Hotels Q2 FY09 Review

November 07, 2008

Hotel sector Q2 results indicate demand slowdown on the back of moderation in both global and domestic economic activity in first half of current fiscal. H1 occupancies declined about 100-600bps yoy in metros like Mumbai and Delhi while ARRs grew at a slower pace of about 15% yoy in major business destinations. Operating margins declined as staff and fuel expenses mounted especially for smaller companies like Hotel Leela and TAJGVK. A weak operating environment coupled with non-recurring costs in the quarter led to nearly 20% yoy fall in adjusted profits for the companies in our coverage. Going forward, we believe Bangalore and Hyderabad market ARRs would decline over next two years while Mumbai and Delhi room rentals would likely remain flat. We remain cautious on the busy season outlook due to moderation in GDP growth, likely reduction of inbound foreign business travel and margin pressures.

Q2 FY09 highlights

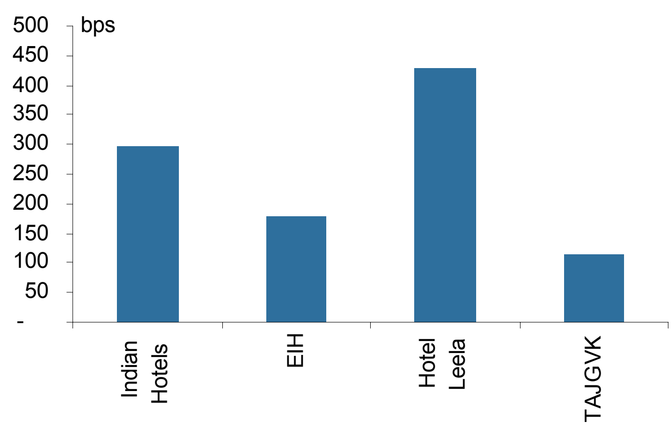
Rs mn	Q2 FY09	Q2 FY08	% yoy
Sales	7,858	7,290	7.8
Operating profit	2,362	2,476	(4.6)
Pre-exceptional PAT	1,410	1,299	8.5
Adj. PAT	1,223	1,523	(19.7)
			Inc/(Dec)
OPM (%)	30.1	34.0	(390)

Source: Companies, India Infoline Research

Aggregate revenues rise 7.8% yoy but margins decline

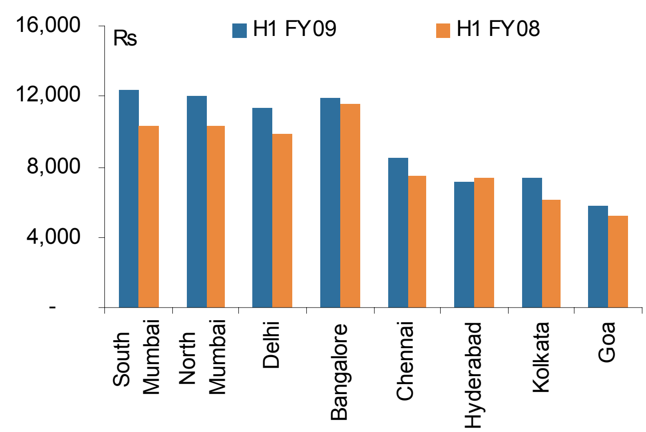
Our universe companies witnessed a 7.8% yoy increase in Q2 sales on the back of a moderate rise in ARRs but higher staff costs impacted operating margins. Smaller capacity players like Hotel Leela and TAJGVK also saw fuel expenses rise yoy.

Margins decline largely due to higher staff cost yoy



Source: Companies, India Infoline Research

ARRs increase 15% yoy in major cities



Source: Indian Hotels

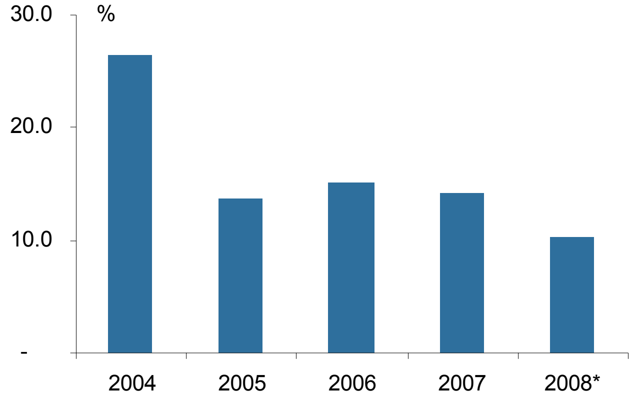
Cumulative adjusted PAT decline ~20% yoy on OPM decline, non-recurring items

Although pre-exceptional PAT improved by 8.5% yoy, non-recurring expenses such as provisions made on FX loans due to Re volatility led to decline in adjusted profit by nearly 20% yoy.

Cautious outlook for busy season; sector faces multiple headwinds

Foreign tourist arrivals in the country increased by 10.4% yoy in Jan-Sep 2008 period which is the slowest yoy rise in the past five years. This could be largely attributed to the recessionary conditions in developed markets which forces companies to cut their travel budgets. Domestic demand has also slowed down from its peak owing to moderation in GDP growth, inflation and rising air fares.

Growth in Jan-Sep foreign arrivals lowest in five years



Source: Ministry of Tourism, India Infoline Research
**provisional*

We expect Bangalore and Hyderabad market to witness ARR decline in next two years while Mumbai and Delhi room rates may remain stagnant as demand is likely to remain tepid. However, a key mitigating factor could be delay in fresh supply as several companies especially in real estate sector go slow on their hotel projects. Even so, we maintain our cautious outlook for the sector.

Valuations Summary

Companies	EPS		P/E		EV/EBIDTA		P/BV	
	FY09E	FY10E	FY09E	FY10E	FY09E	FY10E	FY09E	FY10E
Indian Hotels	5.7	6.1	8.5	8.0	6.7	5.3	0.9	0.8
EIH	5.8	7.2	14.0	11.4	10.4	8.8	2.3	2.0
Hotel Leela	3.4	3.3	7.3	7.4	13.0	12.6	0.9	0.8
TAJGVK	10.5	11.1	4.9	4.6	3.9	3.8	1.2	1.0

Source: India Infoline Research

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