



SMC Ranking

★ ★ ☆ ☆ ☆ (1.5/5)

### Issue Highlights

Industry	Hotels
Offer for sale (Shares)	195,797,000
<b>Net Offer to the Public</b>	<b>195,797,000</b>
Issue Size (Rs. Cr.)	1057-1097
Price Band (Rs.)	54-56
Offer Date	26-Mar-18
Close Date	28-Mar-18
Face Value	10
Lot Size	265 shares

### Issue Composition

	In shares
Total Issue for Sale	195,797,000
QIB	97,898,500
NIB	29,369,550
Retail	68,528,950

### About the Company

Incorporated in 1992, Lemon Tree Hotels Limited operates in the mid-priced hotel sector, consisting of the upper-midscale, midscale and economy hotel segments. The company caters to the Indian middle class guests and deliver differentiated yet superior service offerings, with a value-for-money proposition. As on July 31, 2017, the company operated 4,289 rooms in 40 hotels (including managed hotels) across 24 cities in India. Hotels of the company are located across India, in metro regions Operations of the company range from acquiring land to owning, leasing, developing, managing and marketing hotels. The company undertakes business through, direct ownership of hotel properties, long-term lease or license arrangements for the land on which they construct their own hotels, long-term leases for existing hotels which are owned by third parties and operating and management agreements. As of July 31, 2017, the company has a portfolio of 19 owned hotels, three owned hotels located on leased or licensed land, five leased hotels and 13 managed hotels.

### Strength

**Leading mid-priced hotel chain with a differentiated business model:** Lemon Tree Hotels, operating through 45 properties, is the largest mid-market hotel brand in India. The brand is spread across 28 cities and has a room inventory of about 4700 rooms. The company's other brands include Red Fox (budget) and Lemon Tree Premier (upper mid-scale) along with Lemon Tree (mid-scale). The company has strong operational performance, wherein the company focuses on managing development cost per room, maximizing revenue through higher occupancies and controlling operating expenses through employee engagement and productivity. The average development cost per room (excluding the cost of land), for owned hotels (including owned hotels located on leased or licensed land), developed between the fiscal years 2011 and 2015 was Rs. 59 lakh, Rs. 50 lakh and Rs. 45 lakh in the uppermidscale, midscale and economy hotel segments, respectively.

**Strategically positioned in key geographical areas:** The hotels are located in the metro regions including the NCR, Bengaluru, Hyderabad and Chennai, as well as in tier I and tier II cities such as Pune, Ahmedabad, Chandigarh, Jaipur, Indore and Aurangabad. In the leisure hotel segment, the company operates a resort and a hotel in Goa, one resort in the backwaters of Alleppey, Kerala and one wildlife resort in Bandhavgarh, Madhya Pradesh. The company has strategically developed its hotels at locations with high barriers-to-entry within or close to major business centres, airports and other convenient locations. Further, the company has focused on certain key micro-markets in order to address demand and optimize pricing. The company's geographical spread across India and presence in key micro-markets enables it to cater more effectively to its corporate clients and business travellers. As of July 31, 2017, the company also has a development pipeline of 2,783 rooms.

**Present across the value chain:** The Company has acquired expertise and understanding in site selection, design, development, management and marketing of hotels in the mid-priced hotel sector across India, in ways such as, development and ownership, one of its strengths has been the ability to identify strategically located land at reasonable rates. Its experienced project management team endeavours to develop hotels, within budgeted costs and timelines while adhering to quality standards, and hotel operations, the hotel operations team seeks to ensure standardized pre-opening and seamless day-to-day operations, at high levels of service and cost efficiencies.

### Shareholding Pattern (%)

Particulars	Pre-issue	Post-issue
Promoters & promoters group	31.11%	31.11%
QIB	67.11%	56.44%
NIB	1.78%	3.73%
Employee trust	0.01%	0.01%
Retail	0.00%	8.71%
<b>Total</b>	<b>100.00%</b>	<b>100.00%</b>

\*calculated on the upper price band

### Objects of the Issue

- Achieve the benefits of listing the Equity Shares on the Stock Exchanges
- Sale of up to 195,797,000 Equity Shares by the Selling Shareholders.

### Book Running Lead Manager

- Kotak Mahindra Capital Company limited
- CLSA india Private Limited
- J.P.Morgan india private Limited
- Yes Securities (India) Limited

Name of the registrar Karvy Computershare Pvt. Ltd.

