Lemon Tree Hotels Limited

Q1 FY20 Earnings Conference Call Transcript
August 7, 2019

Moderator: Good day ladies and gentlemen and a very warm welcome to the Lemon Tree Hotels Earnings Conference Call. As a reminder, all participant lines will be in the listen only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Anoop Poojari from CDR India. Thank you and over to you sir.

Anoop Poojari: Thank you. Good evening everyone and thank you for joining us on Lemon Tree Hotels Q1 FY20 Earnings Conference Call. We have with us today Mr. Patanjali Keswani – Chairman and Managing Director; Mr. Rattan Keswani – Deputy Managing Director, Mr. Kapil Sharma – Chief Financial Officer; Mr. Vikramjit Singh – President and Mr. Prashant Mehrotra – Chief Revenue Officer of the company.

Before we begin, I would like to state that some statements made in today's call maybe forward looking in nature and a detailed statement in this regard is available in the results presentation shared with you earlier. I now request Mr. Keswani to make his opening remarks.

Patanjali Keswani: Good evening everybody and thank you for joining this call to discuss our performance for the first quarter ended 30th June 2019.

So, we have delivered a topline growth of 11.8% year-on-year in Q1 FY20 which is driven by a 2.7% year-on-year increase in ADR and the addition of 394 rooms since the year ago period. We continue to maintain our occupancy premium showing a 76-bps year-on-year improvement in Q1 FY20 to 77.5% over 76.8% in Q1 FY19 despite the addition of this new supply of 394 owned and leased rooms.

On a same hotel basis, the occupancy improved by 268 bps to 79.5%. Due to improvement in ADRs and occupancy over the year ago period, our RevPAR grew by 3.7% in Q1 FY20 over Q1 FY19. But on the same hotels basis our RevPAR grew by 6.3% over the same period.

Our EBITDA has grown by 10% year-on-year as per old accounting and by 31.4% as per new AS-116 accounting, the impact of which has been explained in a detailed manner in our earnings presentation. We have posted a profit after tax of Rs 0.9 crore in Q1 FY20 according to old accounting standards as compared to Rs 2.2 crore in Q1 FY19. As per AS-116, our Q1 FY20 PAT stood at a negative 2.2 crore owing to higher interest and depreciation expense. Fees from managed hotels stood at Rs 4.7 crore in Q1 FY20 as compared to Rs 4.2 crore last year.

The hospitality industry in the recent past hasn't panned out as expected due to the challenges faced by the airline industry, election, liquidity crunch owing to the NBFC crisis and the overall consumption slowdown. In such times we have focused on driving more retail business through online and direct sales to push stronger occupancies and derive operating leverage.

We would like to highlight the impact of the new accounting standards AS-116 which came into effect from April 2019. As you were aware, we operate a very large portfolio of leased assets. Leasing expenses under the previous accounting standard were disclosed above the EBITDA line under rent. The new accounting standard mandates recognition of a lease liability in the liability side of the balance sheet and recognition of a corresponding right to use asset on the asset side. This will lead to an increase in the size of the balance sheet. Interest shall be provided in the P&L account on the lease liability and depreciation shall be provided on the right to use assets. Hence absolute EBITDA and EBITDA margins will increase. In our case the net positive impact on EBITDA in Q1 FY20 due to this change is Rs 7.5 crore. Profit before tax on the other hand will decrease due to the new accounting as the total adjustment and interest and depreciation is higher than the adjustment in lease rent. Therefore, the net impact of AS-116 accounting on a PBT has been a negative Rs 4 crore. We have always maintained that the metric we track is cash profits. We would like to highlight that the new accounting standard is merely an accounting adjustment which doesn't impact operating performance in a real sense barring some positive impact on cash flows due to a reduction in tax liability.

Our operational inventory as of 30th June 2019 comprised of 57 hotels with 5,828 rooms of which 3,975 are owned and leased and 1,853 are managed. Our active development pipeline consists of 937 owned and leased rooms and 2,035 rooms under management contract. We have commissioned our 303 room Andheri hotel towards the end of Q1 FY20. This is our first owned hotel in Mumbai, the most demand dense market in the country. We believe this will further increase our brand awareness and result in significant value to our overall business. In the next few months we will open our 142 room Lemon Tree Premier Calcutta property and the 139 room Udaipur property under our new upscale brand Aurika. All these owned properties will operate in demand dense and high barrier-to-entry markets and will help boost our ADRs. We will also open close to 700 rooms under management contracts by the end of this financial year.

