

Company Flash

28 October 2007 | 7 pages

Indian Hotels (IHTL.BO)

Buy: 2Q Results: Strong EBITDA, but Higher Taxes Dampen Growth

- **Strong operating performance, in-line** — Standalone revenues grew 16% YoY with EBITDA up a strong 35%, in-line with expectation; however higher interest costs and taxes dampened earnings growth to 15% YoY. EBITDA expansion of 420bps to 29% was healthy, despite an appreciating rupee – largely driven by ARR growth of 18% YoY, ahead of peers and higher occupancies 68%.
- **We expect a stronger 2H** — 1) Company has moved to rupee based tariff w.e.f from Sep'07 and increased rates by ~15-18% in peak season starting Oct'07; 2) Rooms under refurbishment in 1HFY08 expected to get operational; and 3) higher business and tourist traffic are expected to drive up occupancies.
- **What's new?** — 1) Nine Ginger hotels operational, adding 6 more by Mar'08, taken steep hike in tariffs; 2) Other hotel and air-catering subs doing well; and 3) raising ~Rs23bn through Rights, NCDs and a warrant issue for expansion.
- **Growth overseas remains a focus** — Existing properties doing well, with occupancies of average 70%-plus and healthy ARR's across locations, particularly London. Expects to invest \$80m (vs. \$35m earlier) in 'The Pierre', New York on room refurbishments, starting Jan'08. Increased stake of 11% in Orient Express is in-line with strategy to grow overseas; however company was silent on way forward, post Orient's denial for entering into any alliance.
- **Maintain Buy (1L)** — The stock has underperformed, but with earnings growth visibility intact, valuations of 15x FY09E PE at par with sector appear attractive.

Buy/Low Risk	1L
Price (26 Oct 07)	Rs141.85
Target price	Rs187.00
Expected share price return	31.8%
Expected dividend yield	1.1%
Expected total return	32.9%
Market Cap	Rs85,514M
	US\$2,173M

Price Performance (RIC: IHTL.BO, BB: IH IN)



Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Mar	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2006A	2,487	4.26	66.8	33.3	4.4	15.5	0.9
2007A	3,703	6.14	44.2	23.1	4.1	18.6	1.1
2008E	4,954	8.22	33.8	17.3	3.4	21.6	1.1
2009E	5,672	9.41	14.5	15.1	2.9	20.8	1.1
2010E	6,100	10.12	7.5	14.0	2.5	19.0	1.1

Source: Powered by dataCentral

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See Appendix A-1 for Analyst Certification and important disclosures.

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¹Citigroup Global Markets India Private Limited

Figure 1. 1QFY08 and 2HFY08 Standalone Earnings Summary

Rs in Millions	2QFY07	2QFY08	YoY	2HFY07	2HFY08	YoY
Net Sales	2,667	3,414	16%	5,843	6,879	18%
EBITDA	730	989	35%	1,613	2,085	29%
Margin	24.8%	29.0%		23.5%	30.3%	
Interest	156	257	64%	334	484	45%
Other Income	263	252	-5%	367	431	17%
Depreciation	219	207	-5%	438	420	-4%
PBT	618	777	26%	1,208	1,613	33%
PAT	459	532	16%	847	1,080	27%

Source: Company Reports, Citi Investment Research

Indian Hotels

Company description

Indian Hotels (IHC) is the largest hotel operator in India with a presence in the luxury, business and leisure hotel segments. It owns the 'Taj' brand and operates 81 hotels (9,901 rooms) across India and international locations. It is looking to enter the budget hotel segment through its new brand 'Ginger', and make a foray into the adventure holiday business with wildlife lodges. It already operates eight budget hotels, and plans to expand these to 30 in the next 2-3 years with an investment of Rs4bn. The company is also looking to expand overseas through acquisitions/management contracts. Other new revenue streams being explored include serviced apartments, spas and F&B outlets. IHC is the hotel-sector flagship company of Tata Group, which holds a 29% stake.

