

Lemon Tree Hotels Limited

Transition to asset-light & Aurika MIAL to push growth

Lemon Tree Hotels Ltd. (LTH) is a leader in the midscale-economy segment with a 13.6% market share by branded room inventory. As of Dec'23, the Company has an operational inventory of 9,687 rooms, including a recent addition of a 669 rooms– Aurika MIAL. LTH is now expanding its presence in the Luxury and Upscale segment. The Company owns 5,759 rooms and manages 3,928 rooms with a robust pipeline of 3,677 rooms through Management contracts as of Dec'23. The Company is aggressively adding Managed rooms to achieve its target of 70% managed inventory and total rooms of ~20,000+ by FY28. We believe Lemon Tree Hotels is well-positioned to benefit from the growth in the Indian Hospitality Industry due to the favourable demand scenario. The Company has industry-leading EBITDA margins of ~51% on the back of cost rationalization at granular levels. With no major upcoming capex, the Company is expected to be debt-free by FY28.

Potential in Luxury and Upscale offerings

The introduction of Aurika MIAL marks the Company's strategic entry into the upscale segment. This segment, which accounts for 50% of the market by rooms, offers lucrative opportunities in terms of occupancies and Average Room Rates (ARR) and higher management fees. Our projections suggest that Aurika MIAL alone could contribute 20%+ to the Company's EBITDA by FY26. This highlights the substantial earning potential of this brand, positioning it as a key driver of growth and profitability for the Company in the upscale hospitality segment.

Aggressive Repricing Potential

The hospitality industry is a cyclical industry, and it is currently positioned in the upcycle stage. This is evident as the demand growth (CAGR), estimated at ~10%, is outpacing the supply growth (CAGR), which is ~7%. This demand-supply gap is expected to persist for the foreseeable future, providing the Company with the opportunity to further improve its ARR.

Maintain leadership in the Midscale segment

LTH holds a strong position in the midscale/economy hotel sector with a 13.6% market share, distinct from upscale brands. With 2.8 Mn unbranded hotels potentially convertible to branded properties, there's a substantial growth opportunity. This presents LTH with the chance to further establish itself by expanding into the midscale/economy market segment, solidifying its dominance and capturing a larger share of the market.

View & Valuation

LTH is a leader in the midscale & economy segment, transitioning to an asset-light model through management contracts. The inauguration of Aurika MIAL is a milestone expected to boost both top and bottom-line performance. With demand set to outpace supply in the industry, occupancy and ARR visibility improve. We initiate coverage on LTH with a BUY rating and a target price of Rs. 160 using SOTP valuation method, indicating a 12.6% upside potential.

26th February 2024

BUY

CMP Rs. 142

TARGET Rs. 160 (+12.6%)

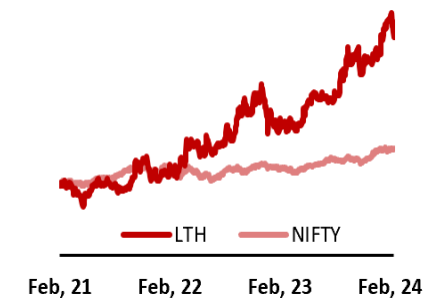
Company Data

Bloomberg Code	LEMONTRE IN
MCAP (Rs. Mn)	1,12,464
O/S Shares (Mn)	792
52w High/Low	147 / 73
Face Value (in Rs.)	10
Liquidity (3M) (Rs. Mn)	880

Shareholding Pattern %

	Dec-23	Sep-23	Jun-23
Promoters	23.21	23.28	23.6
FII's	22.82	24.82	25.48
DII's	15.00	13.41	10.38
Non-Institutional	38.98	38.48	40.54

LTH vs Nifty



Source: Keynote Capitals Ltd.

Key Financial Data

(Rs Mn)	FY23	FY24E	FY25E
Revenue	8,750	10,703	13,596
EBITDA	4,476	5,167	7,012
Net Profit	1,656	2,027	3,480
Total Assets	36,958	39,058	40,114
ROCE (%)	13%	13%	18%
ROE (%)	15%	14%	21%

Source: Company, Keynote Capitals Ltd.

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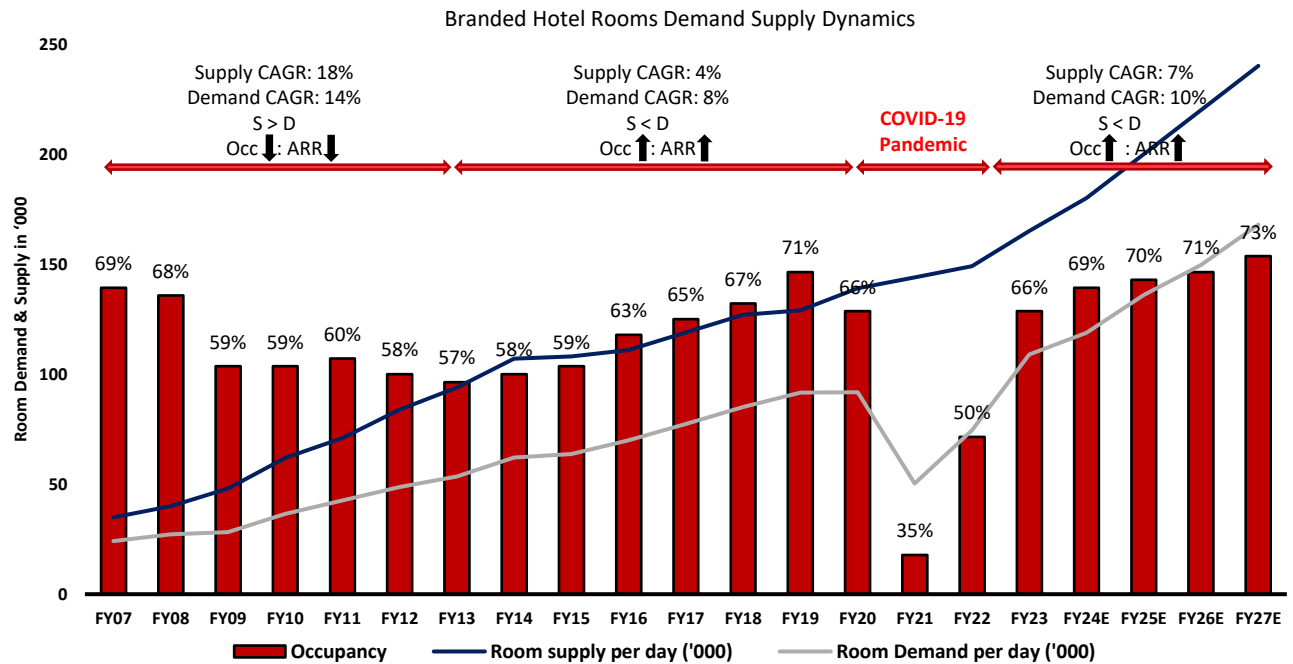
Hospitality Industry

The hospitality and tourism industry encompass a broad spectrum of economic activities that directly or indirectly support or rely on travel and tourism. This includes establishments such as Hotels & Resorts, Restaurants & Catering, Night Clubs & Bars, Spas & Wellness facilities, etc. In FY22, this sector contributed ~6% to the total GDP of the country. The World Travel and Tourism Council (WTTC) has projected a growth rate of 8.4% for the Indian tourism industry over the coming decade.

Expenditures within this sector are deemed discretionary, and given the trends of mounting urbanization, a burgeoning young population, and rising disposable income, it is reasonable to anticipate a substantial surge in these expenditures.

Demand-Supply Growth

As per Horwath in FY 23, India has ~171,000 rooms affiliated with branded hotel chains, with a demand for ~112,000 branded rooms. The Current inventory pipeline suggests that room supplies will elevate to around 230,000 by the end of FY27. In periods marked by demand CAGR surpassing that of supply, room occupancies and ARR experience an upward trend, reaching elevated levels. Conversely, these metrics decline or stabilize when demand registers a lower growth rate than supply.



When the CAGR of demand > CAGR of supply, Occupancies and ARR trend upwards, and vice-versa.

Source: Hotelivate & Horwath, Keynote Capitals Ltd.

Occupancy had been on a rising trend during the FY13-FY19 period when demand outpaced supply. The chart reflects the improving occupancy scenario and the potential for occupancy growth in the foreseeable future as demand is expected to outpace supply in FY24E – FY27E. Improving occupancies is expected to create a base for improvement ARR.

RevPAR (Revenue Per Available Room) is a key performance metric in the hospitality industry, calculated by dividing total room revenue by the total number of available rooms.

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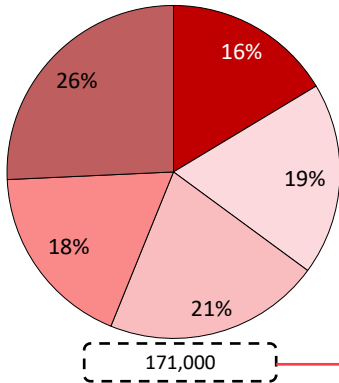
Based on market positioning, rooms can be segmented under various categories:

Luxury and Upper Upscale 5-star deluxe and luxury hotels with highest room rates	Upscale 5-star and 4-star hotels positioned and priced moderately
Upper Midscale 4-star and 3-star hotels with certain lesser conveniences	Midscale Typically, 3-star hotels with a lower standard of services
Economy and Budget 2-star hotels focused on price-conscious travellers	

Segment	ARR	Occupancy %	RevPAR
5 star deluxe	12,923	68%	8,723
5 star	7,275	67%	4,882
4 star	5,481	67%	3,667
3 star	3,885	64%	2,483
2 star	3,092	61%	1,868
Overall	6,869	66%	4,540

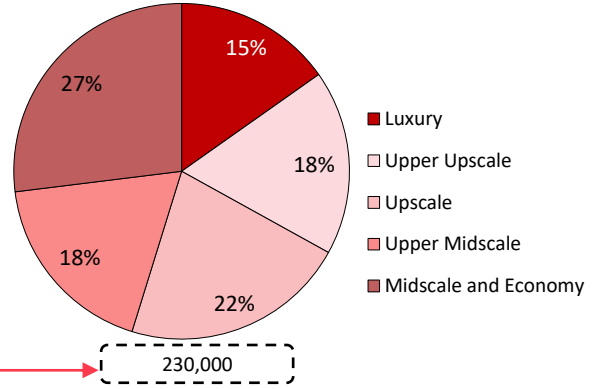
Source: Hotelivate, Keynote Capitals Ltd
Data for FY23

Room Inventory Distribution (Branded) – FY23



~59,000 rooms:
 7,000 Luxury
 9,000 Upper-Upscale
 14,000 Upscale
 11,000 Upper Midscale
 18,000 Midscale and Economy

Proposed Room Inventory – FY27 (Branded)



Source: Hotelivate, Keynote Capitals Ltd.

In FY23, the branded hotel market experienced significant expansion, marked by the addition of 166 new hotels totalling 14,885 rooms through brand signings (management contracts). In addition, 90 hotels comprising 5,702 rooms undergoing rebranding. Notably, hotel chains strategically targeted tier 2 and 3 cities for signings, leveraging local expertise while simultaneously capitalizing on their established brand names to penetrate lesser tapped markets.

