Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Indian Hotels Company

Room for growth to expand

Consumer Discretionary	Sharekhan code: INDHOTEL

Reco/View: Buy	↔	CMP: **Rs. 241**	Price Target: **Rs. 286**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- With the scare of the COVID-19 pandemic reducing, FY2023 will be a comeback year for the hotel sector, led by strong domestic demand and return of foreign tourists (after two muted years).
- Indian Hotels Company (IHCL) is seeing a good pickup in demand since mid-February and has strong room bookings till May 2022. Q1FY2023 revenues are likely to be above pre-pandemic levels.
- The company's fundraising through a rights issue and qualified institutional placement (QIP) of ~Rs. 4,000 crore will be utilised to reduce debt and strengthen its balance sheet in the coming years.
- Hence, we re-iterate a Buy on the stock with an unchanged price target of Rs. 286. The stock is currently trading at 31.7x and 23.2x its FY2023E/24E EV/EBITDA.

The Indian hotel industry was hit by the COVID-19 pandemic over the last two fiscals, as various mobility restrictions hit foreign tourist arrivals, inter-state travel and occupancy rates for the hotel industry. As the pandemic-led restrictions were eased gradually, with a reduction in COVID-19 cases after every wave, Indian Hotels Company Ltd (IHCL) saw strong revival in room demand that helped room occupancies improve sequentially. This was largely led by strong revival in domestic tourism. With a reduction in cases globally, a strong vaccination drive and most countries (including India) removing travel restrictions, the revival in global tourism will be stronger in FY2023. Thus we expect IHCL to clock robust numbers in FY2023 with revenues crossing pre-pandemic levels on the back of high domestic demand and an expected recovery in foreign tourist arrivals. The company is also focusing on strengthening balance sheet by reducing debt on books through equity issuance.

- **Strong room demand for next 100 days:** IHCL posted strong revival in room demand in Q3FY2022 with domestic occupancy ratio improving close to 70% in December 2021. Q4 started with a pause in the month of Jan, 2022 led by emergence of the third COVID-19 wave. Yet, this wave was short-lived and room demand recovered strongly from February 2022. The management has indicated that demand outlook for March-May 2022 is strong with revenues expected to stay ahead of pre-pandemic levels. If there is no further covid wave over the next 4-5 months and as global uncertainties ease, we expect a strong revival in IHCL's business in H2FY2023 led by comeback in foreign tourist arrivals.
- **Focus remains on strengthening balance sheet:** IHCL raised Rs. 1,981 crore in Q3FY2022 through equity infusion from rights issue. In line with its plan, the company reduced the gross debt by Rs. 1,350 crore sequentially to Rs. 2,730 crore. The company will be raising another Rs. 2,000 crore with QIP placement at Rs. 202 per share (issuing 9.9 crore shares). The funds raised will be further utilised to reduce debt on the books in the coming months. Thus the company expects significant portion of debt by end of FY2023.
- **Margins to consistently improve:** IHCL clocked one of the highest margins in Q3FY2022 with EBITDA margins reaching at 29.0% on back of strong cost saving initiatives and overall recovery in the business fundamentals. We expect IHCL to end FY2022 with EBITDA margins of ~13%. With a strong improvement in occupancies and ARRs and scale-up of new businesses, the EBITDA margins are expected to consistently improve in the coming years. Thus, a strong improvement in the profitability and reduction in the interest cost due to reduction in debt will drive up PAT strongly over the next two years. Raising of funds through equity will unlikely to lead to any earnings dilution and would strengthen the balance sheet..

Our Call

View – Maintain Buy with an unchanged price target of Rs. 286: A strong recovery in domestic leisure travel would help IHCL post better performance in the medium term (Q4FY2022 performance would still be affected by emergence of third wave). Room demand is expected to remain ahead of room supply for next 2-3 years and will help occupancies to remain high. Strong focus on building an asset-light model, market share gains in key markets and recovery in the business environment will help IHCL to recover 100% of pre-COVID levels in FY2023 with strong growth in profitability. Further the company is focusing on strengthening its balance sheet through a sustained reduction in debt, which augurs well from a long-term perspective. The stock trades at 31.7x/23.2 its FY2023E/24E EV/EBITDA. We maintain a Buy recommendation on the stock with an unchanged price target of Rs. 286.

Key Risks

Any emergence of fourth COVID-19 wave in next four to five months or slow recovery in inbound and outbound tourism industry would act as a key risk to our earnings estimates.

