Hospitality Industry: Heading Towards Hospitable Territory

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Overview:

After an abysmal FY21, the Indian hospitality sector made a steady recovery in FY22 as successful vaccination drives and reduction in Covid cases have helped improve travel sentiment. Though the Omicron wave caused a temporary blip, FY22 has witnessed a sharp rebound in revenues. The revival can be largely attributed to pent-up demand for leisure and business travel, supported by increased bookings on account of weddings and significant uptick in MICE (meetings, incentives, conferences and exhibitions). The sector also saw some green shoots from international travel, after a lull of nearly two years.

As envisaged in our earlier report "Hospitality Industry: Survival Before Revival", which was published in September 2021, the sector is on track to achieve or even surpass the pre-Covid level occupancies in FY23. Demand for leisure travel, business travel for client meetings as well as project work are gaining steam. Although the uncertainty around new variants of the Covid virus may continue to linger for some more time, CareEdge expects domestic travel (leisure and business) demand to remain strong during the year as travellers and hoteliers have embraced the new normal. The resumption of international flights in March 2022 should also give impetus to foreign leisure travel.

CareEdge believes that with demand outlook improving coupled with the large-scale infrastructure push by the government, the sector is well poised to put the pandemic's destruction behind it. Further, realignment of cost structures by the industry players form a strong base for the profitability of the hospitality sector in the coming months.

Industry RevPAR's Inching to Pre-Covid Levels

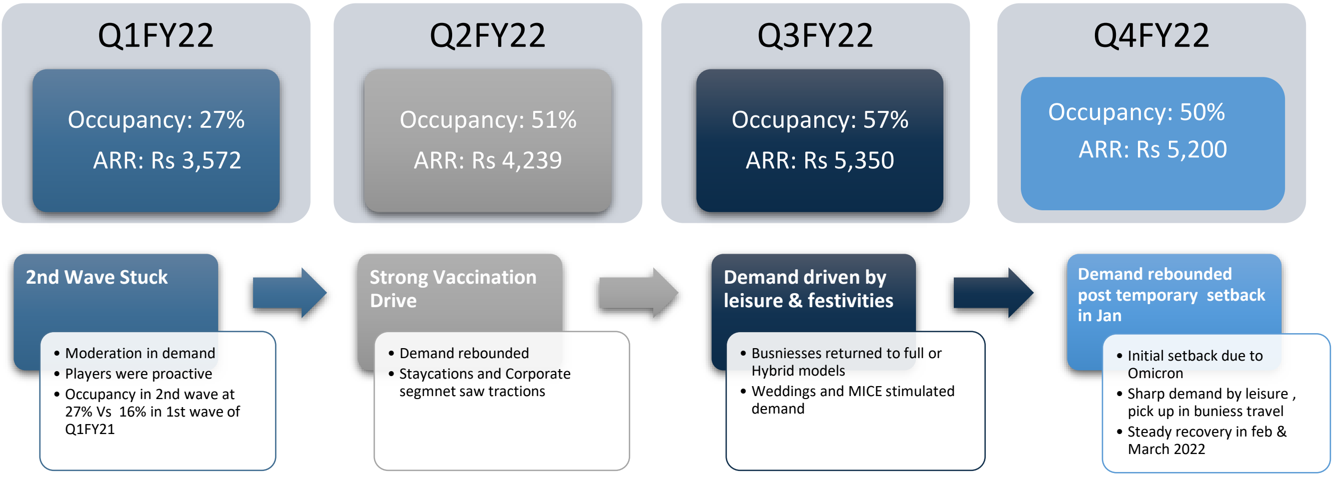
Chart 1: FY22 Performance Review

FY22			
	44-46%	↑	11-13 pp Y-o-Y
		↓	19-21 pp from FY20
	Rs 4,400 - 4,590	↑	13-14 % Y-o-Y
		↓	22 - 24% from FY20
	Rs 1,900- 2,100	↑	55-59 % Y-o-Y
		↓	45 - 47% from FY20

Source: CareEdge, HVS Anarock, Industry data.
pp: percentage points, ARR: Average room rate, RevPAR: Revenue per occupied room