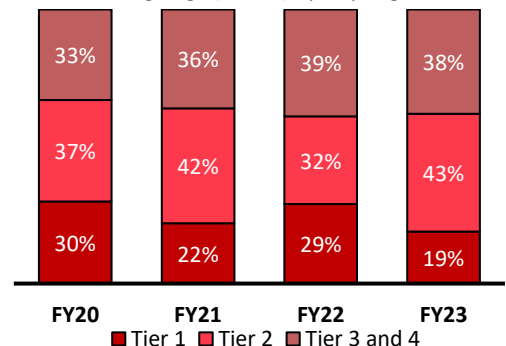
Hotel management contracts is an agreement between owner of a hotel property and a management company to run the business on their behalf. The owner retains ownership and most of the financial risk and reward, while the management company handles day-to-day operations for a fee.

This strategic focus reflects a broader trend observed in the industry, wherein the average room count per property is declining as hotel operators venture into tier 2 & 3 cities where the demand footprint necessitates a smaller room count per hotel.

New Brand Signings by Market Positioning

By Keys	FY20	FY21	FY22	FY23
Luxury	11%	11%	13%	14%
Upscale	35%	37%	32%	41%
Midscale	38%	41%	44%	37%
Economy	16%	11%	11%	8%
Total Rooms	139,000	144,000	149,000	171,000

Brand Signings (rooms) by City Segments



Source: HVS Anarock, Keynote Capitals Ltd.

Key Metrics across Top Indian Cities

Region	Inventory (Rooms)	ARR	Occupancy %	RevPAR
Delhi	14,917	8,013	75%	6,018
Gurugram	6,662	6,793	66%	4,477
Hyderabad	7,465	6,489	73%	4,724
Bengaluru	15,351	7,048	65%	4,581
Mumbai	13,718	9,196	79%	7,228
Pune	6,789	5,446	68%	3,676
Goa	8,805	10,267	69%	7,115
Jaipur	6,557	6,814	62%	4,204
Chennai	9,761	5,679	69%	3,901
Top Cities Total	90,025	7,498	70%	5,305

Top Cities represent ~52% of the total branded inventory room of the industry

Source: Hotelivate, Keynote Capitals Ltd.

Demand Drivers in Top Indian Cities

Weddings and Social Events

The growing preference for domestic travel, specifically for weddings and celebrations, has become a significant driver for the hospitality sector in India. Escalating international travel costs have prompted couples to choose celebrity-style destination weddings within the country, favoring luxury hotels and resorts. This trend has benefitted city hotels, destination resorts and even modest accommodations as the occupancies during such events rise to ~100%, enabling hotels to charge an ARR higher than their normal rates.

Leisure

The leisure sector stands out as a substantial revenue driver, significantly contributing to positive market sentiment. Average Daily Rates (ADRs) in leisure destinations far surpass those in major business cities, with Udaipur commanding Rs. 14K, Goa at Rs. 9.8K, and Himachal Pradesh, Mumbai, and Uttarakhand ranging between Rs. 8.2K to Rs. 8.8K.

It is noteworthy that certain luxury resort ADRs in Rajasthan are nearing the USD 1,000 threshold during peak months. This emphasizes the lucrative potential of the leisure segment and underscores the evolving pricing dynamics in high-demand regions.

Meetings, Incentives, Conventions and Exhibitions (MICE)

The segment primarily caters to corporate needs, covering conferences, training programs, and interactive events. This demand, prevalent throughout the year except during major holidays and March to June, comes with a notable price sensitivity. Business-centric hotels attract MICE demand for training and corporate seminars, while conferences with recreational elements opt for city-center or resort destinations.

Transit/Airline

Crew demand significantly influences hotel occupancy, albeit often at discounted rates. Originating from both international and domestic carriers, major airlines prefer upper-tier hotels, while cost-conscious ones opt for upper-midscale establishments. Concentrated near airports, this demand, though modest, is consistent. Anticipated growth, driven by new airlines in India, emphasizes the sustained demand for strategically positioned hotels catering to crew accommodation.

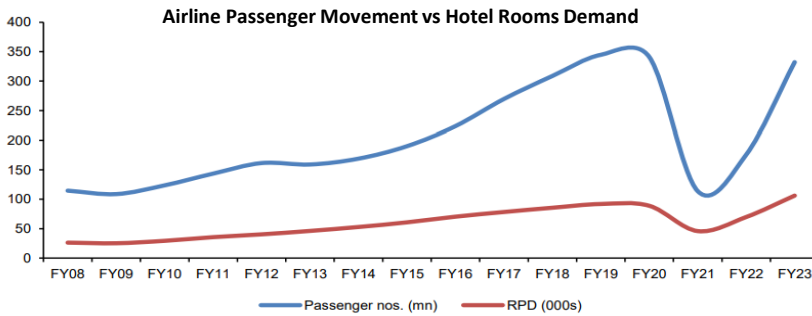
Religious Tourism – An opportunity

As per Hotelivate, India's revered destinations like Amritsar, Varanasi, Rishikesh, Katra, Kedarnath, and Tirupati are shaping the domestic tourism landscape. Post-pandemic, a discernible trend is the rise in spiritual and religious travel, evident in Varanasi attracting 72 Mn tourists, surpassing Goa's visitor count of 8.5 Mn by a factor of eight. Ministry of Tourism data indicates the economic significance, generating nearly Rs. 1.3 Tn in revenue with 1.4 Bn visitors in 2022. This trend spans generations and positively impacts lesser-known cities like Ayodhya, set for a tourism revolution with the inauguration of Ram Mandir. Despite the vast potential, the sector remains largely unorganized, urging stakeholders to recognize and leverage opportunities in developing spiritual and religious destinations.

Factors determining demand

Air Traffic

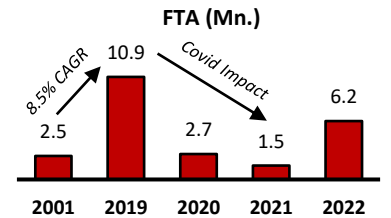
The correlation between air traffic and Room demand per day is paramount in assessing the performance of the hotels. Elevated levels of air travel often signify heightened tourism and business activities, contributing to increased demand for hotel accommodations. Factors such as the number of flights, airline routes, and overall travel trends play a crucial role in influencing the relationship between air traffic and hotel occupancies. Additionally, events like conferences, conventions, and festivals can contribute to variations in hotel occupancies depending on air travel patterns associated with such gatherings.



Source: AAI (Air Traffic Data), Horwath HTL, Keynote Capitals Ltd.

Foreign Tourist Arrivals (FTA)

The influx of international visitors significantly contributes to heightened hotel occupancy rates, thereby positively influencing revenue streams. FTA has consequently grown at a CAGR of 8.5% from 2001-20 as per the Ministry of Tourism. It has taken a dip since COVID-19, and has not yet recovered to pre-COVID levels of ~11 million arrivals in 2019. This is expected to add further demand for hotels in India.



Source: Ministry of Tourism, Keynote Capitals Ltd.

Domestic Demand

According to data from the Ministry of Tourism, domestic travel visits exhibited a robust CAGR of 13.5% between FY01-20. Over this period, domestic travels surged nearly tenfold, from 236.5 Mn visits in FY01 to 2.3 Bn visits in FY20. Estimates suggest that ~2% of domestic visits translate into hotel stays. There is a notable shift in this trend with the emergence of affiliated hotels across various price points in tier 2 & 3 cities, as well as pilgrim centers. As per Horwath, even a modest increase of 0.5% in hotel utilization during domestic visits could result in an estimated 70% occupancy rate for ~50,000 new rooms.

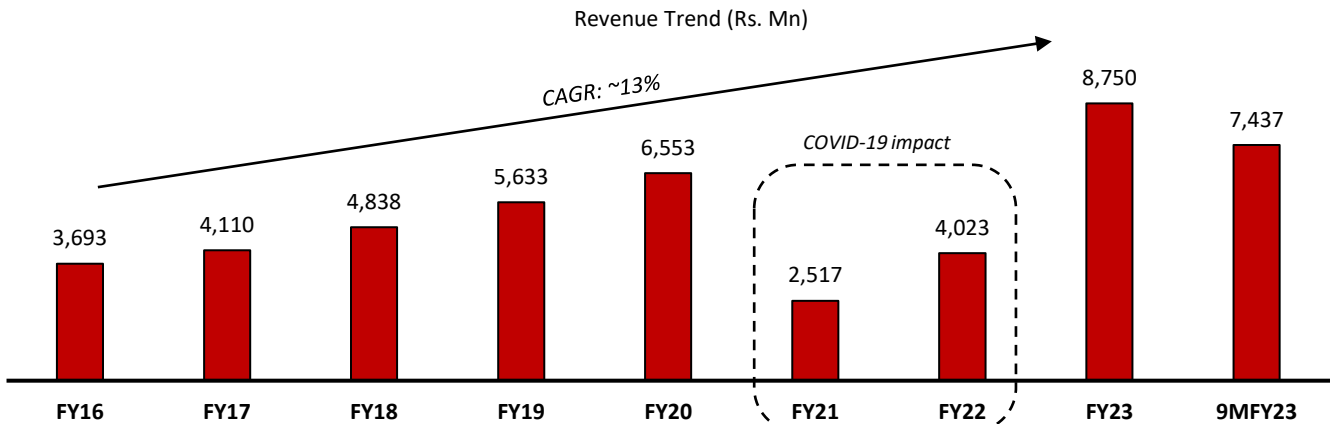
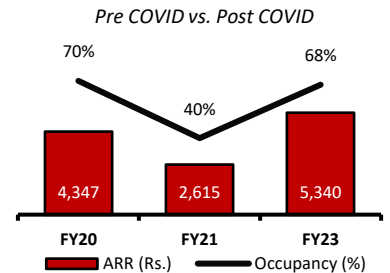
About Lemon Tree Hotels Ltd.

Founded in the year 2002 by Patanjali Keswani, LTH started its operations with its first hotel in 2004 with 49 rooms, and currently, it is the largest hotel chain in the mid-scale segment with 100 hotels and a room inventory of 9,687 rooms. The Company has emerged as the market leader in the midscale segment, and with their brand 'Aurika', they are now targeting the upscale and luxury segment to crown themselves as the largest hotel chain in India. With the recent opening of Aurika in Mumbai with 669 rooms, the Company is set to further improve its ARR and upscale offering.

After going public in 2018, the hotel chain acquired 'Berggruen Hotels Pvt. Ltd.' with 936 owned rooms and 975 managed rooms under its economy brand Keys.

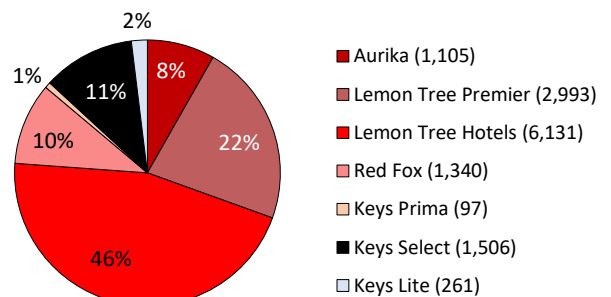
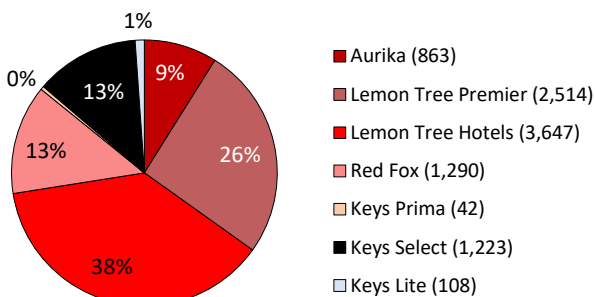
The foray into the management contracts and now the franchise space has helped the Company to significantly boost its growth trajectory by establishing a presence in locations where it has limited to no access while following an asset-light business model. With the Franchise model, the Company is strategically aiming to leverage its brand name and expand its extensive network. Further, the Company is aiming to restructure the existing corporate structure which will result in only two entities instead of three currently.








