

## Company Flash

1 February 2008 | 6 pages

# Hotel Leela Venture (HTLE.BO)

 Results 

## Buy: Strong Operational Performance

- Good results** — Hotel Leela reported 3QFY08 revenues of Rs1,430m and net profit of Rs550m. Results are not comparable on a YoY basis because of merger of Kovalam Hotels, a subsidiary, during the quarter. Net profit for the quarter was augmented by high other income which includes gains of Rs69m on forex debt.
- Healthy EBITDA margin** — The company recorded a healthy EBITDA margin of 51.7% for the quarter on the back of 8% YoY ARR growth, led by 27% growth in Mumbai ARR while Bangalore ARR declined 12%, and high occupancy of 76% which was boosted by higher business and tourist traffic.
- Capex in progress** — Properties on the anvil include hotels at Gurgaon (management contract), Udaipur, Chennai, Delhi, Hyderabad and Pune to be operational over next 2-3 years. However, factoring in some execution delays, we believe most of the growth from these properties will kick in after FY10E.
- Key limitations** — 1) High dependence on the Bangalore (46% of FY07 revenues) where growth is peaking - any pushback in supply should augur well for the company's earnings; 2) Limited room inventory of ~1,086 rooms; 3) Lack of presence in growth markets for the next two years.
- Maintain Buy (1M)** — We find valuations attractive with the stock trading 13.4x FY09 P/E compared to sector valuations of 16.9x.

<b>Buy/Medium Risk</b>	<b>1M</b>
Price (01 Feb 08)	Rs48.70
Target price	Rs62.00
Expected share price return	27.3%
Expected dividend yield	0.8%
<b>Expected total return</b>	<b>28.1%</b>
Market Cap	Rs18,400M
	US\$468M

### Price Performance (RIC: HTLE.BO, BB: LELA IN)



### Statistical Abstract

Year to	Net Profit	Diluted EPS	EPS growth	P/E	P/B	ROE	Yield
31 Mar	(RsM)	(Rs)	(%)	(x)	(x)	(%)	(%)
2006A	724	1.96	72.9	24.8	2.3	9.8	0.8
2007A	837	1.99	1.4	24.5	1.7	8.4	0.9
2008E	1,378	3.28	64.7	14.8	1.5	10.8	0.8
2009E	1,531	3.64	11.1	13.4	1.4	10.9	0.8
2010E	1,584	3.77	3.5	12.9	1.3	10.3	0.8

Source: Powered by dataCentral

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

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<sup>1</sup>Citigroup Global Markets India Private Limited

**Figure 1. Hotel Leela 3Q and 9-months Earnings Summary**

Rs in Millions	3QFY07	3QFY08	YoY	9mFY07	9mFY08	YoY
Net Sales	990	1,430	44%	2,565	3,599	40%
EBITDA	504	739	47%	1,274	1,733	36%
EDITDA Mgn (%)	50.9%	51.7%		49.7%	48.1%	
Interest	67	83	24%	229	267	17%
Other Income	25	84	236%	136	268	98%
Depreciation	84	100	20%	249	295	19%
PBT	378	640	69%	933	1,439	54%
PAT	357	550	54%	799	1,206	51%

Source: Company Reports, Citi Investment Research

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## Hotel Leela Venture

### Company description

Hotel Leela Venture is a well-known hotel chain in India catering primarily to the premium segment. The company operates four hotels (estimated 1,000 rooms) under the 'The Leela' brand across India. The company has a marketing alliance with Kempinski for properties in India. Its luxury properties cater to both business and leisure travelers. With rapid growth in room demand, the company plans to expand its presence in the growth cities of Hyderabad, Chennai, Pune and New Delhi through management contracts. It is the flagship company of Leela Group, which holds a 49% stake in Hotel Leela Venture.