To conclude this has been a busy quarter for us as we have successfully created a strong framework for long term growth. Our ability to adapt to market sentiments and cycles has ensured our operational metrics remain steady. Customer centricity and an emphasis on execution remains the core focus of our business and we continue to strive to enhance value for all shareholders. We are favorably placed going ahead in terms of our market positioning, sector tailwinds and brand visibility. Our brand strength has led to a high proportion of repeat guests and gives us a network advantage due to which we are able to stabilize our hotels in new geographies in a relatively short span of time. We will capitalize on the changing industry dynamics with a large inventory of hotels moving towards steady state that were opened in the last few years. Operationalization of high value inventory in the coming quarter and our cost leadership.

On that note I will come to the end of our opening remarks and would now like to ask the moderator to open the line for question and answer.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question and answer session. The first question is from the line of Nihal Jham from Edelweiss. Please go ahead.

Nihal Jham: Sir, we read your commentary on the current environment and you had highlighted that at the end of the last quarter also. But just wanted a sense of how things are being shaping up incrementally, I am guessing the air fares have normalized and do we still believe that we are targeting organic hikes of 9% to 10% that is still achievable?

Patanjali Keswani: You know, I feel that we are navigating this current scenario quite well in spite of 4 issues we are all aware of, which is the global economic and trade headwinds, the slowdown in India, the closure of Jet Airways and the new AS-116 norms. But the broad point I would like to make Nihal is that while the macro can impact the short term our overall story is still very sound and while topline has been somewhat impacted by the current situation, this is only short-term impairment whereas this part of the cycle has got extended. But what is clear to me is that when the cycle recovers and it will, it will appear much stronger and longer than we expect. If you look at how it has affected us as I said, our occupancy for our stable hotels has in fact gone up by 270 bps. It has not significantly impacted us and we have actually managed to increase our ARR at that time with the old hotels.

So, when I look at our performance broadly, here is what I would like to explain to everybody, to me it is a simple 3 bucket situation. In our existing old hotels which is Q1 last year to Q1 this year, our EBITDA increased from Rs 35 crore last year to Rs 36.1 crore this year and if you look at our PBT, PBT was Rs 4.9 crore for old hotels versus Rs 4.3 crore in the previous year which is about 15% increase. The new hotels which are Lemon Tree Premier Pune, Red Fox Chandigarh and Red Fox Dehradun are still under stabilization and in spite of these headwinds they made a revenue of Rs 9.2 crore and an EBITDA of Rs 2.4 crore. However, since what happened was that since the interest and depreciation obviously started instantly, on a PBT basis they were Rs 2.3 crore negative. So, the first bucket is old hotels were Rs 4.9 crore PBT, the second bucket is new hotels were Rs 2.3 crore negative. So, overall the PBT became Rs 2.6 crore and if you remove tax of Rs 1.6 our PAT became Rs 0.9 crore. Interestingly, however, our cash profits increased. In the last quarter it was Rs 15.4, this year it was Rs 15.9 crore. Now what is the point I am making. For a moment I am avoiding AS-116. Pune, Chandigarh and Dehradun opened really during the last few months. In spite of that they have been EBITDA positive and interestingly in July all three crossed break even. So, in this quarter what I see is you are right, I see an improvement in macro. I also see the 3 hotels that took the last 6 to 9 months and were negative in PBT becoming positive in PBT and the opening of Bombay has been very positive for us. We opened it I think on the 27th of June, but in July Bombay has already crossed 100 rooms per day at over Rs. 6,000 ARR and is close to operational breakeven. So, overall, I am very positive about the company going forward. Bombay will have a similar impact as Pune had obviously in Q2. But on an aggregate, I feel that we will be able to navigate very successfully even this current slowdown.

Nihal Jham: Absolutely. Just one last follow-up on this, so our base occupancy at around 76% for all three brands is in place as you say to take the rate hikes, but considering season time, just say 2-3 months, in October, you think we have enough time for things to fall in place for us to take those double digit ARR hikes?

Patanjali Keswani: Well, double digit ARR hike, I never said we would do. What I had always said was that there would be an ARR hike. It is a little difficult for me to predict based on what is currently in the economy. But what I do know is that Pune's ARR is 1.25

times to 1.3 times our overall ARR and Bombay ARR is 1.5 times our overall ARR. So, this will also blend in into raising the ARR. But I cannot give you an offhand number. If I did some blue sky thinking, it would be anywhere from 7% to 9%.

Nihal Jham: That is helpful. Just one last question, in case we say end up getting the permission of adding the 99 rooms in the Mumbai property, how much would our capex increase by?

