November 26, 2019 (Revised)

# Sayaji Hotels Limited: Ratings reaffirmed at [ICRA]BBB-; removed from watch and Stable outlook assigned

## Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|---|---|---|---|
| Long-Term Loans | 68.95 | 68.95 | [ICRA]BBB- (Stable); reaffirmed; removed from watch with developing implications and Stable outlook assigned |
| Fund-based- Working Capital Facilities | 8.75 | 8.75 | [ICRA]BBB- (Stable); reaffirmed; removed from watch with developing implications and Stable outlook assigned |
| Non-fund Based-Working Capital Facilities | 0.5 | 0.5 | [ICRA]BBB- (Stable); reaffirmed; removed from watch with developing implications and Stable outlook assigned |
| Long-Term Unallocated Limits | 15.68 | 15.68 | [ICRA]BBB- (Stable); reaffirmed; removed from watch with developing implications and Stable outlook assigned |
| **Total** | **93.88** | **93.88** | |

**Instrument details are provided in Annexure-1*

## Material Event

Sayaji Hotels Limited (SHL), on November 15, 2019, intimated the stock exchange that its Board has approved withdrawal of Scheme of amalgamation and arrangement, which sought to realign the businesses under SHL and its promoters. The said Scheme had been approved by the board in September 2018 and had been awaiting approval from National Company Law Tribunal (NCLT) Chennai Bench.

## Impact of Material Event

ICRA has long-term rating of [ICRA]BBB- on the fund-based, non-fund based and unallocated bank facilities of SHL. The rating has been removed from watch with developing implications.

## Rationale

The removal of the rating watch and reaffirmation favourably factors in the steady operating and financial performance of the company in FY2019 and H1 FY2020, despite two new hotels viz. Sayaji Raipur and Vadodara, in early stages of ramp-up and Effotel Vadodara hotel reopening after extensive renovations-cum-expansion (undertaken in H1 FY2019). On consolidated level, the company had reported a 13% and 20% YoY growth in operating income (OI) and operational profits, respectively, in FY2019. Given the seasonality in hospitality business, one-off events – general elections, airline industry issues and generally weak macro-economic sentiments, H1 FY2020 witnessed marginal de-growth in company's performance. Its key Indore property has been under pressure since H2 FY2019, initially due to the Madhya Pradesh State elections and model code of conduct implemented, coupled with increasing competition from new inventory in the micro-market. Moreover, a shorter wedding season impacted the food and beverages (F&B) business in FY2019.

Nonetheless, the company performance is expected to recover on YoY basis in H2 FY2020 with the onset of wedding season on a relatively low base of H2 FY2019.

ICRA continues to take cognisance of SHL's investments in Barbeque Nation Hospitality Limited (BNHL rated [ICRA] A+(Stable)/[ICRA] A1+), whose planned public listing (albeit delayed from last year) would significantly improve SHL's financial flexibility. The ratings continue to factor in the extensive experience of the company's promoters and their demonstrated track record of funding support along with its geographically diversified portfolio, renowned F&B and banqueting segment (offering higher margin business). The ratings draw comfort from its established customer base and brand recall of 'Sayaji' and "Effotel" in the operative micro-markets. ICRA notes the increase in the company's portfolio in FY2020 with the launch of Effotel Gurgaon (50 keys) and Sayaji Rajkot (75+ keys) under management contract. The same has been in line with the management's stated strategy of leveraging its brands and expanding presence through an asset-light model. While a moderately favourable outlook for the hospitality industry is a positive for SHL, the benefits from this managed portfolio (now comprising three properties and over 250 rooms) are expected to accrue over medium term as the properties ramp up.

The ratings, however, remain constrained by the company's modest return on capital employed and debt coverage indicators. This is due to moderating profitability from its Indore property, coupled with high overheads associated with nascent properties (Sayaji Raipur and Vadodara and Effotel Vadodara, post-renovations) and regular debt-funded capex incurred towards capacity expansion and/or renovations. Incremental unsecured loans from promoters in FY2019, purchase of non-core assets from SHL (Aries Hotels investment) and proposed deferment of preference share redemption due in FY2020[1] evidence promoters' commitment to the business. However, the high cost of this debt, coupled with high repayment obligations over the next three years are expected to inhibit any improvement in the company's debt metrics. Inherent cyclicality and seasonality in the hospitality industry exposes its revenues to risks associated with economic slowdown and exogenous shocks, although the same is partially mitigated by SHL's geographically diversified portfolio.

Going forward, the company's ability to stabilise its new inventory, improve the profitability of its mature operational properties (especially Indore), plan the pace (and manner) of its future renovation and expansion plans so as to limit the impact on its business and financial risk profile, will remain the key rating sensitivities. SHL's ability to amicably resolve the legal dispute with Indore Development Authority (IDA) for its flagship Indore property, over the alleged violation of lease terms by the company, remains a key monitorable. Any adverse verdict in the matter can severely impact SHL's credit profile and remains an event risk.