COVID hit the Hospitality industry severely, but LTH was able to cope with the short-term headwinds and has now reached the pre-COVID ARR and occupancy rates. The Company reclaimed its Pre-COVID levels occupancy and ARR; with the Cricket World Cup, surging demand in MICE and resurgence of foreign and domestic tourists, these metrics are expected to improve further.



Brand wise Room Mix (9MFY24)

Brand wise Room Mix (FY27 expected)



Segment	Brand	Brand	ARR	Occupancy %	RevPAR
Upscale Segment		Aurika	10,740	46%	4,904
Upper Midscale Segment	 	Lemon Tree Premier	6,717	78%	5,262
Midscale Segment	 	Lemon Tree Hotels	5,425	73%	3,942
Economy Segment	 	Red Fox Hotels	4,283	70%	2,998
		Keys	3,514	56%	1,980
		Overall	5,613	67%	4,111

Source: Company, Keynote Capitals Ltd.
Data is average of Q1, Q2 & Q3 FY24

Brand portfolio & distribution

Aurika

LTH, diversified into the upscale segment in FY20 establishing through Aurika. Aurika Hotels and Resorts lay an emphasis on design and are a true reflection of the destination they are located in. Stylishly elegant and featuring new age dining and innovative entertainment options with fitness and wellness facilities, Aurika caters to the customers willing to have a 5 star experience with LTH.

The decision to establish the Aurika brand was driven by a combination of strategic and opportunistic factors. With increasing wallet share of loyal customers seeking upscale accommodations for their leisure or business travel needs, there was a clear gap in LTH's offering that was yet to be addressed adequately.

As of 9MFY24, the operational inventory of Aurika consisted of 808 owned rooms (in Udaipur and Mumbai) and 55 managed rooms (in Coorg). However, with the opening of Aurika MIAL, India's largest hotel with a total of 669 rooms, it is expected to be the standout for Lemon Tree Hotels. The ARR in this segment revolves ~Rs. 11,000, almost 100% premium to the current ARR of LTH, and occupancy around 40%-50%. With the stabilization of Aurika MIAL, the numbers are expected to improve further, pushing the EBITDA of LTH higher.

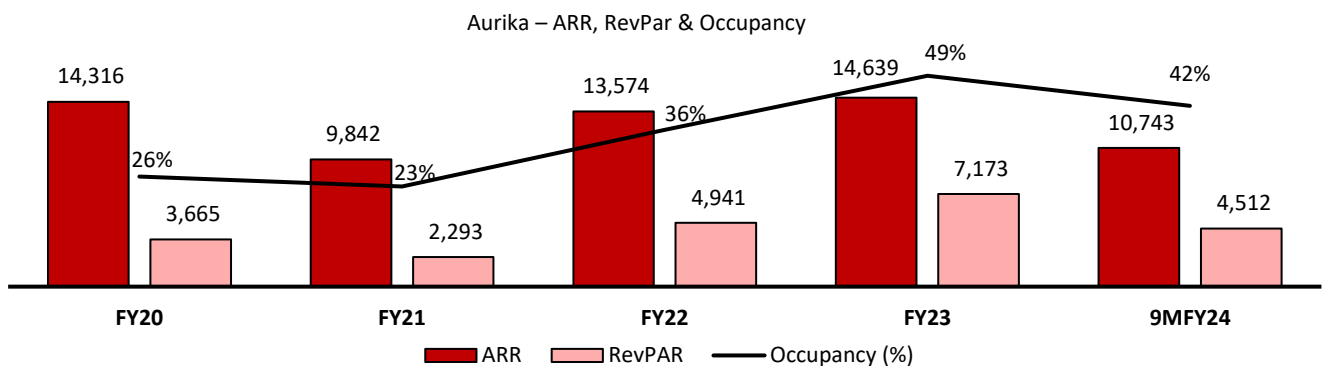
Aurika MIAL (Mumbai)

Aurika MIAL started operations in October 2023 and is the largest hotel in India, with an inventory of 669 rooms. Located right around the Mumbai International Airport, the ARR of this luxury hotel is expected to be in the bracket of Rs. 13,000-15,000. The occupancy reported by the Company in Q3FY24 was ~40%; however, with stabilization in Q4FY24, the occupancy may reach to regular levels of 65%-70%, as a similar trend was observed with Lemon Tree Premier, Mumbai Airport. As the hotel is at its nascent stage, along with the fact that it was launched right in the middle of the festive season (Dussehra, Diwali), keeping inflows in Q3FY24 deflated. However, Q4FY24 could be pivotal moment, showcasing the hotel's true potential as the ARR tends to pick during this period. With the hotel demand anticipated to be robust, this quarter may truly demonstrate the hotel's capabilities.

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The Company has invested ~Rs. 9 Bn in bringing the project to fruition, with ~Rs. 5 Bn sourced from internal accruals and a debt of Rs. 4 Bn. Since the hotel is located in a prime location, it is expected to stabilize soon and turn EBITDA positive by Q4FY24. By FY26, Aurika MIAL is expected to contribute 20%+ to consolidated EBITDA. The cash flows from this property will assist LTH in substantially reducing its debt and attaining a 'debt-free' status.

Currently, under the brand 'Aurika', the Company has 3 hotels with 863 rooms, out of which 2 hotels are owned (incl. of Aurika, Mumbai) by LTH and 1 hotel is managed/franchised. The ARR of Aurika for 9MFY24 stood at Rs. 10,743 with an occupancy of 42%. The ARR and occupancy are set to improve once Aurika, MIAL, is operational at full capacity. Due to the higher ARR in The Aurika brand and an opportunity to increase occupancy, the Company has signed Management/Franchise contracts with 2 properties in Rishikesh and Kasauli, expected to be operational in FY27. These upcoming openings will help the Company make Aurika a recognized brand, which can help it attract more management contracts under this brand, which can significantly increase the management fee income.



Source: Company, Keynote Capitals Ltd.

Lemon Tree Premier

LTH, through Lemon Tree Premier, caters for the upper midscale segment with a total of 18 hotels and 2,514 rooms; these hotels offer plush, spacious interiors with pools, fitness centres, and spas, along with meeting spaces and a business centre. These are entry-level 4-star hotels that provide premium and personalized services to customers. Effectively, at an ARR of ~Rs. 6,000-7,000, these hotels provide their customers with a 5-star experience.

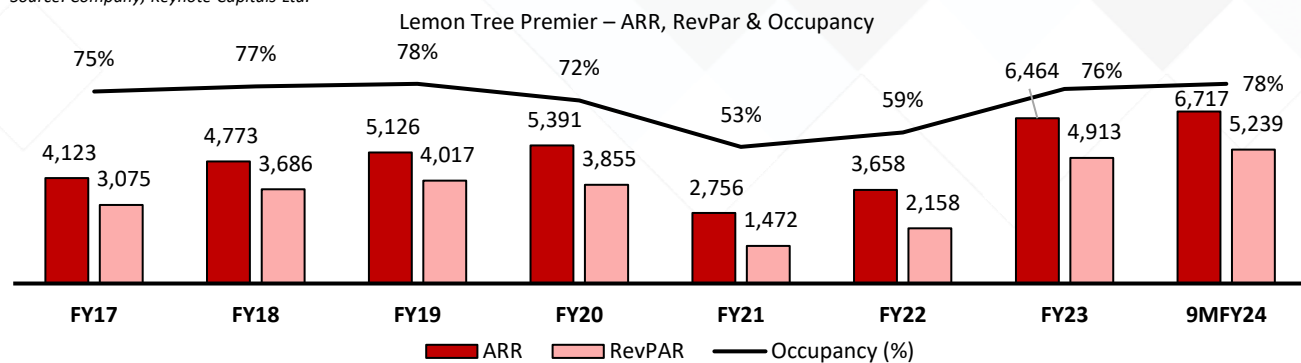
The idea behind the operation of Lemon Tree Premier is to provide 90% of the services and amenities typically offered by a standard 5-star hotel at a 70% cost. The excluded 10% of offerings, which account for about 30% of the expenses, may not be essential for all customers. This strategic approach enables the Company to maintain a high standard of service without compromising on quality while simultaneously achieving cost reduction.

With an average occupancy of 78% and ARR of Rs. 6,717 as of 9MFY24, the Premier range becomes a significant contributor to the earnings of the Company due to the higher occupancies and already saturated ARR. Additionally, the Company has Management and Franchise contracts in its pipeline, enabling it to leverage the brand image of its most highly regarded hotels.

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Category	Owned	Leased	Managed/Franchised	Total
Operational	1,442	161	911	2,514
Pipeline	-	-	479	479
Total	1,442	161	1,390	2,993

Source: Company, Keynote Capitals Ltd.



Source: Company, Keynote Capitals Ltd.

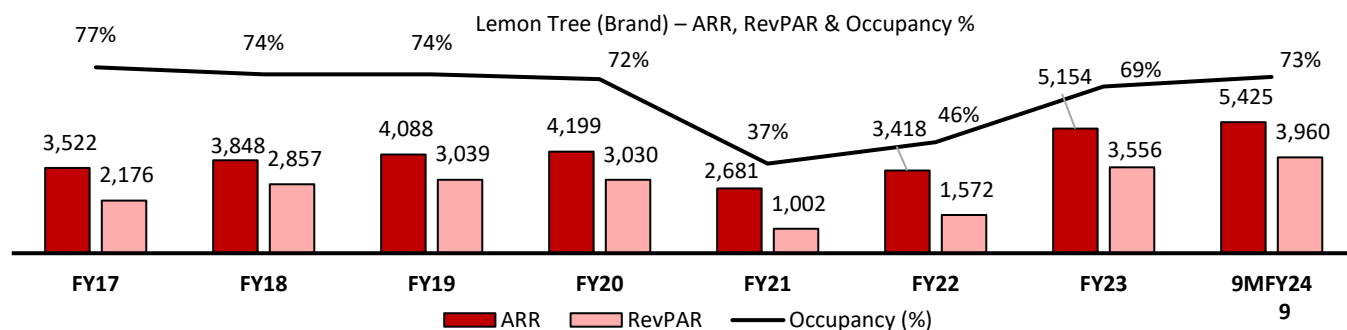
Lemon Tree Hotels

LTH, the flagship brand of the Company, caters to the midscale segment. It is the main enabler for LTH, with a market share of ~20% of the branded midscale and economy segment. With an inventory of 3,647 rooms in 53 hotels, the highest out of all brands, Lemon Tree Hotels is the core product offering of the Company. 'Stylish Business Hotels' at an 'Unbeatable Price' is the locus of this brand.

The brand has consistently maintained an impressive occupancy of ~ 75% from 2015 till pre-COVID. As of 9M FY24, the ARR stood at Rs. 5,425 with an occupancy of 73%. The Company aims to further expand its footprint through Management/Franchise contracts, adding 37 hotels totalling 2,484 rooms, the highest in the pipeline amongst all the brands. In addition, an upcoming property – Lemon Tree Hotel, Shimla, a 69 room property fully owned by the Company with a budgeted capex of Rs. 800 Mn is expected to commence in FY26.

