

November 3, 2008

Rating	Accumulate
Price	Rs26
Target Price	Rs49
Implied Upside	86.7%
Sensex	10,338

(Prices as on November 3, 2008)

Trading Data

Market Cap. (Rs bn)	0.8
Shares o/s (m)	36.9
Free Float	59.6%
3M Avg. Daily Vol ('000)	31.4
3M Avg. Daily Value (Rs m)	1.6

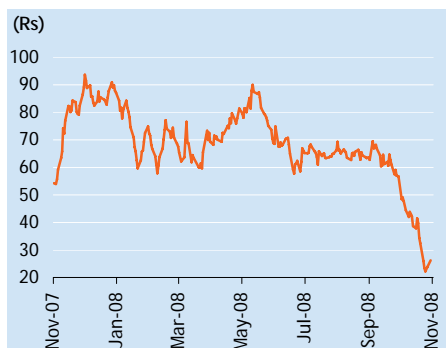
Major Shareholders

Promoters	40.4%
Foreign	21.5%
Domestic Inst.	0.1%
Public & Others	38.0%

Stock Performance

(%)	1M	6M	12M
Absolute	(53.7)	(67.7)	(49.3)
Relative	(36.3)	(26.5)	(1.0)

Price Performance (RIC: BHBH.BO, BB: BBH IN)



Source: Bloomberg

■ **Results:** Bhagwati Banquets & Hotels (BBHL) Q2FY09 results were below our expectations in terms of lower sales growth but were better at net profit level due to higher other income and zero tax provision. Net sales grew by 2% YoY, from Rs117m to Rs119m (our expectation Rs145m) mainly due to a decline in outdoor catering business. BBHL's EBIDTA margin declined by 140bps, from 23.5% to 22.1%YoY (our expectation 22.1%) due to a sharp rise in personnel and other expenses. Personnel cost went up by 450bps, from 8.8% to 13.3% of net sales due to an increase in the staff and salary revision during the year. Other income went up by 113%, from Rs11m to Rs23m (we expected Rs5m). The company did not make tax provision (we expected Rs4m) during the quarter. The company's net profit improved by 57% YoY, from Rs23m to Rs36m (our expectation Rs19m).

■ **Capex update:** BBHL is establishing restaurant and banquet facilities in six cities in FY09, with a total capital outlay of around Rs200m. Of these, Jaipur and Bangalore facilities are expected to go on stream in Q4FY09.

■ **Valuation:** We expect BBHL to report 94% CAGR in net sales and 123% CAGR in net profit over next two years. We expect the EBIDTA margin to improve from 26.5% in FY08 to 33.6% in FY10 due to the expansion of catering and restaurant business and commencement of 5-star hotel and health club at Surat. We have lowered our EPS estimates for FY09 and FY10 by 7% each in view of lower EBIDTA estimates.

At the CMP of Rs26.25, the stock trades at 6.0x FY09E EPS of Rs4.3 and 2.2x FY10E EPS of Rs12.2. We revise our rating for the scrip from 'BUY' to 'Accumulate' with price target of Rs 49.0(4x FY10 earnings) with an upside of 86.7% over CMP in the next 12 months.

Key financials (Y/e March)	FY07	FY08	FY09E	FY10E
Revenues (Rs m)	355	591	979	2,228
Growth (%)	54.1	66.1	65.9	127.5
EBITDA (Rs m)	78	156	263	748
PAT (Rs m)	20	90	160	449
EPS (Rs)	0.5	2.4	4.3	12.2
Growth (%)	42.4	359.5	78.8	180.1
Net DPS (Rs)	NA	1.0	1.5	2.0

Source: Company Data; PL Research

Profitability & valuation	FY07	FY08	FY09E	FY10E
EBITDA margin (%)	21.8	26.5	26.8	33.6
RoE (%)	11.1	13.3	10.7	21.2
RoCE (%)	8.4	11.1	9.7	17.4
EV / sales (x)	0.8	1.6	1.5	0.8
EV / EBITDA (x)	3.7	6.2	5.5	2.3
PE (x)	49.6	10.8	6.0	2.2
P / BV (x)	0.9	0.7	0.5	0.4
Net dividend yield (%)	NA	3.8	5.7	7.6

Source: Company Data; PL Research

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Q2FY09 Result Overview

(Rs m)

