

HOTEL LEELAVENTURES

Low base effect; stress test from Q3FY11

■ Low base effect aided improvement in operations

Hotel Leelaventure's (HLV) Q1FY11 sales increased 25% Y-o-Y, to INR 1.06 bn, due to the low base effect; it, however, declined 20% Q-o-Q due to seasonal factors. The company had 61% and INR 8,679 as ORs and ARR for Q1FY11 against 57% and INR 8,314 in Q1FY10, respectively. We expect sales to increase 42% in FY11 as the Delhi property becomes operational and ARR and ORs improve due to overall buoyant business environment.

■ EBIDTA margins to expand; high depreciation, interest to hit PAT

We expect EBIDTA margins to improve to 36% in FY11 against 29% in FY10. Operating margins are likely to improve due to the opening of Delhi property at the end of Q2FY11 and a better economic environment. We expect PAT in FY11 to come under severe pressure as depreciation and interest on the INR 11 bn capex on the Delhi property start getting reflected from Q3FY11. We are reducing our revenue estimates from the Delhi property to six months from nine months earlier.

■ Equity raising imminent

Issuance of 10 mn equity shares on preferential basis to promoters will increase the promoter stake to 54.5% from 53.3% currently. We expect the company to raise money using the QIB/FCCB route soon as the D/E ratio, estimated at 3.4x in FY10, is on the higher side.

■ Outlook and valuations: Expensive on all counts; maintain 'REDUCE'

With FCCB redemption of EUR 50 mn (with redemption premium of 25.5%) in September 2010 and Delhi property becoming operational by September 2010, we expect interest liability to go up substantially Q3FY11 onwards, unless the company raises money through QIB/FCCB. We believe sale of the office space in Chennai and inflow from Pune land development, along with the QIB/FCCB issue, could be the next milestones. We continue to value HLV based on EV/EBIDTA, and maintain our target price of INR 25. At CMP of INR 50, the stock is trading at 24.1x and 16.4x EV/EBIDTA of FY11E and FY12E, respectively. We maintain our 'REDUCE' recommendation on the stock.

Financials

Year to March	Q1FY11	Q1FY10	% change	Q4FY10	% change	FY10	FY11E
Net rev. (INR mn)	1,058	847	24.9	1,326	(20.2)	4,362	5,937
EBIDTA (INR mn)	316	189	67.5	367	(14.1)	1,266	2,170
Net profit (INR mn)	92	3	2,787.5	95	(2.3)	404	357
Diluted EPS (INR)	0.2	0.0		0.2		1.1	0.9
Diluted PE (x)						64.7	49.0
EV/EBIDTA (x)						24.1	16.4
ROAE (%)						4.8	6.2

July 13, 2010

Reuters : HTLE.BO

Bloomberg : LELA IN

EDELWEISS RATING

Absolute Rating

REDUCE

MARKET DATA

CMP	:	INR 50
52-week range (INR)	:	53 / 26
Share in issue (mn)	:	377.8
M cap (INR bn/USD mn)	:	19.0 / 404.2
Avg. Daily Vol. BSE/NSE ('000)	:	2,070.2

SHARE HOLDING PATTERN (%)

Promoters*	:	53.3
MFs, FIs & Banks	:	7.3
FIIIs	:	2.5
Others	:	36.9
* Promoters pledged shares (% of share in issue)	:	24.5

RELATIVE PERFORMANCE (%)

	Sensex	Stock	Stock over Sensex
1 month	3.7	8.3	4.6
3 months	2.0	0.5	(1.5)
12 months	29.8	77.1	47.2

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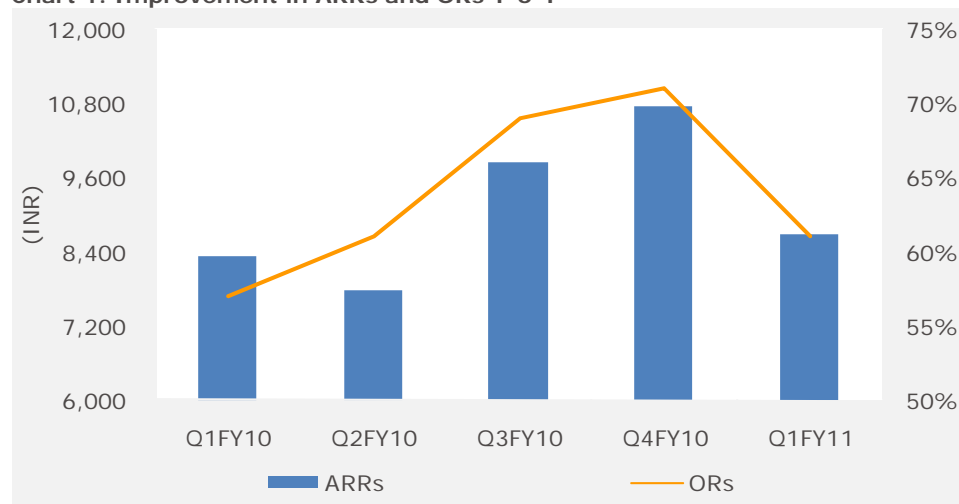
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■ **Low base effect aided improvement in operations**