Valuation (Consolidated) Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
Revenue	1,575	3,003	4,240	4,876
OPM (%)	-23.0	13.4	25.1	27.6
Adjusted PAT	-822	-239	355	598
Adjusted EPS (Rs.)	-7.8	-2.0	2.8	4.7
P/E (x)	-	-	77.2	45.9
P/B (x)	6.7	5.4	5.1	4.7
EV/EBITDA (x)	-	81.6	31.7	23.2
RoNW (%)	-	-	5.9	9.2
RoCE (%)	-	0.9	7.5	10.4

Source: Company; Sharekhan estimates

3R MATRIX

	+	=	-
Right Sector (RS)		✓	
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 24.78

Updated Jan 01, 2022

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

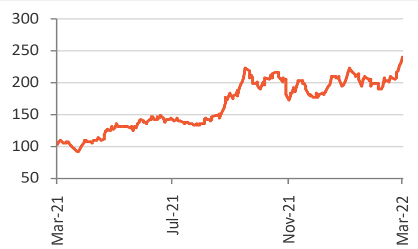
Company details

Market cap:	Rs. 31,786 cr
52-week high/low:	Rs. 240 / 91
NSE volume: (No of shares)	81.5 lakh
BSE code:	500850
NSE code:	INDHOTEL
Free float: (No of shares)	77.9 cr

Shareholding (%)

Promoters	41.1
FII	15.9
DII	25.2
Others	17.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	20.6	32.2	32.4	134.7
Relative to Sensex	17.6	32.0	35.3	119.1

Sharekhan Research, Bloomberg

Q1FY2023 revenues will cross the pre-pandemic level

IHCL posted strong operating performance in Q3FY2022 led by a strong recovery in performance of domestic as well as international properties. In Q4, January was impacted due to the third wave of COVID-19, but the company has witnessed strong revival in business in February-March 2022. Business in March-May 2022 is expected to be higher than pre-pandemic levels of March-May 2019, led by strong domestic as well as foreign demand. According to the management, domestic tourists contribute 80-85% of revenue depending on the brand of Hotel and domestic tourism has always been strong (even before the pandemic). Revival of foreign tourist arrivals will add to overall demand in the country. An improvement in spiritual tourism and business travel and pent up demand through government reservations with foreign delegations coming from different levels will also contribute to the increase in bookings. However, an increase in cases, if a fourth wave strikes, would be a key risk to room demand.