Investment strategy

IHC is our top pick in India's growing hospitality sector with target of Rs187 based on 21x Sept '08 P/E, a premium to the sector average (15x). Our target multiple factors in risk of increased room supply starting in FY09E. Favorable macro environment to increase business and leisure travel traffic to India should trigger strong demand for hotel rooms, increase occupancies and average room rates. Leveraging its large room inventories across key growth cities, premium brand positioning with 'Taj' and leadership in domestic markets, we believe IHC is well positioned for growth. Initiatives to de-risk the company's business model and further aid growth and profitability include: 1) Forays into budget hotels; 2) Expansion of service offering to spas, serviced apartments and F&B outlets; 3) Growth through management contracts; and 4) increased presence in overseas markets.

Valuation

Our target price of Rs187 is based on 21x Sept '08E P/E, a premium to average sector valuations of 15x. The stock's three-year historical range is 15-22x P/E, largely on a par with domestic peers, unwarranted given: 1) IHC's market leadership and advantage of large room inventory; 2) Its premium brand positioning with 'Taj'; and 3) strong business model with reasonable and growing presence in international markets. Factoring this and our expectations of strong 34% earnings growth in FY08E, we expect a re-rating of current stock valuations.

Risks

Our risk rating system, which tracks historical 260-day share price volatility rates India Hotels Medium Risk. However, we assign a Low Risk rating due to: 1) Sustained growth outlook for the hotel industry given the conducive macro environment; 2) Its leadership position in domestic markets, advantage of scale and strong business model; and 3) Its strong brand positioning and pan-India presence. The main risks to our investment thesis and target price are: 1) Bird-flu hitting India, which would be bad for sentiment; 2) Any delay in the rollout of 'Ginger' hotels and planned room increases; 3) Overpaying for hotel acquisitions in international markets given management's push to expand its brand franchise in global markets; and 4) Any slowdown in economic activity, which could lead to lower hotel room demand.

Appendix A-1

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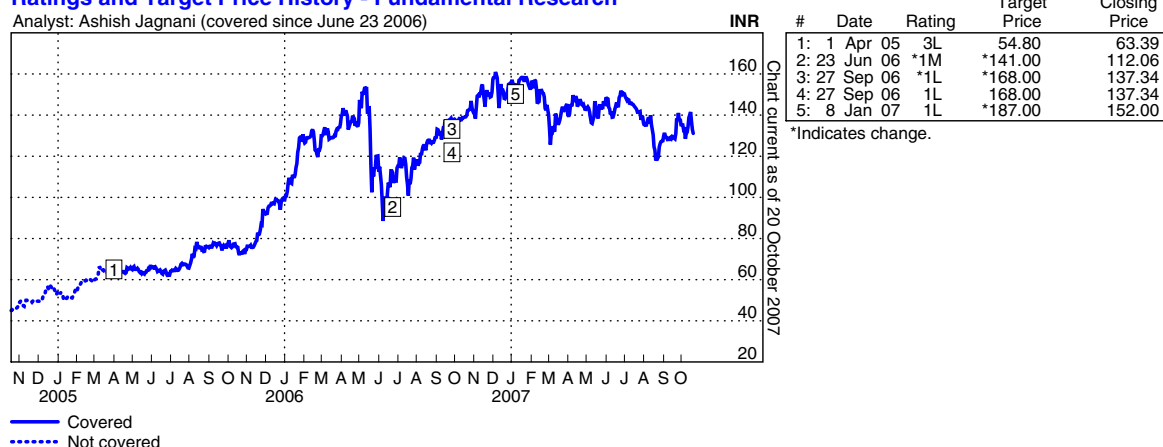
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Indian Hotels (IHTL.BO)

Ratings and Target Price History - Fundamental Research

Analyst: Ashish Jagnani (covered since June 23 2006)



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Indian Hotels (IHTL.BO)

28 October 2007

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