HLV's Q1FY11 sales increased 25% Y-o-Y, to INR 1.06 bn, due to the low base effect; it, however, declined 20% Q-o-Q due to the seasonal factors. In Q1FY11, ARR and ORs were at INR 8,679 and 61% against 57% and INR 8,314 in Q1FY10, respectively. Y-o-Y, ORs improved ~400bps and ARR were up 4.3%.

Chart 1: Improvement in ARR and ORs Y-o-Y



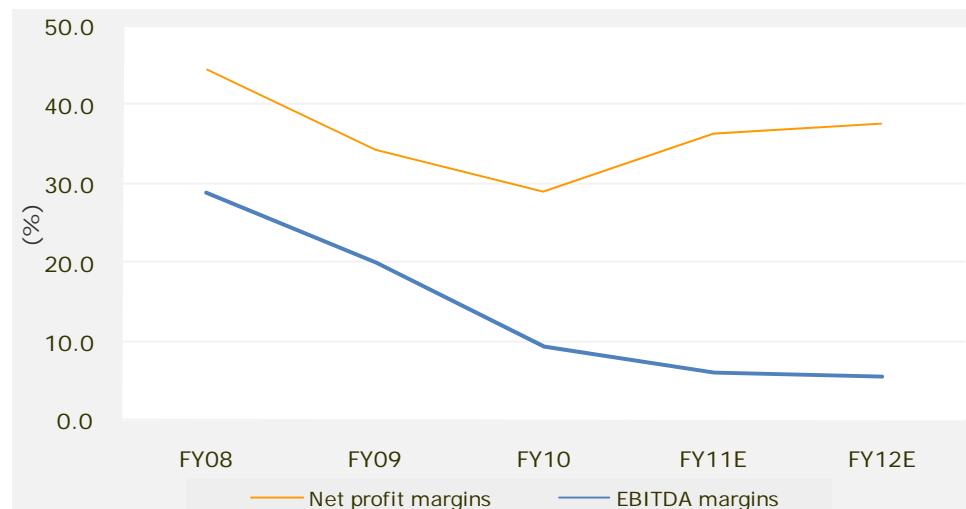
Source: Company, Edelweiss research

Against our earlier expectations of the Delhi property becoming operational in Q2FY11, the property is expected to become operational only at the end of September 2010. The company plans to pitch the property against Imperial, New Delhi, and is looking forward to ARR of more than INR 20,000 per night.

■ **EBIDTA margins to expand; high interest, depreciation to hit PAT**

We expect EBIDTA margins to improve to 36% in FY11 against 29% in FY10. Opening up of Delhi property just at the time of Commonwealth Games in October 2010 is expected to yield average above results for the company during Q3 and Q4FY11. Apart from this, the seasonal impact of improvement in ARR from September 2010 due to better economic activity is expected to help the company post better operating margins.

