May 05, 2020

Apeejay Surrendra Park Hotels Limited: Ratings reaffirmed; outlook revised to Negative

Summary of rated instruments

Instrument	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	430.48	430.48	[ICRA]A+ reaffirmed; outlook revised to Negative from Stable
Fund-based Limits	50.00	50.00	[ICRA]A+ reaffirmed; outlook revised to Negative from Stable
Fund-based Limits	5.00	5.00	[ICRA]A1+; Reaffirmed
Non-fund-based Limits	15.00	15.00	[ICRA]A1+; Reaffirmed
Unallocated	3.55	3.55	[ICRA]A+/ [ICRA]A1+ reaffirmed; outlook revised to Negative from Stable
Total	**504.03**	**504.03**	

Rationale

The revision in the outlook follows the impact of the novel coronavirus (Covid-19) outbreak on the global travel and tourism industry and is in line with ICRA's negative outlook for the sector. Occupancies across most hotels (barring those corralled into supporting the Government's isolation and containment measures, and those which are being used for work-from-alternative office spaces) have crashed across the country, following the pan-India lockdown announced by the GoI on March 24, 2020 and a further extension on April 14, 2020. This is in line with the situation of the hospitality industry globally. ICRA also expects the hospitality industry to witness one of the longest periods of recovery because of the widespread business slowdown over the next couple of quarters.

Given the discretionary nature of spend (especially leisure travel), the travel and tourism industry has always been highly susceptible to exogenous shocks like wars, terror attacks, diseases and economic meltdowns. The impact of Covid-19 is expected to be far more severe and broad based than the previous instances. ICRA expects significant pressure on the revenue-per-available room (RevPARs), initially through occupancies, over the next two quarters. While some deferred travel, particularly for business, will eventually resume following the restoration of normalcy, but room nights are essentially perishable commodities. Given the high operating leverage and debt-servicing requirements, the sharp contraction in revenues will have a detrimental impact on the industry's ability to service its debt. ICRA will continue to monitor the situation, as it evolves in India and globally over the coming weeks, and its impact on the company and will take an appropriate rating action whenever required.

For Apeejay Surrendra Park Hotels Limited (ASHPL), the sub-optimal operations at the hotels, due to the Covid-19 outbreak, are expected to result in a significant reduction in cash accruals in the near term. The average occupancy, at present, has plummeted to below 10%, following the lockdown imposed by the Government. To minimise the impact on cash flows, the company has initiated significant cost containment measures. ICRA also notes that the company had acquired the confectionary chain, Flurys, as well as discontinued payment of royalty for using the Apeejay brand from October 2019. Thus, the full-year benefit of the same will also be visible in FY2021, which is also likely to support the profits and cash accruals of the company to an extent. Nonetheless, the company's financial profile is expected to moderate, the extent of which would depend on the pace at which normalcy returns. The liquidity position of the company would be the key rating monitorable in the short term. ICRA understands that the company has applied for a moratorium of scheduled repayments due in April and May 2020, as a part of the Covid-19 regulatory package announced by the RBI. Nonetheless, the debt obligations for the company are substantial in FY2021, with the total interest and debt repayment estimated to be ~ Rs. 110 crores. Given the Negative outlook, ICRA estimates that the company would need to refinance at least some of the debt obligations falling due during the year. ICRA takes comfort from the healthy relationship of the company and the Apeejay Surrendra Group with domestic banks, with demonstrated ability to refinance debt at attractive terms in the past.

The ratings continue to favourably factor in the established position of ASPHL's brand, THE PARK, in the Indian hospitality industry with presence across attractive locations in key cities. Moreover, the company continues to focus on the asset light management contracts model for expansion, which enables it to increase its presence while limiting the capital outlay. A fixed fee and a share of profit received on these managed properties help the company improve its business returns. ASPHL's properties have recorded a substantial increase in both the average room revenues (ARRs) and occupancy levels over the years, with the average occupancy across the properties standing at 90% in FY2020. The ratings also factor in the sustained growth in food and beverages (F&B) revenues, which are more stable than the cyclical room revenues. The addition of the confectionary business, under the Flury's brand, is expected to further support the operating profile of the company, going forward. Nevertheless, ICRA expects the ongoing pandemic to keep the operating metrices muted in the near term. ICRA also notes that the company had filed the draft red-herring prospectus (DRHP) in January 2020 for the proposed Initial Public offer (IPO). However, given the current situation, an IPO is unlikely in the near term.

ASHPL is seeking a moratorium on payments from its lenders as part of the COVID-19 - Regulatory Package announced by the RBI on March 27, 2020. Accordingly, some of the scheduled repayments were deferred by the company as at April 30, 2020, in anticipation of formal approval from the lenders. However, despite the missed payment and despite the absence of a formal approval from the lenders allowing for a payment relief, ICRA has not recognized this instance as a Default as of now. This is based on ICRA's expectation that a formal approval for rescheduling the loan would be received soon, as permitted by the RBI as part of the relief measures announced recently. Non-recognition of default in this case is as per the guidance provided by the SEBI circular SEBI/ HO/ MIRSD/ CRADT/ CIR/ P/ 2020/ 53 dated March 30, 2020. It may however be noted that if the lenders do not approve of the moratorium in due course, ICRA would review the above stance on default recognition.

