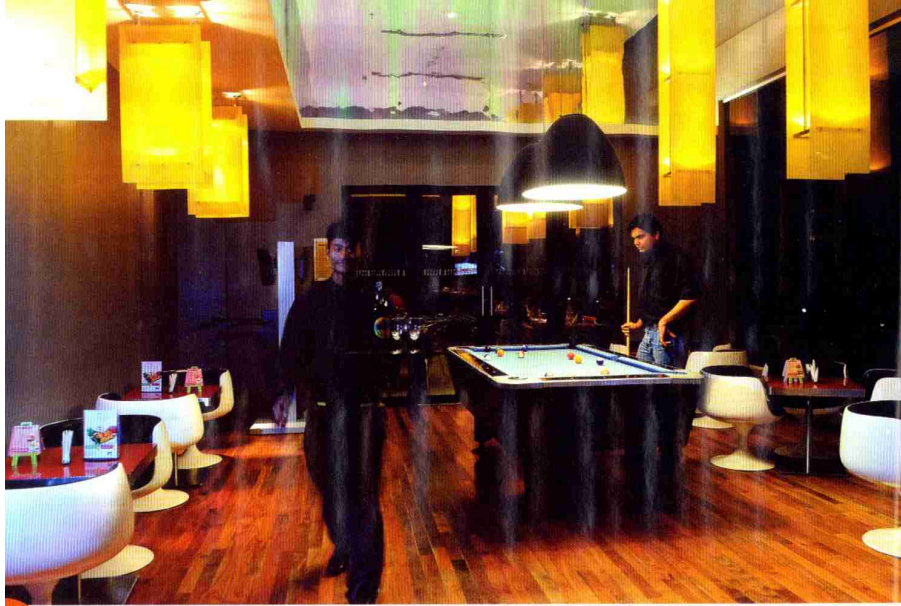


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THE MIDDLE GRO

Baishali Mukherjee, 27, works as a mid-level executive with an auto firm in Mumbai and travels three or four times a month to auto ancillary hubs such as Pune, Aurangabad and Chennai. While she dislikes the incessant travelling, it is a necessary evil. But, on the upside, travelling is a bit more pleasant now. "Earlier, these places only had very expensive luxury hotels or small hotels that were not very reliable when it came to basics like cleanliness, safety and services. But now my company

books me into hotels like Keys, Fortune Park and Lemon Tree that have taken care of these problems," she says. The affordable tariffs even helped Mukherjee enjoy a weekend break in Lonavla with her friends on a whim.

Customers like Mukherjee have caught the eye of the mid-market hotel industry, which caters

to mid-rung business and leisure travellers. She and many others are part of a 300 million-strong middle class that shrinks from shelling high-end tariffs but appreciates good hotels with rack rates of ₹5,000-5,500 per day. At the same time, corporates, which account for over 65% of the luxury hotels business, have cut back on their

spending. "The increase in demand has insulated the mid-market segment from severe price erosion," says Sanjay Sethi, MD, Berggruen Hotels, which runs the Keys brand. Average room realisations (ARR) of mid-market hotels have dropped by 25% compared with luxury hotels, which saw an erosion of about 40-50% from 2008 to 2011, claim industry experts.

No wonder it's this segment of the hotel industry that's seeing maximum action (*See: More to come*). The line-up would tempt even arm-chair travellers, with both domestic and international companies laying out the red carpet to their mid-market properties, among

them Indian Hotels' Ginger and Gateway brands, Berggruen's Keys and Fleur Hotels' Lemon Tree and Lemon Tree Premier. Hilton, Accor, Carlson Hyatt, Marriott and Starwood have also announced plans of expanding their mid-market portfolio. Hospitality industry consultancy HVS India says that 93,355 rooms will get added to the existing 84,000 by March 2017 across major cities, of which over 50% will be in the mid-market and budget segments. "Currently, only about 20% of the hotel rooms in India are in the mid-market space compared with about 65% globally," says Rahul Pandit, presi-

dent, Lemon Tree and Red Fox Hotels. Others like Suresh Kumar, CEO of ITC Fortune Park, too, are gung-ho on the space. "This segment of hotels has become popular as it appeals to both — the investors as well as the guests. While an investor gets a model suited to his capital deployment capability, the domestic traveller gets convenience and comfort at an affordable price," he says.

