August 11, 2021

Lemon Tree Hotels Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Term Loan	108.78	101.84	[ICRA]A- (Negative); Reaffirmed
Long-term/ Short -term – Fund Based Working Capital	30.00	30.00	[ICRA]A- (Negative) /[ICRA]A2+; Reaffirmed
Long-term/ Short -term – Unallocated	7.22	14.16	[ICRA]A- (Negative) /[ICRA]A2+; Reaffirmed
Total	**146.00**	**146.0**	

**Instrument details are provided in Annexure-1*

Rationale

ICRA has taken a consolidated view on Lemon Tree Hotels Limited (LTHL), its subsidiaries, step-down subsidiaries, and associate companies[1], while assigning the credit ratings (together referred to as LTHL or the company), given the common management team and significant operational and financial linkages between the entities.

The rating reaffirmation favourably factors in the diversified business profile of LTHL, with a large and geographically spread hotel portfolio (84 hotels across 52 cities), well-recognised in-house brands across economy, midscale, and upscale segments, and extensive experience of its promoter and management team in the hospitality industry.

With demand being hit by the Covid-19 pandemic, LTHL reported a ~62% YoY decline in operating revenues in FY2021 to ~Rs. 252 crore. Despite this sharp decline and the high operating leverage of the hospitality business, the company managed to report positive OPBITDA of Rs. 61 crore for FY2021, supported by timely and stringent cost control measures. This prevented any major requirement for loss funding and demonstrates the company's ability to effectively manage costs to match the likelihood of low revenues in the near term. LTHL was able to keep nearly 85% of its operational inventory open during FY2021 and despite the large inventory, it managed a healthy recovery in occupancy levels—from 22% in April 2020 to 64% in February 2021. Even as the operational performance of the portfolio had improved sequentially in FY2021, the second wave of the pandemic, and the resulting lockdowns in Q1 FY2022, derailed the demand momentum. Accordingly, ICRA believes that recovery to pre-Covid levels is unlikely in the next one year. Also, the business segment, where LTHL's inventory is concentrated, is expected to witness a relatively gradual recovery compared to the tourist-based destinations, which is likely to witness an early recovery owing to the diversion of outbound leisure travel. The pandemic situation remains uncertain and remains contingent on the pace of vaccination, efficacy of vaccines, high infection rates and possibility of a third Covid-19 wave. Accordingly, developments in this regard and its impact on LTHL's operational metrics will remain a monitorable.

ICRA also notes that LTHL continues to maintain a comfortable capital structure, with the entity pre-emptively raising Rs. 175 crore from its strategic investor, APG Asset Management NV (APG, 15% shareholder in LTHL), in Fleur Hotels Private Limited (a 58.24% LTHL subsidiary) in June 2020. It can also tap into the second tranche of funding from APG (up to Rs. 125 crore, subject to the consent of LTHL and APG), if required. In addition, the company is tying up with its lenders for GECL[2] loans (eligibility of over Rs. 450 crore, of which Rs. 230 crore is already sanctioned), which would be more than sufficient to meet its financial and operational requirements over the next 4-6 quarters. Further, the company is expected to incur a marginal project capex (Rs. 60-80 crore) in FY2022. However, apart from its two ongoing projects (Mumbai airport and Shimla), LTHL is largely

[1] *Enlisted in Annexure 2*

[2] *Loans granted under the Governments Emergency Credit Line Guarantee Scheme (ECLGS)*

targeting portfolio expansion through an asset-light model that involves entering management contract with property owners. Hence, LTHL's overall liquidity position is expected to be adequate for the next few quarters.

