

Royal Orchid Hotels Limited

August 29, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Term loan	10.0	46.0	[ICRA]BBB (Stable); assigned/outstanding
Total	10.0	46.0	

*Instrument details are provided in Annexure-1

Rating action

ICRA has assigned the long-term rating of [ICRA]BBB (pronounced ICRA triple B) to Rs. 46.0-crore (enhanced from Rs. 10.0-crore) enhanced term loan facilities of Royal Orchid Hotels Limited (ROHL/ the company). The outlook on the long-term rating is stable.

Rationale

The assigned rating factors in the extensive experience of the company's promoter in the hotel industry supported by a professional management team, its well-diversified hotel portfolio spread across various price-points (5/4-star, budget and resorts) in key markets in India and its asset light model of operations, involving operations through leased properties and management contracts. Continued improvement in ROHL's top line (with 8.3% YoY growth in FY2018) supported by Revenue per room (RevPAR) improvement, high growth in management income, cost rationalisation, and reduction in interest costs have supported ROHL's financial turnaround. The company reported consolidated profits in FY2018, following six years of losses.

Over the past years, ROHL has added 37 properties through management and franchise contracts, building up its portfolio to 3,294 keys (and 47 properties) with a net asset base of Rs. 295.2 crores as on March 31, 2018. While the focus continues to be on expanding through management contracts, the company is expected to commence operations of three leased hotels (leased) by FY2020, which is expected to provide sizable boost to its top line. While scale-up through managed and leased properties provides rapid low-cost expansion opportunities, it coupled with presence across price-points, reduces volatility to an extent and lowers breakeven.

ROHL witnessed its peak debt of Rs. 293 crores in FY2012, with debt availed by the company for supporting construction of hotels in Hyderabad, Ahmedabad, Jaipur and Mumbai. However, cost overruns in the Hyderabad hotel and an unfavourable macroeconomic scenario led to substantial losses for the company during FY2012-17. Pruning of its portfolio to sell some high cost assets like the Hyderabad and Ahmedabad properties and a future strategy focussed exclusively on asset-light expansion has supported the company's capital structure since FY2014. Currently, ROHL maintains healthier debt and coverage indicators with total debt/net worth and total debt/OPBITDA at 0.5 times and 2.9 times respectively as on March 31, 2018. Low-capital intensive expansion plans are expected to support the company in maintaining its debt indicators going forward also.

The rating is constrained by the high concentration of the company's revenues on the Bangalore region (56% of revenues in FY2018) and the high dependence on online travel agencies (OTA) (~29% contribution in FY2018) for sourcing room nights. While the company has witnessed improvement in profit margins over the past two years (with OPM improving to 19% in FY2018, from 15.1% in FY2017), profits continue to be significantly below past peaks and potential steady state margins. While the expected expansion into other regions is expected to provide revenue diversification to some extent,

with key properties located in Bangalore, Bangalore will continue contributing sizably to revenues. As with any player in the industry, ROHL is also exposed to seasonality and cyclicity; and is vulnerability to risks such as geopolitical disturbances, disease outbreaks and consequent travel advisories, inherent to the industry.

Outlook: Stable

ICRA believes that the company will continue to benefit from the extensive experience of its promoters, expansion through asset light model and continued improvement of the domestic hotel industry. The outlook maybe revised to positive if the RevPAR witnesses sizable growth, margins witness substantial expansion and significant revenue diversification supports revenue visibility. The outlook may be revised to negative if the cash accruals are lower than expected, or if any major debt-funded capital expenditure, or substantial cash outflows, weakens liquidity.

Key rating drivers

Credit strengths

Experienced promoters and professional management team with more than four decades of experience: ROHL is supported by its experienced promoters with more than four decades of experience in the hotel industry. With the company aggressively expanding through its asset light model, guidance from the promoters and professional management has aided the company in swift stabilization of operations of newly added properties.

Asset light model of expansion using management contracts and leased property: Given its past experience with building capex intensive properties, over the last 4-5 years ROHL has followed an asset light model of expansion, using leased properties, and management contracts. Of the group's 47 operational properties, only one hotel is fully owned, four are held under subsidiaries, five are leased from local builders / Government, , seven are under franchise agreements and 30 are under management contracts, limiting the company's net fixed asset base to Rs. 295.2 crores as on March 31, 2018 for 3,294 rooms. Through this diverse model, ROHL is expected to ramp up its scale rapidly at low capital investments, lowering breakeven.