Category	Owned	Leased	Managed/Franchised	Total
Operational	1,241	321	2,085	3,647
Pipeline	69	-	2,415	2,484
Total	1,310	321	4,500	6,131

Source: Company, Keynote Capitals Ltd.



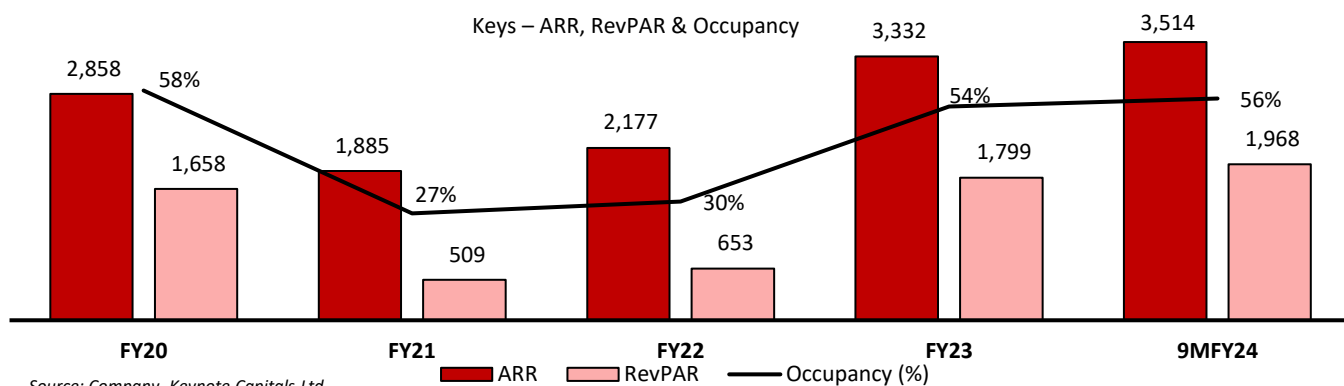
Source: Hotelivate, Keynote Capitals Ltd.

Keys (Prima, Select, Lite)

In 2019, LTH acquired 'Berggruen Hotels Pvt. Ltd.', which has hotels in the Economy to Upper Midscale segment under the brand name Keys. While 'Keys Prime' is equivalent to the offering of Lemon Tree Premier, 'Keys Select' is considered at par with Lemon Tree Hotels. This brand comprises 15%-16% of the total room inventory of the Company as of 9M FY24. Further, through franchisee contracts, 491 rooms are in the pipeline. During 9M FY24, the occupancy and ARR of Keys stand at ~56% and Rs. 3,514, respectively.

Acquired shortly before the onset of COVID-19, the Keys portfolio is up for renovation. ~60% of this brand's portfolio is located where quick EBITDA payback is expected. Renovation budget of Rs. 0.5 Mn per room has been allocated for these properties. The remaining hotels will undergo upgrades, aligning them with Lemon Tree's standards, with an allocated budget of ~Rs. 0.15 Mn per room.

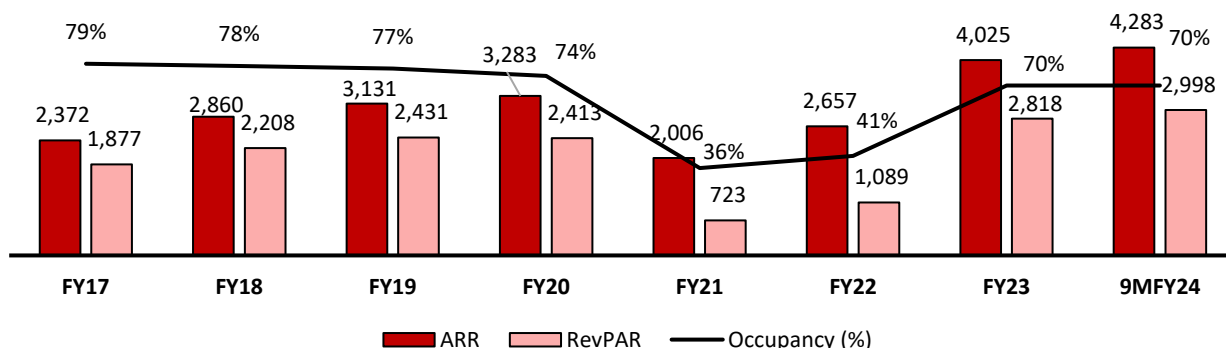
Category	Owned	Leased	Managed/Franchised	Total
Operational	936	-	437	1,373
Pipeline	-	-	491	491
Total	936	-	928	1,863



Red Fox Hotels

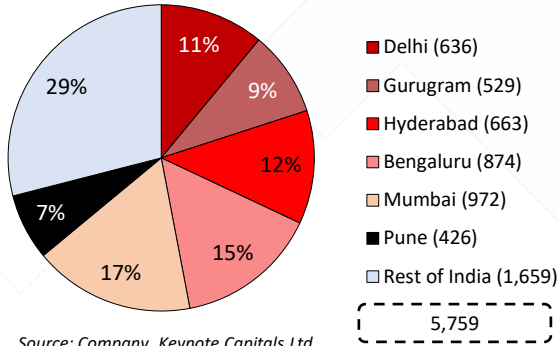
This is another brand in the economy segment that offers all the basic facilities and mainly caters to price-conscious travellers. The current ARR of Red Fox during 9M FY24 stood at Rs. 4,283 with an occupancy of ~73%. Currently, the Company has 1 hotel project in the pipeline with 50 rooms under Red Fox Hotels.

Red Fox – ARR, RevPAR & Occupancy



Geographical Distribution

Geographical Owned Room Mix



Source: Company, Keynote Capitals Ltd.
Data as of Dec'23

Region	ARR	Occupancy %	RevPAR
Delhi	6,101	77%	4,698
Gurugram	5,258	71%	3,716
Hyderabad	6,027	82%	4,962
Bengaluru	4,935	67%	3,290
Mumbai	8,117	75%	6,115
Pune	5,077	69%	3,520
Rest of India	4,961	63%	3,109

LTH operates across 56 cities in India, and currently, 71% of its total rooms (owned and leased) are located in tier-I cities. The Company has successfully established its brand as a leading business hotel in these cities, evident from the high occupancies achieved.

In **Mumbai**, occupancy stood at 87% in H1 FY24 (pre-opening of Aurika). With the opening of Aurika, Skycity, the Company anticipates it to improve further, accompanied by a rise in ARR, potentially reaching Rs. 9,000. LTH's strategic property locations around Mumbai Airport and Kalina have contributed to a higher RevPAR growth compared to the industry average. However, currently, the same is not at the desired levels due to the recent opening of Aurika. It is expected that once Aurika MIAL stabilizes, the numbers will approach the desired levels.

In contrast, the RevPAR in **Bengaluru** is among the lowest in LTH's portfolio due to majority of the portfolio being in the economy and entry-level midscale segment, via their Keys brand. Further, renovations are under progress due to which certain hotels are expected to remain shut. Post renovation of this portfolio, RevPAR is expected to inch upwards, aligning with the city's growing market driven by its status as the IT hub of India.

Delhi witnessed a decline in RevPAR in H1FY24 due to the temporary closure during the G20 summit, redirecting major business to 5-star deluxe hotels. However, that was a short-lived hitch. The business has returned to normal levels in Q3FY24. With repricing on the cards, ARR is expected to further boost in FY25.

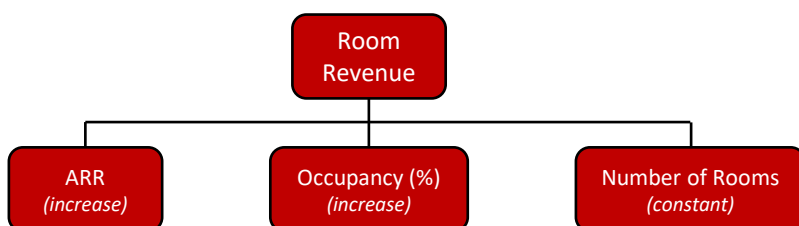
Despite not being at its best efficiency in multiple cities, the Company remains focused on tier I cities and is now strategically foraying into tier II and III cities through Management/Franchise contracts, leveraging its well-established brand from tier I city operations.

Revenue Mix (%)

	FY17	FY18	FY19	FY20	FY21	FY22	FY23
Room Revenue	66%	71%	70%	75%	78%	75%	77%
Management Fees	1%	1%	1%	1%	3%	4%	4%
Food & Beverage	22%	18%	20%	15%	13%	14%	13%
Service Income	11%	10%	9%	9%	5%	6%	5%
Total Revenue (Rs. Mn)	4,121	4,843	5,495	6,694	2,517	4,022	8,750

Source: Company, Keynote Capitals Ltd.

Drivers of Room Revenue



The Company strategically manages its Revenue per Available Room (RevPAR) through a focus on key performance indicators, like Occupancy, Average Room Rate (ARR), and room inventory. Maintaining a stable room inventory, positions the Company to drive revenue growth primarily through optimizing ARR and occupancy metrics.

In FY22, the Company focused on increasing its ARR to filter out some price-elastic customers. In FY23, it focused on capitalizing on its occupancy and replacing the customers lost due to the last repricing. The same is evident in its occupancies in different markets, which are more than 70% in all its major markets. The Company increased its ARR but marginally less than its competition, churning out a RevPAR equivalent to them.

Furthermore, the Company, recognizing the importance of customer loyalty, has implemented a loyalty program. This program aims to enhance customer offerings, fostering increased customer retention and contributing to stabilized occupancy rates.

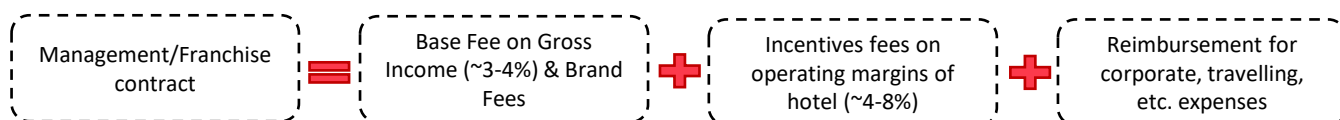
The Company is shifting its customer base from the airline & corporate segment to retail segment, which gives it the power to dynamically price the properties and also reduce dependence on huge corporates for its business. In FY25, the Company plans to raise the ARRs strategically, taking advantage of the fact that its current customers are not highly sensitive to price changes. This would allow them to leverage repricing to its maximum benefit.

Management and Franchise Contracts

Managing and branding hotels is far more profitable compared to owning individual assets. LTH engages in management contracts, emphasizing an asset-light model with third-party owners. This approach allows the Company to deliver quality management and branding services to asset owners, resulting in fee revenues for the Company. Additionally, it facilitates the expansion of LTH's network and brand presence across diverse geographies in India.

The Company's management fee structure comprises three components:

- 1. Management Fees:** These are paid by third-party hotel owners to Carnation Hotels, a 100% subsidiary of LTH.
- 2. Brand Fees:** These are directly paid to LTH by third-party hotel owners.
- 3. Management and Brand Fees:** Paid to LTH by Fleur Hotels, an asset-owning company and a joint venture (JV) with Dutch pension fund APG. LTH holds a ~59% stake in Fleur Hotels.



In FY23, management fees in Carnation were ~Rs. 360 Mn. With the ongoing expansion plans, the Company projects these fees to reach Rs. 500 Mn in FY24, Rs. 750 Mn by FY25, and subsequently stabilize within the range of Rs. 1.3-1.5 Bn.

