# RATING REPORT

# Avari Hotels (Pvt.) Limited

**REPORT DATE:**
May 30, 2022

**RATING ANALYSTS:**
Asfia Aziz
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## RATING DETAILS

| | Latest Rating | Previous Rating |
|---|---|---|
| **Rating Category** | **Long-term** | **Long-term** |
| **Facility Rating** | AA | AA |
| **Rating Date** | *May 30, 2022* | *June 09, 2021* |
| **Rating Action** | *Reaffirmed* | *Reaffirmed* |

## COMPANY INFORMATION

| | |
|---|---|
| **Incorporated in 1968** | **External auditors:** Kreston Hyder Bhimji & Co. |
| **Private Limited Company** | **Chairman of the Board:** Mr. Byram Dinshaw Avari |
| **Key Shareholders (with stake 5% or more):** | **Chief Executive Officer:** Mr. Byram Dinshaw Avari |
| *Beach Luxury Hotel Limited – 85%* | |
| *Avari International Hotels – 12%* | |

## APPLICABLE METHODOLOGY(IES)

**VIS Entity Rating Criteria Methodology – Industrial Corporates (August 2021)**
https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf

# Avari Hotels (Pvt.) Limited

| OVERVIEW OF THE INSTITUTION | RATING RATIONALE |
| --- | --- |

*Avari Hotels (Pvt.) Limited (AHL) was incorporated as a private limited company in 1968. Later, AHL was converted into a public limited and then re-converted into a private limited entity in 2016. Holding company of AHL is Beach Luxury Holdings (Private) Limited. The company is engaged in provision of hospitality services. Shareholding of AHL is primarily vested with Avari Family.*

Avari Hotels (Pvt.) Limited (AHL) is engaged in the hospitality sector for more than five decades. AHL owns and manages two five star hotel properties in Pakistan, namely 'Avari Towers Karachi' (AT) and 'Avari Lahore' (AL). Avari Towers Karachi is a 225 room property which began operations in 1985. Avari Lahore commenced operations in 1978 and has a room count of 175. In order to cater to the mid-tier clientele, the company also manages boutique hotels under the brand name Avari Xpress (AX) in Islamabad, Multan, Lahore and Faisalabad and Avari Boutique Multan; the properties for these hotels have been acquired under lease contracts. AX has a total of 419 rooms at end-June'21.

**Instrument rating draws support from the facility structure**

AHL mobilized a facility to the tune of Rs. 4.3b from two banks, Meezan Bank Limited and Industrial & Commercial Bank of China Limited. The facility was disbursed in October 2019. All principal and markup payments are being serviced by one of AHL's tenant, Unilever Pakistan Limited (Unilever). The facility is secured against a tripartite agreement (lenders, AHL and Unilever)which provides an undertaking from Unilever to pay principal and markup payment on the facility against rent payable in lieu of advance rent they would have ordinarily paid. The facility is additionally secured by a charge on assets of AHL and personal guarantee of sponsors.

Remaining tenor of each facility is 5 years with markup and principal payable in annual installments. First payment was serviced in May 2020 and the last payment will be due in May 2027. All markup and principal payments are made directly by Unilever into an account with the agent bank; this account is under lien with irrevocable instructions to retire debt as payments become due. The agent bank also maintains a profit bearing deposit initially amounting to Rs. 1.3b for servicing of markup relating to rentals of the second 5 year period of the lease discounted to present day.

Principal payments are in correspondence with the agreed upon rental rate, which will be escalated by 10% every year. In accordance with the lease deed between AHL and Unilever, at the end of 10 years, the lease will be renewed automatically unless Unilever gives a minimum months' notice before expiry of the existing term. Additionally, in case Unilever operations are sold or transferred, the new purchaser / transferee will continue the same obligations as defined in the original lease deed along with the existing conditions. In case Unilever plans to sub lease a portion of its leased property, the agreement specifies that there will be no effect on this financing arrangement and all covenants defined will continue to remain Unilever's responsibility till the expiry of the lease agreement.

