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CHALET HOTELS LIMITED

IPO Note

(CAUTIOUS)

Analyst:

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IPO details

Key Data	
Issue Opens	29-Jan-19
Issue Closes	31-Jan-19
Equity Shares Offered (in mn.)	58.61
QIB	Up to 50%
NIB	Min 15%
Retail	Min 35%
Face Value (Rs.)	5
Price Band (Rs.)	275-280
Max. Issue Size (Rs. mn)	16,412
Lot Size (Eq. Shares)	53 and multiple thereof

	Pre Issue		Post Issue^	
	# mn Shares	% Holding	# mn Shares	% Holding
Promoters	171.1	100.0%	146.4	71.4%
Public	0.0	0.0%	0.0	0.0%
Offer For Sale			33.9	16.5%
New Issue			24.7	12.0%
Total	**171.1**	**100.00%**	**205.0**	**100.0%**

Object of the issue

- Repayment/prepayment of certain indebtedness - **INR720 crores**
- General corporate
- purposes Issue expenses

Valuation	@ Rs.275 per share	@ Rs.280 per share
Market Cap (₹ mn)	56,382	57,407
Net Debt (` mn)	23,469	23,469
Enterprise Value (` mn)	79,851	80,876
EV/ Sales	8.9	9.0
EV/ EBIDTA	22.7	25.6
P/B	11.4	11.6
P/E	165.6	168.6

Recommendation

On valuation front, at upper issue price FY18 earnings priced at EV/EBITDA of 25.6x which is fairly priced below its peers and it is best placed hotel company in premium segment on basis of improving occupancy, strategic locations and its strategic partnership with Marriot hotels will also benefit it but with debt equity at 5.5x times which is very high as compare to its peers which are having very low D/E it may be the main concern. By issuing IPO it is looking to use the proceeds to pay of its Debt which may bring its D/E ratio to 1.5x thus reducing pressure on the margins front. We recommend to remain **CAUTION** over the issue for the time being.

Source: Red Herring Prospectus, Dealmoney Research

Globally recognized hospitality brand in luxury-upper scale

- Chalet hotel (Chalet) is an owner, developer and asset manager of high-end hotels in key metro cities in India. The hotel platform comprises five operating hotels, including a hotel with a co-located serviced residence, located in the Mumbai Metropolitan Region, Hyderabad and Bengaluru, representing 2,328 keys, as of September 30, 2018.
- According to the Horwath Report, Chalet hotels are branded with globally recognized hospitality brands and are in the luxury-upper upscale and upscale hotel segments and have developed hotels at strategic locations generally with high barriers-to-entry and in high density business districts of their respective metro cities with greater number of rooms, as well as provide a wide range of amenities, such as, fine dining and specialty restaurants, large banquet and outdoor spaces.
- The company platform emphasizes strategic locations, efficient design and development, appropriate positioning in hotel segments together with branding and operational tie-ups with leading hospitality companies. Chalet has developed commercial and retail spaces, in close proximity to certain of its hotels.
- Chalets hotels are currently branded with global brands such as JW Marriott, Westin, Marriott, Marriott Executive Apartments, Renaissance and Four Points by Sheraton which are held by Marriott Hotels India Private Limited and its affiliates (collectively "Marriott").
- It carries out detailed financial and operational analysis, whether hotel operations should be undertaken directly by them or by engaging third party hotel operators. Currently, the hotel at Vashi, Navi Mumbai, is operated by the company under a license agreement with Marriott, and four of its hotels, including its servicedresidence, are operated pursuant to hotel operation and related agreements with Marriott. It follows an active asset management model for its hotels operated by third parties, pursuant to which it closely monitor, and exercise regular oversight over the performance of its hotel properties.
- It also discusses and agrees on budgeting and operational and financial targets, review performance reports, engage with the hotel management team at each hotel by conducting detailed monthly performance review meetings and provide regular inputs on cost saving initiatives and potential improvements which has allowed our hotels to achieve competitive financial and operational parameters. For example most of its hotels have higher ADR (Average Daily Rate), occupancies and RevPAR compared to the average of other hotels in their respective micro-markets and hotel segments, for the financial year 2018, according to the Horwath Report.
- The total income was ₹ 4,970.43 million for the six months ended September 30, 2018 and ₹ 9,295.14 million for the financial year 2018, and total income grew at a CAGR of 15.81% between the financial years 2014 and 2018. The total comprehensive expense was ₹ 440.45 million and the Adjusted EBITDA before Exceptional Items was ₹ 1,339.58 million, for the six months ended September 30, 2018. The total comprehensive income was ₹ 326.26 million and the Adjusted EBITDA before Exceptional Items was ₹ 3,501.48 million, for the financial year 2018. Adjusted EBITDA before Exceptional Items grew at a CAGR of 22.80%, between the financial years 2014 and 2018. Adjusted EBITDA before Exceptional Items, is a supplemental measure for performance and liquidity.