**Focus on brand excellence, providing a value-for money proposition and strengthening employee culture:** The Company's well-differentiated brands target distinct segments in the mid-priced hotel sector, which enables the company to avoid brand overlap or dilution. The company's brands are recognised for quality and consistency across various price points in the mid-priced hotel sector. The company's three brands have a standardized design, appearance, decor, colour and lighting scheme. The company's hotels are preferred for their convenient locations, value-for-money offerings and its efficient service, the combination of which leads to a differentiated guest experience. As a result of higher occupancy rates than corresponding industry averages, according to the Horwath Report, its RevPAR for owned and leased hotels was Rs. 3001, Rs. 2433 and Rs. 1711 in the upper-midscale, midscale and economy hotel segments respectively, for the fiscal year 2016, compared to the average of all chain affiliated hotels of Rs. 2646, Rs. 1865 and Rs. 1264, in the upper-midscale, midscale and economy hotel segments respectively, for the fiscal year 2016, according to the Horwath Report.

### Strategies

**Strategic allocation of capital:** The approach has allowed the company to allocate capital at opportune times to acquire land and build hotels as per schedule. Once hotels are operational, the company aims to take advantage of growing demand to maximize revenue and returns, as well as to reduce existing debt. Further, as part of their strategy, the company has also divested equity interest in certain operational hotels they own, through their subsidiaries, Fleur Hotels Private Limited, Begonia Hotels Private Limited and Nightingale Hotels Private Limited.

**Grow national footprint and diversify geographically:** The company seeks to diversify its geographical footprint to reduce exposure to local, seasonal and cyclical fluctuations as well as in order to access a more diversified guest base across geographies. As of July 31, 2017, the company has a development pipeline of 2783 rooms across 24 new and two existing hotels. These hotels are spread over 18 additional cities across India .

**Expansion through development, acquisitions, leases and management agreements:** The Company intends to expand its portfolio through development of hotels, acquisition of properties and entering into leases and management agreements that complement its brand attributes, increase its existing guest base and enhance guest loyalty by providing a wider selection of locations, properties and services. The company also intends to lease hotels through long term lease arrangements, based on market dynamics and the feasibility of leasing a hotel. The company plans to increase the number of its leased hotels from five hotels and 397 rooms, to seven hotels and 572 rooms, based on its hotels under development, as of July 31, 2017.

**Improve operating efficiencies to increase returns:** The company intends to improve its operating efficiencies by improving staff productivity and efficiency to reduce payroll costs per room through the use of new technology, streamlining management systems, comprehensive training and performance-linked compensation; implementing energy saving initiatives that are both cost-efficient and environmentally friendly; improving margins in revenue generating departments such as telecommunications, restaurants, laundry, spa operations and transportation; and reducing average per room costs for head office operations, sales and marketing, loyalty program expenses, among others, through the expansion of its network, hotels and rooms.

**Attract consumers through expansion into leisure hotels and through online channels:** The company seeks to increasingly cater to the vacation and leisure travel needs of Indian families and groups in order to address seasonality of demand for its rooms. Further, the company intends to continue to pursue its strategy to grow direct bookings of hotels through its website. The ongoing investments in online advertising and marketing initiatives have allowed the company to target its marketing messages to specific audiences in a cost-effective manner. The company has also introduced a specialist team to work with leading online travel agents.

## Risk Factors

**Dependent on existing brands and quality of services:** Any dilution of brand reputation or failure of quality control systems could adversely affect the business, results of operations and financial condition

**Certain hotels are located on leased or licensed land:** If the company is unable to comply with the terms of the leases or license agreements, renew its agreements or enter into new agreements on favourable terms, or at all, the business, results of operations and financial condition of the company may be adversely affected.

**Significant portion of revenues are derived from a few hotels and from hotels concentrated in a few geographical regions:** Any decrease in revenues from these hotels, including due to increased competition or supply, or reduction in demand, in the markets in which these hotels operate, may have an adverse effect on the business, results of operations and financial condition of the company.

**Inability to meet financial obligations and other covenants under its debt financing arrangements:** Financing agreements of the company contain certain restrictive covenants that limit its ability to undertake certain types of actions, which could adversely affect the business and financial condition of the company.

## Peer comparison

Co_Name	Operating Income	PAT	EPS	P/E	P/BV	BV	FV	Price	Mcap
EIH	1287.54	108.14	2.57	63.89	3.61	45.38	2.00	163.90	9367.70
Indian Hotels	4009.48	22.07	0.19	0.00	3.82	33.77	1.00	128.90	15329.54
Lemon tree	411.93	-7.17	-ve	-ve	3.56	15.73	10.00	56.00	4403.91

\* Financials are annualised

\*\*Peer companies financials are based on TTM

## Valuation

Considering the P/Bv valuation at upper price band of Rs.56 , book value and P/B of FY2017 are Rs. 15.73 and 3.56multiple respectively and at a lower price band of Rs. 54, P/B multiple is 3.43. No change in pre and post issue Book Value as the company is not making fresh issue of capital.