## Key rating drivers and their description

## Credit strengths

**Steady operational performance in FY2019 despite competition –** SHL registered a steady portfolio revPAR in FY2019, driven by healthy ramp up of the newly-added Sayaji Vadodara and Raipur properties. The growth was, however, moderated due to increased competition faced by its core Indore property and closure of Effotel-Vadodara for renovation-cum-expansion in H1 FY2019. In H1 FY2020, the company has reported flattish YoY ARRs across properties with some decline at Indore and Pune. F&B income also impacted due to weak MICE[2] demand. Going forward, ICRA

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[1]*Preference Shares of Rs. 20.5 crore (debt and equity component) as of March 31, 2019 have been subscribed to by the promoter family and were due for redemption, inclusive of dividend payments of 5 years in arrears, in FY2020. While announcing its Q1 FY2020 results, the company informed regarding Board approval for deferment of this redemption by 5 years.*

[2] *MICE: Meetings, Incentives, Conferencing, Exhibitions*

expects the operating metrics to improve at a modest pace, benefiting from expectation of limited supply and stable local demand. However, its ability to navigate the increasing competition in Indore remains crucial.

**Experienced promoters with demonstrated record of funding support** – SHL is promoted by the Dhanani family, which has been a part of the hospitality industry for over 30 years. The promoter family demonstrated a track record of providing funding support to the company for its periodic capex and short-term funding mismatches. As of Sep 2019, SHL (standalone) had outstanding unsecured promoter loans of around Rs. 19.7 crore, in addition to preference share capital of around Rs. 20.5 crore. Purchase of non-core investments of SHL by the promoters, like the stake in Aries Hotel, is likely to support cash flows in the current fiscal. All these are indicative of the promoters' commitment to its business and ICRA expects this need-based support to continue.

**Healthy geographical diversification; strong brand recognition of Sayaji in the operative micro-markets –** Under its in-house brand, Sayaji and Effotel, the company has established itself as a reputed hotel chain primarily in the tier-II and tier-III cities. With nearly 1,200+ rooms across ten operational properties in eight cities, the brands Sayaji and Effotel are rapidly expanding their market presence leading to healthy geographical diversification. It has recently launched another brand, Enrise, as a mid-scale segment operating in Indore and plans to expand this brand in other cities, where it already has an established presence. ICRA expects that this would further aid in increased brand visibility and rapid expansion of SHL in diversified markets through an asset-light model.

**Portfolio expansion through management contracts limit capex requirement and project implementation risk** – Over the past two to three years, the management has shifted its focus from building capex-intensive properties to follow an asset-light model of expansion, through leasing of properties and management contracts. The last two Sayaji properties (land and building) – Raipur and Vadodara – have been acquired on lease, while it has expanded its portfolio of properties under management contract with the launch of Effotel-Gurugram and Sayaji-Rajkot in YTD FY2020. This would help the company conserve its funds, while allowing the scope for quick scale-up of revenues and profitability**.**

**Sizeable investments in profit generating BNHL offers potential for leverage and financial flexibility** – SHL owns a chain of 119 restaurants (as of December 2018) through its 45.7%-owned associate, BHNL. Having received a SEBI approval, BNHL was expected to go public in FY2018, however, the plan was postponed. Going forward, the listing of its investee company would lead to enhanced financial flexibility for SHL, as it would have the option to monetise this to reduce or pay off its debts.

## Credit challenges

**Subdued profitability and returns on capital employed** – SHL generates over 50% of EBITDA (FY2019) from its properties located in Indore. In FY2019, both Sayaji and Effotel Indore registered a 2-3.5% YoY decline in profitability margins. This was primarily owing to competition from incremental inventory (JW Marriott, other unorganised sector players) and banqueting spaces in the micro-market. Further, with incremental debt taken for Raipur and Vadodara (renovations), the properties are yet to start contributing meaningfully to profits. The return on capital employed remained modest (despite YoY improvement). Over the medium term, ICRA expects the profitability margins to remain constrained in 17-18% range. Anticipated benefits from expansion of portfolio under management contract and pace of flow through to profitability remain a key monitorable.

**Moderate debt coverage indicators with sizeable medium-term repayment** – The company has large debt repayment obligation worth approximately Rs. 68 crore over the next three years. This is expected to result in moderation in its debt coverage metrics with DSCR ranging between 0.9 times and 1.2 times (FY2020-FY2022). Nonetheless, ICRA expects stable cash flows from operations, supported by sales proceeds from divestment of investment in Aries Hospitality and Malwa Hospitality, to ensure timely repayments. With scheduled debt reduction and increasing net worth (owing to share of profit contributions from BNHL), the consolidated gearing is likely to improve substantially over the medium term.

