

Bhagwati Banquets & Hotels

BUY

Rs 79

Sensex: 19,003

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Key Figures

(Rs m)

Y/e Mar	'07	'08E	'09E	'10E
Net Sales	355	555	830	1,823
EBITDA	80.0	288.3	410.2	837.5
PAT	19	150	196	458
PAT Gr. (%)	42.7	671.4	31.0	133.3
EPS (Rs)	0.4	3.3	4.3	10.0

Key Ratios

(%)

Y/e Mar	'07	'08E	'09E	'10E
EBITDA Mar.	22.5	51.9	49.4	45.9
RoCE	13.0	16.2	11.6	24.1
RoE	10.4	6.1	7.6	15.7

Valuations

(x)

Y/e Mar	'07	'08E	'09E	'10E
PER	187.5	24.3	18.5	7.9
EV / Sales	1.7	6.6	4.6	2.0
EV / EBITDA	8.0	25.4	14.6	5.5
MCap / Sales	1.4	6.6	4.4	2.0

Key Data

Bloomberg Code	: BBH@IN
Reuters Code	: BHBH.BO / NS

Shareholding Pattern (%)

Promoters	: 38.6
Foreign	: 10.6
Non-promoters	: 19.4
Public & Others	: 31.4

Price Relative to Sensex (%)

1 month	: 63.1
3 months	: 100.9
12 months	: NA

Shares Outstanding	: 29m
Market Cap	: Rs 2,317m
	\$ 59m

Average Volume (3 months)	: 0.7m shares
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(Price as on November 29, 2007)

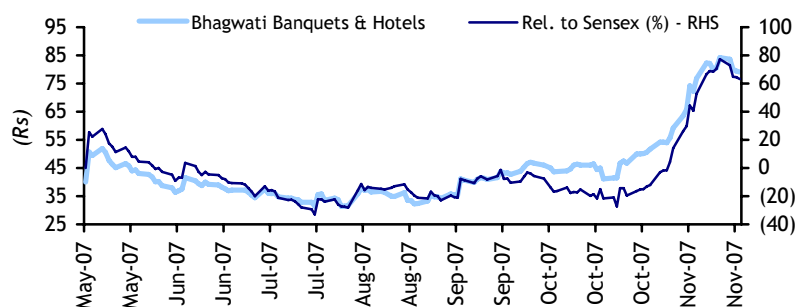
Redefining hospitality

Bhagwati Banquets & Hotels (BBH), operating on a unique business model of providing catering, banquet and club facilities under a single umbrella, commenced operations in Ahmedabad. The company has spread its wings to other cities in Gujarat, Rajasthan and Maharashtra. BBH is setting up a 180-room 5-star hotel in Surat, which is likely to be operational in March 2009.

BBH is the only organised player in high-end catering for conferences, weddings, parties and social gatherings in Gujarat. The company has established a 3-star hotel with banquet facility in Ahmedabad and also manages three elite clubs and a revolving restaurant in the city. In addition to these, BBH has also started supplying corporate lunch packs in Ahmedabad. It has also started catering services in Mumbai and plans to expand its business into other major cities in the country.

We expect the company, led by its ambitious expansion plans, to report 49% CAGR in net sales and 45% CAGR in net profit over the next three years. We expect EBITDA margin to improve from 21.8% in FY07 to 37.2% in FY10, due to reduction in material cost and the Surat Hotel going on stream in FY10. At the CMP of Rs79, the stock trades at 18.5x FY09E and 7.9x FY10E earnings. We initiate coverage on the company and recommend Buy rating with a target price of Rs120 in the next 12 months, which is an upside of 52% over the CMP.

Stock price performance



Source: Bloomberg, PL Research

Please see important disclaimer and disclosure at end of the report.

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Investment Arguments

Bhagwati Banquets & Hotels (BBH) provides catering and banquet services to its customers. Currently, it runs a 3-star hotel in Ahmedabad, which has 37 rooms and three banquet facilities having over 80% occupancy. BBH is the only company in Ahmedabad, which provides these high-end facilities.

BBH has been a pioneer in developing a professional approach to catering, and currently provides outdoor catering services in Gujarat. The company is spreading its wings in Rajasthan, Maharashtra, UP and other states. BBH holds a monopolistic position in high-end catering in Ahmedabad and Surat. The company plans to become a national player in catering business with a corporate identity. Its catering business has an operating margin of over 35%.

The company has recently commenced catering services in Mumbai and expects revenue of Rs40m in FY09 and Rs50m in FY10.

BBH has entered into contracts with three prestigious clubs - Rajpath Club, Karnavati Club (with 46 rooms) and GCA Club - in Ahmedabad for providing F&B and room services. It has also undertaken F&B contract for Patang Revolving Restaurant in Ahmedabad. BBH is exploring similar F&B servicing opportunities in Gujarat and Maharashtra. These contracts are likely to generate revenue of Rs130m in FY08, Rs195m in FY09 and Rs230m in FY10.