Y/e March	Q2FY09	Q2FY08	YoY gr. (%)	Q1FY09	H1FY09	H1FY08	YoY gr. (%)
Net sales	119	117	1.8	131	250	228	9.7
Expenditure							
Raw materials	36	40	(11.3)	42	78	85	(8.1)
<i>as % of net sales</i>	<i>30.0</i>	<i>34.4</i>		<i>32.3</i>	<i>31.2</i>	<i>37.2</i>	
Personnel expenses	16	10	53.4	14	30	21	41.8
<i>as % of net sales</i>	<i>13.3</i>	<i>8.8</i>		<i>10.5</i>	<i>11.8</i>	<i>9.1</i>	
Other expenses	41	39	5.9	47	88	75	17.9
<i>as % of net sales</i>	<i>34.6</i>	<i>33.3</i>		<i>35.9</i>	<i>35.3</i>	<i>32.8</i>	
Total Expenditure	93	89	3.6	103	196	180	8.5
OPBDIT	26	27	(4.2)	28	54	47	14.2
<i>OP Margin (%)</i>	<i>22.1</i>	<i>23.5</i>		<i>21.3</i>	<i>21.7</i>	<i>20.8</i>	
Other income	23	11	112.7	3	26	19	38.9
PBDIT	50	38	29.3	31	81	66	21.3
Depreciation	7	6	16.1	6	14	12	8.9
Interest	7	3	159.3	6	13	6	120.0
PBT	36	30	20.1	18	54	48	12.2
Prov. For tax	-	7		3	3	10	(70.0)
<i>% of PBT</i>	<i>-</i>	<i>23.7</i>		<i>16.3</i>	<i>5.6</i>	<i>20.8</i>	
PAT	36	23	57.4	15	51	38	33.8

Highlights

Marginal Revenue growth of 2% YoY

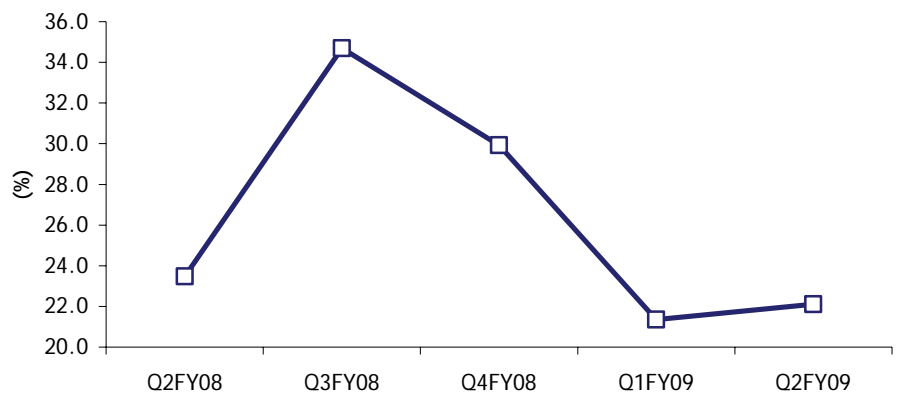
BBHL posted marginal revenue growth of 2% YoY, from Rs117m to Rs119m, primarily from the banquet, F&B services at revolving restaurant Patang and three prestigious health clubs in Ahmedabad namely Karnavati Club, Rajpath Club and GCA Club. The growth was lower than our expectation due to the fall in outdoor catering business during the quarter.

Margin declined by 140bps

BBHL's EBIDTA margin declined by 140bps, from 23.5% to 22.1% YoY mainly due to an increase in the personnel and other expenses. Personnel cost increased by 450bps, from 8.8% to 13.3% of net sales on lower sales growth and due to the additional staff employed and increase in the salaries during the year. Other expenses increased by 130bps, from 33.3% to 34.6% of net sales due to a rise in the selling and administration (S & A) cost. S & A cost increase by 120bps, from 20.2% to 21.4% of net sales.

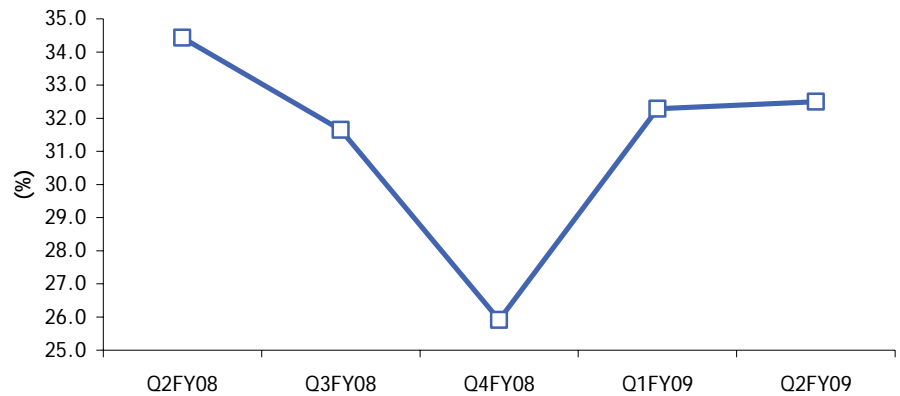
The company's material cost declined by 4400bps, from 34.4% to 30.0% of net sales due to a change in the product mix with an increase in F&B contracts during the year. The EBIDTA margin and material cost movement over the last five quarters is indicated in the following charts:

EBITDA Margin



Source: Company Data, PL Research

Material Cost as % of Net Sales



Source: Company Data, PL Research

As seen from the above charts, BBHL's EBIDTA margin improved from 23.5% in Q2FY08 to 34.7% in Q3FY08 due to a reduction in the material cost and due to festival and wedding season during the quarter. The margin fell to 21.3% in Q1FY09 due to a sharp rise in the material cost. The margins improved by 80bps QoQ to 22.1% during Q2FY09. As the company's business falls in three different segments namely outdoor catering, banquet and room service, the material cost and margin vary according to the sales mix.