The Company is strategically planning an expansion, aiming to have ~70% of its hotels managed or franchised by FY28. Its long-term strategy focuses on managing and branding hotels due to their high return potential and core competence. Initial hotel ownership was undertaken to build a brand and ensure product coherence.

Additionally, the goal is to achieve a total operational inventory of 20,000 rooms across ~300 hotels by the end of FY28. Quarter by quarter, the Company is consistently adding more rooms to its pipeline through management contracts. In Dec'23, LTH is operating 5,759 owned rooms and managing 3,928 rooms, the goal of reaching 20,000+ rooms by FY28 is ambitious.

The Company is venturing into less-explored markets through these contracts, allowing them to tap into markets where local franchise partner has a better understanding, leveraging its existing brand strength.

	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24	Q3FY24
Pipeline as on beginning of quarter	1,686	1,867	2,051	2,547	2,984	3,354
(+) Additions to Pipeline	240	332	538	548	639	621
(-) Inventory commissioned/(decommissioned) during the quarter	59	148	42	109	269	298
Pipeline as of end of quarter*	1,867	2,347	2,547	2,986	3,354	3,677

Source: Company, Keynote Capitals Ltd.

*Pipeline of Management contract only.

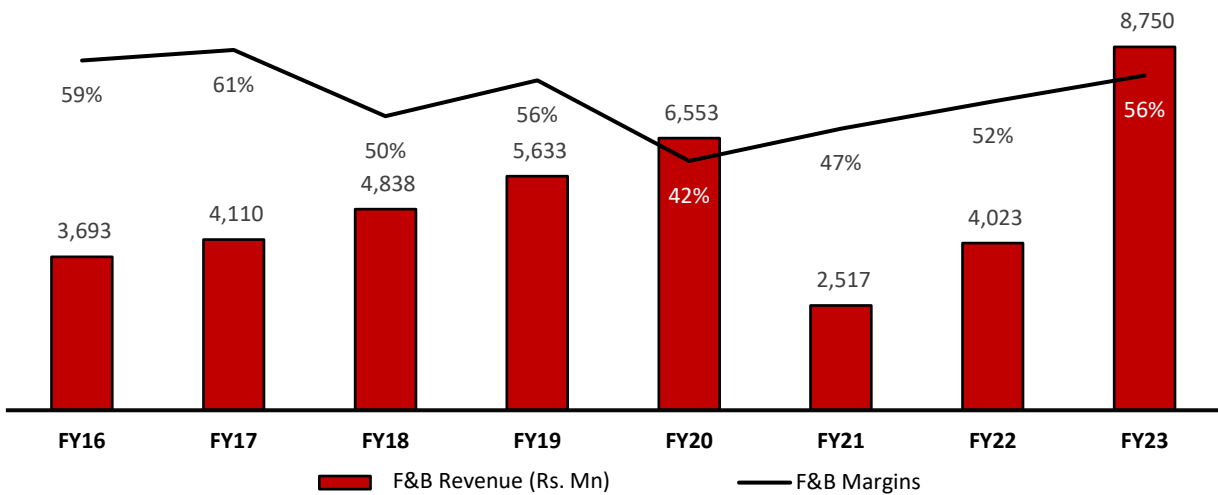
Food and Beverages

Food & Beverages revenue is mainly driven by the number of operational rooms and occupancy % of those rooms. However, compared to its peers as Indian Hotels, LTH offers only basic restaurant and banquet facilities. This results in the Company's revenue being skewed towards owned room rental rather than F&B revenue. In contrast, other 5-star hotels in the industry tend to have a more balanced composition between room rentals and F&B revenue. However, this balance is poised to shift for LTH, particularly with the introduction of properties like Aurika MIAL and other Lemon Tree Premier's which boast expansive banquet and convention center facilities.

Management has indicated a higher share of earnings from food and beverages in Aurika MIAL. This proportion is anticipated to further increase due to the boost in MICE demand. Coupled with the revenue surge from weddings, the sale of food and beverages is projected to experience notable growth.

F&B segment generates gross margin of more than 50%.

F&B Revenue (Rs. Mn) and Gross Margins (%) trend

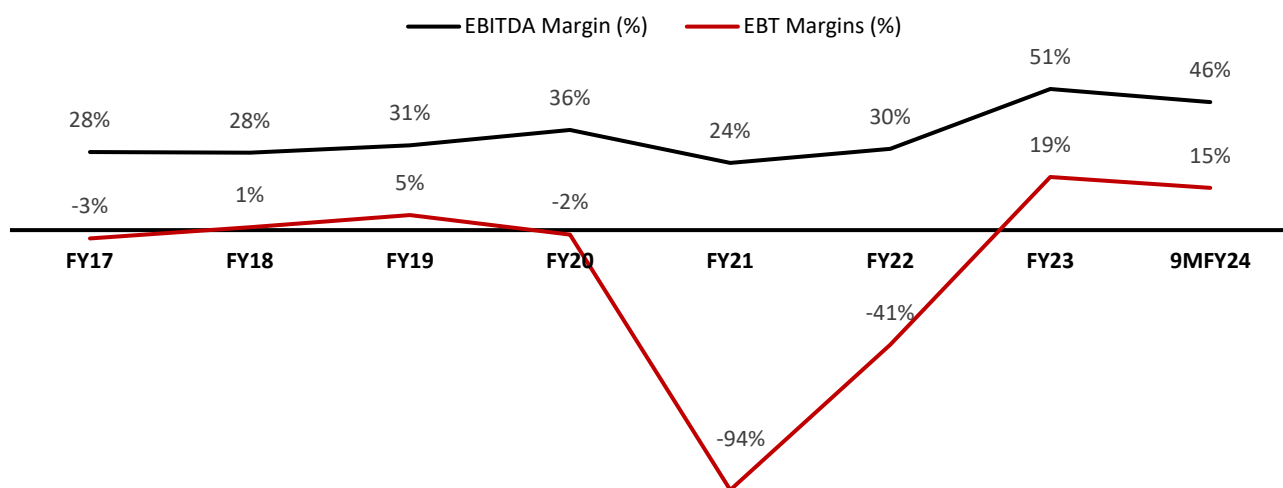


Source: Company, Keynote Capitals Ltd.

Common Size Statement for Expenses (to Revenue)

Expense Head/Year	FY17	FY18	FY19	FY20	FY21	FY22	FY23
Cost of Food Beverages	8%	9%	9%	9%	7%	7%	6%
Employee Benefit Expense	23%	22%	21%	23%	27%	23%	17%
Power and Fuel	9%	10%	9%	9%	12%	11%	8%
Other Expense	30%	30%	28%	24%	26%	24%	18%
Depreciation Amortisation	12%	11%	9%	13%	41%	25%	11%
Finance Cost	18%	15%	14%	24%	69%	42%	20%

Source: Company, Keynote Capitals Ltd.



Source: Company, Keynote Capitals Ltd.

Expenses

The Company's EBITDA margins are currently the highest in the industry, primarily attributed to its diligent cost optimization efforts implemented since the onset of COVID-19.

Streamlining the food menu and keeping only the requisite items, it has been able to cut down its food and beverage costs. Further, the Company had an opportunity to lower its employee costs by renegotiating contracts, but as things have normalized, employee salaries will revert to industry standards. Although the fuel and power expenses have not been reduced compared to FY19 as a baseline, we expect energy consumption to stabilize as the Company is investing to meet 50% of the energy needs through renewable sources.

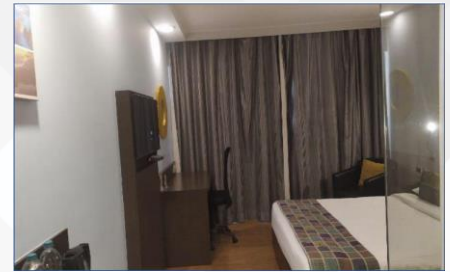
LTH has focused on removing those offerings that cost the Company a hefty amount but are required by very few customers. For instance, earlier, guest transportation used to cost the Company 3% of its revenue; however, now, it has removed that service and provides the same only on express request by the customer. Likewise, the Company has targeted granular expenses, successfully lowering current expenditures by tailoring services based on customer needs rather than obligatorily offering them universally.

Lemon Tree Hotels | Initiating Coverage Report

Renovation Expenses

The Company is revamping its Keys' portfolio by incorporating renovations across all properties, including seasoned hotels. In FY23, it had spent around Rs. 200 Mn, both in Capex and Opex, on renovations and in FY24 they expect the same to be ~Rs. 550 million, wherein Rs. 430 million will be opex and balance being capex. Because of these renovations, the Company is expected to take a hit of ~2.0%-2.5% on the EBITDA margins. These renovations are expected to be carried out in a phased manner in a 3-year timeline, with roughly Rs. 500 million to be spent every year on ~1,000 rooms each year. These renovations are typically carried out in the first half of the year wherein the business is a bit lean.

The Company expects to recover the lost EBITDA margin from increased occupancy and ARR in the already renovated hotels. These renovations are vital to the Company as it will help the Company reprice their rooms and improve occupancy.

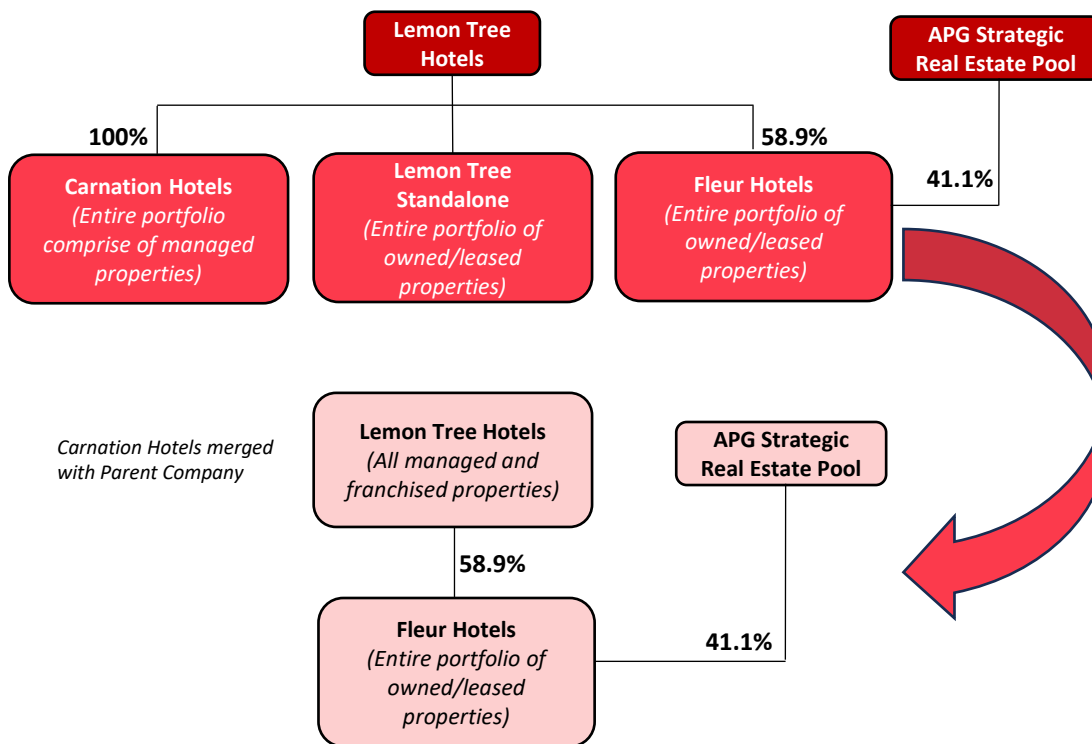


Before



After

A change in the current Corporate Structure



The Company's management has recently announced plans to streamline the corporate structure, aiming to recycle capital, reduce related party transactions, and reduce the number of entities from three to two. Under this restructuring, Fleur will become the sole proprietor of all owned or leased properties (with LTH divesting its 41% stake in independently owned properties), while Lemon Tree Hotels will focus solely on hotels under management or franchise contracts. This strategic move is anticipated to result in a substantial transfer of funds from Fleur Hotels to LTH, enabling the latter to pay down the Company's debt.