The company has commenced supply of food packets to corporates, BPO centers, shopping malls, theatres, etc. The corporate lunch pack business is likely to generate revenue of Rs105m in FY09 and Rs153m in FY10.

BBH has set-up *Murugan Express*, an exclusive chain of south Indian restaurant, in malls and theatres. This is likely to be a major growth driver for the company. The company's revenue from *Murugan Express* is likely to double every year for the next three years.

The company is setting up a 180-room 5-star hotel with banquet facilities in Surat with a capital of Rs800m. This hotel will have 65,000 sq.ft. for its banquet facility, business center and boardrooms. The hotel is likely to be operational in March 2009. This is likely to be the future growth driver of the company.

BBH is setting up its first exclusive club called *TGB Club*, with world-class amenities and facilities in Surat adjoining its 5-star hotel. It has plans to enroll 500 life members with membership fee of Rs200,000 each. This is likely to generate revenue of Rs100m in FY08.

BBH has a centralised kitchen facility at Chandodar near Ahmedabad and in Surat. This helps in cooking activity at a single location, resulting in substantial cost and energy savings. The company has its own transport vans (including a refrigerated van) for the transport of cooked food.

Its catering business generates free cash, as it receives payments in cash and obtains credit from its suppliers. Hence, working capital required for the catering business is low.

BBH has a track record of organising 1,100 parties in FY07 and the same is likely to increase in the coming years. Hence, the company has established a strong brand image in Gujarat.

The company's three businesses - catering, banquet and F&B services - are under a single umbrella. All these services are unique and the company has set very high standards of quality and service.

Rapid rise in revenue

Table 1: Sales composition (Rs m)

Y/e March	FY06	FY07	FY08E	FY09E	FY10E
Room sales	34	58	33	36	266
Food & beverages	67	112	39	45	122
Banquets, catering	128	185	481	747	1,337
Other services	2		2	3	98
Total	231	355	555	830	1,823

% of total

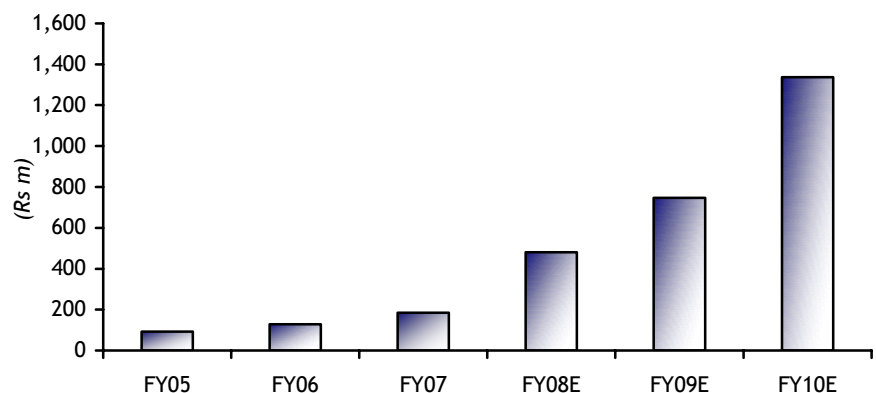
Room sales	14.8	16.4	6.0	4.4	14.6
Food & beverages	28.9	31.6	7.0	5.4	6.7
Banquets, catering	55.5	52.0	86.6	89.9	73.3
Other services	0.8	-	0.4	0.3	5.4

Source: Company Data, PL Research

As seen from the above table, the company derives maximum revenue from banquets and catering services. With the commencement of its Surat hotel, revenue from room rent is likely to shoot-up from 4.4% in FY09 to 14.6% in FY10. Income from other services like theatre, discotheque, shop rentals, beauty parlour and club activities is also likely to increase from 0.3% in FY09 to 5.4% in FY10.

The expected sharp rise in banquet and catering revenue is shown in the following chart:

Chart 1: Banquet, catering revenue

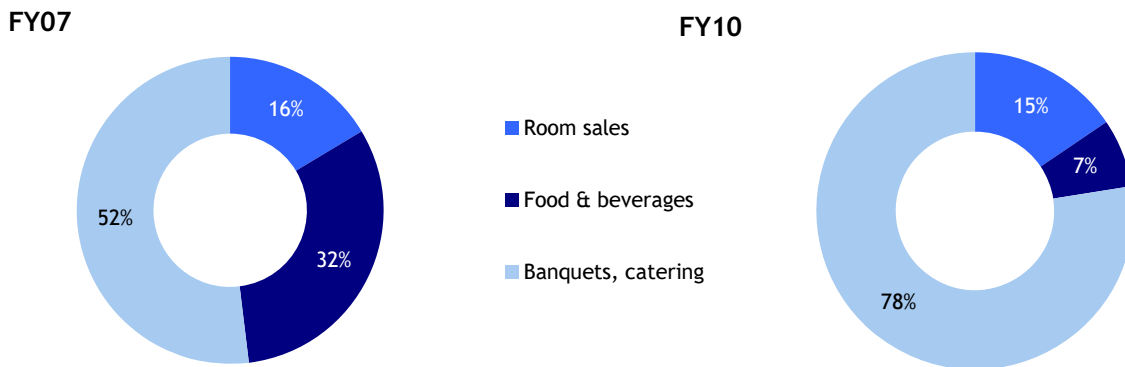


Source: Company Data, PL Research

The sharp rise in banquet and catering revenue in FY10 can be attributed to the commencement of its Surat hotel by the end of FY09.

Sales composition of BBH for FY07 and FY10E is indicated in the following chart:

Chart 2: Sales composition



Source: Company Data, PL Research

As seen from the above graphs, banquet and catering revenue is likely to increase from 52% in FY07 to 73% in FY10 due to the commencement of its Surat hotel. F&B revenue is likely to decline from 32% in FY07 to 7% in FY10. Revenue from other services, which has been nothing so far, is likely to be 5% in FY10.

High capacity utilisation

BBH hotel rooms are expected to have high occupancy of around 80% from FY08 to FY10, and the Surat hotel rooms are likely to have an occupancy of 75% in FY10, mainly due to shortage of premium hotels in these cities.

The banquet facilities at Ahmedabad and Surat are likely to have an average occupancy of around 75%, due to its presence in high-end catering and banquet facilities. High capacity utilisation is likely to drive future growth as there is no organised player in this segment.

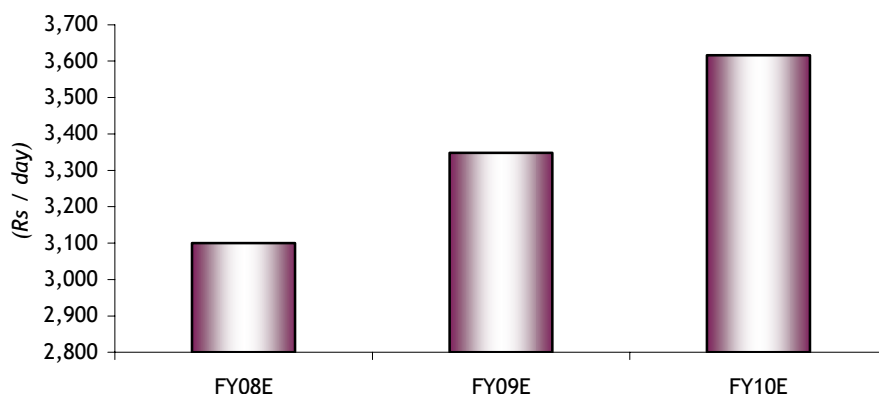
Table 2: Expected revenue from room sales and banquet

Particulars	FY08E	FY09E	FY10E
Room sales - Ahmedabad			
No. of rooms	37	37	37
Rent Rs/day	3,100	3,348	3,616
<i>Average occupancy (%)</i>	<i>80</i>	<i>80</i>	<i>80</i>
Room rent - Ahmedabad	33.49	36.17	39.07
Room sales - Surat			
No. of rooms			180
Rent Rs/day			4,000
<i>Average occupancy</i>			<i>75</i>
Room rent - Surat			197.10
Room services - Surat			30
Banquet facility - Ahmedabad			
Average rent per day - 1,500 people	390,000	429,000	471,900
Average rent per day - 700 people	189,000	207,900	228,690
Average rent per day - 500 people	140,000	154,000	169,400
Average rent per day - 50 people	15,000	16,500	18,150
Total	734,000	807,400	888,140
<i>Average occupancy (%)</i>	<i>75</i>	<i>75</i>	<i>75</i>
Banquet revenue - Ahmedabad	200.93	221.03	243.13
Banquet facility - Surat			
Average rent per day - 1500 people			525,000
Average rent per day - 1000 people			380,000
Average rent per day - 700 people			294,000
Average rent per day - 500 people			230,000
Boardroom - 4 nos.			33,000
Total			1,462,000
<i>Average occupancy</i>			<i>75</i>
Banquet revenue - Surat			400
Exhibition hall - Surat			
			10

Source: Company Data, PL Research

As seen from the above table, the company derives maximum revenue from its banquet facility. Moreover, the Surat hotel will be a major revenue earner from FY10 onwards.

