November 06, 2017

The Indian Hotels Company Limited Revised

Summary of rated instruments

Instrument*	Rated Amount (Rs. crore)	Rating Action
Non-convertible Debentures (NCDs) #	1,600	[ICRA]AA (Stable); re-affirmed

*Instrument details are provided in Annexure-1

 # Aggregate amount outstanding against the rated NCDs is Rs. 800 crore

Rating action

ICRA has re-affirmed the long-term rating of [ICRA]AA (pronounced ICRA double A) on the Rs. 1,600 crore[1] non-convertible debenture programmes of The Indian Hotels Company Limited ('IHCL')[2]. The outlook on the long-term rating is Stable.

Rationale

The reaffirmation of the long-term rating factors in IHCL's dominant position in the Indian hotel industry and the established 'Taj' brand. IHCL has a well-diversified hospitality portfolio across India and overseas, business segments and price points. The rating also favourably factors in the recent uptick in the operating environment of the domestic hospitality industry, as supply additions slowed down across several key markets in the country, while demand momentum continues to remain strong.

The rating also favourably factors in the sizeable reduction in consolidated debt levels through the sale of non-core assets, and the further reduction in debt levels expected from the recently concluded equity rights issue proceeds, wherein the company has raised upto Rs. 1,500 crore. The consolidated capital structure of the company improved in FY2017 owing to retirement of overseas debt from the proceeds of the sale of Taj Boston and investments in Belmond Limited. The consolidated debt levels decreased from Rs. 4,539 crore as of March 31, 2016 to Rs. 3,472 crore as of March 31, 2017, resulting in an improved gearing of 1.07x (PY: 1.37x) as of March 31, 2017. Furthermore, IHCL has earmarked Rs. 1,273 crore out of the rights issue size of Rs. 1,500 crore towards debt repayment. Upon successful completion of rights issue and the repayment of debt thereof, and in the absence of any fresh debt-funded capex or investments, the consolidated leverage as of March 31, 2018 is expected to improve (gearing of less than 0.50x and Total Debt/OPBDITA of less than 3.00x). The reduction in debt levels has been in line with the company's stated intension to reduce its leverage levels, which was factored in the rating. As a Tata Group company, IHCL enjoys considerable financial flexibility to raise funds (equity and/or debt) to meet its investment and capital expenditure (capex) requirements.

The rating, however, is constrained by the subdued consolidated operating performance and the high revenue and profit concentration of the standalone operations on luxury properties in Mumbai and New Delhi. Currently, there is an uncertainty over the extension of license of one of its hotels in Delhi and any adverse outcome arising out of this matter could negatively impact the financial profile of the company.

IHCL's consolidated performance has historically been dragged down by the weak performance of some of its key overseas properties, particularly in the USA. While the company has sold one of its US properties (Taj Boston) for US$ 125 million during FY2017 (retaining the operations of the hotel through a management contract) and has used the bulk of the proceeds to repay its debt in the US subsidiary, the

[1] *100 lakh = 1 crore = 10 million*

[2] *For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications*

other two US properties—especially The Pierre, New York—continue to remain a concern, as they post losses. The performance metrics of these properties would remain a key rating sensitivity, going forward.

While ICRA notes that the management has continued with its stated policy of future growth largely via the asset light strategy (management contracts), limiting capex, it also notes that the development of the Sea Rock asset could entail significant capital outlays, although the timelines and funding mix for the same has not yet been finalised. ICRA would review the impact of these investments, as and when there is further clarity on this project.