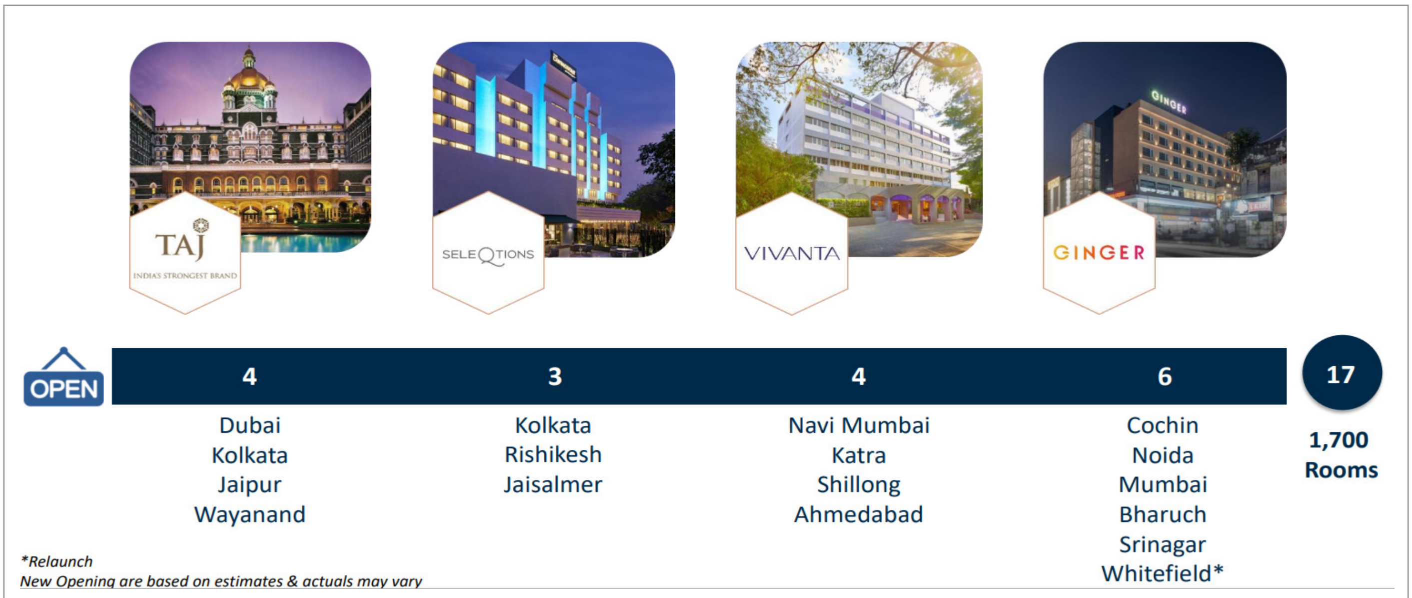
QIP funds to strengthen balance sheet

The board of Indian Hotels Company (IHCL) in its meeting held on 25th March 2022 decided to raise Rs. 2,000 crore through Qualified Institutional Placement (QIP) which the company plans to utilize for repaying debt of ~Rs. 1,900 crore (Gross debt as on December 31, 2021 was at ~Rs. 2,730 crore). The company has declared Rs. 202 per share as the issue price for the QIP; which reflects a discount of Rs. 1.48 per share to its floor price. This would lead to allotment of 9.9 crore shares of face value of Re. 1 each. Pursuant to the allotment of equity shares in the issue, the total number of equity shares will stand at 142 crore shares (with equity dilution of ~7%). IHCL raised Rs. 1,981 crore in Q3FY2022 through equity infusion from right issue. In-line with its plan, the company reduced the gross debt by Rs. 1,350 crore sequentially to Rs. 2,730 crore through the rights issue.

Continues to add properties under the asset-light model

IHCL reimagined the Ginger brand three years ago and has repositioned it better suit the customers. The company plans to open a flagship Ginger hotel with ~375 rooms in Mumbai in the next 10 months. Along with this IHCL aims to open 6-10 Ginger properties and a total of ~18 properties among various brands in the next 12 months. Apart from this, the company targets to reach a portfolio of 100 homestays and significantly scale up its home delivery and QSR business through its Qmin brand. The company opened its third Taj branded hotel in UAE - Taj Exotica Resort & Spa, The Palm in Dubai in early March 2022 taking the total number of Taj hotels in UAE to four, including one under development. In April, the company plans to open its second Taj branded property in Kolkata and launch a Vivanta hotel in Katra soon. IHCL plans to open more than one hotel during January-December 2022 with a target to open 17 hotels with 1,700 rooms during the same period.

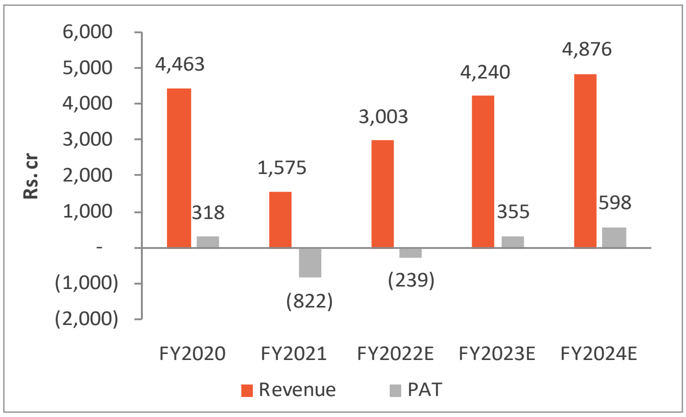
Aggressive hotel openings lined up for 2022



