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HOTEL KARACHI TOWERS: Bank Lending Decision Analysis

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In the early seventies, the Government of Pakistan placed high priority on development of tourism and related industries. It was argued that the vacuum created in the tourist trade by political strife in Beirut and other places in the Middle East could be filled in by the expansion of tourist facilities in Pakistan. It was decided to establish a series of four and five-star hotels in the major cities of Karachi, Lahore, Islamabad and Peshawar. Several sanctions were issued for building first class hotels such as Holiday Inn, The Sheraton, The Hyatt Regency, The Towers and The President.

Karachi Towers was one of the many hotels which was established in the wake of this government decision. Its construction started in 1975.

Even after a lapse of 12 years and an investment of over Rs 472 million, the hotel was not yet complete. In fact, it was a rather modest version of what was originally envisaged. Initially mooted as a 600-room hotel, it had barely 300 guest rooms, nearly 1/3 of which were yet to be furnished. Betchels, the foreign consultant appointed for reappraisal of the hotel, had pointed out way back in 1980 that:

"Though this hotel could be considered an appropriate addition to the city supply of first class hotel accommodations, it is not a financially viable venture under its present financial structure and the prevailing market conditions."

The consultant's remarks echoed time and again in the room where representatives of the promoters of the hotel and its financiers were locked in heated discussions over the project failure. In the process, they were hurling accusations at one another. Mr Jamal Rustamjee, Resident Director of the hotel, was colliding head-on with Mr Nesar Hameed, Chief, Underwriting Department, Investment Bank of Pakistan (IBP). He held Mr Hameed responsible for rocking the boat by withholding disbursements to the company at critical junctures. In return, Mr Hameed accused the sponsors of bad management and siphoning of funds.

Such squabbles would have continued but for the Chairman of the meeting, Mr Farooq Sheikh, who asked loudly and clearly, "What do we do now?" A pin-drop silence ensued. All faces went blank as none had a ready answer. The meeting had to be adjourned till next day when everyone was expected to come up with a solution.

The hotel made a soft opening with about 60 rooms in 1986. There were 180 rooms operational out of which 6 were occupied by the hotel staff and 174 were available for sale. In their last joint inspection, the DFIs estimated that to put the hotel on sound footing, additional funds of at least Rs 75.0 million were required for:

- (i) Completion of work on the remaining 100 rooms – Rs 11.60 million
- (ii) Interior decoration, furniture and fixtures – Rs 50.0 million
- (iii) Kitchen equipment – Rs 2.5 million
- (iv) Electric motors, machinery and equipment – Rs 3.90 million
- (v) Interest during construction – Rs 7.0 million

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As all had burnt their fingers, no one was ready to foot the bill. Three alternatives would be placed in the final meeting of the representatives of the DFIs and the promoters:

- (i) Persuade State Insurance Company to renew its sanction of Rs 20.00 million as the sponsors were ready to arrange the balance fund requirements.
- (ii) Convert the unfurnished 100 rooms into offices. [Many multinationals like IBM, Lipton and Lever Brothers had shown interest in renting out these rooms against bank guarantee to cover the 3 years rent (Rs 30 million). This guarantee could be used as collateral for raising bank loans to meet immediate requirements].
- (iii) Exercise the right of possession and control of the hotel and bring about a change in the management.

TASK FOR PARTICIPANTS

You have attended the said meeting as a representative of the Industrial Finance Corporation of Pakistan (IFCP). Your company has extended a foreign currency loan of Rs 26 million in May 1976 for import of lifts, air conditioning plant, two dry cleaning units, kitchen equipment and electrical goods such as water coolers, cleansers etc. The loan has been fully utilised and the items imported under the loan have since been installed, trial tested and found satisfactory.

Your company has not made any more investment but the foreign loan has increased to Rs 103.889 million by December 31, 1986, due to the depreciation of the Pakistan Rupee and appreciation of major currencies under the loan specially Swiss Franc, Deutsch Mark and Yen.

Over the past 12 years, substantial data have been gathered regarding implementation of the project which include 3 rehabilitation reports and local and foreign consultants' reports.

Pertinent data are attached in a file marked "Hotel Karachi Towers".

You are required to examine in detail the contents of the file and evaluate various options available to the DFI for taking a stand in the forthcoming meeting.

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