Key rating drivers

Credit strengths

- **One of the largest hotel chains in India backed by a balanced property portfolio, strong brands and corporate customer relationships** – Taj Hotels Palaces Resorts and Safaris, which encompasses hotel properties under IHCL and its subsidiaries, joint ventures and associates, consisted of 137 hotels and 16,825 rooms as of August 31, 2017 at over 60 locations across India and 10 countries (Maldives, Nepal, Zambia, Malaysia, UK, USA, Bhutan, Sri Lanka, South Africa, and the UAE). The hotel portfolio is diversified across categories, with presence in luxury ('Taj' brand), upper upscale ('Vivanta by Taj'), upscale ('Gateway') and budget ('Ginger') segments, and price points. These brands have an established presence in the market (IHCL has set out to rebrand its premium—other than Ginger—hotel portfolio under the more prominent 'Taj' brand), attracting business from business and leisure customers alike.
- **Presence across price points—from luxury to economy—helps capture down trading volumes during a downturn and provides revenues stability**
- **Diversified business model with a mix of ownership and asset light strategy; gradual migration up the value chain (from ownership to management)** – IHCL's hotel portfolio comprises a mix of owned properties, properties in subsidiaries, joint ventures and associates, and hotels run by IHCL under management contracts. While currently ~26% of the consolidated inventory of 16,675 rooms (as on March 31, 2017) is held / owned by IHCL directly, it has a stated policy to derive future growth under the asset light strategy, a strategy adopted by the leading global hotel chains. Majority of the new room additions by IHCL has been through the management contract route. Scale up in managed properties, coupled with its presence across price points, will provide revenue stability even during times of industry moderation, while boosting profitability.
- **Improvement in industry operating metrics, with room tariffs witnessing improvement across major cities in FY2017, on the back of robust demand and slower supply additions** – The Indian hospitality industry, which had 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 years. This was driven by improvement in occupancy levels in FY2015–FY2016, as pace of supply additions slowed down across markets amid robust demand growth. Scale up in room occupancy offered considerable pricing power to the industry, as witnessed by the improvement in Average Room Rates (ARRs) across cities during FY2017. Over the next 18-24 months, despite a sizeable supply pipeline, ARRs are expected to improve further, driven by robust demand conditions.
- **The Tata Group parentage; financial flexibility stemming from this lineage and the demonstrated funding support by the parent group from time to time** – The Tata Group ('the Group') holds 38.65% stake in IHCL through Tata Sons Limited and other Group companies/trusts. The Group has demonstrated its support to IHCL from time to time by subscribing to various fund raising activities of the company. The Tata Group lineage also imparts considerable financial flexibility in raising funds from the debt market and from banking and financial institutions.

Credit weaknesses

- **Weaker performance of the US properties continues to drag the consolidated performance** – The operating metrics of the US properties (The Campton Place, San Francisco and The Pierre, New York) have been subdued over the past eight quarters. While The Campton Place is making marginal cash profits, The Pierre continues to make losses (cash loss of ~US$ 14.5 million in FY2017), dragging IHCL's consolidated performance. The management is focusing on reduction of losses under the US portfolio, which, if achieved, will improve the credit profile of the company.
- **Delay in Sea Rock asset development constrains profitability** – Requisite permissions to develop the Sea Rock asset in Mumbai, bought by the Group in FY2009, are still pending. As this acquisition was largely debt-funded, the delay in development has led to increase in cost of the asset, impacting the profitability and credit metrics. However, IHCL is planning to retire the entire asset related debt from the proceeds of the recently concluded equity rights issue. This will reduce the interest burden and improve profitability.
- **Profitability and debt coverage, though improving, continues to remain sub-par for the rating category** – Weak performance of the overseas properties and investments (primarily in Belmond Limited; liquidated fully in FY2017) has been constraining IHCL's profitability (as measured by Return on Capital Employed, or RoCE, of 5.4% in FY2017, on a consolidated basis). IHCL's debt coverage indicators, though improved over the levels a year ago, continued to remain stretched as of March 31, 2017 with interest cover of 1.89x (PY: 1.48x), Total Debt/OPBDITA of 5.68x (PY: 8.17x) and Net Cash Accruals/Total Debt of 6% (PY: 2%). Post retirement of debt from the proceeds of recently concluded rights issue, the profitability and the debt coverage metrics are expected to improve.
- **Possible loss of license to operate Taj Mahal Hotel, New Delhi, or an increase in license fee in the ensuing fresh auction as well as potential increase in the rentals for the Mumbai Port Trust land (on which the Taj Mahal Palace, Mumbai, is located) could impact operating margin** – As the license to operate the Taj Mahal Hotel, New Delhi (known as Taj Mansingh), has expired and the Supreme Court of India has allowed the New Delhi Municipal Council (NDMC), the land owner, to proceed with the fresh auction for the property, there exists an uncertainty around the continuation of the said property under IHCL. Taj Mansingh accounted for ~8% of IHCL's standalone revenues and EBITDA for FY2017. Any loss of license or an increase in license fee post the auction could impact IHCL's profitability. Furthermore, there is a long-pending lease rental related dispute with Mumbai Port Trust (MPT), wherein MPT has demanded an additional rental of Rs. 344.50 crore for the period FY2007–FY2017. The matter is sub-judice and any adverse outcome could impact IHCL's liquidity.
- **Cyclical industry, vulnerable to general economic slowdown and exogenous shocks (geo-political crises, terrorism, disease outbreaks, etc.)** – Following a prolonged down cycle, the Indian hospitality industry has started witnessing significant improvement in operating metrics from FY2016. This is expected to lead to pick up in new project announcements over the medium term, strengthening the supply pipeline, which could constrain improvement in operating metrics.