Chart 2: Better EBIDTA margins in FY11; PAT decline to continue



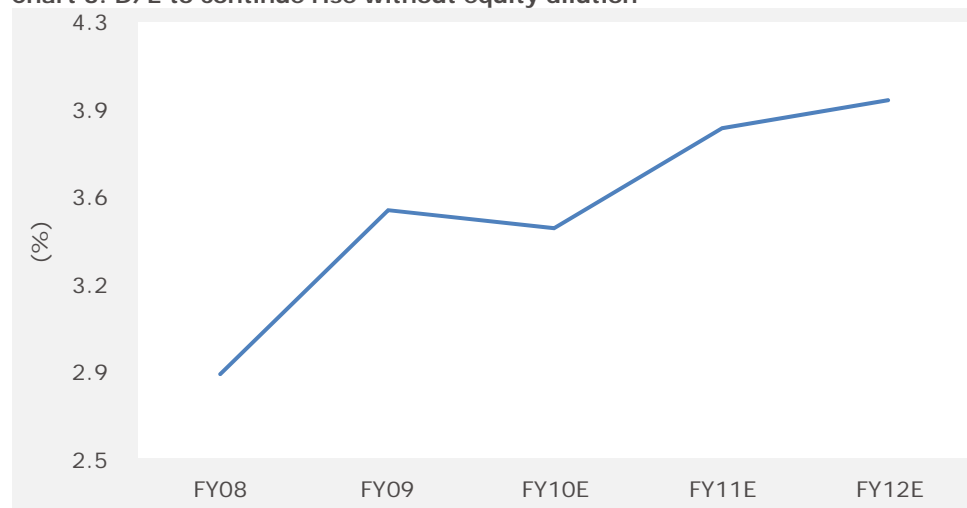
Source: Company, Edelweiss research

We expect PAT in FY11 to come under severe pressure as depreciation and interest on the INR 11 bn capex on the Delhi property start getting reflected from Q3FY11. We are reducing our revenue estimates from the Delhi property to six months from nine months earlier.

- **Equity raising imminent**

Issuance of 10 mn equity shares on preferential basis to promoters will increase the promoter stake to 54.5% from the current 53.3%. The company has deferred the QIB/FCCB issue and is waiting for the right time to open the issue again. We expect the company to come again in the market around November-December 2010 when the Delhi property would be up and running. We expect the company to raise money using the QIB/FCCB route soon as the D/E ratio, estimated at 3.4x in FY10, is on the higher side.

Chart 3: D/E to continue rise without equity dilution



Source: Company. Edelweiss research

- **Pune land development and Chennai office space sale**

The company has decided to enter into a joint development agreement with a reputed local builder to develop the land in Pune (4 acres) into a premium residential and commercial property. Details with regards to cost of development, number of flats and time-frame are still not available. Proceeds of the sale will get distributed at 50:50 between Hotel Leela and the developer.

The company is still to take a decision regarding its 3 lakh sq ft commercial office space at Chennai. We have estimated in our calculation six months of lease rentals at INR 60 per sq ft. The company can also decide to sell the space at INR 2.5-3.0 bn.

Financial Snapshot**(INR mn)**

Year to March	Q1FY11	Q1FY10	% Change	Q4FY10	% Change	FY10	FY11E	FY12E
Sales	1,058	847	24.9	1,326	(20.2)	4,362	5,937	8,571
Total sales	1,058	847	24.9	1,326	(20.2)	4,362	5,937	8,571
Expenditure								
Consumption of raw material	75	67	12.6	85	(11.6)	306	398	574
Employee costs	248	214	15.5	257	(3.5)	954	1,247	1,800
Fuel, power and light	116	107	8.2	116	0.2	440	594	857
Other expenditure	304	271	12.3	502	(39.4)	1,396	1,811	2,528
Total expenditure	742	659	12.7	959	(22.6)	3,096	4,050	5,759
EBIDTA	316	189	67.5	367	(14.1)	1,266	2,170	3,224
Depreciation	186	161	15.7	220	(15.3)	683	842	1,011
EBIT	130	28	369.2	148	(12.2)	583	1,328	2,214
Interest	57	64	(11.2)	76	(25.4)	245	1,464	2,187
Other income	42	40	5.2	135	(68.6)	262	669	678
PBT	115	4	2,645.2	206	(44.1)	600	533	705
Tax	23	1	2,190.0	112	(79.5)	196	176	233
PAT	92	3	2,787.5	95	(2.3)	404	357	472

as % of net revenues

Employee costs	23.4	25.3		19.3		21.9	21.0	21.0
Fuel, power and light	10.9	12.6		8.7		10.1	10.0	10.0
Other expenditure	28.7	32.0		37.9		32.0	30.5	29.5
EBIDTA	29.8	22.3		27.7		29.0	36.6	37.6
PAT	8.7	0.4		7.1		9.3	6.0	5.5

- **Company Description**

Hotel Leelaventures (HLV), a chain of luxury resorts and business hotels, operates 1,617 rooms across six locations in India. Five properties with 1,205 rooms are owned by the company and 409 rooms are under the management contract. Compared with other hotel chains in India, HLV is small, but has presence across prominent cities where it operates.

HLV has a marketing alliance with Kempinski for its properties in India. The company caters to both business and leisure travelers. In 2009, HLV added its property through management contract in Gurgaon (Haryana). Delhi and Chennai property are expected to become operational in FY11 and FY12, respectively.