Expected rise in realisation of room rent in Ahmedabad for FY08 to FY10 is shown in the following chart.

Chart 3: Room rent - Ahmedabad


Source: Company Data, PL Research

As seen from the chart, the company is likely to increase room rent by 8% per annum from FY08 to FY10.

Capex

BBH is setting up a 5-star hotel in Surat with 65,000 sq.ft. (two halls of 32,500 sq.ft. each) convention and banquet hall to accommodate at least 3,000 people at a time. This hotel will have 180 rooms (deluxe, suites and presidential suites). It will also have three multi cuisine restaurants and a 24-hour coffee shop. The Surat hotel will have a business centre with boardrooms, conference rooms, two swimming pools, world-class spa, pub, health club, salon, discotheque and shopping centre. The club amenities will include - billiard room, table tennis, squash court, tennis court and card room. The hotel is likely to be operational in March 2009. The total capex for this project is estimated at Rs1,153m.

Table 3. Cost allocation for the Surat project

(Rs m)

Particulars	Amount
Land	61
Building	901
Plant & machinery	40
Vehicles	4
Consultancy	13
W/C margin	7
IPO & PO expenses	81
Contingencies	46
Total	1,153

Source: Company Data, PL Research

BBH is likely to fund the project through proceeds of a public issue, debt and internal accruals.

Club membership - Surat

BBH plans to enroll 500 life members for its Surat club at a membership fee of Rs200,000 per member. This is likely to generate revenue of Rs100m in FY08. The exclusive *TGB Club* will have world-class facilities and will be adjoining its 5-star hotel. Surat is one of the fastest growing cities in the world due to the flourishing diamond and textile businesses. Earning and spending power in Surat is one of the highest in India. Hence, it will be easy for BBH to rope in 500 life members.

Realisation to improve

Room rent at Ahmedabad and Surat, and revenue from its banquet facilities are likely to improve year on year, as the company will be able to pass the increase in cost to its customers due to its monopolistic position and shortage of hotel rooms in the premium segment.

Realisation from catering is also likely to improve, as the company is likely to pass the increase in cost to its customers.

Business Overview

The 3-star Grand Bhagwati Hotel, with banquet facility, commenced operations in June 2002. This hotel has 37 rooms, three banquet halls measuring 11,000, 7,000 and 5,000 sq.ft. and a large lounge. The banquet halls are ideal for weddings, social gatherings, business conferences and company meetings. The Grand Bhagwati has three restaurants - a 24-hour coffee shop, a vegetarian restaurant and a terrace restaurant. It also has small meeting rooms for business and company conferences.

The company provides special outdoor catering service for weddings, receptions, company meetings, social gatherings, etc. Currently, BBH commands a monopoly in high-end catering in Ahmedabad and Surat. It has set-up centralised kitchens at Chandodar, Ahmedabad (25,000 sq.ft) and Surat (10,000 sq.ft). The company has its own fleet of eight vehicles, including a refrigerated van to transport food items. The catering rates range from Rs350 to Rs900 per person.

BBH has recently proposed to commence the supply of ready-to-eat lunch packs to corporate. The company proposes to establish a facility to make 10,000 packs per day and will supply them at Rs50 per pack.

BBH provides F&B services to prestigious clubs - Rajpath Club, Karnavati Club (both clubs having over 7,000 members each) and GCA Club - in Ahmedabad. It has recently entered into contract to provide F&B services to a revolving restaurant, Patang.

BBH provides personalised services, with different food delicacies, different tastes, menus and decorations. It has organised parties for 300 to 10,000 guests.

TGB Foods operates bakery shops and has eight outlets in Ahmedabad. These shops sell confectionery and bakery products.

Acquisitions

During FY06, the company made the following acquisitions:

Table 4: Acquisitions

Company	Business
Bhagwati Caterers Private Limited	Outdoor catering
TGB Resorts Karnavati	Outdoor catering & restaurant
Bhagwati International	Restaurant
Lov Kush Properties Private Limited	Land for Surat hotel

Source: Company Data, PL Research

All these acquisitions are likely to improve sales and profitability of the company. Moreover, this will strengthen the outdoor catering business of the company.

Club Management

During FY07, BBH entered into a tie-up with three elite clubs of Ahmedabad for providing F&B services to their members. All three are prestigious clubs in Ahmedabad and hence the company can leverage the contacts of their members for outdoor catering and banquet facilities.

Moreover, BBH has entered into a contract with Patang Restaurant for providing F&B services. Patang Restaurant is the only revolving restaurant in Ahmedabad located at a height of 221 feet. This gives the company rich experience of providing catering services to high-end customers.