**<u>Brief on Performance of Avari Hotels Limited</u>**

**Topline of the company has decreased on account of lower occupancy levels amidst Covid-19 pandemic in the outgoing year. However, with improved global conditions, occupancy rate has jumped back to 70% in the ongoing year resulting in improved profitability profile of the company.**

Revenue base of the company decreased by 14% to Rs. 2.0b (FY20: Rs. 2.3b) in FY21. Decrease in revenue base was primarily a function of lower occupancy levels, which culminated to lower revenue from all segments event halls, rooms, food barring beverages. AX facilities were the only exception out of three properties, which witnessed stability in the occupancy levels during FY21 in comparison to the preceding year. Pharmaceutical corporate meetings during the pandemic also supported the topline in FY21. AX in Multan resulted in a favorable response in relation to improved local leisure travel on account of international travel restrictions. Despite the same, gross profits were reported lower at Rs. 191.1m (FY20: Rs. 657.3m) and a net loss of Rs. 742.0m (FY20: Profit of Rs. 5.4m), was noted attributable to relatively lower revenue, higher depreciation charged and annual lease rental payments. Given recovery in dynamics of the country post-Covid19, occupancy rate has jumped back to 70% during the ongoing year. Moreover, AHL's management is targeting higher business volumes from the corporate clients in the ongoing year with resumption in business activities and conferences. Going forward, the management also plans to add new boutique hotels under the umbrella of Avari Xpress in Gilgit, Naltar Valley, Gujranwala, Sargodha, Murree and Skardu as these locations witness considerable inflow of tourists across the year.

Equity base (excluding surplus on revaluation of fixed assets) decreased to Rs. 1,796.6m (FY20: Rs. 2,538.6m) at end-June'21 on account of erosion due to loss to the tune of Rs. 742m. Surplus on revaluation of property continues to represent a sizeable proportion of the total equity base. Total equity including surplus amounted to Rs. 16.6b (FY20: Rs. 17.3b) at end-FY21. The company maintains a highly leveraged capital structure with more than two-thirds of total capital in the form of debt. Total debt of the company was maintained at Rs. 5.2b (FY20: Rs. 5.2b) at end-FY21. The company mobilized a facility amounting to Rs. 4.3b from two banks, Meezan Bank Limited (MBL) and Industrial & Commercial Bank of China Limited (ICBC). Proceeds from this facility are being partly utilized for expanding the properties while the remaining proportion was used for retiring other debt on the books. Given the significant quantum of debt on the books and dip in equity, leverage and gearing ratios remained elevated at 4.4x (FY20: 3.1x) and 2.9x (FY20: 2.1x) at end-June'21.

Rental income from prominent client of AHL, Unilever, is expected to provide liquidity cushion for debt repayment of this facility. As per management, improved profitability in the ongoing year will provide liquidity cushion.