Post restructuring, the Company plans to list Fleur Hotels independently via IPO/REIT/INVIT by or before FY28.

Peer Comparison

Lemon Tree and Indian Hotels have similar operations but of different scale and segments



THE INDIAN HOTELS COMPANY LIMITED

Key Data Points

Incorporation Year - 2002

Room-Inventory (Q3FY24) (including pipeline) – 13,433 rooms

Niche – Mid-scale, Upper Mid-scale segment

Owned : Managed (current) – 60:40

Owned : Managed (expected) – 30:70

Key Data Points

Incorporation Year - 1902

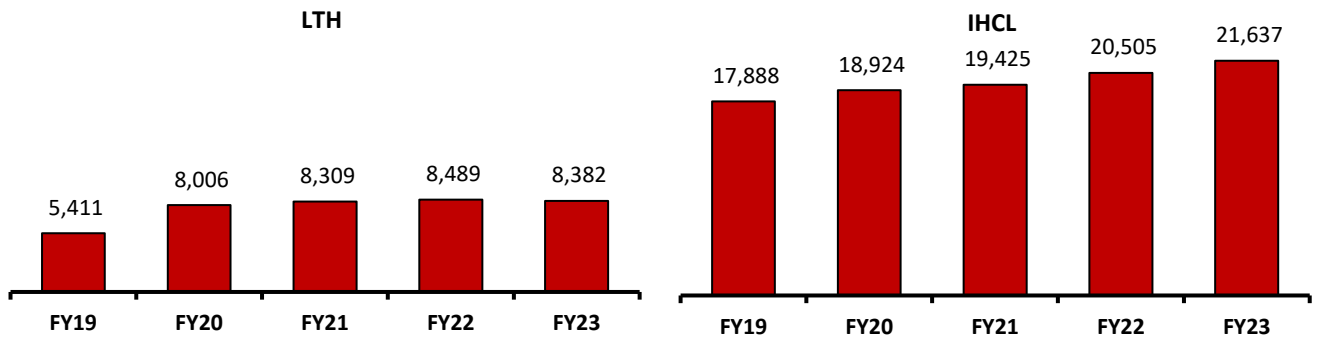
Room-Inventory (Q3FY24) (including pipeline) – 34,282 rooms

Niche – Luxury, Upscale segment

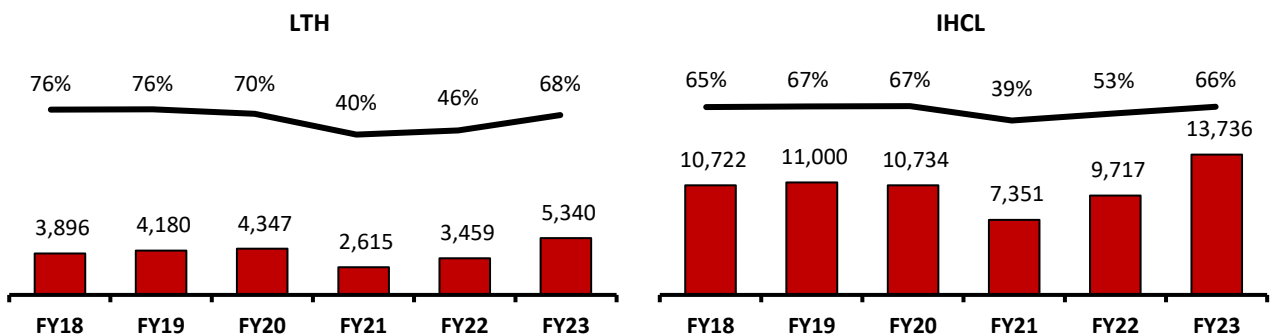
Owned : Managed (current) – 58:42

Owned : Managed (expected) – 50:50

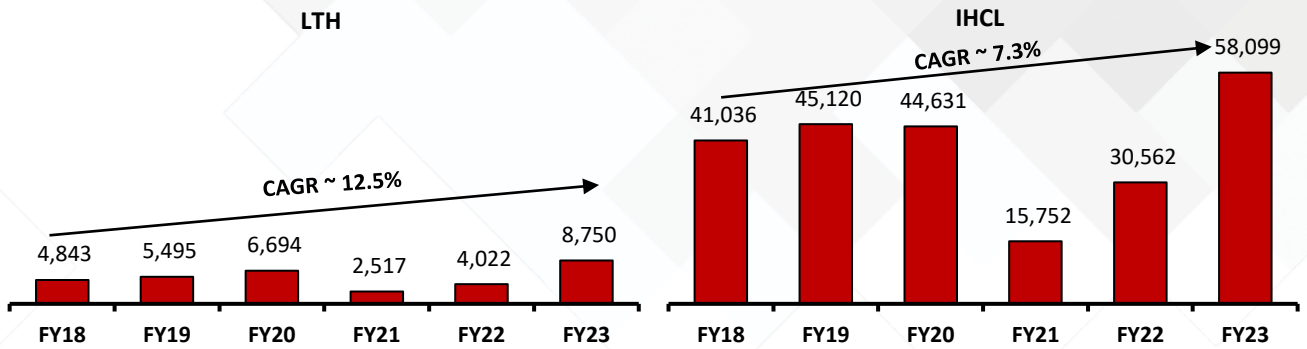
Operational Room Inventory (excl Pipeline)



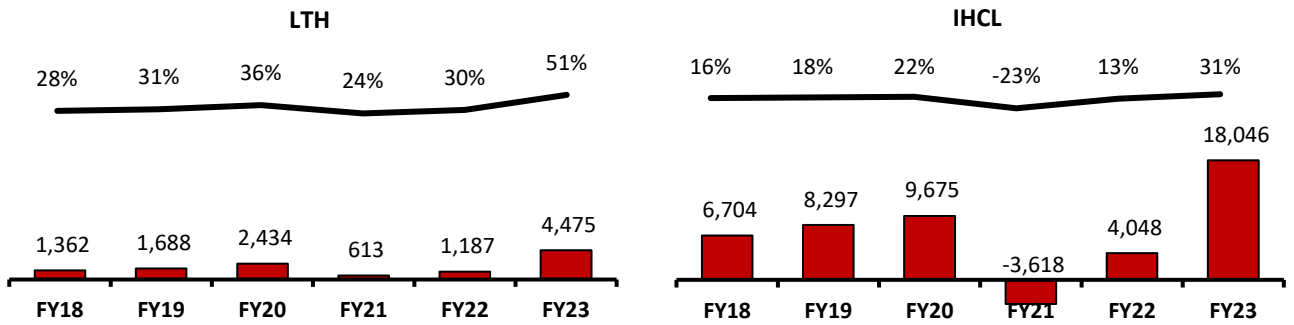
Operating Metrics – Occupancy (%) & ARR (Rs.)



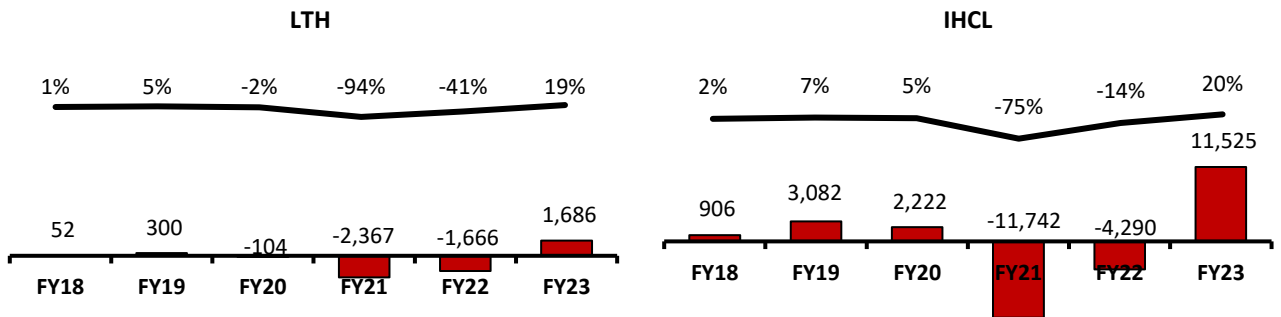
Revenue Growth (Rs. Mn)



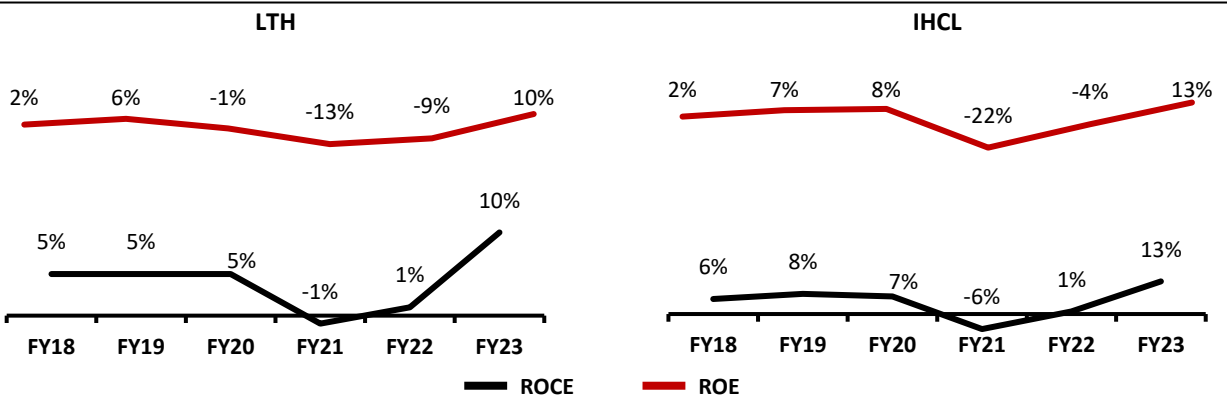
EBITDA (Rs. Mn) and EBITDA Margin Trend



EBT (Rs. Mn) and EBT Margin Trend



ROE & ROCE %



Management Analysis

The Management team of LTH consists of a mix of promoter family members and professionals.

Name	Designation	Promoter / Professional	Experience with LTH (Yrs.)
Mr. Patanjali Keswani	Chairman and MD	Promoter	20+
Mr. Aditya Keswani	Non-Executive Director	Promoter	5+
Mr. Davandar Tomar	Vice President	Professional	20+
Mr. Kapil Sharma	CFO	Professional	15+

Source: Company, Keynote Capitals Ltd.

Promoter Holding and Management Compensation

Promoter holding has fallen from FY20 onwards. The compensation received by the top management of LTH is in the comfortable range. Further, during Covid, the promoter has taken a salary cut as well.