Domestic scenario

Demand for hotel accommodation has remained buoyant due to the arrival of business travellers and tourists to Ahmedabad. The per capita income of Gujarat is Rs1,300 as compared to Rs450 for India. A lot of business and industrial activities keep hotels in Ahmedabad occupied throughout the year. As against India's GDP growth of around 9%, service sectors such as trade, hotels, transport and communication has reported 13% growth.

Increase in number of low cost airlines, infrastructure development and increase in outsourcing from India have increased tourist arrival. Moreover, India is recognised for medical tourism. We expect the hotel industry to do well in Ahmedabad, due to the increase in FDI and setting up of SEZs in Gujarat.

The catering segment in India is estimated at Rs500bn and is growing at over 20% per annum. Catering business is divided into flight kitchens such as Tajsats, Skygourmet, Ambassador Flight Kitchen, etc. Other organised players are Radhakrishna Hospitality (Foodland), Mars Hospitality Group, etc. There are no organised players in the catering segment in Gujarat, and hence the company has first mover advantage. Moreover, the company will have cost advantage as compared to other unorganised caterers as it has set-up a centralised kitchen in Ahmedabad. BBH is expanding its catering operations to other cities in Rajasthan, Madhya Pradesh, Uttar Pradesh and Maharashtra, and is likely to become a national player.

Growth drivers

Major growth drivers for BBH are:

- Increase in GDP and improvement in lifestyle with higher disposable income
- Higher spending on weddings and other social functions, especially in Gujarat and Rajasthan
- Increase in corporate spending on meetings, seminars and conferences
- Growing trend of malls, BPOs and corporates providing lunch packs to their employees
- 5-star hotel in Surat with banquet facility
- New elite health club facilities at Surat

- Opening of *Murugan Express*, an exclusive chain of south Indian restaurant, in malls and theatres

Competition

The company faces competition from unorganised regional players, who mainly cater to weddings and other social gatherings. However, they lack a centralised kitchen facility and have to cook at the site of the function, which causes inconvenience.

Unorganised players have the advantage of collecting their fees in cash, and hence are more competitive than BBH. While BBH conducts its entire business through cheque, and hence collects the following taxes from its customers:

Table 6: Taxes on service

Service	Tax rate	Effective Tax Rate
Service tax on banquet charges - indoor	12.36%	7.42%
Service tax on catering - indoor	12.36%	7.42%
Service tax on catering - outdoor	12.36%	6.18%
VAT - on food items	4%	4%

Source: Company Data, PL Research

Indoor services are eligible for 40% tax exemption, whereas outdoor services are 50% tax exempt. With the above exemption, the effective tax charged to the customer has come down.

BBH's closest competitor in Ahmedabad in the catering segment is Gordhan Maharaj, which manages F&B services for two restaurants in the city.

Major competitors for BBH in the hotel segment in Surat are: Taj Gateway (5-star hotel with 132 rooms), Lords Park Inn (3-star hotel with 110 rooms) and Yuvaraj Hotel (3-star hotel with 55 rooms). However, demand for rooms in Surat outpaces supply, and this trend is likely to continue in future as well.

Edge over competition

Being the only organised player, the company can participate in big events like marriages, cricket matches and in corporate events such as seminars, conferences, etc. Unorganised players lack financial, human and administrative resources and hence are unable to compete with BBH.

BBH is the only company having large banquet facility in Ahmedabad to suit various requirements and different group sizes. There are no other facilities in Ahmedabad that can be compared to BBH, thus all major functions are held at The Grand Bhagwati.

The company operates centralised kitchens in Ahmedabad and Surat, where cooking takes place and then distributed to various locations, resulting in substantial savings in energy and cost. It will be difficult for an unorganised player to replicate this facility.

BBH is setting up a 5-star hotel in Surat, which is located at a distance of 1.5 km from the airport, and an exclusive health club adjoining the hotel. Currently, there are no 5-star hotels in Surat, and hence the company will have first mover advantage.

BBH is setting up an exhibition hall at its Surat hotel. This will attract corporates and will complement its restaurant revenue. Currently, there is no such facilities in Surat.

New offerings

The company has planned several new initiatives as follows:

- Supply of corporate lunch packs in Ahmedabad
- Exhibition hall, theatre, discotheque, shops, beauty parlour in its Surat hotel
- Elite health club facilities in Surat
- Outdoor catering across the country in cities like Mumbai, New Delhi, Jaipur, Udaipur, Jodhpur, Goa, Hyderabad, Aurangabad, etc.

All these initiatives are likely to be future growth drivers for the company.

Company & Management Background

Mr. Narendra Somani and Mr. Devanand Somani, first generation entrepreneurs, started Bhagwati Banquets Private Limited in November 1999. This business was later converted into a public limited company in April 2000.

In 1997, the company commenced its catering operations in Surat. It bagged F&B and room management contract from Karnavati Club in 1999. BBH has received an award from CNBC TV18 for the 'Most Promising Small Enterprise' in 2006. The company issued an IPO in May 2007.

