

## Lemon Tree Hotels Limited

### Renovation to hamper margins

12<sup>th</sup> August 2024

In Q1 FY25, Lemon Tree Hotel's revenue increased by 19.5% on a YoY basis, driven by growth in ARR by 9.2% and owned rooms by 13.1% on a YoY basis. Revenue growth was also supported by growth in management fees by 21.8% on a YoY basis. Despite strong topline growth, EBITDA margins declined by 455 Bps due to ongoing renovations, expansion of business development team and overall payroll increase. Renovation expenses accounted for ~223 Bps contraction in operating margins during the quarter.

#### 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. Revenue from management & franchise fees which contributed 10.9% of total revenue in Q1 FY25, a slight improvement from 10.7% of the total revenue in Q1 FY24. Further, rooms in the pipeline via managed rooms have increased by 32.9% on a YoY basis.

#### Renovation of the entire owned portfolio

Renovations are underway for LTH-owned properties, including Keys' portfolio, and are expected to be completed in the next couple of years. A total of ~4,100 rooms are expected to be renovated by the end of FY26, which will negatively impact margins for the next couple of years. Management expects renovation expenses to payback within 2 years via incremental operating profit post-renovation as renovated properties result in improved ARR and occupancy %.

#### Repricing opportunity

The hospitality industry is currently in an upcycle stage. Demand growth is ~10%, outpacing supply growth at 7%. This trend is expected to continue, providing the Company with an opportunity to improve its ARR. Management expects ARR growth of 9-10% in FY25.

#### Sweating of assets & debt repayment

With Aurika MIAL going live in Oct'23, no further capex are scheduled for the Company. With no capex planned, the Company anticipates generating sufficient cash flow from its properties to repay its debt. Management aims to bring debt to zero in the next four years.

#### 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 have revised our estimates and maintained our BUY rating on Lemon Tree Hotels Ltd with a target price of Rs. 146 (21x FY25E EV/EBITDA Multiple).

**BUY**

CMP Rs. 121

TARGET Rs. 146 (+20.6%)

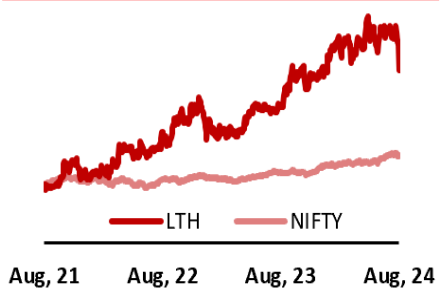
#### Company Data

Bloomberg Code	LEMONTRE IN
MCAP (Rs. Mn)	95,890
O/S Shares (Mn)	792
52w High/Low	158 / 90
Face Value (in Rs.)	2
Liquidity (3M) (Rs. Mn)	535

#### Shareholding Pattern %

	Jun'24	Mar'24	Dec'23
Promoters	22.80	22.88	23.21
FIIIs	27.61	27.09	22.82
DIIIs	15.20	15.35	15.00
Non-Institutional	34.39	34.68	38.98

#### LTH vs NIFTY



Source: Keynote Capitals Ltd.

#### Key Financial Data

(Rs Bn)	FY24	FY25E	FY26E
Revenue	10.7	13.0	14.7
EBITDA	5.2	6.2	7.3
Net Profit	1.5	2.0	2.9
Total Assets	40.0	40.9	39.0
ROCE (%)	14%	15%	18%
ROE (%)	10%	17%	20%

Source: Company, Keynote Capitals Ltd Estimates

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## Lemon Tree Hotels | Quarterly Update