- **Investment Theme**

HLV currently is the most expensive stock available in the hotel industry space and is trading at almost 50-60% premium to other bigger players. The heavy investment made by the company in the Delhi property is weighing heavily on it. With the shifting of airport from the city to the outskirts in Bengaluru, the super-normal profit generations from the Bangalore property are no longer available. To take care of the high debt on books, the company plans to raise money through QIB/FCCB.

- **Key Risks**

Better-than-expected improvement in the Bengaluru ARRs, and sale of land bank and Chennai general office space are some of the risks to our estimates.

Financial Statements (Consolidated)

Income statement	(INR mn)				
Year to March	FY08	FY09	FY10	FY11E	FY12E
Income from operations	5,146	4,522	4,362	5,937	8,571
Employee costs	815	884	954	1,247	1,800
Other expenses	2,034	2,081	2,142	2,803	3,960
Total operating expenses	2,849	2,965	3,096	4,050	5,759
EBITDA	2,297	1,557	1,266	2,170	3,224
Depreciation and amortisation	453	549	683	842	1,011
EBIT	1,843	1,008	583	1,328	2,214
Interest expenses	356	267	245	1,464	2,187
Other income	745	653	262	669	678
Profit before tax	2,233	1,393	600	533	705
Provision for tax	747	485	196	176	233
Core profit	1,485	909	404	357	472
Extraordinary items	-	542	-	-	-
Profit after tax	1,485	1,450	404	357	472
Profit after minority interest	1,485	1,450	404	357	472
Shares outstanding (mn)	378	378	378	378	378
EPS (INR) basic	3.9	2.4	1.1	0.9	1.3
Diluted equity shares (mn)	483	463	463	463	463
EPS (INR) diluted	3.1	2.0	0.9	0.8	1.0
Dividend per share (INR)	0.5	0.4	0.2	0.3	0.5
Dividend payout (%)	14.9	12.2	14.7	37.1	46.8

Common size metrics- as % of net revenues

Year to March	FY08	FY09	FY10	FY11E	FY12E
Operating expenses	55.4	65.6	71.0	68.2	67.2
Depreciation and Amortization	8.8	12.1	15.7	14.2	11.8
Interest expenditure	6.9	5.9	5.6	24.6	25.5
EBITDA margins	44.6	34.4	29.0	36.6	37.6
Net profit margins	28.9	20.1	9.3	6.0	5.5

Growth metrics (%)

Year to March	FY08	FY09	FY10	FY11E	FY12E
Revenues	23.8	(12.1)	(3.5)	36.1	44.4
EBITDA	19.0	(32.2)	(18.7)	71.4	48.6
PBT	52.1	(37.6)	(56.9)	(11.1)	32.2
Net profit	75.9	(38.8)	(55.5)	(11.6)	32.2
EPS	72.4	(38.8)	(55.5)	(11.6)	32.2

Balance sheet					(INR mn)
As on 31st March	FY08	FY09	FY10E	FY11E	FY12E
Equity capital	756	756	756	756	756
Reserves & surplus	8,545	18,643	19,071	19,212	19,380
Shareholders funds	9,301	19,399	19,827	19,968	20,135
Secured loans	12,911	18,186	20,336	26,336	27,836
Unsecured loans	7,445	6,309	5,159	2,659	2,659
Borrowings	20,357	24,495	25,495	28,995	30,495
Deferred tax liability (net)	914	1,004	1,004	1,004	1,004
Sources of funds	30,571	44,898	46,325	49,966	51,634
Gross block	25,531	38,870	38,870	53,715	55,715
Depreciation	3,364	3,985	4,762	5,688	6,782
Net block	22,167	34,885	34,108	48,027	48,933
Capital work in progress	4,058	9,345	11,345	0	0
Total fixed assets	26,225	44,231	45,453	48,027	48,933
Investments	1	1	1	1	1
Inventories	387	420	332	488	704
Sundry debtors	386	315	310	455	657
Cash and equivalents	2,958	306	401	(80)	766
Other current assets	2,675	2,846	3,046	3,246	3,446
Total current assets	6,406	3,887	4,089	4,110	5,574
Sundry creditors and others	933	1,713	1,711	1,664	2,367
Provisions	1,129	1,508	1,508	508	508
Total CL & provisions	2,061	3,221	3,218	2,172	2,874
Net current assets	4,344	666	871	1,938	2,700
Uses of funds	30,571	44,898	46,325	49,966	51,634
Adjusted BV per share (INR)	13.9	13.5	14.5	14.8	15.1