## Industry Overview

India is the seventh largest economy in the world with nominal GDP of USD 2.26 trillion and third in terms of purchasing power parity as per 2016 estimates. (Source: World Development Indicators Database, World Bank, 17 April 2017). The Indian economy grew by 7.1% in the fiscal year 2017 (estimates) as against 7.6% growth for the fiscal year 2016 (Source: Central Statistics Office, Govt. of India). India has moved from having more luxury and upper scale rooms, at the start of the century, to a more balanced supply scenario, with 19.8 % of the supply estimated to be available in each of the upscale and upper midscale segments, 22.5% of the supply estimated to be available in the midscale and economy segments and 38% of the supply estimated to be available in the luxury and upper upscale levels. The mid-priced hotel sector has traditionally been underserved in terms of chain-affiliated products carrying consistent standards and marketing reach. This sector had been typically served by independent hotels with fragmented and mainly localized ownerships, inconsistent physical products, upkeep and services. The trend of increasing supply in the mid-priced hotel sectors is expected to continue, as can be seen from the supply scenario expected for the fiscal year 2021.

## Outlook

The company's chain of hotels is quite huge and it has pan-India presence, however, the company has been incurring losses in the last few years. Also the business of the company is capital intensive and cyclical. As this issue consists of Offer For Sale , the company will not be getting funds to repay the debt.

An Indicative timetable in respect of the Issue is set out below:

EVENT	INDICATIVE DATE (On or about)
Bid/Offer Opens Date	March 26, 2018
Bid/Offer Closing Date	March 28, 2018
Finalisation of Basis of Allotment with the Designated Stock Exchange	April 04, 2018
Initiation of refunds (if any, for Anchor Investors)/unblocking of funds from ASBA Account	April 05, 2018
Credit of Equity Shares to depository accounts of Allottees	April 06, 2018
Commencement of trading of the Equity Shares on the Stock Exchanges	April 09, 2018

## Annexure

### Consolidated Financials

#### Profit & Loss

Rs. in Cr.

Particulars	Period ended 31-Mar-17 (12 Months)	Period ended 31-Mar-16 (12 Months)
Total Operating Income	411.93	367.95
Total expenditure	295.57	266.79
<b>Operating Profit</b>	<b>116.36</b>	<b>101.17</b>
OPM%	2.82	2.75
Other Income	6.20	2.12
<b>PBDIT</b>	<b>122.57</b>	<b>103.29</b>
Depreciation	51.01	52.26
<b>PBIT</b>	<b>71.55</b>	<b>51.03</b>
Interest	74.03	68.30
<b>PBT</b>	<b>-2.48</b>	<b>-17.28</b>
Tax	4.70	12.52
<b>PAT</b>	<b>-7.17</b>	<b>-29.80</b>

Balance sheet is on next page

## Balance Sheet

Rs. in Cr.

Particulars	As on 31-Mar-17	As on 30-Sep-16
<b>Non-current liabilities</b>		
Financial liabilities borrowings	690.70	523.73
Financial liabilities other non current	0.49	1.45
Long term provisions	1.36	1.19
Deferred tax net	6.75	6.90
Other Long Term Liabilities	20.83	14.34
<b>Total Non- Current liabilities</b>	<b>720.12</b>	<b>547.60</b>
<b>Current liabilities</b>		
Short-term borrowings	67.46	69.49
Trade Payables	60.43	51.13
Other current liabilities	105.84	85.32
Other	18.69	13.00
Short term provisions	2.27	1.73
<b>Total currentli abilities</b>	<b>254.68</b>	<b>220.68</b>
<b>Total liabilities</b>	<b>974.80</b>	<b>768.28</b>
<b>Assets</b>		
<b>Non-current assets</b>		
Property, plant	1407.232	1227.551
Capital work in progre	349.406	259.247
Investment property	2.50	2.55
Goodwill on consolidation	6.734	0
Intangible assets	1.876	1.332
Intangible assets under development	1.404	0
Financial assets investment	0.002	0.011
Financial assets loans	10.856	7.616
Other non current financial assets	39.702	34.919
Non current tax assets	20.998	19.397
Other non-current assets	290.616	382.626
<b>Total of non-current assets</b>	<b>2131.33</b>	<b>1935.24</b>
<b>Current Assets</b>		
Inventories	4.94	5.39
Trade receivables	31.45	24.48
Cash and bank balances	17.59	13.81
Investments	6.34	5.77
Loans	0.47	0.64
Other current financial assets	0.32	0.58
Other current assets	19.308	20.01
<b>Total current Assets</b>	<b>80.41</b>	<b>70.67</b>
<b>Total Assets</b>	<b>2211.73</b>	<b>2005.91</b>
<b>NET Worth</b>	<b>1236.93</b>	<b>1237.63</b>
Net worth represented by:		
Share capital	781.21	778.041
Other equity	27.36	31.858
Reserves and surplus	428.36	427.73
<b>Net Worth</b>	<b>1236.93</b>	<b>1237.63</b>

## RANKING METHODOLOGY

WEAK	★
NEUTRAL	★★
FAIR	★★★
GOOD	★★★★
EXCELLENT	★★★★★

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