**Vulnerability of revenues to inherent industry cyclicality, economic cycles and exogenous events** – The operating performance of the properties remains vulnerable to seasonal industry, general economic cycles and exogenous factors (geopolitical crisis, terrorist attacks, disease outbreaks etc). Nonetheless, since the impact varies across markets, the risk to revenues is partially mitigated by SHL's geographically diversified portfolio.

## Liquidity position: Adequate

SHL's liquidity has remained **Adequate** with positive cash flows from operations in the past few years, coupled with continued funding support from the promoters. The company had cash and liquid investments of approx. Rs. 3.0 crore as and unavailed bank lines of Rs. 4.75 crore (of the available sanction of Rs. 8.75 crore) at end of Sep 2019. Major funding requirements in FY2020 and FY2021 will emanate from repayment obligations of approximately Rs. 20 crore and Rs. 35 crores, respectively. The company reportedly received sales consideration of Rs. 5.7 crore from stake sale in Aries Hotels. Further, stake sale from Malwa Hospitality (51% subsidiary) is expected to yield Rs. 6.89 crore by the end of FY2020. With no-major capacity expansion or new project plans, ICRA expects SHL to be able to meet its near-term commitments through internal cash flows, proceeds from asset sale and continued funding support from the promoters. The proposed listing of associate company – Barbeque Nations - would enhance financial flexibility of SHL, which would then have the option to monetise or leverage its investment to reduce or pay off its debts.

## Rating sensitivities

**Positive triggers** – ICRA could upgrade SHL's rating if the company demonstrates a sustained improvement in its operational metrices leading to improvement in profitability and ROCE, along with reduction in leverage metrics on a consolidated basis. Debt reduction through incremental equity infusion or sale of assets, could also be a rating positive. Specific credit metrics that could lead to an upgrade of SHL's rating include Total Debt/ OPBITDA below 2.5 times and DSCR over 1.5x on a sustained basis.

**Negative triggers** – Negative pressure on SHL's rating could arise if, for reasons including a shift in the industry conditions or increasing competitive pressures in key micro-markets lead to slower than anticipated ramp-up of its portfolio. Other triggers for adverse rating action would include, *inter alia*, increase in debt-funded capex resulting in delay in improvement in ROCE and coverage metrices (say DSCR remaining below 1.5x). SHL's ability to amicably resolve the legal dispute with Indore Development Authority (IDA) for its flagship Indore property, over the alleged violation of lease terms by the company, remains a key monitorable. Any adverse verdict in the matter can severely impact SHL's credit profile and remains an event risk.

## Analytical approach

| Analytical Approach | Comments |
|---|---|
| Applicable Rating Methodologies | Corporate Credit Rating Methodology<br>Rating Methodology for Entities in the Hotel Industry<br>Consolidation and Rating Approach |
| Parent/Group Support | None |
| Consolidation / Standalone | The rating is based on consolidated financial statements of the issuer. The consolidated entities are listed under Annexure-2. |

## About the company

Incorporated in 1982, SHL commenced operations of its first hotel property at Vadodara in 1990. As on date, it has a portfolio of 1200+ rooms across ten hotel properties located in Vadodara (two properties), Indore (two properties), Pune, Bhopal, Raipur, Kolhapur, Gurgaon and Rajkot. The properties are operated under its in-house brands - Sayaji and Effotel. It has a banquet hall property, Amber Garden, in Indore. The Effotel Indore hotel is owned through its 51.67% owned subsidiary Malwa Hospitality Private Limited (MHPL), while the properties at Kolhapur, Gurgaon and Rajkot (cumulative room inventory of 250 keys) are under management contract.

The company has been listed on BSE since 1992. It also owns a chain of 119 restaurants (as of December 2018) through its 45.73% owned associate - BNHL, which is owned through SHL's wholly owned subsidiary Sayaji Housekeeping Services Limited). SHL is promoted by the Indore-based Dhanani family, which directly held 74.9% stake as of September 30, 2019.

## Key financial indicators (Audited)

| Consolidated | FY2018 | FY2019 | H1 FY2020* |
|---|---|---|---|
| Operating Income (Rs. crore) | 215.8 | 244.4 | 103.1 |
| PAT (Rs. crore) | (5.8) | (1.0) | (8.7) |
| OPBDIT/OI (%) | 16.0% | 17.6% | 18.1% |
| RoCE (%) | 4.7% | 7.1% | -- |
| | | | |
| Total Outside Liabilities/Tangible Net Worth (times) | 1.3 | 1.3 | -- |
| Total Debt/OPBDIT (times) | 4.3 | 3.4 | -- |
| Interest Coverage (times) | 2.1 | 2.3 | 1.2 |
| DSCR (times) | 1.0 | 1.3 | -- |