### Q1 FY25 Result Update

#### Result Highlights (Rs. Mn)

Particulars	Q1 FY25	Q1 FY24	Change % (Y-o-Y)	Q4 FY24	Change % (Q-o-Q)	FY24
Revenue	2,680	2,242	19.5%	3,273	-18.1%	10,711
Employee Cost	507	426	19.0%	499	2%	1,878
F&B Cost	164	124	32.2%	205	-20%	628
Power & Fuel Cost	234	193	21.3%	197	18%	780
Other Expenses	624	435	43.7%	657	-5%	2,193
EBITDA	1,151	1,065	8.1%	1,715	-33%	5,232
<b>EBITDA %</b>	<b>42.9%</b>	<b>47.5%</b>	<b>-455 Bps</b>	<b>52.4%</b>	<b>-946 Bps</b>	<b>48.8%</b>
Depreciation	346	228	52%	334	4%	1,121
EBIT	805	837	-4%	1,381	-42%	4,111
<b>EBIT %</b>	<b>30.0%</b>	<b>37.3%</b>	<b>-728 Bps</b>	<b>42.2%</b>	<b>-1215 Bps</b>	<b>38.4%</b>
Finance Cost	543	492	10%	554	-2%	2,085
Other Income	28	14	96%	65	-56%	125
PBT	291	359	-19%	892	-67%	2,151
Tax	91	87	5%	50	81%	341
Profit from Associates/JV	1	3		-2		7
PAT	201	275	-27%	840	-76%	1,817
Minority Interest	-3	-41		-170		-332
<b>Net Profit</b>	<b>198</b>	<b>235</b>	<b>-16%</b>	<b>670</b>	<b>-70%</b>	<b>1,485</b>
<b>EPS</b>	<b>0.25</b>	<b>0.30</b>	<b>-</b>	<b>0.85</b>	<b>-</b>	<b>1.88</b>

Source: Company, Keynote Capitals Ltd.

#### Operating Metrics

Particulars	Q1 FY25	Q1 FY24	Change % (Y-o-Y)	Q4 FY24	Change % (Q-o-Q)
Total Operational Rooms	10,125	8,491	19%	9,863	3%
Owned Rooms %	57%	60%	-307 Bps	58%	-151 Bps
Managed/Franchised %	43%	40%	307 Bps	42%	151 Bps
Total Rooms in Pipeline	4,036	3,724	8%	4,156	-3%
Total Rooms	14,161	12,215	16%	14,019	1%
ARR (Rs.)	5,686	5,207	9.2%	6,605	-14%
Occupancy %	66.6%	70.2%	-360 Bps	72.0%	-540 Bps
Management Fees (Rs. Mn)	291	239	22%	412	-29%

Source: Company, Keynote Capitals Ltd.

## Lemon Tree Hotels | Quarterly Update

### Q1 FY25 Conference Call Takeaways

#### General Highlights

- In Q1 FY25, despite the temporary headwinds faced by the hotel sector due to the election process and extreme heat wave, LTH reported healthy revenue growth of ~19% on a YoY basis.
- EBITDA margins declined by 455 Bps primarily due to increased renovation expenses, which accounted for 223 Bps contraction in margins. The remaining factors contributing to the decline were the expansion of the business development team and an overall increase in payroll costs. The Company has increased its business development team by 4x, and the sales team has increased by 50% in the last 3 months.
- Occupancy for the quarter stood at 66.6%, but if we adjust for number of rooms not available due to renovations, occupancy would have been 10% higher than reported occupancy.
- The management aims to bring down the current debt to 0 in the next 4 years. They will use the free cash flow generated during the winter season to pay down debt. Free cash flow generated during the winter season is generally 2-2.5x that of the summer season.
- During the quarter, LTH signed 3 new management & franchise contracts, which added 187 new rooms to the pipeline and operationalized 4 hotels, which added 331 rooms to the portfolio.
- The Company is strategically reducing dependence on crew contracts in Aurika MIAL. Management believes they need to reduce dependence on crew and crew contracts, as they are long term in nature. So strategically, they are not renewing some contracts because ARR from crew contracts is poor and they want to have inventory during winter, which will give better ARR.
- It will take at least a year for Aurika MIAL to stabilize, so real results should be visible by Q4 FY25.

#### Renovations

- Keys portfolio EBITDA margin decreased on a YoY basis due to an increase in renovation expenses over Q1 FY24, which is a 100% increase. During the quarter, 25% of the Keys portfolio was shut for renovation, which impacted Keys portfolio to increase occupancy, which decreased by 148 Bps.
- Currently, LTH-owned rooms are ~5,900. Out of these, ~4,100 rooms will undergo renovations, which will be complete by the end of FY26. Generally, it takes 2-2.5 months to renovate a hotel, and at any given point of time, 600-700 rooms will be closed for renovation.
- Winter season is generally peak season for the Company, and they will strategically minimize the number of rooms closed for renovation during that period. Hence, most of the renovation will happen during the summer season, i.e., H1 of each year.
- The payback period for any renovation is 2 years.