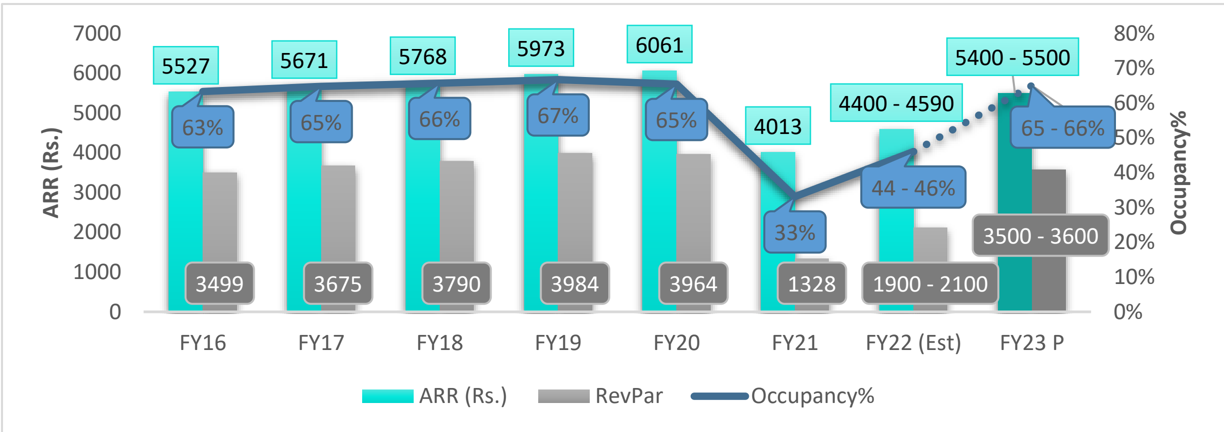
CareEdge had, in the last release in September 2021, forecasted average room rate (ARR) of Rs.4,414 and occupancy of 51% for FY22. As per the estimated data available for the hospitality industry, the fiscal year 2022 closed at ARR in the range of Rs.4,400 - 4,590 and occupancy of 44-46%. The performance of the industry improved significantly despite the temporary roadblock caused due to emergence of the third Covid wave (Omicron). The recovery, while slow, is visible quarter-on-quarter in FY22, though the same was again marred marginally in Q4FY22 by the impact of a temporary jolt of Omicron.

Chart 2: Quarterly Revival Journey



The onset of the Covid-19 outbreak in March 2020 was followed by a nationwide lockdown to contain the pandemic. The lockdown, which was implemented on March 24, 2020, continued till May 31, 2020, leading to a significant deterioration in the operating parameters of hotels in FY21. The occupancy plunged to 33% in FY21 from over 65% earlier. ARRs dropped by 35% in FY21. FY22 has been a promising year for the sector wherein the revival in the occupancy and RevPAR's has led to green shoots for the industry players. The decline in Covid cases, resumption of international flights from March 2022, and strong leisure and wedding demand are the positive factors that should lead to growth in occupancy and ARRs in FY23.

Chart 3: Occupancy Inching Back to Pre-pandemic Levels

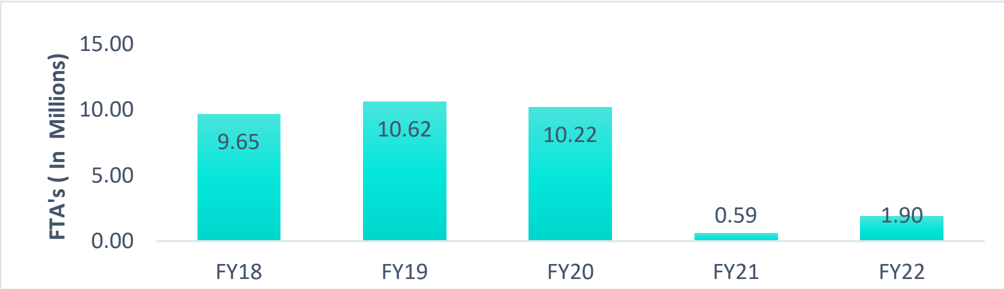


Source: HVS Anarock, CareEdge

Uptick in Foreign Tourist Arrivals

The sudden emergence of the Covid-19 pandemic forced countries to close their borders and suspend their international airline services, leading to an unprecedented fall in international tourism. According to CareEdge, the annual air passenger traffic in India registered a healthy compounded annual growth rate (CAGR) of 14% during FY17-FY19, thereafter, the same remained stagnant in FY20 and witnessed a steep decline during FY21 following Covid-19-induced disruptions. Foreign tourist arrivals (FTAs) witnessed a y-o-y de-growth of 94% during FY21. The impact began from March 2020, and on March 02, 2020, the government also started issuing travel restrictions in a phased manner.