Credit strengths

Established five-star luxury hotel brand under the name of THE PARK; presence across attractive locations in key geographies in India – With a portfolio of 22 hotels (7 own properties, 13 under the management contract and the balance under the lease model), comprising 1,937 rooms spread across attractive locations in key geographies in India, ASPHL is a medium sized, but well established player in the Indian hotel industry. ASPHL's hotel portfolio is diversified across categories, with presence in luxury and upscale segments through THE PARK brand, and in the upper mid-market segment through Zone by THE PARK brand (operated through management contracts). A bulk of the company's revenue is derived from domestic business travellers because of favourable locations of most of the properties in business destinations.

The company has been increasing its presence in the management contract segment, and is expected to further increase its room inventory. This asset light model enables the company to increase its presence while limiting the capital outlay. A fixed fee and a share of profit received on these managed properties also help the company improve its business returns, although ICRA notes that the returns remain moderate on an absolute basis at present. In FY2019 end, ASPHL commissioned a property in Kolkata- Biswa Bangla under the long-term lease model, which has 117 rooms and has been developed by the Government of West Bengal and will be managed by ASPHL. ICRA notes that the terms of the associated management contract are favourable, and the property is expected to generate revenues and profits, going forward.

Healthy operating metrics in FY2019 and FY2020 (before lockdown); near-term revenue visibility to be impacted by the Covid-19 outbreak – The Indian hospitality industry, which experienced a prolonged downturn during FY2009-FY2015 because of excess supply in several key markets in India, posted improvement (as measured by Revenue per Available Room or RevPAR) over the past two-three years. ASPHL's properties have recorded a considerable increase in both ARRs and occupancy levels in last few 2-3 years, with average occupancy across the properties standing at 90% (before lockdown). Nevertheless, ICRA expects the ongoing pandemic to keep the operating metrices muted in the near-term, which will remain a key rating monitorable.

High share of food and beverage income provides some cushion against cyclicality of hotel business – The share of revenue from the F&B income has historically been high for ASPHL, relative to peers, at 45-46% of total revenues on an average over the period FY2013-2019, notwithstanding some decline in the quarters post demonetisation because of an overall economic slowdown. Even though the F&B margins are lower than that of rooms, high F&B revenues provide stability to the hotel in the event of falling occupancies and ARRs. Addition of the confectionary business, under the Flury's brand, is expected to increase the F&B income of the company. The number of Flury's stores has increased from 27 in March 2019 to 40 in December 2019, which will also support the revenue in the current year. However, in line with the room revenue, the overall F&B revenue is also expected to remain muted in the near term.

Credit challenges

Impact of Covid-19 outbreak on operating metrices and credit profile – Given the discretionary nature of consumer spending, the travel and tourism industry has always been highly susceptible to exogenous shocks like wars, natural disasters, terror attacks and disease outbreaks. Following the recent virus outbreak, ICRA expects significant pressure on industry RevPARs, initially through occupancies, over the next two quarters for the hospitality industry. As hotels have high operating and financial leverage, it renders them highly susceptible to any fall in revenues. While the current liquidity buffer provides some cushion for the next couple of months, sizeable debt-servicing requirements and a sharp decline in revenues will impact ASHPL's credit profile, the extent of which will remain contingent upon the pace of recovery following the pandemic. However, the decline in revenues is likely to be at least partially offset by the cost control measures being undertaken by the company. Also, the discontinuation of royalty payment and additional profits from the confectionery business are likely to provide some support to the operating profits.

Sub-optimal returns on capital employed and moderate coverage indicators – The returns on capital employed (RoCE) remained sub-optimal at ~6% in FY2019 primarily led by royalty payment and non-yielding large investment in land. Adjusting for the same, RoCE would be around 10% in FY2019. In addition, ASHPL's debt coverage indictors also remained moderate with an estimated interest cover of ~2.0 times and Total Debt/OPBDITA of ~5.7 times in FY2020. Following the Covid-19 outbreak, the near-term capex is likely to be deferred. The expected decline in profitability is likely to adversely impact the returns indicators and debt protection metrics. However, ICRA derives comfort from the management's demonstrated track record of refinancing debt at favourable terms.

Cyclical industry, vulnerable to general economic slowdown and exogenous shocks – The operating performance of the properties remained vulnerable to the seasonality, general economic cycles and exogenous factors (geopolitical crisis, terrorist attacks, disease outbreaks, natural disasters, etc).