Source: Red Herring Prospectus, Dealmoney research

Strengths

- ***High-End Branded Hotels Strategically Located in Key Metro Cities of India:*** Chalet hotel is an owner, developer and asset manager of high-end hotels in key metro cities in India. Its platform comprises of five operating hotels, including a hotel with a co-located serviced residence, located in the Mumbai Metropolitan Region, Hyderabad and Bengaluru, representing 2,328 keys, as of September 30, 2018. The hotel are branded with globally recognized hospitality brands and are in the luxury-upper upscale and upscale hotel segments, according to the Horwath Report. Its hotel platform emphasizes strategic locations, efficient design and development, appropriate positioning in hotel segments together with branding and operational tie-ups with leading hospitality companies.
- ***Active Asset Management Model:*** The company follows an active asset management model for four hotels including a hotel with a co-located serviced residence, which are operated by Marriott pursuant to hotel operation and related agreements. These agreements give us access to Marriott's management expertise, industry best practices, online reservation systems, marketing strategies, systems and processes, human resources and operational know-how. As part of active asset management model it regularly engage with the hotel management team at each hotel in order to discuss and agree on budgeting, cost management initiatives and operational and financial targets for each of our hotel properties, review performance reports generated by each hotel, conduct periodic meetings with hotel operator's management teams, discuss and optimize pricing strategies to maximize room yield, review furniture, fixtures and equipment deployment plans and assist with execution of these plans, review competitor set performance and penetration across relevant micro-markets and assist in renewing licenses and consents.
- ***Well Positioned to Benefit from Industry Trends:*** According to the Horwath Report, growth in per capita income, changing demographic dynamics, rising urbanization, growth in travel and higher discretionary spending trends, are expected to assist the growth of the hospitality industry in India. Given the hotel's presence in key metro cities which are expected to benefit from the growth in these parameters, it is well placed to benefit from the potential growth opportunity.
- ***Experienced Management Team:*** The strong management team with significant industry experience. The promoters, Mr. Ravi Raheja and Mr. Neel Raheja, have been instrumental in the growth of its hospitality and retail business and actively advise on finance, corporate strategy and planning. Further, Managing Director and CEO, Mr. Sanjay Sethi has three decades of experience in the hospitality industry, including with leading Indian hotel chains, and across hotel segments.
- ***Backed by Leading Indian Real Estate Developer***: It is a part of K. Raheja Corp group which is a leading business group in India and it believes to have derive significant benefit from the confidence that consumers, lenders, commercial partners, vendors and others place in the group. The K. Raheja Companies have extensive experience in developing large scale real estate and commercial projects resulting in a strong understanding of industry and market trends, which it helps to identify suitable locations and opportunities.