Particulars	FY19	FY20	FY21	FY22	FY23
% Promoter Holding (~)	30.9%	31.2%	25.9%	23.9%	23.6%
Promoter Salary (Rs Mn)	33.4	33.4	2.8	16.8	35.1
As a % of PBT (~)	7.3%	NA	NA	NA	1.9%

Source: Company, Keynote Capitals Ltd.

Top Shareholders with more than 1% stake (%)

Particulars	FY19	FY20	FY21	FY22	FY23	Q3 FY24
APG Strategic Real Estate Pool N.V	15.0	15.0	15.0	15.0	15.0	15.0
SBI Large & Midcap Fund	7.2	8.5	8.4	8.4	7.6	7.3
RJ Corp Limited	6.7	4.1	4.1	4.1	4.1	4.1
Nomura India Investment Fund					2.4	2.1
HSBC Consumption Fund						1.7
Nippon Life India Trustee						1.7
Pacific Horizon Investment Trust Plc			1.7	1.6	1.6	1.2
The Nomura Trust And Banking Co						1.2
Franklin India Smaller Companies Fund				3.0	1.8	1.2
Vanguard Total International Stock Index Fund					1.0	1.0

Source: Company, Keynote Capitals Ltd.

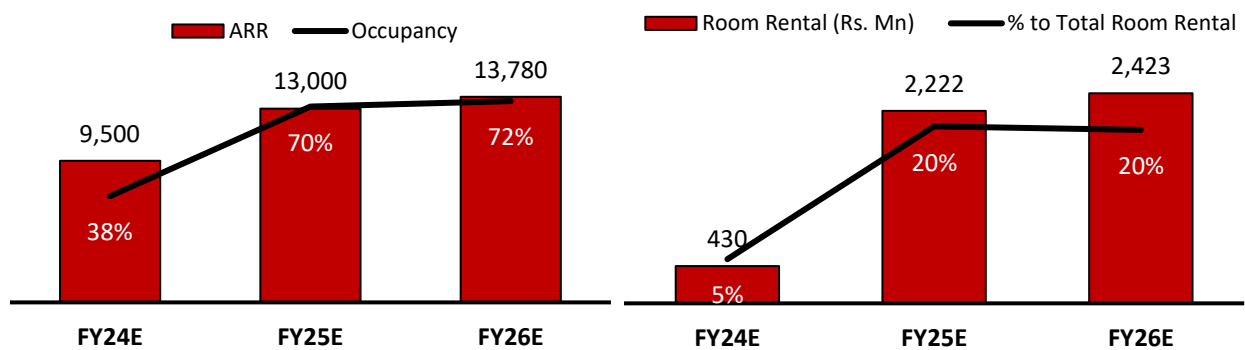
Opportunities

Potential in Luxury and Upscale offerings

The introduction of Aurika MIAL signifies a strategic move by LTH into the upscale segment within the Indian hospitality industry. With the upscale to luxury segment constituting 50% of the market by branded rooms, it presents a prime avenue for tapping into the most lucrative segment in terms of occupancies and ARR. The established brand name of Aurika MIAL provides a robust foundation for the Company to further expand its footprint in this upscale category, either through capital expenditure (CAPEX) or management contracts. Importantly, the envisaged higher management fees from these upscale establishments add an additional layer of attractiveness to this expansion strategy.

Projections indicate that Aurika MIAL alone is poised to make a substantial contribution, accounting for an estimated 20%+ to the Company's EBITDA by FY26. This underscores the significant earning potential inherent in this brand, positioning it as a key driver of growth and profitability for the Company in the upscale hospitality segment.

Aurika MIAL Metrics



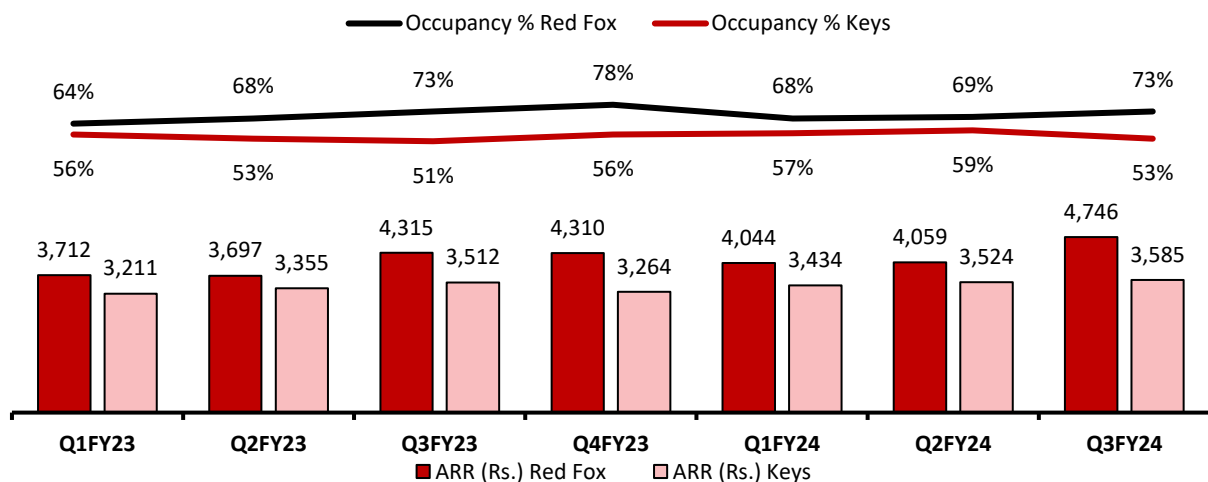
Source: Company, Keynote Capitals Ltd estimates

Renovation in the Keys' Portfolio

The Company is renovating the Keys' Portfolio, focused on economy and budget-level hotels acquired in 2019. Hindered by the onset of COVID-19, concentrated efforts on phased renovations. With ARR's yet to be repriced (Rs. 3,500-3,600 in Q3 FY24) and current occupancies at 53% (in Q3 FY24), Keys could become a significant player in the portfolio with 936 owned rooms.

Red Fox is another Midscale/economy brand of LTH, whose Occupancy% and ARR are much better than Keys.

We expect post-renovation, Keys operational metrics to look similar to Red Fox



Source: Company, Keynote Capitals Ltd.

Strong Management contracts pipeline to drive margins

The Company has a strong pipeline of management contracts, and the pipeline figures are consistently growing. With a seamless 100% flow-through of management income and zero capital investment, this asset – light business positions the Company to achieve enhanced profit margins, given the absence of associated expenses with management fee income.

Brand	Operational Rooms	Pipeline Rooms	Total Rooms
Aurika	863	242	1,105
Lemon Tree Premier	2,514	479	2,993
Lemon Tree Hotels	3,647	2,484	6,131
Red Fox Hotels	1,290	50	1,340
Keys	1,373	491	1,864
Total	9,687	3,746	13,433

Majority of room addition is in **mid-scale category**

This number is expected to **touch 20,000 Rooms** by FY28

All pipeline room additions are **via a management contract** except 69 room property developed in Shimla

All these properties will be operational **by FY27**

Source: Company, Keynote Capitals Ltd.

Leader in Mid scale to economy segment with huge untapped potential

LTH is a leader in the midscale and economy segment with almost ~14% share in branded industry inventory. Unlike prominent brands such as Taj, ITC, Oberoi, Hyatt, Leela, etc., which primarily cater to the upscale and luxury segment, they have left the midscale & economy categories largely unaddressed.

Further, ~2.8 Mn unbranded hotels could potentially be converted into branded properties through management contracts within midscale and economy segments. This vast pool offers a compelling market for LTH to penetrate and capture, to further solidify its position.

Segment	Industry Inventory	Lemon Tree Inventory	LTH inventory as % of Industry
Luxury and Upper Upscale	60,000		
Upscale	36,000	863	0.9%
Upper Midscale	31,000	2,556	8.2%
Midscale and Economy	44,000	6,268	14.2%
Total Branded Inventory	171,000	9,687	5.7%
		~300,000	
		(suitable for branding under Lemon Tree)	
Unbranded Standalone		~2,500,000	
		(suitable for branding under Keys)	

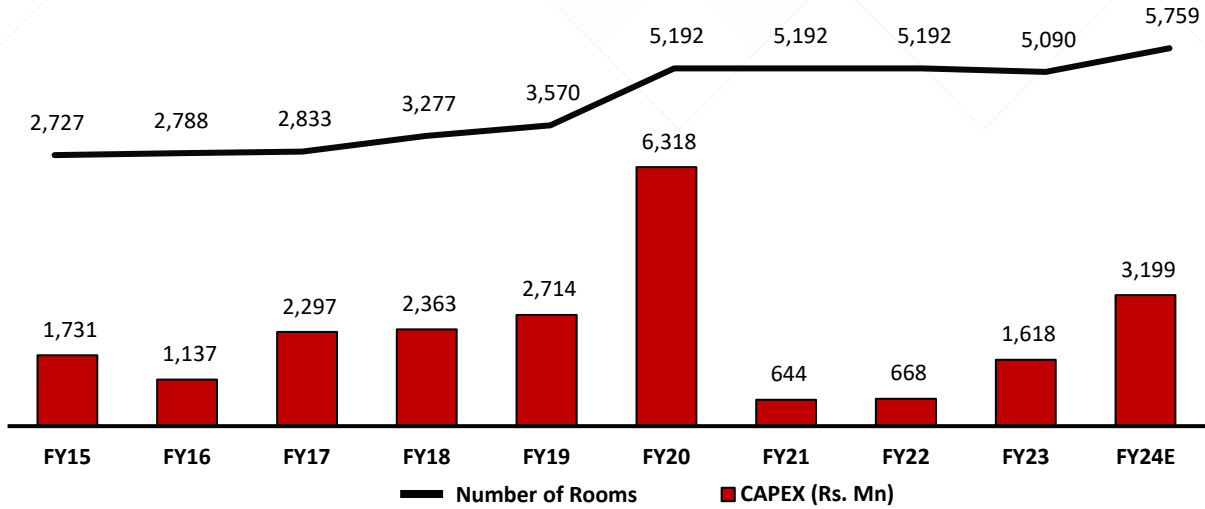
Source: Horwath HTL, Company, Keynote Capitals Ltd.

Aggressive Repricing Opportunity

The hospitality industry is a cyclical industry, and it is currently positioned in the upcycle stage. This is evident as the demand growth (CAGR), estimated at approximately 10%, is outpacing the supply growth (CAGR), which is around 7%. This demand-supply gap is expected to persist for the foreseeable future, providing the Company with the opportunity to further improve its ARR.

Sweating of Assets – No further Capex

The Company's capital expenditure cycle is nearing completion post spending ~Rs. 23 Bn (includes capex on Aurika MIAL) in the last decade. During this period, LTH has increased their owned rooms by 2x. For the development of Lemon Tree, Shimla, ~Rs. 200 million remains to be spent, with only minor capex required annually for renovation purposes. With no additional capital investment planned, the Company anticipates generating sufficient cash flow from its properties to repay its debt.



Source: Company, Keynote Capitals Ltd. estimates

Challenges

Lesser Autonomy in Management Contracts

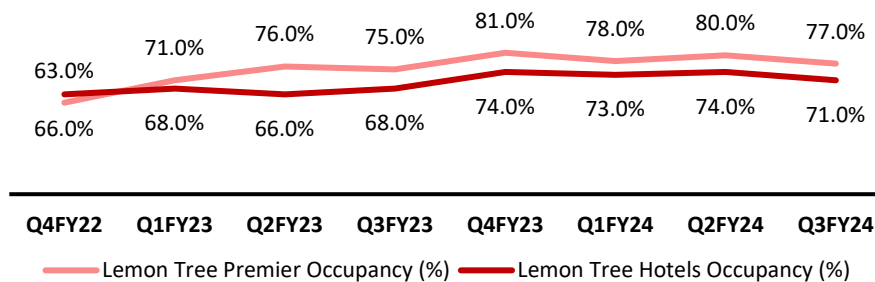
With target to have 70% of room inventory under Management contracts, it would be a challenge for the Company to maintain their quality and brand image. Further, management contracts are long term agreements, which can limit LTH's flexibility to adapt to changing market conditions or pursue alternative strategies.