Chart 4: FTA's Rising from the Lows of FY21



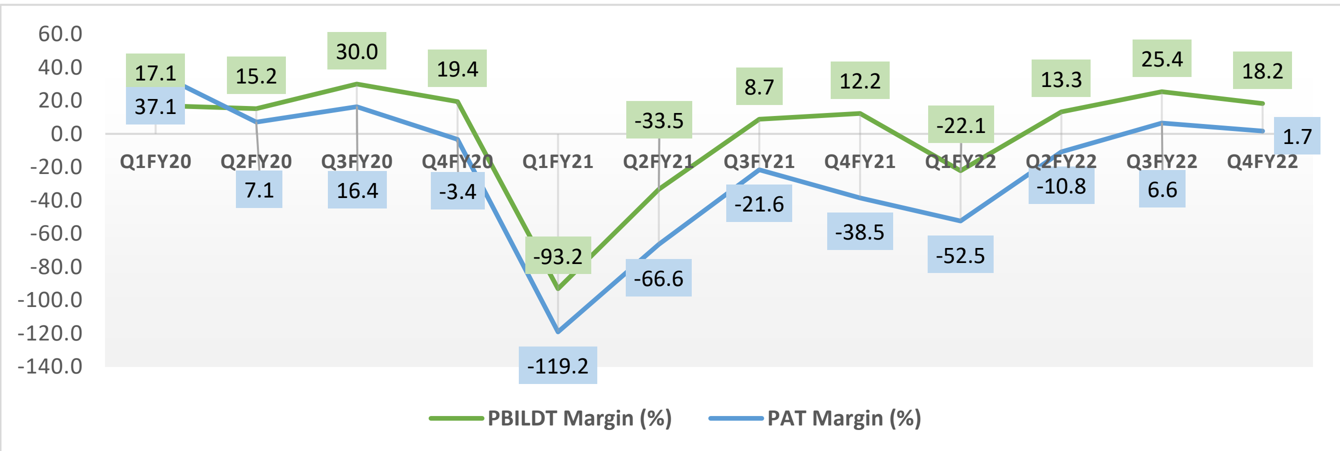
Source: CMIE, CareEdge

Though international travel continued to suffer in FY22 as well, there was a sharp recovery as compared to the previous year. Despite the strong upward movement, FTAs remained at about 20% of the pre-Covid levels. With the resumption of international flights from March 27, 2022, the international travel demand is expected to recover gradually through FY23 till the end of FY24. In April 2022, the number of FTAs recovered to reach 21% of total arrivals in FY21.

Improved Financial Performance and Tighter Cost Control Measures

The hotel industry's financial parameters reported significant improvement in FY22 as compared to the previous year. During the first Covid wave, apart from the room revenue, the hotel players also lost significantly on the food & beverages (F&B) portion, which typically contributes around 35%-40% of the total revenue. The same was restored to some extent in FY22, primarily due to the shorter impact of the second wave as well as no nationwide lockdown. Besides looking at alternative customer segments and revenue streams, albeit weak, the industry's focus has shifted to controlling and reducing costs significantly which include redeployment of manpower, downward salary revisions, renegotiating terms with utility service providers including internet, telecom, laundry, limiting buffet menus, centralisation, and automation of business functions. Sustenance in fixed cost-saving initiatives undertaken by all the players in the industry in FY21 and better operating leverage have been the supportive factors in FY22 as well. With the rise in occupancies, costs in FY22, though inched up marginally, the same were still lower than the pre-covid levels. As revenues improved amidst continued cost control, the industry has been able to post profits at the operating level this fiscal year. There has also been a marked reduction in net losses with the sector reporting a positive net margin for Q3 and Q4 of FY22.