| FINANCIAL SUMMARY | | | |
|---|---|---|---|
| **BALANCE SHEET** | **FY19** | **FY20** | **FY21** |
| Property, Plant and Equipment | 21,737.3 | 22,642.4 | 18,036.8 |
| Investments | 0.1 | 0.1 | 0.1 |
| Long Term Deposits | 37.8 | 37.8 | 633.2 |
| Stock-in-Trade | 16.8 | 15.7 | 15.8 |
| Stores and spares | 58.8 | 48.2 | 39.4 |
| Trade Debts | 615.3 | 106.7 | 150.6 |
| Cash & Bank Balances | 98.3 | 1,092.7 | 381.2 |
| Total Assets | 24,535.3 | 25,118.9 | 24,557.1 |
| Rent Received in Advance | 1,602.9 | 463.3 | 662.5 |
| Deferred Liabilities | 1,189.4 | 819.9 | 450.0 |
| Trade and Other Payables | 646.7 | 786.7 | 1,455.0 |
| Long Term Debt *(*incl. current maturity)* | 2,236.2 | 4,464.1 | 4,405.4 |
| Short Term Debt | 1,124.7 | 774.9 | 774.9 |
| Total Debt | 3,360.9 | 5,239.0 | 5,180.3 |
| Total Liabilities | 7,323.8 | 7,785.8 | 7,965.9 |
| Equity *(*excl. surplus on revaluation of assets)* | 2,533.2 | 2,538.6 | 1,796.6 |
| Total Equity | 17,211.5 | 17,333.1 | 16,591.2 |
| Paid up Capital | 747.3 | 747.3 | 747.3 |
| | | | |
| **INCOME STATEMENT** | **FY19** | **FY20** | **FY21** |
| Net Sales | 2,810.7 | 2,311.4 | 1,980.8 |
| Gross Profit | 1,087.5 | 657.3 | 191.1 |
| Operating Profit | 637.8 | 469.1 | -122.7 |
| Profit Before Tax | 138.7 | 40.1 | -618.7 |
| Profit After Tax | 75.2 | 5.4 | -742.0 |
| | | | |
| **RATIO ANALYSIS** | **FY19** | **FY20** | **FY21** |
| Gross Margin (%) | 38.7% | 28.4% | 9.6% |
| Net Margin (%) | 2.7% | 0.2% | -37.5% |
| Net Working Capital | 33.3 | 92.4 | 2336.6 |
| Current Ratio (x) | 1.0 | 1.0 | 1.7 |
| Funds from Operations (FFO) | 2.20 | (87.80) | (530.38) |
| FFO to Total Debt (%) | 0.1% | -1.7% | -10.2% |
| FFO to Long Term Debt (%) | 0.1% | -2.0% | -12.0% |
| Debt Servicing Coverage Ratio (x) | 0.4 | 0.3 | 0.001 |
| Leverage(x) | 2.9 | 3.1 | 4.4 |
| Gearing(x) | 1.3 | 2.1 | 2.9 |
| ROAA (%) | 0.31% | 0.02% | -2.99% |
| ROAE (%)* | 3.0% | 0.2% | -34.2% |

## ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

**Medium to Long-Term**

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

**Short-Term**

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

**Rating Watch:** JCR-VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.jcrvis.com.pk/images/criteria_watch.pdf

**Rating Outlooks:** The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.jcrvis.com.pk/images/criteria_outlook.pdf

**(SO) Rating:** A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

**(blr) Rating:** A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

**'p' Rating:** A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.jcrvis.com.pk/images/policy_ratings.pdf

**'SD' Rating:** An 'SD' rating is assigned when JCR-VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

## REGULATORY DISCLOSURES — Appendix III

| | |
|---|---|
| **Name of Rated Entity** | Avari Hotels (Pvt.) Limited |
| **Sector** | Hospitality (Miscellaneous) |
| **Type of Relationship** | Solicited |
| **Purpose of Rating** | Instrument Rating |

**Rating History**

| Rating Date | Medium to Long Term | Short Term | Rating Outlook | Rating Action |
|---|---|---|---|---|
| **RATING TYPE: BLR** | | | | |
| **05/30/2022** | AA | - | Stable | Reaffirmed |
| 06/09/2021 | AA | - | Stable | Reaffirmed |
| 04/10/2020 | AA | - | Stable | Final |
| 09/17/2018 | AA | - | Stable | Preliminary |

| | |
|---|---|
| **Facility Structure** | Islamic musharaka amounting Rs. 2b and conventional syndicated financing amounting Rs. 2.3b, was acquired in October 2019, at a mark-up rate of KIBOR plus 1% and a tenor of 8 years. The issue is secured by a first pari passu floating charge over Avari Hotel Karachi with a 25% margin. Principal repayments are to be made in eight annual stepped up installments which will begin from May 2020. |
| **Statement by the Rating Team** | VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities. |
| **Probability of Default** | VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default. |
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**Due Diligence Meetings Conducted**

| | Name | Designation | Meeting Date |
|---|---|---|---|
| 1 | Mr. Xerxes B. Avari | Director | April 14, 2022 |
| **2** | Mr. Saeed Ahmed Patel | Corporate Director Finance | April 14, 2022 |
| **3** | Mr. Dinshaw X. Avari jr. | Director | April 14, 2022 |
| **4** | Mr. Byram Avari jr. | - | April 14, 2022 |