Patanjali Keswani: It will increase by about Rs 20 crore because fundamentally to answer your question, we have initially designed a 577 room hotel in MIAL with 100,000 sq. ft. of commercial space. However, when we put in this application, we were informed by MMRDA that we would have to pay Rs. 6000 a square foot as additional fees for the one lakh square foot commercial which means Rs 60 crore more. So, we took a decision to redesign this hotel and we have added close to 100 rooms. So, now this hotel will be 669 rooms and the incremental cost because it was already the shell was structured in will be less than Rs 20 lakh a key, so not material.

Moderator: Thank you. The next question is from the line of Deepika Mundra from J P Morgan. Please go ahead.

Deepika Mundra: Just a couple of things on the demand point of view. Given the fact that last quarter was a little volatile for the industry I think, your company still delivered a fairly good number. Just from a segmentation outlook, the incremental pressure you would say is more on the budget hotels or more on the luxury side?

Patanjali Keswani: Well, I find that the incremental pressure is across the board. So, if I look at some segments, if we look at the airline segment, the defense segment, government, automobiles, oil and gas, consumer durables, healthcare, FMCG and consumer discretionary, they accounted of our corporates for 37.2% of our total business in Q1 FY19 and Q1 FY20 it dropped to 23.4%, which means a 14% drop in demand from these segments. Other segments like IT and ITeS consulting, BFSI, logistics, Ecommerce, telecom and retail actually went up, which is why on an aggregate basis our occupancy for the same hotels went up from 76.8% last year to 79.5% this year, close to 80%.

Deepika Mundra: Understood. Lastly, as you mentioned, the part of the cycle that is extended a bit. How far along do you think until we see a more significant recovery?

Patanjali Keswani: It is very difficult for me to project how the cycle will go. But what I would urge you to look at, Deepika, is our performance which in this cycle with actually March-April-May being quite volatile as somebody said we have managed to increase our occupancy by 268 bps and there is no way we see this reducing. Okay, sure, there may be occasional minor headwinds but irrespective of macro I am personally very confident, and I am quite happy with this performance based on what has happened in the last 4 months.

Moderator: Thank you. The next question is from the line of Tushar Sarda from Athena Investments. Please go ahead.

Tushar Sarda: Couple of quarters ago you had announced entry into student housing. So, what is the progress on that?

Patanjali Keswani: So, student housing we have signed term sheets for about 2,500 beds and once we finish the due diligence, we will proceed on it. So, right now, it is in high business development mode. I expect that by the next earnings call I will be able to give definite figures on what has been signed off on.

Tushar Sarda: Okay. So, when do we expect your actual business to start? From which quarter onwards would the revenue start coming in?

Patanjali Keswani: Well, some of these are conversions and some of these are acquisitions, but conversions take time. So, I would reckon definitely by, well, second half of Q3 we should be able to start generating EBITDAs.

Moderator: Thank you. The next question is from the line of Himanshu Shah from HDFC Securities. Please go ahead.

Himanshu Shah: Sir, just want to check with you, when can we expect Key Hotels transactions to be consummated and be a part of the financials?

Patanjali Keswani: Well, we have signed the share purchase agreement. The hard stop date is in the middle of October. So, assuming we go through the transaction then it will be from Q3 onwards.

Himanshu Shah: Okay and are there any approvals or anything required from any statutory bodies for this?

Patanjali Keswani: None that we are aware of.

Himanshu Shah: Fair enough sir. Secondly, I just want to understand, in the last quarter we had 3,570 rooms as of March, and I think in the owned list we have added only Mumbai hotels, 303 rooms. But then, in the addition it shows 405 rooms. So, am I missing out on something here?

Patanjali Keswani: Chandigarh was a managed hotel which has now become a leased hotel.. As of today, we have 3,672 rooms, excluding Bombay which is another 303 rooms. So, at the end of Q1 really the operating rooms Bombay was only for 3 or 4 days, we had 3,672 owned/leased rooms, of these the same hotels which we compared to Q1 in the previous year were 3,278 which is 89% of this total amount. We then opened 394 rooms under our owned/leased portfolio after Q1 FY19. So, this is an additional 11% bringing it totally to 3,672. Now, as I explained to you, and I think I neglected to mention this, the old hotels, same hotels occupancy increased to 79.5%. The new hotels their occupancy in Q1 FY20 was 58.2% which is why we had a negative PBT. However in July all these 3 hotels have crossed 65% occupancy and we expect to do much better with these 3 hotels specifically in Q2.