ICRA notes that there has been a deterioration in LTHL's leverage and debt coverage indictors in FY2021. These are expected to deteriorate further in the near to medium term, as despite gradual improvement, the revenues and profitability are likely to remain subdued. Meanwhile, drawdown of GECL loans and likely project debt for the Mumbai Airport project (over the next 1.5-2 years) will keep the company's financial leverage elevated. While debt is yet to be tied up for the said project, ICRA does not anticipate any delays in financing a tie-up, given the favourable location and almost entire project equity having been invested upfront. Further, while project implementation risk has reduced for LTHL in the past few years, it has a significant (37%) toddler inventory (hotels operational for <3 years as on March 31, 2021,) which may take longer to stabilise and start meaningfully contributing to the profits. ICRA, however, continues to draw comfort from the company's financial flexibility emanating from its healthy asset base, access to capital markets and the management's demonstrated track record of refinancing of high-cost debt and raising project debt in a timely manner.

As on June 30, 2021, the promoters held 25.88% equity stake in the company, of which around 20.75% was pledged or encumbered; while there has been a healthy decline in the pledging status from the previous year levels (33.76% as on March 31, 2020), the same would remain a monitorable.

The Negative outlook on the long-term rating continues to reflect the likelihood of the extended impact of the Covid-19 pandemic on the global travel and hospitality industry, which is in line with ICRA's Negative outlook for the sector. While the easing of restrictions led to sequential improvement in occupancies in H2 FY2021, corporate travel and MICE[3] activities are expected to remain subdued in the near term. However, commencement of the vaccination programme (in India and globally) and improving economic outlook are favourable for the industry's recovery trajectory and remain a key monitorable.

Key rating drivers and their description

Credit strengths

Well-recognised brands and geographically diversified product portfolio; likely to support faster recovery from pandemic - LTHL is one of India's largest hotel chains, with 84 operational properties spread across 52 cities, and benefit emanating from a robust distribution system, loyalty programmes and corporate relationships. The company has well-established and recognised midscale (Lemon Tree) and economy segment (Red Fox) brands. With the successful launch of its upscale brand, Aurika, and acquisition of the Keys brands in FY2020, it has further diversified and consolidated its presence across price points. This diversified presence reduces the vulnerability of the Group's revenues to cyclical downturns to some extent. The favourable location of its properties in prominent business and tourist districts supports revenue growth prospects and reduces concentration risk.

Experienced promoters and management team - LTHL is promoted by Mr. Patu Keswani, who has been associated with the hospitality industry for over 30 years. An experienced management team with a track record of delivering consistent performance through well-planned refurbishments and project development, professional and centralised sales and marketing, and disciplined cost control measures, remain a positive. From two properties in 2004, the Group has expanded its portfolio to 84 properties (owned/leased and managed) under seven brands.

Comfortable capital structure backed by regular equity infusion - Healthy equity infusions from private equity players (Warburg Pincus and APG) in the past has helped LTHL maintain a comfortable capital structure (TOL/TNW+ Minority Interest of 1.5x as on March 31, 2021, and ~1.0x till FY2019) despite undertaking significant and consistent capex towards portfolio expansion. After funding the majority of the Keys' hotel portfolio acquisition in FY2020, APG had infused Rs. 175 crore in June 2020 with the commitment to infuse a further Rs. 125 crore, if required, subject to the consent of LTHL and APG. The

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[3] *Meetings, Incentives, Conferences and Exhibitions*

management policy of relying on debt against cash flows of operational properties for funding ongoing projects, deferment of project debt towards later stages and its ability to raise low-cost debt, continues to be a credit positive for LTHL.

Strategy to expand through management contract route to limit capital requirement and minimise development risk - The company has been expanding its footprint through an asset-light model that involves leasing of properties or entering management contract with property owners. These models are expected to provide long-term operational benefits to LTHL, as properties can be quickly put into operation with minimal (or nil) capex and limited project implementation risk.