Source: Company presentation

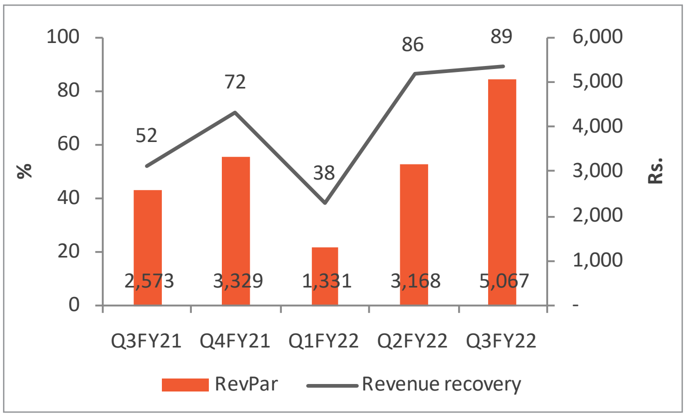
Financials in charts

Revenue and profits to grow in coming years



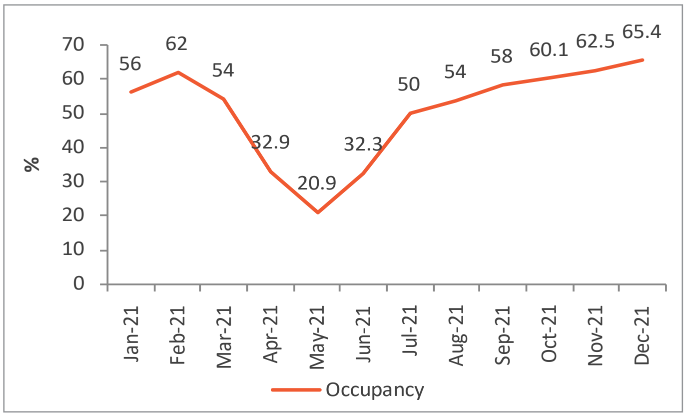
Source: Company, Sharekhan Research

Strong recovery in Q2 & Q3 after second wave in Q1



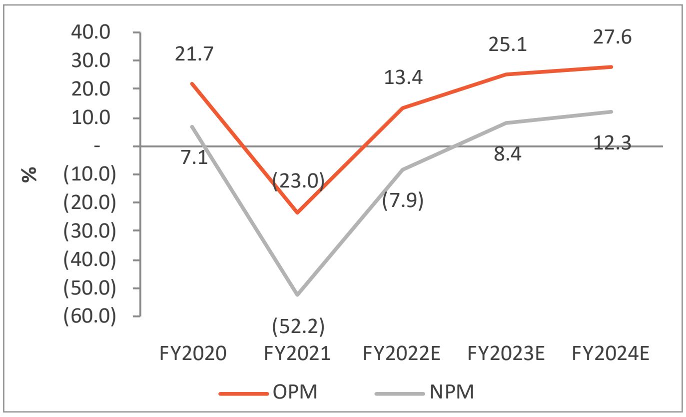
Source: Company, Sharekhan Research

Trend in occupancy ratio



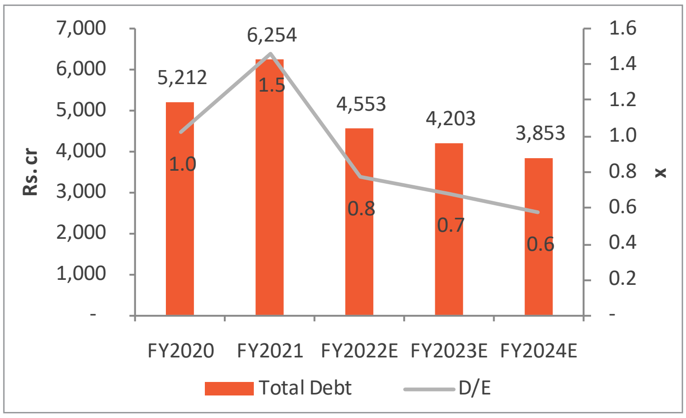
Source: Company, Sharekhan Research

Margins to improve significantly



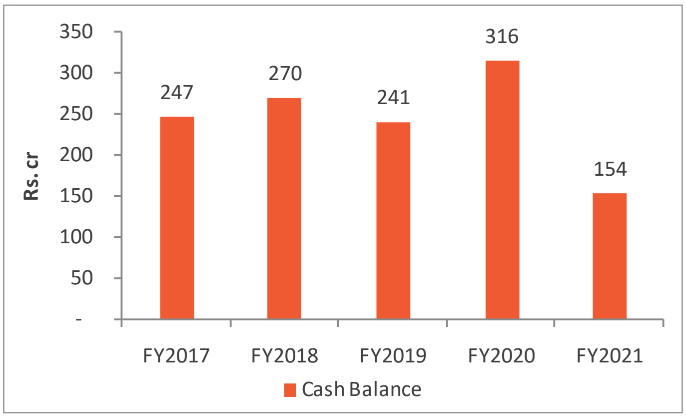
Source: Company, Sharekhan Research

Company to reduce debt



Source: Company, Sharekhan Research

Cash balance stays adequate



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - FY2021/22 were disrupted; recovery expected in FY2023

FY2021 and FY2022 were tough years for the Indian hotel industry with some silver lining being visible in the second half of FY2022 as hotel industry RevPAR recovered to ~80% of pre-COVID levels in Q3FY2022 due to improve domestic mobility resulting higher demand for leisure travel. Most hoteliers are confident of a strong recovery once the pandemic pressure eases out (mass vaccinations is creating hope for all). On the supply front, financial constraints would delay most hotel projects by a year or two, while some standalone hotels are likely to close their operations in the domestic market. However, concerns around rising COVID-19 cases in domestic and international markets will continue to act as a key risk on occupancies and business performance of hotel companies in the short term.