Particulars	No. of Rooms
Total Owned Rooms	5,900
New Rooms that don't need renovation	1,500
Total Rooms for Renovation	4,400
<b>Keys Room for Renovation</b>	<b>900</b>
Rooms already renovated	250-300
<b>Pending rooms for renovation</b>	<b>3,200</b>

## Lemon Tree Hotels | Quarterly Update

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### Other Important things

- Growth levers the Company is focused on for the future are: a) Stabilization of Aurika MIAL, b) Accelerated growth in management and franchise contracts and c) Timely completion of renovation activities in the owned portfolio to improve ARR and occupancy.
- The Company is in the midst of digitally transforming itself by focusing on a) Dynamic Repricing algorithm, b) New sales system led by digital capabilities, c) Reimagining loyalty program and d) Reimagining website with an element of mass-scale personalized offers.

## Lemon Tree Hotels | Quarterly Update

### Financial Statement Analysis

#### Income Statement

Y/E Mar, Rs. Mn	FY23	FY24	FY25E	FY26E	FY27E
<b>Net Sales</b>	<b>8,750</b>	<b>10,711</b>	<b>12,964</b>	<b>14,690</b>	<b>16,385</b>
Growth %		22%	21%	13%	12%
Raw Material Expenses	499	628	664	729	800
Employee Expenses	1,497	1,878	2,132	2,309	2,506
Other Expenses	2,278	2,973	3,950	4,321	4,753
<b>EBITDA</b>	<b>4,476</b>	<b>5,232</b>	<b>6,217</b>	<b>7,331</b>	<b>8,327</b>
Growth %		17%	19%	18%	14%
Margin%	51%	48.8%	48.0%	49.9%	50.8%
Depreciation	966	1,121	1,369	1,393	1,408
<b>EBIT</b>	<b>3,510</b>	<b>4,111</b>	<b>4,849</b>	<b>5,938</b>	<b>6,919</b>
Growth %		17%	18%	22%	17%
Margin%	40%	38%	37%	40%	42%
Interest Paid	1,823	2,085	1,900	1,603	1,178
Other Income & exceptional	88	125	226	144	162
<b>PBT</b>	<b>1,774</b>	<b>2,151</b>	<b>3,174</b>	<b>4,479</b>	<b>5,903</b>
Tax	377	341	793	1,120	1,476
<b>PAT</b>	<b>1,397</b>	<b>1,810</b>	<b>2,380</b>	<b>3,359</b>	<b>4,427</b>
Others (Minorities, Associates)	-251	-325	-419	-470	-525
<b>Net Profit</b>	<b>1,146</b>	<b>1,485</b>	<b>1,961</b>	<b>2,890</b>	<b>3,902</b>
Growth %		30%	32%	47%	35%
Shares (Mn)	792.2	792.2	792.2	792.2	792.2
<b>EPS</b>	<b>1.45</b>	<b>1.87</b>	<b>2.48</b>	<b>3.65</b>	<b>4.93</b>

#### Balance Sheet

Y/E Mar, Rs. Mn	FY23	FY24	FY25E	FY26E	FY27E
Cash, Cash equivalents & Bank	275	537	1,717	546	807
Current Investments	10	81	81	81	81
Debtors	560	715	778	881	983
Inventory	105	138	139	153	168
Short Term Loans & Advances	294	550	550	550	550
Other Current Assets	116	32	32	32	32
<b>Total Current Assets</b>	<b>1,360</b>	<b>2,053</b>	<b>3,297</b>	<b>2,243</b>	<b>2,621</b>
Net Block & CWIP	34,264	36,660	36,329	35,508	34,264
Long Term Investments	45	52	58	64	70
Other Non-current Assets	1,288	1,206	1,206	1,206	1,206
<b>Total Assets</b>	<b>36,958</b>	<b>39,972</b>	<b>40,890</b>	<b>39,021</b>	<b>38,161</b>
Creditors	668	859	1,815	2,057	2,294
Provision	56	60	60	60	60
Short Term Borrowings	575	192	192	192	192
Other Current Liabilities	2,402	2,480	2,480	2,480	2,480
<b>Total Current Liabilities</b>	<b>3,701</b>	<b>3,591</b>	<b>4,547</b>	<b>4,789</b>	<b>5,026</b>
Long Term Debt	15,174	16,767	14,767	9,767	4,767
Deferred Tax Liabilities	-329	-306	-306	-306	-306
Other Long Term Liabilities	4,278	4,456	4,456	4,456	4,456
<b>Total Non Current Liabilities</b>	<b>19,123</b>	<b>20,917</b>	<b>18,917</b>	<b>13,917</b>	<b>8,917</b>
Paid-up Capital	7,916	7,918	7,918	7,918	7,918
Reserves & Surplus	621	1,750	4,138	7,505	11,939
Shareholders' Equity	8,537	9,669	12,056	15,423	19,858
Non Controlling Interest	5,597	5,795	5,369	4,892	4,360
<b>Total Equity &amp; Liabilities</b>	<b>36,958</b>	<b>39,972</b>	<b>40,890</b>	<b>39,021</b>	<b>38,161</b>