Credit challenges

Weak revenue visibility over the medium term due to demand disruption caused by the Covid pandemic; cash flows and profitability expected to remain muted in FY2022 - LTHL's performance has been impacted by the Covid-19 pandemic, which resulted in a sharp decline in global and domestic travel, disrupting the demand for the entire hospitality sector. With most of the company's hotels located in business-focused locations and a large majority of corporates continuing with work-from-home policies, the occupancy levels plummeted to 40% for LTHL in FY2021 (from nearly 70% in FY2020) and its revenues declined by ~62%. While the hospitality segment witnessed some sequential recovery in Q3 FY2021 and Q4 FY2021, aided by ramp up in leisure travel and social MICE (including weddings), the recovery was halted post the onset of the second wave of the pandemic. Given the prevailing uncertainties due to the pandemic, ICRA expects significant pressure on industry revPARs over the next few quarters. While wider vaccine rollout could help in restoring confidence to an extent, concerns on the third wave of Covid-19 persist. Further, corporate meetings are anticipated to remain virtual for a large part of FY2022 because of safety and slowdown-related cost saving measures, which will impact business travel demand. Consequently, the company's performance is likely to remain subdued in FY2022.

Leverage expected to remain high over 1-2 years and coverage metrices to remain subdued – Given the sharp decline in profitability in FY2021, LTHL's debt coverage indicators deteriorated to sub-optimal levels. DSCR declined to <1x and TD/OPBDITA jumped to 35x as on March 31, 2021, on a consolidated debt of Rs. 2,153 crore as of March 31, 2021[4]. While the company continues to incur capex on the Mumbai airport project using internal accruals, it may also draw upon project debt as the project nears completion (in CY2023). Given the expectation of subdued profitability and increase in debt levels due to drawdown of GECL loans (eligibility up to Rs. 450 crore) in FY2022 and possible project debt, LTHL's leverage and debt coverage indicators would continue to remain stretched over the medium term. Nonetheless, ICRA draws comfort from the company's financial flexibility emanating from its healthy asset base, and the management's demonstrated track record of maintaining low leverage and raising debt at competitive terms. Focus on network expansion via the management contract route would also limit capex requirement and support growth in returns over the long-term.

Liquidity position: Adequate

Despite the severe impact of Covid-19 on the demand in FY2021, the company reported only a marginal cash loss, which averted any major loss funding requirements. LTHL's liquidity is expected to remain **adequate**, supported by cash and liquid investments of ~Rs. 140 crore and undrawn overdraft, and term loan limits of ~Rs. 60 crore as on March 31, 2021. The company also had eligible GECL loans of nearly Rs. 275 crore as on June 30, 2021. Against the available sources of cash, LTHL has capex obligations of ~Rs. 60-80 crore and term loan repayments of ~Rs. 120 crore in FY2022. While the operations are expected to remain adversely impacted in the near-term due to the pandemic, the liquidity would be sufficient in covering its obligations in the near term. LTHL also has stand-by funds of up to Rs. 125 crore, which it can draw from APG at short notice (subject to the consent of LTHL and APG), in addition to accessing the capital markets. ICRA expects LTHL's large asset base, strategic partnership, and financial flexibility with its lenders to continue supporting its refinancing options and liquidity profile.

Rating sensitivities

Positive factors – ICRA could change the outlook to Stable if the company demonstrates improvement in its operational metrics leading to improvement in debt coverage and leverage indicators on a sustained basis.

[4] *TD includes operating lease liabilities of Rs. 468 crore as on March 31, 2021*

Negative factors – Negative pressure on LTHL's rating could arise due to deeper and longer economic disruption caused by the pandemic leading to sustained pressure on its earning and profitability; higher than expected debt addition or deterioration in liquidity position will also be a credit negative. Timely raising of equity funds, in case of unanticipated/ severe impact of the pandemic on cash accruals, would also be a key monitorable.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Consolidation and Rating approach Rating Methodology for Entities in the Hotel Industry
Parent/Group Support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of LTHL. As on March 31, 2021, the company had 13 subsidiaries, 10 stepdown subsidiaries (under indirect control), three associates, and a limited liability partnership, which are all enlisted in Annexure-2.