Source: Prospectus, Dealmoney researchRed Herring

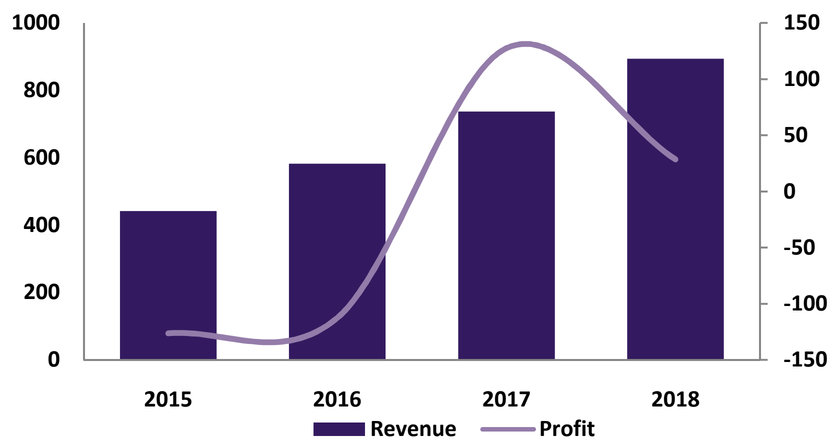
Future road ahead

- ***Focus on Maximizing Performance in Existing Portfolio through Active Asset Management*:** A critical part of the growth strategy is to continue focus on maximizing the cost efficiency of portfolio by following a disciplined approach to asset management, and a collaborative working arrangement with hotel operators to drive strategic and tactical initiatives, to drive profitability.
- ***Disciplined Development of Assets in the Current Pipeline*:** It is in the process of developing three additional hotel projects which are expected to have 588 keys and two projects representing commercial office space with built-up area (excluding car parking/utilities) of approximately 1.12 million square feet. It has traditionally acquired large parcels of land at competitive prices with the intention to develop hotel-led mixed-use projects. It seek to leverage unutilized FSI at some of its hotel locations which allows them to develop additional commercial or retail spaces.
- ***Expand Portfolio by way of Opportunistic and Accretive Acquisitions:*** The hospitality industry in India has recently experienced some consolidation according to the Horwath Report, and it will continue to explore opportunities for acquiring operating hotel assets. The hotel industry has seen considerable debt-related stressed assets, including projects that are left incomplete or completion prolonged due to lack of funding which creates acquisition opportunities, according to the Horwath Report.
- ***Maintain a Sustainable Capital Structure and Ensure Prudent Capital Allocation:*** The company aim to expand its portfolio of hotel properties organically or inorganically, based on industry developments and supply and demand movements across the hotel sector and in and specific locations and micro markets. The strategy is to invest in buying completed projects in demand dense markets when acquisition costs are low and obtain financing at suitable rates. It leverage the Company's and K. Raheja Companies' development strength to construct and develop the hotels and thereafter actively manage properties along with a suitable hospitality brand partner. The approach has allowed them to allocate capital at opportune times to acquire land and build hotels efficiently. Once the hotels are operational, it aim to take advantage of growing demand to maximize revenue and returns by partnering with well-renowned hotel operators, as well as to reduce existing debt.
- ***Opportunity for reflagging hotels or renegotiating hotel operation contracts:*** The hotel operation contracts for operational hotels, including the serviced residence, at Powai, Mumbai and Hyderabad will be due for renewal in March 2020 and December 2021, respectively. Further, the license agreement for its hotel at Vashi, Navi Mumbai will be due for renewal in December 2021. This provides the company with an opportunity to rebrand hotel assets or reposition its properties by using alternate brands at these hotels to better cater to expected demand in the respective micro markets where the hotels are located.

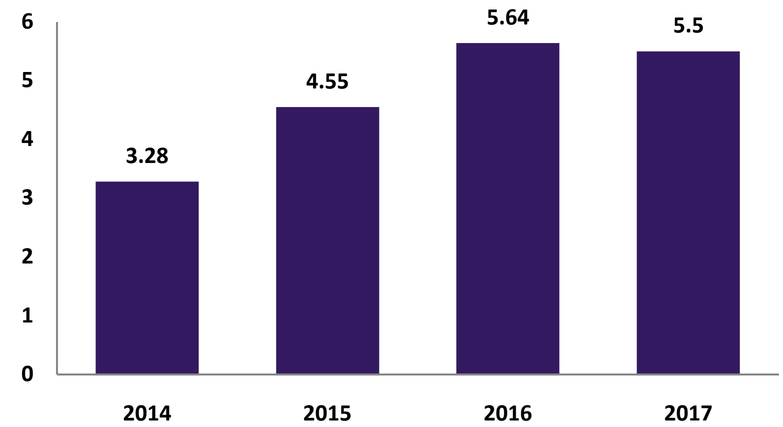
Source: Red Herring Prospectus, Dealmoney research

Operating metrics

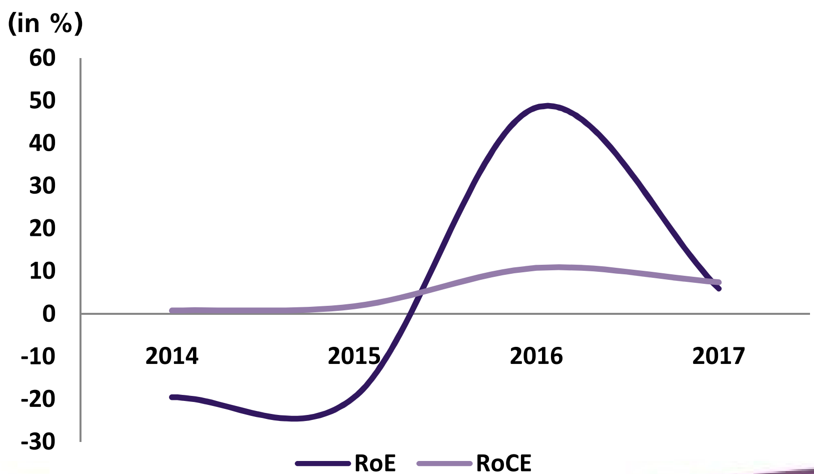
Revenue and PAT (In Crs)