Liquidity position- Adequate

ASHPL's liquidity position is **adequate** with current account balance and undrawn CC facility of ~Rs. 27.0 crore as on March 31, 2020. Despite the expectation of muted cash flows from operations in the near-term, due to the Covid-19 pandemic, the liquidity would be sufficient for covering the fixed cost over the near-term. ICRA also understands that the company has applied for a moratorium of scheduled repayments due in April and May 2020, as a part of the Covid-19 regulatory package announced by the RBI. In addition, ICRA takes comfort from the healthy relationship of the company and the Apeejay Surrendra Group with domestic banks, with demonstrated ability to refinance debt at attractive terms in the past.

Rating Sensitivities

Positive triggers – An upgrade in the near term is unlikely, given the Negative outlook on the industry due to concerns over the severe impact of the Covid-19 outbreak on the travel and tourism business. Nonetheless, a sustained improvement in operational metrices and profitability margins following the pandemic and improvement in debt coverage indicators and liquidity position, could be triggers for a change in the outlook.

Negative triggers –Pressure on ASHPL's ratings may arise for reasons including a prolonged impact of the pandemic, leading to slower-than-anticipated recovery in operating metrices, more-than- expected weakening of its debt servicing indicators and a deterioration in its liquidity position.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Hotel Industry
Parent/Group Support	ICRA notes that there is fungibility of cash flows within different businesses of the Group. However, ICRA does not expect any support for ASHPL. Also, ASHPL is not expected to support other Group entities.
Consolidation / Standalone	The ratings are based on the standalone financial profile of the company

About the company

Apeejay Surrendra Park Hotels Ltd. (ASPHL) is a part of the diversified Apeejay Surrendra Group, based in Kolkata. A private equity firm, which had a 15% stake in ASPHL, sold a 7.5% back to ASPHL in Q3 FY2018. The company has seven owned and operating luxury boutique hotels with an inventory of 1,108 rooms, diversified across Bangalore, Chennai, Hyderabad, Kolkata, Navi Mumbai, New Delhi, and Vishakhapatnam. In addition, the company manages two hotels in Goa under the brand, THE PARK and recently launched THE PARK in Juhu Mumbai. ASPHL also manages ten operational properties in Coimbatore, Jaipur (two), Chennai, Raipur, Jodhpur, Bangalore (two), Gurgaon and Jammu with a total inventory of 595 rooms under the brand Zone by THE PARK. The company has also added one property in Kolkata under the lease model, which has 117 rooms and has been developed by the Government of West Bengal. It will be managed by ASPHL under the brand Zone by THE PARK. ASPHL is planning additional hotels under management contract under the brands THE PARK and Zone by THE PARK over the next two to three years. ASPHL reported a net profit of Rs.12.57 crore on an operating income of Rs. 421.67 crore in FY2019. In FY2018, the company reported an operating income of Rs. 385.21 crore, and a net loss of Rs. 8.10 crore.

Key financial indicators (audited, standalone)

	FY2018	FY2019
Operating Income (Rs. crore)	385.21	421.67
PAT (Rs. crore)	-8.10	12.57
OPBDIT/ OI (%)	20.20%	21.60%
RoCE (%)	4.44%	5.77%*
Total Debt/ TNW (times)	0.82	0.82
Total Debt/ OPBDIT (times)	6.13	5.32
Interest Coverage (times)	1.86	1.84
NWC/ OI (%)	5%	1%

*the calculation includes payment of royalty as an expense and investment in land, which is not yielding any returns as of now. Adjusting for both, adj RoCE would be ~10% in FY2019.

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Rating (FY2021)				Rating History for the Past 3 Years			
		Type	Amount Rated	Amount Outstanding (March 31, 2020)	Current Rating	FY2020		FY2019	FY2018
					05-May-2020	14-Jun-2019	30-Apr-2019	28-Aug-2018	31-Jan-2018
1	Term Loans	LT	430.48	493.41	[ICRA]A+ (Negative)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)
2	Fund-based Limits	LT	50.00	-	[ICRA]A+ (Negative)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)
3	Fund-based Limits	ST	5.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4	Non-fund-based Limits	ST	15.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
5	Unallocated	LT/ST	3.55	-	[ICRA]A+ (Negative) / [ICRA]A1+	[ICRA]A+ (Stable) / [ICRA]A1+	[ICRA]A+ (Stable) / [ICRA]A1+	[ICRA]A+ (Stable) / [ICRA]A1+	[ICRA]A+ (Stable) / [ICRA]A1+
6	Commercial Paper/ Short-Term Debt	ST	-	-	-	-	Withdrawn	[ICRA]A1+	[ICRA]A1+

LT: Long term; ST: Short term

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	FY2016-FY2020	NA	FY 2022 – FY2027	430.48	[ICRA]A+ (Negative)
NA	Fund-based Limits	NA	NA	NA	50.00	[ICRA]A+ (Negative)
NA	Fund-based Limits	NA	NA	NA	5.00	[ICRA]A1+
NA	Non-fund-based Limits	NA	NA	NA	15.00	[ICRA]A1+
NA	Unallocated	NA	NA	NA	3.55	[ICRA]A+ (Negative)/ [ICRA]A1+

Source: ASPHL

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