About the company

Incorporated in 2002 by Mr. Patanjali Keswani and his friends and associates, Lemon Tree Hotels Limited (LTHL) is a publicly listed company that owns and operates 84 hotels with 8,309 rooms under seven brands across 52 cities in India and abroad. The company's portfolio spans across upscale, midscale and economy segments. The company's brands include—Aurika (upscale), Lemon Tree Premier and Keys Prima (upper midscale), Lemon Tree and Keys Select (midscale), Red Fox and Keys Lite (economy). In terms of ownership, ~26% stake in the company is held by the promoters (Keswani family), ~15% by APG (a Dutch pension fund) and the balance is owned by foreign portfolio investors, mutual funds, employees, and the public.

The company designs, develops, and manages properties directly or under its subsidiaries (collectively referred to as the Lemon Tree Group). While most of the properties in the portfolio are owned by the company directly or through its subsidiaries, a few are operated on long-term lease basis. As on June 15, 2021, the Group had 41 owned and leased operational properties, with two properties in the pipeline. The total owned/leased inventory of operational properties stood at 5,192 rooms. Further, 738 rooms were under development and are expected to be added over the next 2.5-3 years.

To facilitate rapid expansion of LTHL's brands across the country, the Group's subsidiary, Carnation Hotels Private Limited, enters management contracts with asset owners. As on June 15, 2021, 3,117 rooms across 43 properties were under management contracts with additional 1,371 rooms (19 properties) under negotiation.

Key financial indicators (audited)

LTHL (Consolidated)	FY2020	FY2021*
Operating Income (Rs. crore)	669.4	251.8
PAT (Rs. crore)	-10.4	-182.5
OPBDIT/OI (%)	36.4%	24.4%
PAT/OI (%)	-1.6%	-72.5%
Total Outside Liabilities/Tangible Net Worth (times)	1.3	1.4
Total Debt/OPBDIT (times)	8.3	35.1
Interest Coverage (times)	1.5	0.3

*Source: Company results, ICRA Research *Limited results*

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net Worth + Deferred Tax Liability - Capital Work in Progress); DSCR: (PBIT + MAT Credit Entitlements - Fair Value Gains through P&L - Non-cash Extraordinary Gain/Loss)/ (Interest + Repayments made during the Year)

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Sl. No.	Instrument	Current Rating (FY2022)				Chronology of Rating History for the past 3 years				
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore) as on Jun 30, 2021	Date & Rating	Date & Rating in FY2021		Date & Rating in FY2020^		Date & Rating in FY2019
					Aug 11, 2021	Nov 2, 2020	Apr 13, 2020	Nov 27, 2019 Nov 5, 2019	Jul 8, 2019	Mar 19, 2019 Jan 3, 2019 Jun 15, 2018
1	Term Loans	Long-term	101.84	101.84	[ICRA]A- (Negative)	[ICRA]A- (Negative)	[ICRA]A- (Negative)	[ICRA]A- (Stable)	[ICRA]A-&	[ICRA]A- (Stable)
2	Fund-based Working Capital facilities	Long-term and short term	30.00	-	[ICRA]A- (Negative)/ [ICRA]A2+	[ICRA]A- (Negative)/ [ICRA]A2+	[ICRA]A- (Negative)/ [ICRA]A2+	[ICRA]A- (Stable)/ [ICRA]A2+	[ICRA]A-&/ [ICRA]A2+&	[ICRA]A-(Stable)/ [ICRA]A2+
3	Unallocated	Long-term and short term	14.16	-	[ICRA]A- (Negative)/ [ICRA]A2+	[ICRA]A- (Negative)/ [ICRA]A2+	-	-	-	-

& = Under watch with developing implications

^A PR for update on delay in periodic surveillance was published on Sep 27, 2019 in FY2020

Complexity level of the rated instruments

Instrument	Complexity Indicator
Term Loans	Simple
Fund-based Working Capital facilities	Simple
Unallocated	Not applicable

