
Non-fund-based limits (BG)	USD	0.60	-	
Total NPR Million		**983.06**	**787.85**	
Total USD Million		**4.59**	**6.68**	

Rating action

ICRA Nepal has reaffirmed the long-term loan rating of Tara Air Private Limited (Tara) at [ICRANP] LB- (pronounced ICRA NP L B minus) and also reaffirmed the company's short-term loan rating at [ICRANP] A4 (pronounced ICRA NP A four). The ratings have also been removed from 'Issuer not cooperating category'.

Rationale

The ratings continue to remain constrained by the company's weak capitalisation and coverage indicators, mainly owing to the major losses sustained during pandemic years (FY2020 and FY2021), thus leading to negative net worth (excluding the aircraft revaluation reserves) as of mid-April 2024. The company's debt levels remained largely steady during pandemic years (aided by rescheduling/restructuring relaxations) and has increased further with the recent purchase of previously leased aircraft at ~NPR 645 million (debt funding of 75%) in December 2023. Tara has also reported gradual increase in working capital intensity (net working capital to operating income ratio) in recent years, further pressurizing its liquidity profile as evident from the sustained overutilisation of drawing power (~227% as of mid-April 2024). In addition to this, the repayment of the restructured loan is set to commence from mid-July 2024 and given the high debt burden, the promoter's ability to extend timely and adequate support would remain crucial. Tara's high dependence on the Lukla sector (~71% as of 9MFY2024 revenues) also continues to be a rating concern, in addition to its reduced market share after the loss of an aircraft through the crash in May 2022.

Nonetheless, the ratings positively factor in the gradual improvement in Tara's operating profit margins (OPM) to ~28% in 9MFY2024 which has surpassed the pre-pandemic levels. The improvement was mainly supported by the increase in share of high-margin USD based revenues, reduction in fuel prices, along with the regulation mandated VAT registration (thus enabling Tara to claim input tax credit) from start of FY2024. Furthermore, the ratings continue to factor in the company's long operational track record (>15 years) in the Nepalese domestic short take-off and landing (STOL) aviation industry, along with its association with the Thamserku Group having a long and diverse presence across a range of tourism-related businesses. Going forward, Tara's ability to generate adequate revenues/margins and manage timely debt servicing will remain a key monitorable. Any delays in debt servicing amid shortfall from operational cash flows amid delayed support from promoters would exert a downward pressure over the ratings.

Key rating drivers

Credit strengths

Adequate track record with experienced promoters/management – Tara was established in 2008 to takeover STOL operations from its sister concern viz. Yeti Airlines Private Limited. Tara's adequate traction in the industry and experienced promoters from the Thamserku group remain its key strengths. The cross-selling opportunities within the group's diverse tourism sector units is expected to aid in the financial and operational performance of Tara. However, despite a limited companies operating in the STOL segment, Tara's market share declined in recent period on account of the loss of an aircraft. Tara's ability to regain its lost market share while improving its operating income after the addition of the proposed new aircraft remains to be seen.

Improvement in margins – With gradual improvement in foreign tourist arrival in Nepal, the company's share of high margin USD-based revenues (emanating from foreign tourists) improved to ~61% in 9MFY2024 from ~29% in FY2022. This along with the reduced fuel prices and the benefit of new regulation mandated VAT registration from start of FY2024 (which led to eligibility in claiming input tax credit on capex and operating expenses, including fuel costs) has contributed to improvement in margins for Tara (OPM of ~28% in 9MFY2024 from ~20% in FY2022), despite the reduction in passenger volume. However, the sustainability of the margins and the yield (reported higher than the pre-Covid levels) remains to be seen.

Credit challenges

Weak capitalisation and coverage indicators – The company sustained sizeable losses during the pandemic years (FY2020 and FY2021), thereby eroding its net worth (negative net worth of ~NPR 34 million as of mid-April 2024 excluding the aircraft revaluation reserve). Further, purchase of the earlier leased aircraft at ~NPR 645 million (75% debt funding) in December 2023 and spike in working capital intensity has significantly increased the debt level for the company leading to total debt to OPBDITA[1] of ~7 times for 9MFY2024. This has led to muted debt service coverage indicators (debt service coverage ratio of ~0.8 times for 9MFY2024), which could witness continued pressure as the regular repayments of restructured loans start from mid-July 2024. Hence, the timely servicing of the debt from the operational cash flows and promoters support (as may be required) remains a key rating sensitivity.

Stretched liquidity; promoter support to remain vital – Tara has availed the rescheduling/restructuring of the principal and interest obligations (90% of interest accrued during mid-January 2024 to mid-April 2024, has also been restructured to be paid over a period of two years), in line with the facilities provided by the Nepal Rastra Bank, the central bank. This has ensured timely debt repayments (10% interest only) despite stretched liquidity profile. The repayment of the restructured facility is scheduled to start from mid-July 2024, in addition to start of loan repayments related to the recently purchased aircraft. The company is already utilising short-term loans, significantly in excess of its drawing power (~227% as of mid-April 2024), while the working capital intensity has been gradually increasing (~15% as of mid-April 2024), thus accentuating the concerns. Going forward, the promoters' ability to timely infuse the committed equity and extend further support, to tide over the exigencies, would remain a key rating sensitivity.

High dependence on top routes along with inherent industry cyclicality – The cyclical/seasonal nature of the tourism industry creates volatility in Tara's revenues and cash flow pattern. This could pose challenges in meeting regular bank obligations, especially during periods of weak demand. Further, Tara's reliance on few sectors remains high as seen from ~71% revenue contribution from the Lukla sector in 9MFY2024. Further, the company's reduced fleet size (after the last crash incident) led to decline in market share and is likely to increase its dependence in these key routes, increasing the vulnerability in case of operational disturbances during the peak season or the unpredictable weather conditions.

[1] *Operating profit before depreciation, interest, taxes, and amortization.*

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]

Link to the last rating rationale:
[Rationale -Tara Air BLR Surveillance INC_March 2024]

About the company

Incorporated in 2008, Tara Air Private Limited (Tara) is a domestic airlines company, which operates in STOL destinations with a fleet of three Twin Otter aircraft. Tara is a part of the Thamserku Group, which has presence in multiple tourism-related sectors. The company was promoted by Mr. Lhakpa Sonam Sherpa and the Late Ang Tshiring Sherpa, both renowned tourism sector entrepreneurs of Nepal. Mr. Lhakpa Sonam Sherpa is currently the chairman of Tara while Mrs. Chanda Sherpa is the Managing Director. Tara was started as a spin-off from its sister concern, Yeti Airlines Private Limited, which operates in trunk routes.

Key financial indicators

	FY2021 (Audited)	FY2022 (Audited)	FY2023 (Audited)	9MFY2024 (Provisional)
Operating income – (OI; Revenues in NPR million)	470	950	1,019	672
OPBDITA/OI (%)	-27.3%	19.6%	21.4%	27.5%
Total debt/Tangible net worth (TNW; times)	-6.1	-7.6	-17.1	-50.6
Total outside liabilities/TNW (times)	-8.4	-14.6	-36.7	-68.7
Total debt/OPBDITA (times)	-10.45	6.6	5.1	7.1
Interest coverage (times)	-1.4	2.0	1.7	1.9
DSCR (times)	-0.7	2.8	0.8	0.8
Net working capital/OI (%)	6%	11%	12%	15%
Current ratio	0.5	0.6	0.6	0.6

Source: Company data

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About ICRA Nepal Limited:

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