The company entered into F&B contracts with Rajpath Club and GCA Club in 2007. BBH has an employee strength of around 1,500 of which around 270 are in the catering section.

Major strengths

- The company has major strengths in managing indoor and outdoor catering services, due to its professional approach and reputation built over the years.
- BBH has a centralised kitchen at Chandodar and has service vans, including a refrigerated van. This helps easy movement of cooked food to the venue and helps in maintaining cleanliness and hygiene.
- Being a corporate entity, the company is preferred as compared to its competitors in the unorganised sector.
- The banquet facility is one of its kinds in Ahmedabad, and it has no major competitors in the city.
- BBH has gained expertise in catering and banquet services and hence was able to bag F&B contracts for elite clubs in Ahmedabad. Moreover, it has developed expertise in managing revolving restaurants - a unique dining experience in Ahmedabad.
- The company has trained master chefs, waiters and room attendants and has staff strength of over 460 employees. BBH has invested in training and development program for its employees to meet the highest level of service standards.

Entry barriers

- Major entry barrier for the catering business is supply of quality food for the masses. Majority of BBH's competitors are in the unorganised sector and lack the human, financial and managerial resources.
- Another major barrier is the availability of centralised kitchen, where all the resources are available under one roof. Majority of the unorganised players do not have centralised cooking facility and hence have higher costs.
- Being a corporate entity, the company is well accepted amongst MNCs and Indian companies operating in and around Gujarat. BBH is the only organised player in Gujarat.

- The company enjoys economies of scale due to the size of its operation.

Major raw materials

Major raw materials for catering are: grains, pulses, vegetables, fruits, dry fruits, milk and milk products, etc. The company purchases these materials on credit and charges its customers on cash basis and hence the catering business generates surplus cash from its operations. Except few reputed corporates, it does not extend any credit and hence its debtors are at the lowest. Moreover, there are no major bad debts in the company's business.

The banquet facility requires furniture, curtains, chair covers, decoration materials and flowers. Most of these materials are available on credit and hence the banquet business also generates surplus cash. Similarly, the club management and restaurant business generate surplus cash. Since all major businesses of BBH generate surplus cash, the company requires minimal working capital.

Being the market leader, the company can pass on any increase in material cost to its customers. The company revises tariff for various services on a periodic basis.

Risks

- The company is in the hospitality segment and caters to the masses for food and beverages. Any lapse in quality at its end could lead to loss of reputation, which may result in substantial fall in revenue and profitability.
- BBH's major strength lies in the master chefs (cooks) and service waiters. Entry of any other major player may result in staff attrition from the company.
- The hotel industry depends on the arrival of tourists and business executives. In the event of tourist flow slowing down, occupancy ratio will come down.
- Club management contracts are subject to periodic renewals and are dependent upon the level of service provided. Any lapse in rendering efficient services may result in the termination of these contracts.

Financials & Valuation

Equity history

Table 7: History of capital raised by the company

Particulars	Month	(Rs m)	Total	No. of shares
Equity shares	Mar.05	40.6	40.6	4.1
Equity shares issue @ Rs 25 (10+15)	Mar'06	22.3	62.9	6.3
Public issue @Rs 40 (10+30)	May'07	230.0	292.9	29.3
Pref issue@ Rs 70 (10+60)	FY08	166.7	459.6	46.0

Source: Company Data, PL Research

In May 2007, the company came out with a public issue of 23 million equity shares at Rs40 (10+30) per share aggregating Rs920m. The proceeds of this issue are being utilised for setting up a 5-star hotel at Surat. Apart from this, BBH has plans to issue 16.67 million shares through an equity issue of around Rs75 per share aggregating Rs1.25bn.

Q2FY08 results

For Q2FY08, the company reported 5.5% QoQ rise in net sales from Rs110.8m to Rs116.9m. As the company came out with an IPO in May 2007, the comparative results for the previous year are not available. Operating profit grew by 37% from Rs20.0m to Rs27.5m. Operating margin improved by 540bps from 18.1% to 23.5%, mainly due to decline in material cost. BBH's material cost declined QoQ from 40.2% to 34.4%. Net profit grew by 46% QoQ from Rs15.5m to Rs22.6m due to margin improvement and decline in interest cost.