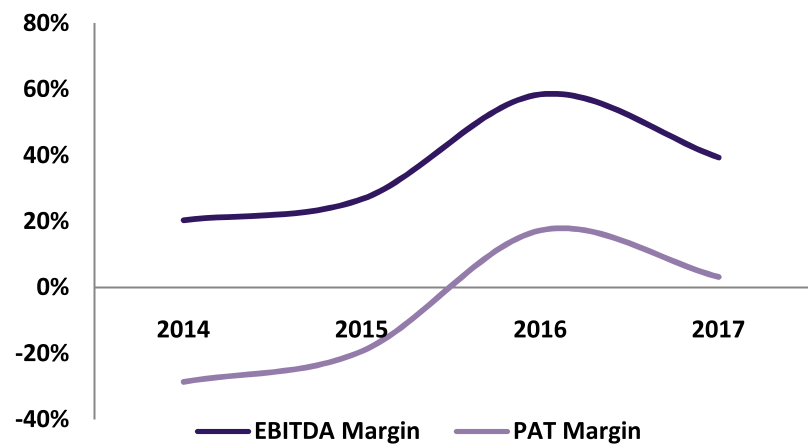
Debt-to-Equity Ratio



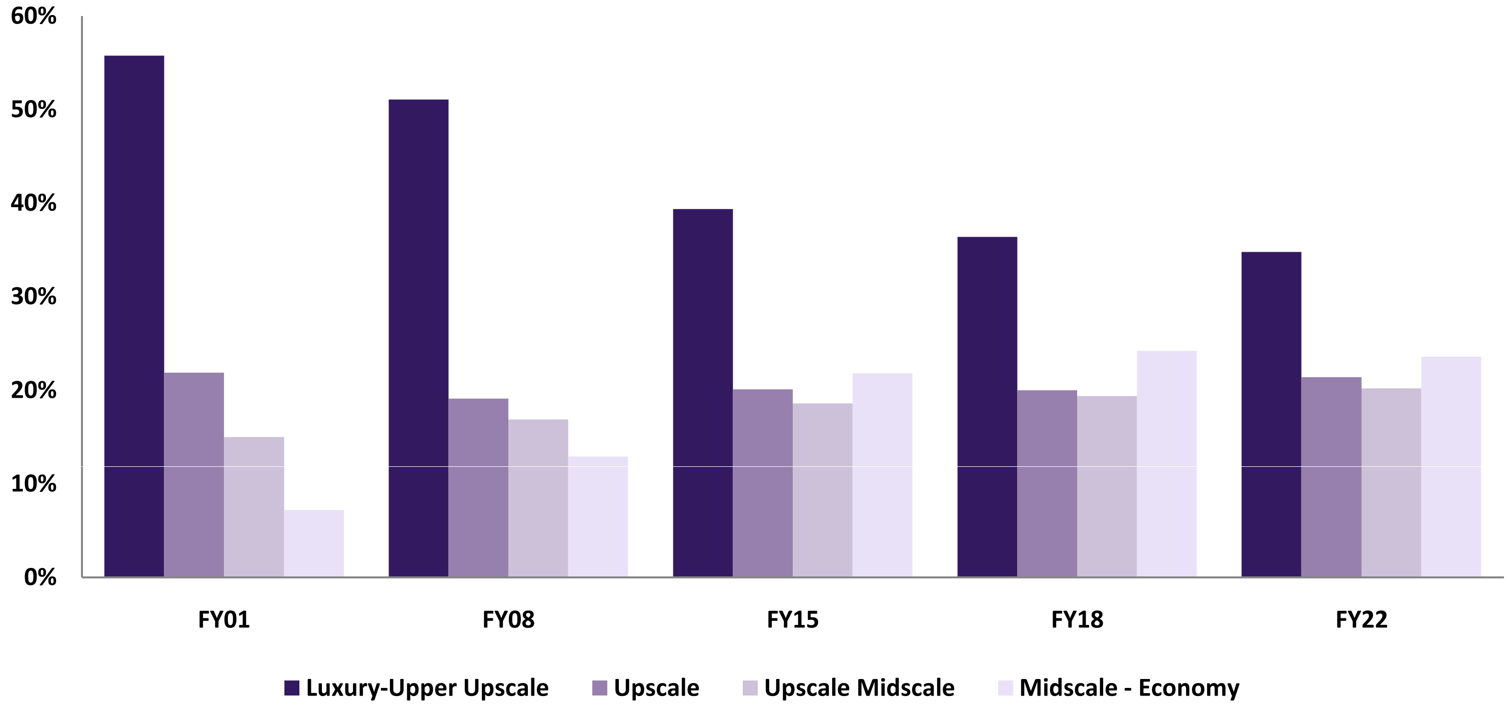
Return Ratio



EBITDA and PAT Margin



Industry Structure



Peer Comparison

Company	Revenue(Cr)	EBITDA	EBITDA Margins	Debt/Equity	EV (Cr)	EV/EBITDA	RONW (%)
Lemon Tree	492	144	29.30%	0.81	6292	43.7	6.2
Chalet Hotel	894	316	35.35%	5.5	5975	25.6	2.1
EIH	1704	405	24%	0.13	10672	26.4	6.6
Indian Hotel	2639	686	25%	0.35	17907	26.1	1.2

Source: Red Herring Prospectus, Dealmoney Research

Consolidated Summary Financials

Income Statement

₹ Cr	FY14	FY15	FY16	FY17	FY18
Total Income	501	441	582	737	894
Operating Expense	402	378	442	494	578
EBIDTA	**99**	**64**	**141**	**244**	**316**
Depreciation	60	62	99	127	112
Other Income	33	26	15	187	36
Finance Costs	137	161	216	218	212
PBT	**(64)**	**(133)**	**(159)**	**86**	**28**
Exceptional items	(77)	(8)	(7)	(7)	(5)
Profit before tax	**(141)**	**(141)**	**(166)**	**79**	**22**
Provision for Tax	(32)	(14)	(54)	(48)	(6)
Profit for the year	**(109)**	**(126)**	**(112)**	**127**	**28**

Balance Sheet

₹ Cr	FY14	FY15	FY16	FY17	FY18
Liabilities					
Share capital	152	152	152	152	171
Share Warrants & Outstandings	-	-	-	-	-
Reserves and surplus	508	480	365	315	324
Minority Interest	-	-	-	-	-
Long-Term Borrowings	1,421	1,539	1,902	2,051	2,215
Deferred tax liabilities(Net)	62	76	25	(27)	(31)
Other Long Term Liabilities	2	3	5	14	18
Long term provisions	4	5	6	6	4
Long Term Trade Payables	-	-	-	-	-
Trade payables	59	60	65	85	86
Other current liabilities	523	668	454	491	575
Short term borrowings	141	181	258	325	163
Short Term Provisions	119	117	122	115	96
Total Liabilities	**2,991**	**3,280**	**3,355**	**3,525**	**3,621**
Assets					
Net Block	1,116	1,945	1,938	2,196	2,146
Intangible assets	-	-	-	-	-
Capital work in progress	572	49	32	21	22
Non Current Investments	606	740	787	643	678
Long Term Loans & Advances	46	45	37	46	58
Other Non Current Assets	6	6	6	7	12
Inventories	295	322	326	319	312
Sundry Debtors	16	10	18	30	55
Cash and Bank	102	32	35	33	32
Other Current Assets	43	32	38	45	68
Short Term Loans and Advances	190	101	139	184	239
Total Assets	**2,991**	**3,280**	**3,355**	**3,525**	**3,621**