*Source: Annual reports; ICRA research; * Published interim results post Ind-AS 116 adjustment*
*PAT: Profit after Tax excluding share of profit/loss from associate/JVs; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net Worth + Deferred Tax Liability - Capital Work in Progress)*

## Status of non-cooperation with previous CRA: Not applicable

## Any other information: None

## Rating history for last three years

| | Instrument | Current Rating (FY2020) | | | | | Chronology of Rating History for the past 3 years | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | Type | Amount Rated (Rs. crore) | Amount Outstanding 30-Sep-19 (Rs. crore) | Date & Rating | | Date & Rating in FY2019 | Date & Rating in FY2018 | | Date & Rating in FY2017 |
| | | | | | 26-Nov-19 | 30-Aug-19^ | 27-Sep-18 | 16-Feb-18 | 27-Dec-17 | 11-Jan-17 |
| 1 | Long term - Term Loans | Long Term | 68.95 | 55.25 | [ICRA]BBB- (stable) | [ICRA]BBB-&; on watch with developing implications | [ICRA]BBB-&; on watch with developing implications | [ICRA]BBB- (stable) | [ICRA]BBB- @; on watch with negative implications | [ICRA]BBB- (stable) |
| 2 | Long term- Cash Credit Facilities | Long Term | 8.75 | 4.06 | [ICRA]BBB- (stable) | [ICRA]BBB-& | [ICRA]BBB-& | [ICRA]BBB- (stable) | [ICRA]BBB- @ | [ICRA]BBB- (stable) |
| 3 | Long term - Non-fund-based facilities | Long Term | 0.5 | NA | [ICRA]BBB- (stable) | [ICRA]BBB-& | [ICRA]BBB-& | [ICRA]BBB- (stable) | [ICRA]BBB- @ | [ICRA]BBB- (stable) |
| 4 | Unallocated | Long term | 15.68 | NA | [ICRA]BBB- (stable) | [ICRA]BBB-& | [ICRA]BBB-& | [ICRA]BBB- (stable) | [ICRA]BBB- @ | [ICRA]BBB- (stable) |

*^ PR for delay in periodic surveillance published in May 2019*

## Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the 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 1 | Jan-15 | NA | Jul-21 | 7.10 | [ICRA]BBB- (Stable) |
| NA | Term Loan 2 | Sep-16 | NA | Mar-22 | 12.37 | [ICRA]BBB- (Stable) |
| NA | Term Loan 3 | Sep-16 | NA | Mar-21 | 1.43 | [ICRA]BBB- (Stable) |
| NA | Term Loan 4 | Jan-17 | NA | Jan-25 | 21.05 | [ICRA]BBB- (Stable) |
| NA | Term Loan 5 | Oct-16 | NA | Oct-21 | 7.43 | [ICRA]BBB- (Stable) |
| NA | Term Loan 6 | Oct-16 | NA | Sep-23 | 5.72 | [ICRA]BBB- (Stable) |
| NA | Term Loan 7 | Oct-16 | NA | Sep-20 | 2.71 | [ICRA]BBB- (Stable) |
| NA | Term Loan 8 | Mar-18 | NA | Jul-26 | 8.70 | [ICRA]BBB- (Stable) |
| NA | Term Loan 9 | Mar-18 | NA | Sep-26 | 2.44 | [ICRA]BBB- (Stable) |
| NA | Cash Credit | Mar-18 | NA | NA | 8.75 | [ICRA]BBB- (Stable) |
| NA | Bank Guarantee | Mar-18 | NA | NA | 0.50 | [ICRA]BBB- (Stable) |
| NA | Unallocated Limits | NA | NA | NA | 15.68 | [ICRA]BBB- (Stable) |

*Source: Company*

## Annexure-2: List of entities considered for consolidated analysis

| Company Name | Ownership | Consolidation Approach |
|---|---|---|
| Sayaji Hotels Limited | 100.00% (Rated entity) | Full Consolidation |
| Malwa Hospitality Private Limited | 51.67% | Full Consolidation |
| Sayaji Housekeeping Services Limited | 100.00% | Full Consolidation |
| Aries Hotels Private Limited | 52.37% | Full Consolidation |
| Barbeque Nations Hospitality Limited | 45.73% | Equity Method |
| Sayaji Hotels Management Limited | 100.00% | Full Consolidation |
| Sayaji Hotels (Pune) Limited | 100.00% | Full Consolidation |
| Sayaji Hotels (Vadodara) Limited | 100.00% | Full Consolidation |

*Source: SHL's Annual report FY2019 and company discussion*

## Corrigendum

Document dated November 25, 2019 has been corrected with revisions as detailed below:

a) Revision on page 1 under the table headed –Material Event- The date of intimation to exchange revised to November 15, 2019.

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