Himanshu Shah: Fair enough sir. Thirdly, there is a significant gap between the increase in liability due to Ind-AS 116 and right of use-of-asset, so I'm just trying to understand why is there such a large gap of almost Rs 108 crore?

Kapil Sharma: Himanshu, the fact is that this accounting standard has been applied retrospectively. So, what has happened is from the day when the lease started, we have identified the liability on that account for the previous years and the years that have been already lapsed; and the differential is getting adjusted into the retained earnings. So, this is a normal practice which most of the companies have done. So, there were two options, one is to do from 1st April 2019 only taking into account the future rentals and then discounting it to the current period or going ahead with it when the lease is started. So, what we have done is, right from when the lease period started and accordingly the differential is getting adjusted into the retained earnings.

Himanshu Shah: Kapil, some color feasible as a portfolio what would be the lapse period and the remaining period proportion?

Kapil Sharma: Actually, it will differ from lease to lease. So, some leases are we have done in 2008. So, there are several.

Himanshu Shah: And lastly any reason for creation of pledge on shareholding?

Kapil Sharma: Pledge on shareholding is not a new transaction and there is no new borrowing as such but in terms of the loan agreement with the lender, this pledge has been created when the lock in is over on the shares. So, what has happened is, earlier the pledge was on the holding company, because as you enter into an IPO there is a lock in for the entire shareholding for all the existing shareholder for one year on the listed shares. Whatever is in the lock in cannot be pledged. So, that is why the pledge was on the unlisted shares of the holding company. In terms of the agreement this has been now created on the shares which are free from lock-in. Additionally,, the major part of this loan which was taken, was towards the investment into Lemon Tree shares itself.

Moderator: Thank you. The next question is from the line of Sumant Kumar from Motilal Oswal. Please go ahead.

Sumant Kumar: For Lemon Tree, in the Delhi market we have seen occupancy decline by 376 bps. So, might be because of election and others. So, how are things panning out from July onwards?

Patanjali Keswani: So, Delhi specifically which is Delhi Aerocity, Red Fox is doing about 10% higher revenue than last year. It is doing very strongly. As far as Lemon Tree Premier Delhi goes, we have shut down a large part of the hotel to upgrade it. So, normally we renovate 1/6th of the hotel every year. So, while we are renovating the rooms, we have also shut down the banquet halls and the bar and the Republic of Noodles, the Pan Asian restaurant because we have a lot of demand for larger banquet functions. So, we expect to open this on the 1st of September. So, that is the reason there has been a drop in revenue in Lemon Tree Premier Dial by about Rs 1.2 crore in Q1 not due to a drop in rooms. It is due to a drop in F&B because of the shutdown of these facilities which are now going to open.

Sumant Kumar: Okay. So, the occupancy in this, in Q1 FY20 as per the presentation has declined with 370 bps. So, we can expect recovery in the demand?

Patanjali Keswani: That is because about 60 rooms are shut, reflecting on the full inventory whereas actually a bunch of rooms are under what is called renovation.

Sumant Kumar: So, it is really not demand related?

Patanjali Keswani: No it is not. In fact, the room revenue this year in both Lemon Tree Premier Dial and Red Fox Dial is above last year.

Moderator: Thank you. The next question is from the line of Tushar Sarda from Athena Investments. Please go ahead.

Tushar Sarda: This is more of a housekeeping question. On slide #9, you have given owned rooms, leased rooms, managed rooms and total rooms also the average daily rate. So, does this average daily rate refer to only owned/leased rooms or it includes managed rooms?

Patanjali Keswani: Only owned and leased.

Tushar Sarda: Okay and similarly on slide #16, where this operational performance is , this also refers only to owned and leased rooms, right? The average daily rate and the hotel level EBITDA and all?

Patanjali Keswani: Yes. These are all owned and leased.

Tushar Sarda: And one more request, since your future is going to be through the management fees, if some information on the traction in management fee could be given in the presentation, so we can track that separately?

Patanjali Keswani: On page #12, in the revenue section there is a commentary on management fees.

Moderator: Thank you. As there are no further questions, I would now hand the conference over to the management for their closing comments.

Patanjali Keswani: Thank you once again for your interest and support. We will continue to stay engaged. Please be in touch with our investor relations team of CDR India for any further details or discussions. Look forward to interacting with you soon.

Moderator: Thank you very much. Ladies and gentlemen, on behalf of Lemon Tree Hotels that concludes this conference call for today, thank you for joining us and you may now disconnect your lines.