Analytical approach: For arriving at the ratings, ICRA has analysed the consolidated business and financial profile of IHCL.

Links to applicable criteria:
[Rating Methodology for Entities in the Hotel Industry]

About the company:
Incorporated in 1902 by Mr. Jamshed N. Tata of the Tata Group, IHCL is India's largest hospitality company. IHCL and its subsidiaries are collectively known as the 'Taj Hotels Palaces Resorts and Safaris' (earlier known as 'Taj Hotels Resorts and Palaces'). Taj Hotels Palaces Resorts and Safaris comprises 137 hotels at over 60 locations across India and 10 countries (Maldives, Nepal, Zambia, Malaysia, UK, USA, Bhutan, Sri Lanka, South Africa, and the UAE). IHCL's total room inventory, which stood at 16,759 rooms and 136 hotels as of March 2016, decreased marginally to 16,675 rooms and 134 hotels as of March 2017 (16,825 rooms and 137 hotels as of August 2017). The company proposes to add another 11 properties with 871 rooms during FY2018, of which only one property (75 key resort at Andaman) is being developed directly under IHCL. While eight of the properties are under management contracts, the rest are being developed through subsidiaries ('Ginger', under Roots Corporation Limited). The company anticipates future growth in revenues to be derived from management contracts.

Taj Hotels Palaces Resorts and Safaris has set out to rebrand its hotels into one among 'Taj Hotels', 'Taj Palaces', 'Taj Resorts', and 'Taj Safaris', depending upon the location of the property. As on date, the hotel portfolio is grouped into four distinct business segments—luxury (Taj), upper upscale (Vivanta), upscale (Gateway), and economy/budget (Ginger). While 'Ginger Hotels' will continue as they are, the other hotels will undergo rebranding. Of these, the luxury properties in metro and key leisure destinations are largely in the books of IHCL, while the rest are held through subsidiaries and associates. The Group also operates a number of properties on pure management contracts, a business model that is expected to increase significantly over the medium term.

During FY2017, IHCL (standalone) posted an operating income (OI) of Rs. 2,391.25 crore (PY: Rs. 2,267.85 crore) and profit after tax (PAT) of Rs. 141.94 crore (PY: Rs. 84.15 crore). During FY2017, IHCL (consolidated) posted an OI of Rs. 4,010.26 crore (PY: Rs. 4,023.02 crore) and a net loss of Rs. 45.60 crore (PY: Rs. 203.21 crore).

During Q1 FY2018, IHCL reported 10.4% y-o-y growth in standalone revenues to Rs. 523.85 crore with a PAT of Rs. 6.86 crore. For its consolidated revenue, IHCL reported a 4.2% y-o-y decline to Rs. 907.30 crore with a net loss of Rs. 29.71 crore during Q1 FY2018.

Key Financial Indicators (Audited)

Consolidated	FY2016	FY2017
Operating Income (Rs. crore)	4,023.02	4,010.26
Adjusted PAT (Rs. crore)	(203.21)	(45.60)
OPBDIT/ OI (%)	13.8%	15.2%
RoCE (%)	3.4%	5.4%
Total Debt/ TNW (times)	1.37	1.07
Total Debt/ OPBDIT (times)	8.17	5.68
Interest coverage (times)	1.48	1.89
NWC/ OI (%)	-9.4%	-6.6%

OI: Operating Income; 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); NWC: Net Working Capital

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years:

Table:

S. No.	Instrument	Current Rating (FY2018)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as on June 30, 2017 (Rs. crore)	Date & Rating	Date & Rating in FY2017	Date & Rating in FY2016	Date & Rating in FY2015
					October 2017	October 2016	November 2015	November 2014
1	Non-convertible Debentures	Long-term	1,600.00	800.00	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
2	Commercial Paper	Short-term	-	-	-	-	-	[ICRA]A1+ withdrawn

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	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE053A07174	NCD 1	18-Nov-2011	10.10%	18-Nov-2021	300.00	[ICRA]AA (Stable)
INE053A07166	NCD 2	27-Jul-2011	9.95%	27-Jul-2021	250.00	[ICRA]AA (Stable)
INE053A08057	NCD 3	09-Dec-2009	9.86%	09-Dec-2019	250.00	[ICRA]AA (Stable)

Source: IHCL

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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