BBHL's material cost declined from 34.4% in Q2FY08 to 25.9% in Q4FY08 due to an increase in the banquet facility, F&B services at three prestigious clubs in Ahmedabad and economies of scale. The material cost increased to 32.5% of net sales in Q2FY09 due to lower sales growth and high inflation during the quarter.

PAT improved by 57% YoY

BBHL's other income increased by 113%, from Rs11m to Rs23m. The company's depreciation increased by 16%, from Rs6m to Rs7m. Interest cost enhanced by 159%, from Rs3m to Rs7m, on a lower base. BBHL's PBT for the quarter grew by 20%, YoY, from Rs30m to Rs36m. The company did not make any tax provision during the quarter against Rs7m in the previous quarter. Higher other income and no tax provision have resulted in a 57% increase in PAT from Rs23m to Rs36m.

Outlook

BBHL is establishing restaurant and banquet facilities in six cities in FY09 namely: Mumbai, Hyderabad, Pune, Jaipur, Bangalore and Chandigarh. It has plans to invest around Rs30m in each of the facilities. The Jaipur and Bangalore facilities are likely to commence operations in Q3FY09. All these facilities will be on lease and hence the capex is low. BBHL will also undertake outdoor catering services in each of these cities. These will contribute for the full year from FY10 onwards.

The company's 5-star hotel and TGB health club facility at Surat is likely to go on stream in FY10. BBHL has plans to register over 500 members for its health club in FY09. The initial payment will be Rs2.5lac for the life membership. Surat is one of the fastest growing cities of India. The spending power of Surat is the highest among the major cities of India due to the diamond and textile businesses. Both the 5-star hotel and health club are likely to perform well.

The company has management and F&B contracts for prestigious clubs like Rajpath Club, Karnavati Club and GCA Club at Ahmedabad. Moreover, it has F&B contract of Patang - the only revolving restaurant in Gujarat. The company has plans to undertake similar contracts in other cities of Gujarat.

BBHL has plans to undertake F&B services at the SEZs coming near Ahmedabad. Gujarat is likely to have over 150 SEZ facilities and the company is exploring offering F&B facilities.

Issue of warrants for expansion plans

BBHL has allotted 7.56m warrants at Rs82 per warrant aggregating to Rs620m to promoters and non-promoters in February 2008. The entire proceeds of the issue have been utilized for establishing the restaurant and banqueting facilities and for outdoor catering services across various cities.

Concerns - slowdown in economy

The slowdown in domestic economy is likely to affect the sales and profitability of BBHL. The rise in inflation is likely to put a pressure on its margins due to an increase in the material cost. The global economic slowdown may also affect the inflow of foreign tourists.



As the company's business is in the hospitality segment, any deterioration in quality of foods or service levels is likely to affect the performance of the company.

Any delay in the execution of 5-star hotel and TGB Club projects at Surat may affect the sales and profitability of the company.

Valuation

We expect BBHL to report 94% CAGR in net sales and 123% CAGR in net profit over next two years. We expect the EBIDTA margin to improve from 26.5% in FY08 to 33.6% in FY10 due to the expansion of catering and restaurant business, introduction of corporate lunch packs and commencement of 5-star hotel and health club at Surat. We expect the company's RoE to improve from 13.3% in FY08 to 21.2% in FY10. Similarly, its RoCE is likely to improve from 11.1% to 17.4% during similar period.

We have revised the FY09 EPS estimates downward by 7%, from Rs4.6 to Rs4.3 and FY10 EPPS estimates by 7%, from Rs13.1 to Rs12.2 in view of lower EBIDTA estimates.

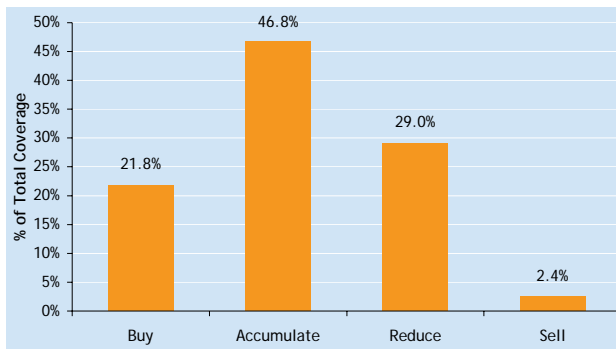
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Rating Distribution of Research Coverage



PL's Recommendation Nomenclature

BUY	: Over 15% Outperformance to Sensex over 12-months	Accumulate	: Outperformance to Sensex over 12-months
Reduce	: Underperformance to Sensex over 12-months	Sell	: Over 15% underperformance to Sensex over 12-months
Trading Buy	: Over 10% absolute upside in 1-month	Trading Sell	: Over 10% absolute decline in 1-month
Not Rated (NR)	: No specific call on the stock	Under Review (UR)	: Rating likely to change shortly

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