Cyclical nature of the industry

The hospitality industry depends on discretionary spending by the customers; it is thus highly susceptible to various externalities, making it cyclical in nature. Further, seasonality plays an important role in the traffic at hotels. All these factors clubbed together may result in ARR or occupancy not increasing as per expectations.

Saturated levels in the midscale segment

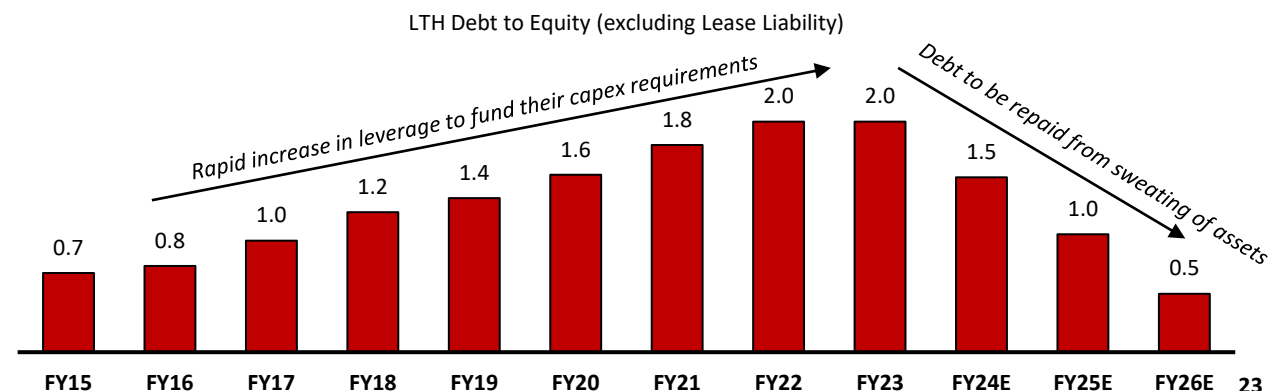
LTH is a pioneer in the midscale segment wherein the occupancies are at potentially maximum levels, or there is not much scope to benefit from an increase in occupancies. Thus, it puts the Company's ability to earn in jeopardy as it does not plan to increase the number of hotels owned; occupancies do not hold much scope for improvement; it then solely becomes dependent on increasing ARR to drive its revenue growth.



Source: Company, Keynote Capitals Ltd.

Highly leveraged, the success of Aurika MIAL is critical to paying down debt

LTH's Debt to equity (excluding lease liability) stands at 1.35x as of Sep'23. The Company plans to reduce its debt using cash flow generated from the business, especially Aurika MIAL, which is expected to contribute upwards of 22-26% at the EBITDA level by FY26. However, if Aurika MIAL underperforms or the industry experiences a downturn, it could substantially hinder the Company's capacity to repay its debt.



Source: Company, Keynote Capitals Ltd. estimates

Financial Statement Analysis

Income Statement

Y/E Mar, Rs. Mn	FY22	FY23	FY24E	FY25E	FY26E
Net Sales	4,022	8,750	10,703	13,596	15,219
Growth %		118%	22%	27%	12%
Raw Material Expenses	279	499	609	669	725
Employee Expenses	973	1,497	1,877	2,095	2,275
Other Expenses	1,584	2,278	3,049	3,820	4,354
EBITDA	1,187	4,476	5,167	7,012	7,865
Growth %		277%	15%	36%	12%
Margin %	30%	51%	48%	52%	52%
Depreciation	1,043	966	1,110	1,232	1,254
EBIT	143	3,510	4,057	5,780	6,610
Growth %		2352%	16%	42%	14%
Margin %	4%	40%	38%	43%	43%
Interest Paid	1,809	1,823	1,942	1,948	1,650
Other Income & exceptional	210	88	118	218	125
PBT	-1,456	1,774	2,233	4,051	5,085
Tax	-72	377	558	1,013	1,271
PAT	-1,384	1,397	1,675	3,038	3,814
Others (Minorities, Associates)	-498	260	352	442	494
Net Profit	-1,882	1,656	2,027	3,480	4,308
Growth %		-188%	22%	72%	24%
Shares (Mn)	792.2	792.2	792.2	792.2	792.2
EPS	-1.11	2.09	2.56	4.39	5.44

Balance Sheet

Y/E Mar, Rs. Mn	FY22	FY23	FY24E	FY25E	FY26E
Cash, Cash equivalents & Bank	543	275	169	1,182	280
Current Investments	59	10	10	10	10
Debtors	291	560	642	816	913
Inventory	81	105	128	140	152
Short Term Loans & Advances	255	294	294	294	294
Other Current Assets	81	116	116	116	116
Total Current Assets	1,310	1,360	1,360	2,559	1,766
Net Block & CWIP	33,456	34,264	36,365	36,221	35,560
Long Term Investments	37	45	45	45	45
Other Non-current Assets	1,087	1,288	1,288	1,288	1,288
Total Assets	35,890	36,958	39,058	40,114	38,660
Creditors	585	668	1,445	1,903	2,131
Provision	198	56	56	56	56
Short Term Borrowings	355	575	575	575	575
Other Current Liabilities	1,396	2,402	2,402	2,402	2,402
Total Current Liabilities	2,533	3,701	4,478	4,937	5,164
Long Term Debt	15,535	15,174	15,174	13,174	8,174
Deferred Tax Liabilities	-441	-329	-329	-329	-329
Other Long Term Liabilities	4,274	4,278	4,278	4,278	4,278
Total Non Current Liabilities	19,368	19,123	19,123	17,123	12,123
Paid-up Capital	7,908	7,916	7,916	7,916	7,916
Reserves & Surplus	404	621	2,296	5,334	9,148
Shareholders' Equity	8,312	8,537	10,212	13,250	17,064
Non Controlling Interest	5,676	5,597	5,245	4,804	4,309
Total Equity & Liabilities	35,890	36,958	39,058	40,114	38,660

Cash Flow

Y/E Mar, Rs. Mn	FY22	FY23	FY24E	FY25E	FY26E
Pre-tax profit	-1,456	1,774	2,233	4,051	5,085
Adjustments	2,788	2,676	2,582	2,519	2,285
Change in Working Capital	27	-403	672	272	118
Total Tax Paid	-17	-207	-558	-1,013	-1,271
Cash flow from operating Activities	1,343	3,840	4,929	5,830	6,217
Net Capital Expenditure	-668	-1,618	-3,211	-1,088	-594
Change in investments	132	8	0	0	0
Other investing activities	81	-1,222	118	218	125
Cash flow from investing activities	-454	-2,832	-3,093	-870	-469
Equity raised / (repaid)	8,426	17,067	0	0	0
Debt raised / (repaid)	134	471	0	-2,000	-5,000
Dividend (incl. tax)	0	0	0	0	0
Other financing activities	-1,773	-1,811	-1,942	-1,948	-1,650
Cash flow from financing activities	-1,630	-1,323	-1,942	-3,948	-6,650
Net Change in cash	-742	-315	-106	1,013	-902

Valuation Ratios

	FY22	FY23	FY24E	FY25E	FY26E
Per Share Data					
EPS	-1	2	3	4	5
Growth %		-289%	22%	72%	24%
Book Value Per Share	10	18	20	23	27
Return Ratios					
Return on Assets (%)	-2%	5%	5%	9%	11%
Return on Equity (%)	-10%	15%	14%	21%	22%
Return on Capital Employed (%)	1%	13%	13%	18%	20%
Turnover Ratios					
Asset Turnover (x)	0.1	0.2	0.3	0.3	0.4
Sales / Gross Block (x)	0.1	0.2	0.3	0.3	0.3
Working Capital / Sales (x)	-23%	-20%	-25%	-20%	-19%
Receivable Days	27	18	20	20	21
Inventory Days	101	68	70	73	74
Payable Days	62	26	36	45	48
Working Capital Days	66	60	54	48	46
Liquidity Ratios					
Current Ratio (x)	0.5	0.4	0.3	0.5	0.3
Interest Coverage Ratio (x)	0.2	2.0	2.1	3.1	4.1
Total Debt to Equity	2.0	1.1	1.0	0.8	0.4
Net Debt to Equity	2.0	1.1	1.0	0.7	0.4
Valuation					
PE (x)	-57.2	30.3	53.9	31.4	25.4
Earnings Yield (%)	-2%	3%	2%	3%	4%
Price to Sales (x)	12.5	5.7	10.2	8.0	7.2
Price to Book (x)	6.0	7.2	10.7	8.2	6.4
EV/EBITDA (x)	56.2	17.5	24.4	18.0	16.1
EV/Sales (x)	16.6	9.0	11.8	9.3	8.3

Source: Company, Keynote Capitals Ltd. estimates

LTH's SoTP valuation

LTH's Stndl Valuation (Rs. Mn)	FY25E
EV/EBITDA Multiple (x)	22
EBITDA	3,028
EV	66,611

Carnation's Valuation (Rs. Mn)	FY25E
EV/EBITDA Multiple (x)	35
EBITDA	484
EV	16,931

SoTP Valuation (Rs. Mn)	FY25E
Standalone EV	66,611
Fleur EV	55,716
Carnation EV	16,931
Total EV	1,39,258
Less: Debt	13,749
Add: Cash	1,192
Est. Mcap	1,26,700
Outstanding Shares	792
Target Price	160
Current Mcap	142
Upside / (Downside) %	12.6%

Fleur's Valuation (Rs. Mn)	FY25E
EV/EBITDA Multiple (x)	22
EBITDA	4,299
EV	94,578
Less: APG's stake	38,862
Adjusted EV	55,716

Source: Company, Keynote Capitals Ltd. Estimates

LTH is positioned as a dominant player in the midscale & economy segment, strategically pivoting its business model from asset ownership to asset-light model via a management contract. The inauguration of Aurika MIAL marks a significant milestone, which will boost the Company's topline and bottom-line. Further, future growth will be fueled via the management contract route.

Further, the industry is positioned in a sweet spot, with anticipated demand surpassing supply, leading to better visibility on occupancy and ARR.

In light of these promising factors, we initiate coverage on LTH with a BUY rating with SoTP valuation target price of Rs. 160, implying an upside of 12.6%.

Lemon Tree Hotels | Initiating Coverage Report

Our Recent Reports

PI Industries Ltd.

I G Petrochemicals Ltd.

Cigniti Technologies Ltd.

Rating Methodology

Rating	Criteria
BUY	Expected positive return of > 10% over 1-year horizon
NEUTRAL	Expected positive return of > 0% to < 10% over 1-year horizon
REDUCE	Expected return of < 0% to -10% over 1-year horizon
SELL	Expected to fall by >10% over 1-year horizon
NOT RATED (NR)/UNDER REVIEW (UR)/COVERAGE SUSPENDED (CS)	Not covered by Keynote Capitals Ltd/Rating & Fair value under Review/Keynote Capitals Ltd has suspended coverage

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