Source: Company, Keynote Capitals Ltd. estimates

#### Cash Flow

Y/E Mar, Rs. Mn	FY23	FY24	FY25E	FY26E	FY27E
Pre-tax profit	1,774	2,151	3,174	4,479	5,903
Adjustments	2,676	3,070	2,617	2,375	1,892
Change in Working Capital	-403	-218	892	125	121
Total Tax Paid	-207	-360	-793	-1,120	-1,476
<b>Cash flow from operating Activities</b>	<b>3,840</b>	<b>4,643</b>	<b>5,890</b>	<b>5,859</b>	<b>6,440</b>
Net Capital Expenditure	-1,618	-3,305	-1,037	-573	-164
Change in investments	8	-242	0	0	0
Other investing activities	-1,222	-418	227	145	164
<b>Cash flow from investing activities</b>	<b>-2,832</b>	<b>-3,965</b>	<b>-810</b>	<b>-428</b>	<b>0</b>
Equity raised / (repaid)	17,067	5,126	0	0	0
Debt raised / (repaid)	471	1,418	-2,000	-5,000	-5,000
Dividend (incl. tax)	0	0	0	0	0
Other financing activities	-1,811	-2,008	-1,900	-1,603	-1,178
<b>Cash flow from financing activities</b>	<b>-1,323</b>	<b>-585</b>	<b>-3,900</b>	<b>-6,603</b>	<b>-6,178</b>
<b>Net Change in cash</b>	<b>-315</b>	<b>93</b>	<b>1,180</b>	<b>-1,172</b>	<b>261</b>

#### Valuation Ratios

	FY23	FY24	FY25E	FY26E	FY27E
<b>Per Share Data</b>					
EPS	1.4	1.9	3.6	4.9	6.3
Growth %		30%	89%	37%	29%
Book Value Per Share	18	20	22	26	31
<b>Return Ratios</b>					
Return on Assets (%)	3%	4%	7%	10%	13%
Return on Equity (%)	10%	10%	17%	20%	22%
Return on Capital Employed (%)	14%	14%	15%	18%	21%
<b>Turnover Ratios</b>					
Asset Turnover (x)	0.2	0.3	0.3	0.4	0.4
Sales / Gross Block (x)	0.2	0.3	0.3	0.3	0.3
Working Capital / Sales (x)	-20%	-18%	-11%	-13%	-15%
Receivable Days	18	22	21	21	21
Inventory Days	68	71	76	73	73
Payable Days	26	26	38	48	48
Working Capital Days	60	67	60	46	46
<b>Liquidity Ratios</b>					
Current Ratio (x)	0.4	0.6	0.7	0.5	0.5
Interest Coverage Ratio (x)	2.0	2.0	2.7	3.8	6.0
Total Debt to Equity	1.1	1.1	0.9	0.5	0.2
Net Debt to Equity	1.1	1.1	0.8	0.5	0.2
<b>Valuation</b>					
PE (x)	53.4	73.4	33.7	24.7	19.1
Earnings Yield (%)	2%	1%	3%	4%	5%
Price to Sales (x)	7.0	10.2	7.3	6.5	5.8
Price to Book (x)	7.2	11.3	7.9	6.2	4.8
EV/EBITDA (x)	17.5	23.9	18.2	15.4	13.6
EV/Sales (x)	9.0	11.7	8.7	7.7	6.9

### KEYNOTE Rating History

Date	Rating	Market Price at Recommendation	Upside/Downside
26 <sup>th</sup> February 2024	BUY	142	+12.6%
4 <sup>th</sup> June 2024	BUY	133	+13.5%
12 <sup>th</sup> August 2024	BUY	121	+20.6%

## Lemon Tree Hotels | Quarterly Update

## 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
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