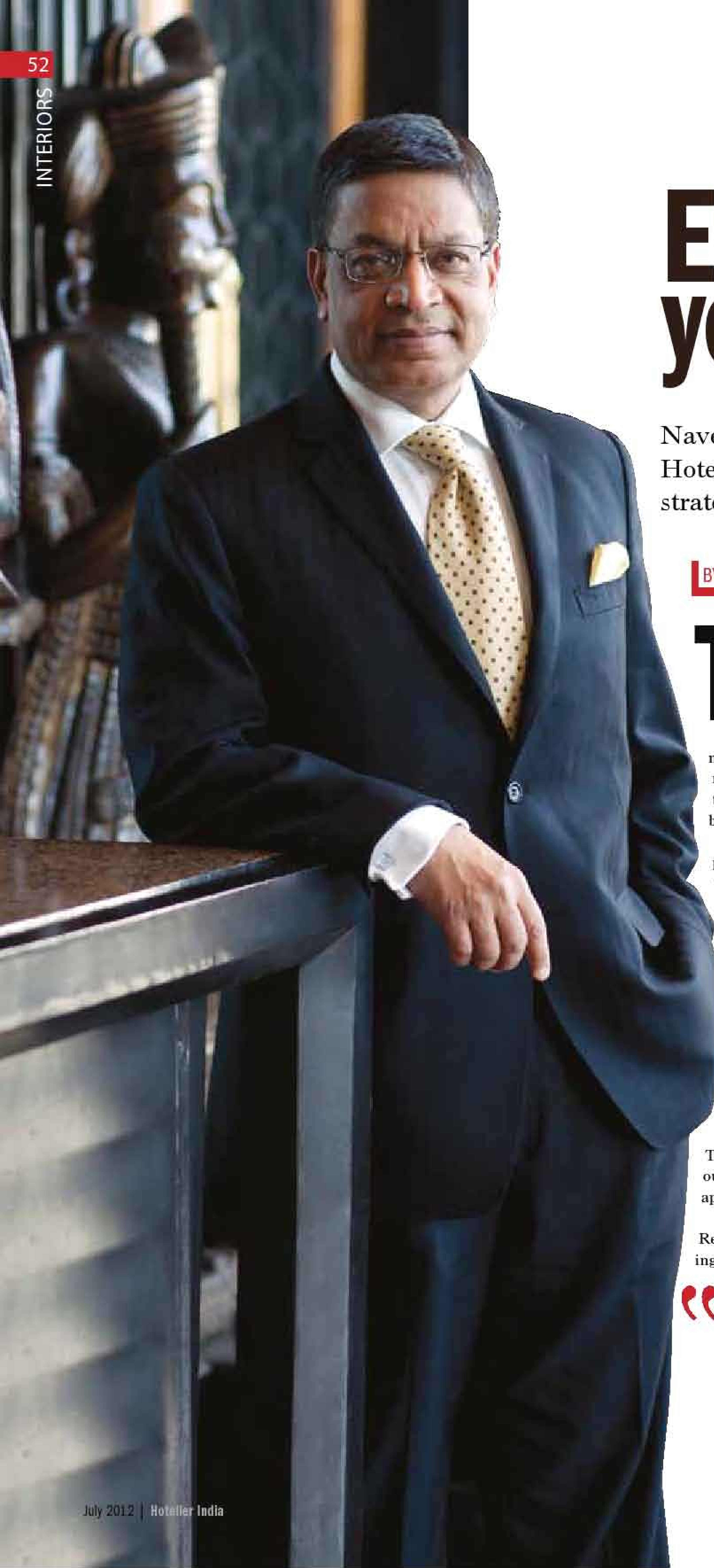


Efficiently yours

Naveen Jain, president of Duet India Hotels, shares secret of building and exit strategies of hotels asset.s

BY SHALINI SETH

Traditionally, Indian hospitality has had plenty of passion. Taking a cue from the Maharajas and often tracing their beginnings to a reaction to the Raj, Indian hospitality has been a bit of personal affair, with flamboyance as its calling card.

Naveen Jain, president, Duet India Hotels represents the new breed of Indian hotelier – his knowledge of the sector is matched by his astute financial acumen, his financial expertise is underlined by a desire to stay efficient and let the numbers do the talking.