Table 8: Q2FY08 results

(Rs m)

Y/e March	Q2 FY08	Q1 FY07	QoQ gr. (%)
Net sales	117	111	5.5
Total expenses	89	91	(1.5)
<i>As % of net sales</i>	<i>76.5</i>	<i>81.9</i>	
Raw materials	40	45	(9.6)
<i>As % of net sales</i>	<i>34.4</i>	<i>40.2</i>	
Personnel expenses	10	11	(1.9)
<i>As % of net sales</i>	<i>8.8</i>	<i>9.5</i>	
Other expenses	39	36	8.7
<i>As % of net sales</i>	<i>33.3</i>	<i>32.3</i>	
Operating profit	27	20	37.3
<i>Operating margin (%)</i>	<i>23.5</i>	<i>18.1</i>	
Other income	11	8	37.5
EBIDTA	38	28	37.3
<i>EBITDA margin (%)</i>	<i>32.9</i>	<i>25.3</i>	
Interest	3	3	(18.2)
Depreciation	6	6	-
Profit before tax	30	19	59.7
Total tax	7	3	133.3
<i>Tax rate (%)</i>	<i>23.7</i>	<i>16.2</i>	
PAT	23	16	45.5

Source: Company Data, PL Research

Growth

We expect BBH to report 49% CAGR in net sales over next three years due to steady rise in income from existing operations and commencement of Surat hotel in FY10. The company is likely to report 120% YoY growth in revenue in FY10 due to commencement of Surat hotel and health club.

Margin

We expect BBH's EBIDTA margin to improve from 21.8% in FY07 to 26.2% in FY08, 31.3% in FY09 and 37.2% in FY10. Improvement in margin is likely to come from better sourcing ability of raw materials, improved operational efficiencies, economies of scale and commencement of Surat hotel. We expect material cost to drop from 37.3% in FY07 to 31.1% in FY10 due to change in product mix with increased revenue from banquet facilities, which has lower material cost. We expect the company to report 67% CAGR in EBIDTA from Rs78m in FY07 to Rs678m in FY10 due to improvement in margin.

Net profit

We expect BBH's net profit to grow by 45% CAGR over the next three years from Rs19m in FY07 to Rs458m in FY10. This growth is likely to come from sharp jump in sales and improvement in margin.

Sharp rise in equity capital

BBH's equity capital is likely to rise sharply from Rs63m in FY07 to Rs460m in FY08 due to issue of 23 million shares in IPO and expected preferential issue of 16.7 million shares. Proceeds of the proposed preferential issue are likely to be utilised for constructing a new 5-star hotel in Ahmedabad.

Ratio

We expect BBH's RoCE to improve from 13% in FY07 to 24% in FY10. The company's RoE is likely to improve from 10% in FY07 to 16% in FY10, despite the sharp rise in equity capital.

Valuation and outlook

We expect the company, led by the commencement of its Surat hotel in FY10, to report 49% CAGR in net sales and 45% CAGR in net profit over the next three years. We expect EBIDTA margin to improve from 21.8% in FY07 to 37.2% in FY10. At the CMP of Rs79, the stock trades at 24.3x FY08E, 18.5x FY09E and 7.9x FY10E earnings. We initiate coverage on the company and recommend Buy rating with a target price of Rs120 in the next 12 months, which is an upside of 52% over the CMP.

Income Statement

(Rs m)

Y/e March	FY06	FY07	FY08E	FY09E	FY10E
Net sales	231	355	555	830	1,823
<i>YoY gr. (%)</i>	<i>72.7</i>	<i>54.1</i>	<i>56.3</i>	<i>49.5</i>	<i>119.5</i>
Operating expenses	180	278	410	570	1,146
Material cost	97	133	195	274	567
<i>% of sales</i>	<i>42.2</i>	<i>37.3</i>	<i>35.1</i>	<i>33.0</i>	<i>31.1</i>
Staff cost	17	26	48	71	159
<i>% of sales</i>	<i>7.5</i>	<i>7.4</i>	<i>8.6</i>	<i>8.6</i>	<i>8.7</i>
Selling & admin. exps	36	71	95	126	231
<i>% of sales</i>	<i>15.6</i>	<i>20.1</i>	<i>17.0</i>	<i>15.1</i>	<i>12.7</i>
Misc expenses	29	47	73	100	189
<i>% of sales</i>	<i>12.5</i>	<i>13.3</i>	<i>13.1</i>	<i>12.0</i>	<i>10.3</i>
Operating profit	51	78	145	260	678
<i>Operating margin (%)</i>	<i>22.2</i>	<i>21.8</i>	<i>26.2</i>	<i>31.3</i>	<i>37.2</i>
Other income	1	3	143	150	160
EBIDTA	51.8	80.0	288.3	410.2	837.5
<i>EBIDTA margin (%)</i>	<i>22.5</i>	<i>22.5</i>	<i>51.9</i>	<i>49.4</i>	<i>45.9</i>
Depreciation	16	34	51	100	127
Avg gross block	276	357	662	1,436	2,224
<i>Amortisation rate (%)</i>	<i>5.8</i>	<i>9.5</i>	<i>7.7</i>	<i>6.9</i>	<i>5.7</i>
EBIT	36	46	237	310	710
<i>EBIT margin (%)</i>	<i>15.5</i>	<i>13.0</i>	<i>42.7</i>	<i>37.4</i>	<i>39.0</i>
Interest	11	16	9	13	16
Avg debt	109	134	89	105	126
<i>Av. int. rate (%)</i>	<i>8.7</i>	<i>11.0</i>	<i>9.0</i>	<i>10.5</i>	<i>10.4</i>
Profit before tax	25	30	228	298	695
Tax provision	11	11	78	102	237
<i>Effective tax rate (%)</i>	<i>44.8</i>	<i>36.2</i>	<i>34.3</i>	<i>34.1</i>	<i>34.1</i>
Net profit	14	19	150	196	458