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, is available on ICRA’s website: www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan -I	Aug 2019	NA	FY2025	1.92	[ICRA]A-(Negative)
NA	Term Loan -II	Dec 2020	NA	FY2026	6.48	[ICRA]A-(Negative)
NA	Term Loan-III	Aug 2019	NA	FY2025	7.42	[ICRA]A-(Negative)
NA	Term Loan-IV	Jan 2021	NA	FY2026	8.10	[ICRA]A-(Negative)
NA	Term Loan-V	Jun 2021	NA	FY2027	8.10	[ICRA]A-(Negative)
NA	Term Loan-VI	Oct 2019	NA	FY2031	43.33	[ICRA]A-(Negative)
NA	Term Loan-VII	Dec 2020	NA	FY2026	8.84	[ICRA]A-(Negative)
NA	Term Loan-VIII	Apr 2016	NA	FY2027	17.65	[ICRA]A-(Negative)
NA	Overdraft limit	NA	NA	NA	30.00	[ICRA]A-(Negative)/[ICRA]A2+
NA	Unallocated limit	NA	NA	NA	14.16	[ICRA]A-(Negative)/[ICRA]A2+

Source: Company

Annexure-2: List of entities considered for consolidated analysis

Company Name	LTHL Ownership	Consolidation Approach
Lemon Tree Hotels Limited	100% Rated entity	Full Consolidation
Carnation Hotels Private Limited	74.90%	Full Consolidation
Fleur Hotels Private Limited	58.24%	Full Consolidation
Dandelion Hotels Private Limited	100.00%	Full Consolidation
Lemon Tree Hotel Company Private Limited	100.00%	Full Consolidation
PSK Resorts & Hotels Private Limited	100.00%	Full Consolidation
Canary Hotels Private Limited	100.00%	Full Consolidation
Grey Fox Project Management Company Private Limited	100.00%	Full Consolidation
Oriole Dr Fresh Hotels Private Limited	100.00%	Full Consolidation
Red Fox Hotel Company Private Limited	100.00%	Full Consolidation
Sukhsagar Complexes Private Limited	100.00%	Full Consolidation
Manakin Resorts Private Limited (Subsidiary of PSK Resorts & Hotels Private Limited)	100.00%	Full Consolidation
Poplar Homestead Holdings Private Limited	100.00%	Full Consolidation
Madder Stays Private Limited	100.00%	Full Consolidation
Jessamine Stays Private Limited	100.00%	Full Consolidation
Manakin Resorts Private Limited (Subsidiary of PSK Resorts & Hotels Private Limited)	100.0%	Full Consolidation
Celsia Hotels Private Limited (Subsidiary of Fleur Hotels Private Limited)	58.24%	Full Consolidation
Inovoa Hotels & Resorts Limited (Subsidiary of Fleur Hotels Private Limited)	58.24%	Full Consolidation
IORA Hotels Private Limited (Subsidiary of Fleur Hotels Private Limited)	58.24%	Full Consolidation
Hyacinth Hotels Private Limited (Subsidiary of Fleur Hotels Private Limited)	58.24%	Full Consolidation
Bandhav Resorts Private Limited (Subsidiary of Fleur Hotels Private Limited)	58.24%	Full Consolidation
Ophrys Hotels Private Limited (Subsidiary of Fleur Hotels Private Limited)	58.24%	Full Consolidation
Valerian Management Services Private Limited (Subsidiary of Grey Fox Project Management Company Private Limited)	100.00%	Full Consolidation
Berggruen Hotels Private Limited (Subsidiary of Fleur Hotels Private Limited)	58.24%	Full consolidation
Mind Leaders Learning India Private Limited	36.56%	Equity Method

Company Name	LTHL Ownership	Consolidation Approach
Pelican Facilities Management Private Limited (Subsidiary of Mind Leaders Learning India Private Limited)	36.56%	Equity Method
Glendale Marketing Services Private Limited of Pelican Facilities Management Private Limited	36.56%	Equity Method
Hamstede Living Private Limited (subsidiary w.e.f. March 31, 2021)	100.00%	Full Consolidation
Mezereon Hotels LLP (Capital contribution by Fleur Hotels Private Limited & Celsia Hotels Private Limited)	58.24%	Full Consolidation

Source: *Company*

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