Chart 5: Quarterly Profitability Trend from Pre-Covid to Post-Covid



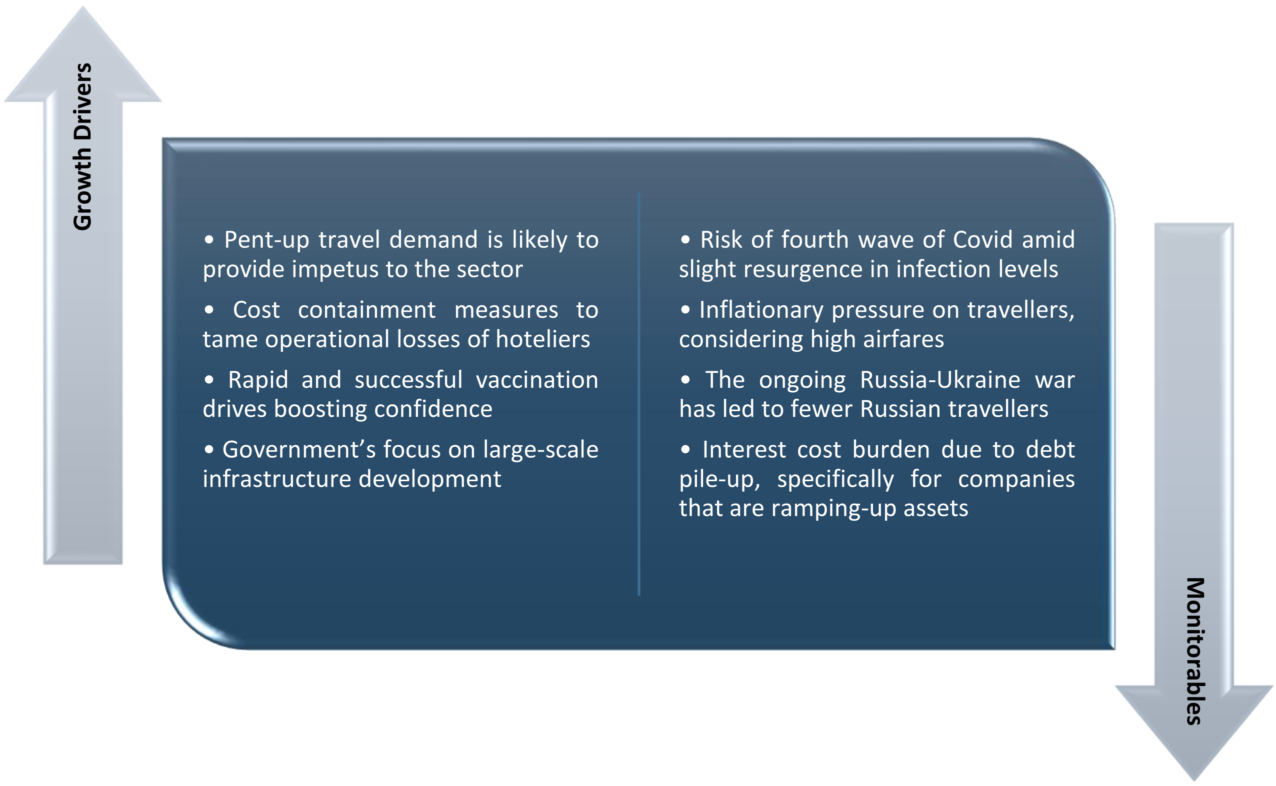
Source: CMIE, CareEdge (sample set of listed players)

However, the capital structure has deteriorated in comparison to the pre-pandemic period, as the operational losses pushed the hoteliers to mount up debt levels. Hotel companies with recent expansions or groups with a higher portfolio of new assets compared to matured assets are expected to face additional stress on their already weak financials. On the other hand, groups backed by strong promoters/ institutional support have been able to manage the difficult pandemic period with comparatively lower reliance on debt. From a credit perspective, such groups shall be better placed and are expected to have some liquidity reserves remaining post the covid years.

CareEdge View

With the pandemic leaving a long-lasting impact on consumer lifestyle and preferences, the travel industry is seeing a renaissance in the post-Covid era. New trends such as 'stress on sanitisation', 'escapism travel' and 'wellness tourism' are likely to shape the future of the industry.

According to CareEdge, the hospitality sector is slowly moving into 'hospitable territory', anticipating recovery of domestic and international travel gradually through FY23 till the end of FY24 to the pre-Covid levels. For FY23, CareEdge estimates the majority of its portfolio of hotel companies to report improved performance, largely restored to pre-Covid levels. Domestic tourism is expected to be the key growth driver, with international travel slowly gaining momentum, specifically post resumption of international flights. The situation is, however, still evolving and the same remains contingent on the possibility of another Covid wave and its severity on the sector. The operational profitability margins, which remained in the positive zone post Q1FY22, are expected to further improve to the pre-Covid levels during FY23, owing to improved demand outlook and sustained cost optimisation measures adopted.



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