For this new hotelier, being bigger and better is not a goal playing out at each property, but crystallises in the long-term vision for the company. Steering clear of luxury and resort segments, Duet India Hotels currently has a portfolio of eight hotels with approximately 1,400 rooms. This includes two operational hotels branded Four Points by Sheraton located in Jaipur (114 rooms) and Pune (217 rooms), and six under construction hotels located in Indore, Ahmedabad, Hyderabad, Bangalore and two hotels in Chennai.

"The next year is crucial for Duet India," says Jain, who has set yearly targets for the company until 2015. "Not only the next year, but the next three years are crucial for us. By that time our strategic goal would have completed. Then we will be a full-fledged hotel company. To take it public we have to have a particular inventory in our portfolio. We had the money and we are aggressive in our approach," he says.

Duet has strategic tie-ups with IHG, Starwood Hotels & Resorts, Interstate Hotels & Resorts and JHM Hotels, including a joint venture with IHG to develop 3,000 Holiday Inn

> "ZZZZZ ZZ SOFTENERS AND FILTERS IN INDIA ARE MOSTLY MANUAL, MEANING THAT THEY CREATE WASTAGE OF WATER AND SALT, AND ALSO REDUCE THE LIFESPAN OF EQUIPMENT."

THE DUET GRAPH

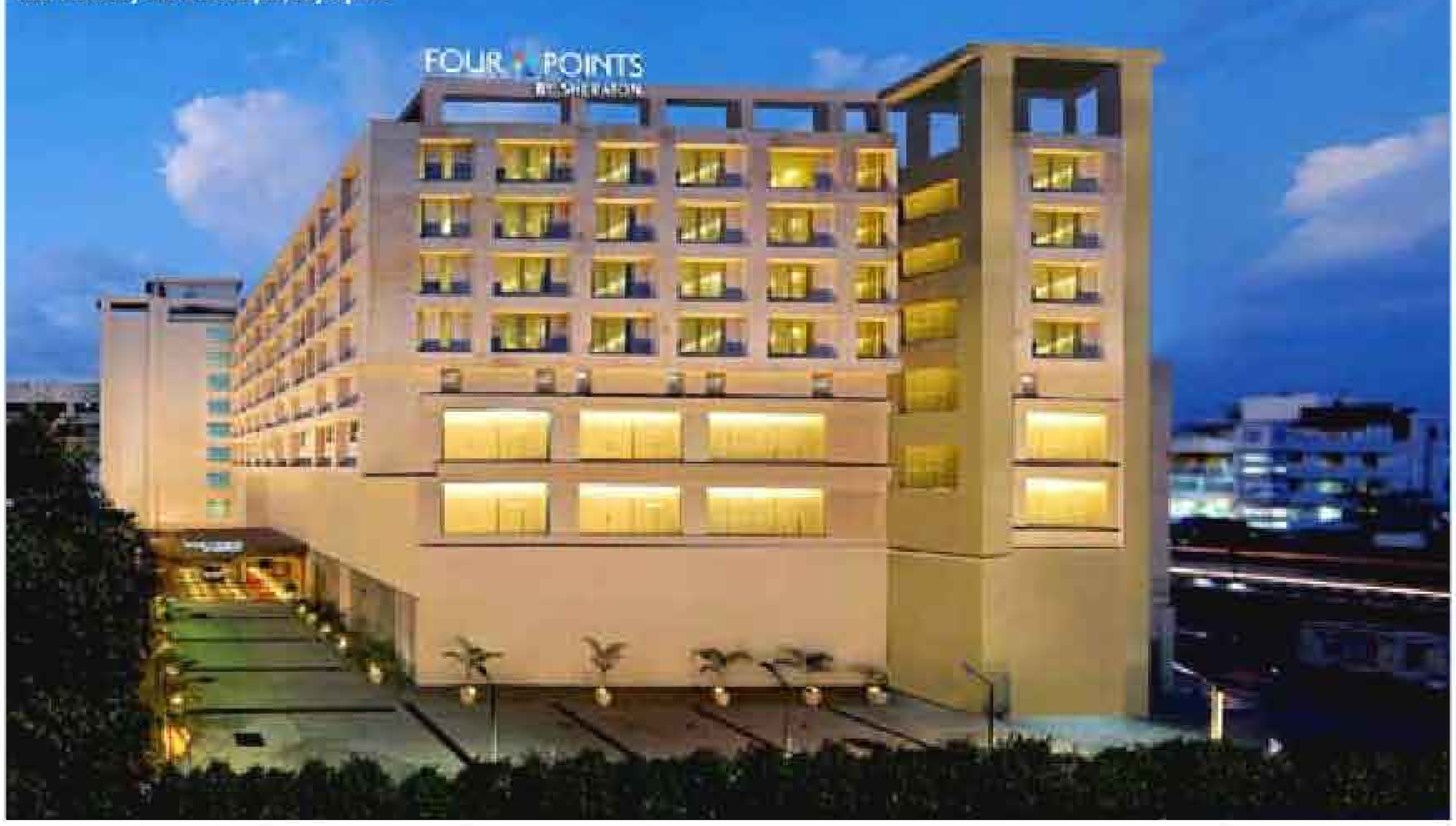
Operating Hotels:

- Four Points by Sheraton, Jaipur
- Four Points by Sheraton, Pune

Hotels under development:

- Ahmedabad
- Bangalore
- Chennai (two hotels)
- Hyderabad

Four Points by Sheraton Jaipur, City Square



Express rooms in India by 2015.

"Our first target will be to create hotels with our partner. Wherever we cannot do that and we think that particular location is suitable for us, we go ahead," says Jain.

Jain is quick to acknowledge how much he learnt during his tenure at the Oberoi Hotels, but he is not one to brag about achievements, which include being known as the man who introduced modern financial systems to the company's mammoth operations.

In his avatar at Duet India, which he joined at its inception as chief operating officer in 2008, he is credited with having raised debt from India's traditional public sector banks to match equity in a difficult financial climate.

Dilip Puri, managing director india and regional vice president, South Asia, at Starwood Hotels and Resorts worked with Jain at both Oberoi and Duet.

Puri, who was heading Duet India Hotels then, says Jain's remarkable feat as the COO was to give Duet the ability to raise debt in a difficult market at the start of the world economic downturn in 2008.

"No bank was willing to lend, we had no promoters, no guarantees to give to the bank. Yet we managed to raise Rs200 crore debt across our projects all from public sector banks, who are conservative and traditional. It was because of the solid business model," Puri says.

Puri relates that under Jain's financial stewardship, Duet India completely used its equity to buy land and start building, creating an important asset to mortgage, going against the developers' norm of approaching the bank at stage one.

"We had something tangible to show them and it showed we were serious. It was an innovative way to raise loans," says Puri.

Typically side-stepping from praise, Jain says: "Being an institutional player, Duet is able to leverage on the high credibility of its investors (which include large global names such as Goldman Sachs, Forum Partners, KCIC and JHM Interstate) and its vast development experience and network to have access to a funding pipeline at reasonable interest rates."

The strength of Duet India as a hotel company is that it is completely different from family-run construction giants, traditional Indian owner-operator companies and single-unit developers who work with large brands.

"Duet is different from all three," he says, explaining, "unlike a family-owned construction giant such as DLF or Unitech, Duet's focus is limited to a single asset class and it has in-house management overseeing capability."

"An owner-operator such as ITC or Taj has a long-term focus and does not look to exit investments. Duet – being lacked by large institutional investor – has a clear focus by way of maintaining strict cost and operating efficiencies in order to realise investor profit in a limited (seven to 10 year) investment horizon."

HOW TO GET THE RIGHT BRAND: NAVEEN JAIN'S MANUAL FOR OWNERS

Brands typically choose to invest in markets where:

- They believe they can get access to prime assets at a reasonable valuation resulting in significant capital growth
- They have a prominent and stable presence by way of their operating and marketing infrastructure
- Ability to partner with a stable, knowledgeable and well-funded development partner whose investment goals are in consonance with that of the brand.

This will lead to the brand being able to develop, own and manage marquee assets across the country and profit by way of:

- A steady income by way of management contracts
- Share in the operating profits by way of the ownership structure
- Capital appreciation of the underlying asset and gains during exit

On the other hand, "large brands such as Starwood, Marriott and IHG typically do not have acquisition, development, fund-raising and exit capabilities. Their expertise is limited to hotel management and operation," he says.

Duet, with its focus on mid-scale and upper mid-scale is asset-focused intent on delivering best in class investment returns by staying both world-class and efficient. It's carving a niche in the high-growth market where branded hotels (India has 130,000 hotel rooms of which 62,000 are branded) are conspicuous by their absence. The strong projected demand growth for 75,000 new hotel rooms given business and leisure travel CAGR forecast to be 11.6 per cent and 13.7 per cent through 2015, and very low hotel penetration vis-à-vis international markets is another indicator that Duet is on the right track.