Source: Red Herring Prospectus, Dealmoney research

Key Risks

- A slowdown in economic growth in India could have an adverse effect on the business, results of operations and financial condition.
- It has entered into hotel operation and related agreements with Marriott to receive operation and marketing services in relation to the hotels. If the hotel operators decide to terminate or not renew any agreement then the business, financial condition and results of operations may be adversely affected
- It has utilized the brands of third party licensors, and rely on third parties for the quality of services at the hotels. Any adverse impact on the reputation of our hotels or a failure of quality control systems at the hotels could have adverse effect.
- A significant portion of the revenues are derived from a few hotels and from hotels concentrated in a few geographical regions and any adverse developments affecting such hotels or regions could impact business and weak operations and financial condition.
- The residential project at Koramangala, Bengaluru is the subject matter of litigation with Hindustan Aeronautics Limited. Any adverse order in relation to this litigation may adversely affect ability to complete the project, and business, results of operations and reputation.
- The promoters, Group Companies, subsidiary and certain directors are involved in certain legal proceedings.
- Operational risks are inherent in business as it includes rendering services at high quality standards at hotels. A failure to manage such risks could have a negative impact on business structure.
- The business is subject to seasonal and cyclical variations that could result in fluctuations in the quarterly results of operations.
- The hotel is exposed to risks associated with the development of hotel properties and commercial and retail projects. Delays in the constructions of new buildings or improvements of those properties may have an adverse effect.

Source: Red Herring Prospectus, Dealmoney research

Dealmoney Securities Private Limited

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