Portfolio comprising of a wide range of hotels across price points: ROHL has a healthy mix of brands catering to various segments of customers, which helps it to reduce the impact of industry cyclicity to an extent. Going forward, the company is expected to expand under its budget brand, Regenta Inn, in tier II cities, focusing on the midscale business traveller.

Financial profile characterized adequate capitalization and coverage indicators, low debt funded capex plans provides further comfort: The company reported revenue growth of 8.3% YoY in FY2018 to Rs. 196.2 crores from Rs. 181.2 crores in FY2017 supported by improvement in RevPAR (grew by 5.8% in FY2018) across its key properties. Following over six years of net losses, ROHL witnessed positive net profit margin of 1.2% in FY2018, supported by improving top line and lower interest cost. The company's total debt/net worth stood at 0.5 times as on March 31, 2018. Coverage indicators are also adequate with total debt/ OPBITDA and interest coverage at 3.0 times and 2.4 times respectively as on March 31, 2018. With improving cash accruals supported by growing top line and expanding margins, total debt/ net worth and total debt/ OPBITDA is expected to moderate over the next two-three years.

Credit challenges

High revenue (56% in FY2018) concentration on the Bangalore market: With its key revenue generating properties loacted in Bangalore, ROHL derives 56% of its revenues from the city. With ARR in the range of Rs. 3,500- 6,000, across its four hotels in Bangalore, Bangalore accounts for 14% of total number of ROHL's rooms, 56% of revenues and 44% of gross profits (FY2018). While healthy demand is expected to support its occupancy, high competition will constraints

Average room rate (ARR) growth opportunities. However, ROHL's diversification into new locations to broaden revenue mix is expected to mitigate the same to an extent going forward.

High revenue contribution from OTA caps margin expansion: While the revenue contribution from OTA was low at 14% and 18% in FY2016 and FY2017 respectively, it increased sharply to 29% in FY2018. The company pays upto ~20% as commission for bookings done through the OTAs, thereby capping ARR and margins. Going forward, the company is expected to cap its revenues from OTAs to 30% and focus on expansion through other channels such as ROHL's website, loyalty program, etc.

Cyclical industry, vulnerable to general economic slowdown and exogenous factors: The company is exposed to inherent cyclicality of the hotel industry and exogenous factors such as geo-political crisis, terrorist attacks, disease outbreak, etc. ICRA maintains a stable outlook for the industry with 5-6% growth in RevPAR supported by improving ARR in FY2019.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria:

[Corporate Credit Rating Methodology](#)

[Rating Methodology for hotel industry](#)

About the company

The Royal Orchid Group of Hotels has a portfolio of 47 operating hotels with a collective inventory of 3,294 rooms located in various cities (~34 cities) spread across the country. Of this portfolio, 195 rooms (5.9%) are owned (building is owned, land is on lease), 349 rooms (10.6%) operated under subsidiaries, 433 rooms (13.1%) are leased (warm shell in most cases), 420 rooms (7 hotels, 12.7%) under franchisee agreements, while the balances 1,897 (57.5%) rooms are operated under management contracts. The company has the following brands: 5 star (Royal Orchid), 4 star (Royal Orchid Central, Regenta Hotels), Service Apartment and budget hotel (Regenta Inn).

Hotels are spread across a wide spectrum ranging from 5-star to budget category hotels focussed on domestic business travellers. The group's strategy is to focus on low set-up costs through a combination of ownership and asset light properties (leased) leading to higher returns.

Key financial indicators (Consolidated, audited)

	FY2017	FY2018
Operating Income (Rs. crore)	181.2	196.2
PAT (Rs. crore)	-4.6	2.4
OPBDIT/OI (%)	15.1%	19.0%
RoCE (%)	5.7%	8.2%
Total Debt/TNW (times)	0.5	0.5
Total Debt/OPBDIT (times)	4.2	2.9
Interest coverage (times)	1.7	2.4

Source: company

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

		Current Rating (FY2019)			Chronology of Rating History for the Past 3 Years		
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating August 2018	Date & Rating in FY2018	Date & Rating in FY2017	Date & Rating in FY2016
1	Term Loan	46.0	100.7	[ICRA]BBB (Stable)	-	-	-

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	March 21, 2018	NA	2030	46.0	[ICRA]BBB (Stable)

Source: BFPL

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