### Investment strategy

We rate Leela Buy/Medium Risk (1M), with a target price of Rs62 based on 18x Sept 08 P/E. Our positive view on the stock is premised on: 1) Leela's solid 65% earnings growth, vs. 38% for the sector, in FY08E, leveraging on additional rooms operational in Mumbai and Bangalore (ahead of expected supply in mid-2008); and 2) the stock's laggard performance (it has underperformed the Sensex by 22% over the last three months).

Leela's high dependence on the Bangalore market (where ARR growth is peaking) and lack of a presence in key growth markets - are growth limitations. However, with Mumbai refurbishments (133 rooms) complete and Bangalore room expansion (101 rooms) starting in 4QFY07, we see additional rooms and sustained high ARR's driving Leela's outperformance with earnings growth of 65% vs. sector growth of 38% in FY08E. With growth momentum strong due to room additions and the stock currently trading at 15x Sept 08E P/E, at a 6%, discount to sector P/E of 16x and at the lower end of the stock's two-year historical P/E band of 16-25x, we see upside potential from here.

### Valuation

Our target price of Rs62 is based on 18x Sept 08E P/E. Our target multiple places the stock at a premium to sector valuations of 16x. We assign this premium due to Leela's earnings outperformance vs. the sector.

We use P/E as our primary valuation tool, as we think this captures the company's rapid earnings growth potential. While risk of high dependence on Bangalore and lack of scale remain, with the stock's 23% underperformance over past three months and valuations currently at 15x Sept 08E P/E (at a discount to the sector and at the lower end of the stock's two-year historical P/E band of 16-25x), we see upside potential from here.

## **Risks**

We rate Leela Medium Risk based on our quantitative risk-rating system, which tracks 260-day stock volatility. Company-specific downside risks include: 1) Any further plans to raise equity for funding some of the company's capex requirements could be detrimental to our target price; 2) Significant supply of rooms in Bangalore ahead of expectations would likely adversely impact our ARR growth and occupancy assumptions; and 3) Any delay in execution of its new hotels in Chennai, Pune, and Hyderabad, which would push back growth assumptions and dampen sentiment on the stock.

# Appendix A-1

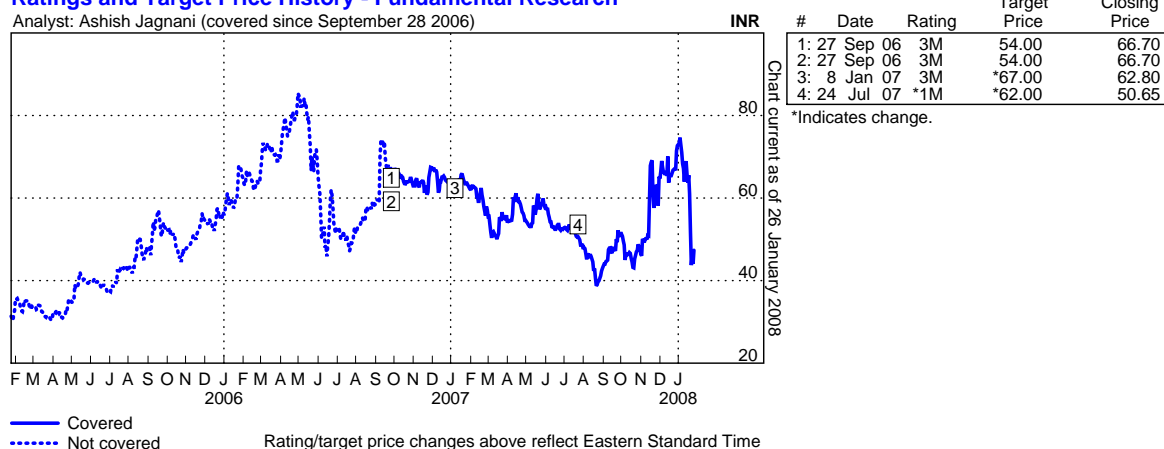
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Analyst: Ashish Jagnani (covered since September 28 2006)



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