Free cash flow					(INR mn)
Year to March	FY08	FY09	FY10E	FY11E	FY12E
Net profit	1,485	1,450	600	357	472
Depreciation	453	549	694	842	1,011
Deferred tax	199	90	0	0	0
Others	(293)	(764)	(216)	973	1,697
Gross cash flow	1,845	1,325	1,078	2,173	3,180
Less: Changes in WC	657	(647)	110	548	(84)
Operating cash flow	1,188	1,972	968	1,625	3,264
Less: Capex	(9,320)	(6,547)	(2,000)	(3,500)	(2,000)
Free cash flow	(8,131)	(4,575)	(1,032)	(1,875)	1,264

Cash flow metrics					
Year to March	FY08	FY09	FY10E	FY11E	FY12E
Operating cash flow	1,188	1,972	968	1,625	3,264
Financing cash flow	10,316	891	453	904	(908)
Investing cash flow	(8,671)	(5,515)	(1,326)	(3,010)	(1,510)
Net cash flow	2,833	(2,653)	95	(481)	846
Capex	(9,320)	(6,547)	(2,000)	(3,500)	(2,000)
Dividend paid	(221)	(177)	(88)	(133)	(221)

Ratios

Year to March	FY08	FY09	FY10E	FY11E	FY12E
ROAE	21.2	12.8	5.6	4.8	6.2
ROACE	8.0	3.3	1.8	3.7	5.8
Inventory days	26.0	32.5	31.5	25.2	25.4
Debtors days	29.1	28.3	26.2	23.5	23.7
Payable days	131.2	162.8	201.8	152.1	127.7
Cash conversion cycle	(76.1)	(102.0)	(144.2)	(103.3)	(78.6)
Current ratio	3.1	1.2	1.3	1.9	1.9
Debt/EBITDA	8.9	15.7	20.1	13.4	9.5
Interest coverage	5.2	3.8	2.4	0.9	1.0
Fixed assets t/o (x)	0.3	0.2	0.1	0.1	0.2
Debt/equity	2.8	3.5	3.4	3.8	3.9

Du pont analysis

Year to March	FY08	FY09	FY10E	FY11E	FY12E
NP margin (%)	28.9	20.1	9.3	6.0	5.5
Total assets turnover	0.2	0.1	0.1	0.1	0.2
Leverage multiplier	3.6	5.3	6.3	6.4	6.6
ROAE (%)	21.2	12.8	5.6	4.8	6.2

Valuation parameters

Year to March	FY08	FY09	FY10E	FY11E	FY12E
Diluted EPS (INR)	3.1	2.0	0.9	0.8	1.0
Y-o-Y growth (%)	53.1	(36.1)	(55.5)	(11.6)	32.2
CEPS	5.1	3.9	2.9	3.2	3.9
Diluted P/E (x)	16.3	25.5	57.2	64.7	49.0
Price/BV (x)	3.6	3.7	3.5	3.4	3.3
EV/Sales (x)	7.9	10.5	11.1	8.8	6.2
EV/EBITDA (X)	17.6	30.4	38.1	24.1	16.4
EV/EBIDTA (x)+1 yr forward	26.0	37.4	22.2	16.2	
Dividend yield (%)	1.0	0.8	0.4	0.6	1.0

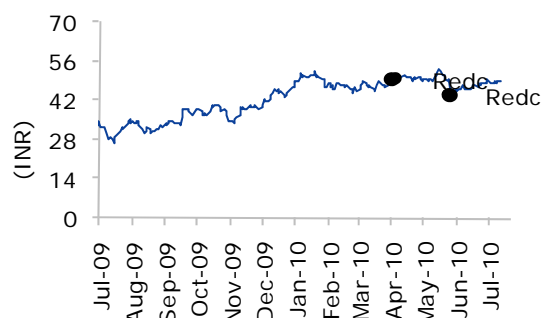
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Coverage group(s) of stocks by primary analyst(s): Hotels

Cox & Kings, EIH, Hotel Leela Venture, Indian Hotels Company and Mahindra Holidays & Resorts India.

Hotel Leelaventures



Recent Research

Date	Company	Title	Price (INR)	Recos
12-Jul-10	Thomas Cook	Good times ahead; Visit Note	63	Not Rated
02-Jun-10	Cox and Kings	Acquisitions driving growth; EBIDTA margins close to the best; Result Update	434	Hold
01-Jun-10	East India Hotels	Healthy ORs; subdued ARR; Result Update	1,115	Hold

Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	109	52	12	177

* 4 stocks under review

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	108	54	15

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	depreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

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