Source: Company Data, PL Research

Balance Sheet

(Rs m)

Y/e March	FY06	FY07	FY08E	FY09E	FY10E
SOURCES OF FUNDS					
Equity share capital	63	63	460	460	460
Reserves & surplus	104	123	1,995	2,110	2,460
Networth	167	186	2,455	2,570	2,920
Total debt	144	123	54	155	96
Avg debt	109	134	89	105	126
Deferred tax liability	19	22	32	52	92
Total	330	377	2,541	2,777	3,107
APPLICATION OF FUNDS					
Gross block	324	389	935	1,936	2,511
Avg gross block	276	357	662	1,436	2,224
Less: accum. depreciation	39	73	51	100	127
Net block	285	317	884	1,837	2,384
Capital work-in-progress	-	-	50	80	120
Investments	40	-	1,650	870	530
Current assets, loans & advances	45	159	201	310	709
Inventories	8	25	27	50	120
Sundry debtors	22	56	65	115	280
Cash and bank balance	5	11	20	29	81
Other current assets					
Loans and advances	10	67	89	116	228
Less: current liab. & prov.	42	105	251	327	642
Current liabilities	37	86	119	153	322
Provisions	5	18	132	175	320
Net current assets	3	54	(51)	(17)	67
Miscellaneous exp not w/off	2	7	7	7	7
Total	330	377	2,540	2,776	3,108

Source: Company Data, PL Research

Cash Flow

(Rs m)

Y/e March	FY06	FY07	FY08E	FY09E	FY10E
Net cash from operations	45	26	232	205	509
Net cash from investments	(137)	(31)	(2,370)	(285)	(382)
Net cash from financing	91	10	2,148	88	(75)
Net increase/(dec.) in cash	(1)	6	10	9	53
Opening balance	6	5	10	20	29
Closing balance	5	10	20	29	81

Source: Company Data, PL Research

Key Ratios

Y/e March	FY06	FY07	FY08E	FY09E	FY10E
Valuation (x)					
P/E	265.6	187.5	24.3	18.5	7.9
P/BV	3.0	2.7	1.5	1.4	1.2
Market cap/sales	2.2	1.4	6.6	4.4	2.0
EV/EBIDTA	12.6	8.0	25.4	14.6	5.5
EV/sales	2.8	1.7	6.6	4.6	2.0
Profitability (%)					
Operating margin	22.2	21.8	26.2	31.3	37.2
EBIDTA margin	22.5	22.5	51.9	49.4	45.9
EBIT margin	15.5	13.0	42.7	37.4	39.0
PBT margin	10.8	8.6	41.0	35.9	38.1
Net margin	5.9	5.5	27.0	23.6	25.1
RoE	8.2	10.4	6.1	7.6	15.7
RoCE	13.3	13.0	16.2	11.6	24.1
Growth (%)					
Revenue	72.7	54.1	56.3	49.5	119.5
Operating profit	54.3	51.7	87.5	79.0	160.4
EBIDTA	56.4	54.5	260.4	42.3	104.2
Net profit	50.9	42.7	671.4	31.0	133.3
EPS	50.4	41.7	671.4	31.0	133.3
CEPS	69.2	78.9	276.9	47.3	97.7
Efficiency Ratios					
Working capital (days)	2.1	29.2	1.2	(15.0)	4.9
Inventory (days)	8.1	16.6	17.0	16.9	17.0
Debtors (days)	21.3	40.3	39.8	39.6	39.5
Creditors (days)	53.8	81.3	91.4	86.9	75.6
Net fixed assets (x)	0.9	1.2	0.9	0.6	0.9

Source: Company Data, PL Research



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PL's Recommendation Scale

BUY	: > 15% Outperformance to BSE Sensex	Outperformer	: 5 to 15% Outperformance to Sensex
Market Performer	: -5 to 5% of Sensex Movement	Underperformer	: -5 to -15% of Underperformance to Sensex
Sell	: <-15% Relative to Sensex		

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