■ Company outlook - Business will recover close to 100% of pre-COVID levels in FY2023

Amid the second wave of COVID-19 in India, IHCL's business continued because there were no nationwide lockdowns and this helped maintain business momentum in less-affected areas with safety protocols. For 9MFY2022, IHCL reported consolidated business revenue of Rs. 2,184.1 crore with domestic occupancies improving to 51% coupled with a month-on-month recovery in room rentals. With international markets such as US and UK opening up gradually, properties in these markets saw consistent improvement in two consecutive quarters. Emergence of the third wave of COVID-19 might lead to short-term hiccups in Q4. However, we expect the industry to recover faster compared to earlier waves. We expect business to recover to 67% of FY2020 levels in FY2022 and 90% of FY2020 levels in FY2023. Cost-saving initiatives undertaken in FY2021 will help operating profit to substantially improve in the coming years.

■ Valuation - Retain Buy with an unchanged price target of Rs. 286

A strong recovery in domestic leisure travel would help IHCL post better performance in the medium term (Q4FY2022 performance would still be affected by emergence of third wave). Room demand is expected to remain ahead of room supply for next 2-3 years and will help occupancies to remain high. Strong focus on building an asset-light model, market share gains in key markets and recovery in the business environment will help IHCL to recover 100% of pre-COVID levels in FY2023 with strong growth in profitability. Further the company is focusing on strengthening its balance sheet through a sustained reduction in debt, which augurs well from a long-term perspective. The stock trades at 31.7x/23.2 its FY2023E/24E EV/EBITDA. We maintain a Buy recommendation on the stock with an unchanged price target of Rs. 286.

Peer Comparison

Companies	P/E (x)			EV/EBIDTA (x)			RoCE (%)		
	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
Lemon tree Hotels	-	75.9	52.6	-	59.5	25.5	-	1.2	6.2
Indian Hotels Company	-	-	77.2	-	81.6	31.7	-	0.9	7.5

Source: Company, Sharekhan estimates

About company

IHCL and its subsidiaries bring together a group of brands and businesses that offer a fusion of warm Indian hospitality and world-class service. Incorporated by the founder of the Tata Group, Jamsetji Tata, the company opened its first hotel - Taj Mahal Palace, in Bombay in 1903, and currently has 232 hotels (61 under development) globally in its portfolio, including presence in India, North America, UK, Africa, Middle East, Malaysia, Sri Lanka, Maldives, Bhutan, and Nepal.

Investment theme

The hotel industry's business fundamentals have improved in recent times with room demand outpacing room supply. A strong recovery in domestic leisure travel would help IHCL in posting better performance in the medium term (Q4 performance will be affected by emergence of third wave). Strong focus on building an asset-light model, market share gains in key markets and recovery in the business environment will help IHCL recover to 100% of pre-COVID levels in FY2023 with strong growth in profitability. Further the company is focusing on strengthening its balance sheet by a sustained reduction in debt, which augurs well from the long term perspective.

Key Risks

- On the backdrop of economic slowdown, room supply is going ahead of room demand, which will affect overall business fundamentals of the hotel industry and performance of hotel companies.
- Any disruption in the performance of international properties will affect the consolidated performance of IHCL in the coming years.

Additional Data

Key management personnel

N Chandrasekaran	Chairman
PuneetChhatwal	CEO & Managing Director
GiridharSanjeevi	Chief Financial Officer
Beejal Desai	Company Secretary

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	HDFC Asset Management Co Ltd	4.5
2	Nippon Life India Asset Management	3.5
3	SBI Fund Management	3.0
4	Amansa Capital Pvt. Ltd	2.3
5	Life Insurance Corp of India	2.1
6	ICICI Prudential Life Insurance Co.	1.9
7	Vanguard Group Inc	1.8
8	L&T Mutual Fund Trustee Ltd	1.7
9	Norges Bank	1.6
10	Government Pension	1.6

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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by BNP PARIBAS

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