"These are assets created for the domestic traveller. There is a gap between five-star hotels and guest houses," says Jain.

According to Jain, given the economic growth story of India and the burgeoning demand for hotel rooms due to increasing domestic demand and international travel, hospitality as a sector remains a profitable investment option in India.

He says: "There are broadly three investment options for an

Dilip Puri

COST-SAVING DURING CONSTRUCTION

- Commission designs after thorough discussions with brand and the local building regulations.
- Domestic procurement to avoid import duties and time-lag between purchase and receipt.
- Local advisors and consultants such as interior decorators, architects, project managers, etc., who understand the local consumer and development best practices.
- A cookie-cutter approach which helps us cut down on the development time and effort and saves costs.

investor interested to invest in Indian hospitality Industry – the listed companies, operating hotels and Greenfield hospitality projects. Of the three options, Greenfield projects offer maximum return in India – v/s acquisition of operating hotels and investment in listed entities, which are the preferred investment routes overseas, such as Blackstone's acquisition of Hilton Hotels in 2007."

Last year, two major global brands entered into joint venture arrangements with India-focused investors: IHG with Duet India Hotels and Marriott with SAMHI. For international brands the emerging Indian market is different in that it is one of the few that they choose to invest in. Jain says that the availability of larger institutional players and investors focused on hotel-sector investment is one of the key factors, apart from the obvious demand.

Traditional hotel companies often stay wary of that institutional capital since it comes in at value and gets out in too little time – five to seven years as compared to the eight to 10 years that hotel companies think is optimum.

Jain says, "Hotel investment is very different from conventional real estate investment, especially in developing markets, in the way that hospitality requires specialised asset management skills to be able to deliver the anticipated returns. Duet's investment strategy is to own, develop and operate assets in an efficient and professional manner. Duet typically projects a two to three year development period for its assets, followed by a four to five year operating term until the asset's operations stabilise."

Even though exit options for investments in India are limited since existing regulations do not allow presence of Real Estate Investment Trusts (REIT) which are a viable exit option in mature markets. To add to that, India has not seen too many sales of individual hotel assets or portfolios. Valuations for operational properties in India are very high and do not offer a significant return to a rational investor. However, says Jain, "Capital markets in India are mature and provide a decent exit option."

Profitable it may be, but in choosing to develop hotels in India, an investor opts for a difficult market. The investment decision into a Greenfield project includes screening, planning, implementing and operating hotels.

"The biggest barriers for India include high land prices in key Tier I markets, coupled with related issues on land ownership and titles. The land titles and the governing development norms are many times not clear and require detailed legal and technical due diligence. Further, obtaining approvals is time consuming and obscure as a process, especially for institutional investors," says Jain.

Being dispassionate about risks can help minimise them and create viable rescue plans. Jain says, "The industry has seen the entry of several institutional players and funds, which are leading to greater organisation in and bringing more stability to this sector. Hotel industry in India has a lot of potential given the current demand and supply scenario. Hospitality has mostly given consistent returns and thus not very risky for an investor who understands the supply-demand dynamics. However, one has to take a long term view as the assets take time to stabilise. Being cyclical in nature it is important to time the investment and exits."

Efficiency is the mantra for the new Indian hotelier, different from the norm. International brands acknowledge that India is one country where the owner is likely to push the brand right out of its original segment by ego-based construction.

"At Duet," Jain says, "we are very brand focussed. Right in the start we have a discussion on the design, we sign off the design and then the construction begins. It is efficient from the viewpoint of cost. We don't keep changing our design. We don't keep working out the product. We are also value engineering in our construction – it reduces the duration to bring the cost to the optimum level."

While operational efficiency is now prevalent in Indian hotels, construction efficiencies are important in the new way of doing business. Jain says Duet has introduced many of these, including using local products which earlier used to be imported. Taking a long-term view, Jain is hopeful that as infrastructure development quickens in India, efficient construction would mean setting up factories here.

With efficiencies that cover the gamut of hotel sector – design, construction and operations, one wonders why Jain shies away from the limelight. He says: "Let us first achieve something. Then, automatically, one comes to the forefront." HI