CHEAP AND BEST

There are a few other big reasons why mid-market hotels have become hot properties. Building and running a mid-market hotel

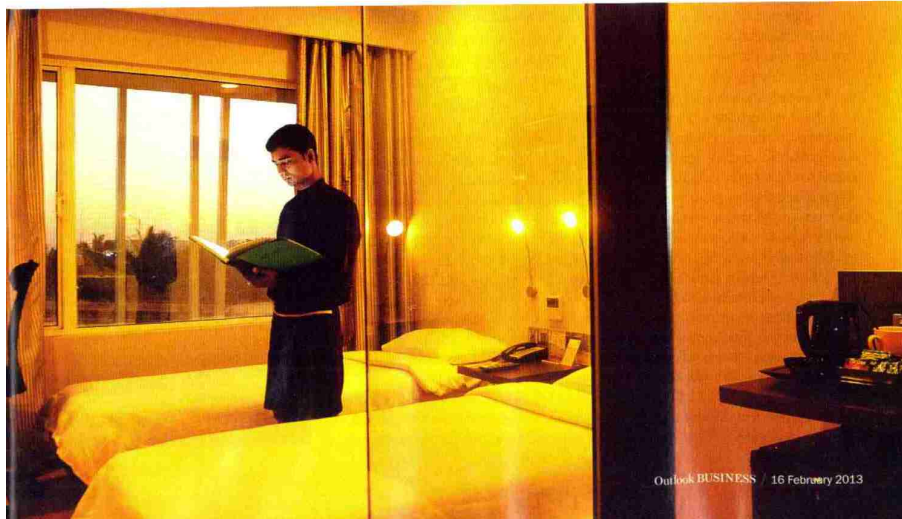
is much cheaper than a luxury hotel. This means that breakeven and profits come faster. It is not surprising when hoteliers such as Jean-Michel Cassé, senior VP, Accor India, say, "Even as the company is planning to develop hotels under the luxury brands, our main focus will be the economy and middle scale segment." First off, the cost of running a mid-market hotel, which needs about 60 staffers per 100 rooms, is considerably lower than the 200-250 required for a 5-star hotel of a similar size. The development cost is also much less. HVS India says it takes between ₹1 crore and ₹2.75 crore to devel-

IS LOOKING UP

ND

Mid-market hotels are finally offering guests better-than-budget properties for cheaper-than-luxury prices
Taneesha Kulshrestha

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op one room in a luxury property while the cost incurred for the same is between ₹35 lakh and ₹85 lakh for a mid-market hotel.

That said, hotel developers have to factor in the cost of land that is, on average, 20% of the final cost of the property in the US and 10% in China but 50% in India. Moreover, luxury hotel rooms are bigger (375-400 sq ft) compared with mid-market rooms (about 300 sq ft). "Assuming the same plot area, you get more rooms and hence, higher revenue," says Om Goenka, owner, Citrus Hotels, which has eight properties in cities such as Goa, Pune, Bengaluru and Alleppey. On average a mid-market hotel breaks even in about four years.

"Our aim is to have an 18% return on capital across properties and that is why we go the extra mile at the construction stage," says Pandit. Citing the example of a basic 300 sq ft room, he explains, "If market research shows that a third of the probable customers will be couples, a third singles, and the rest two-bed singles, then, a third of the hotel will have 285 sq ft rooms that can accommodate a single queen-sized bed. This 15 sq ft saved translates into an additional two rooms in a 100-room hotel."

With the lower cost model, the hotels are also able to tap the latent demand in non-metros. For instance, in the pilgrim town of Rameswaram, a one-night stay at Daiwik will set you back by ₹2,800. "Travelling for religious purposes does not mean you have to stay in a *dharamshala*," points out Debashish Ghoshal, managing director and CEO of Daiwik Hotels. "I do not think we are ready for 5-star hotels at these locations yet but it made sense to open a mid-market hotel," he adds. Over a two-year period, the company plans to have 2,000 hotel rooms in 15 pilgrimage centres, including Madurai, Varanasi and Srisailam.

More to come

Mid-market hotels are growing thanks to overwhelming demand

CITY	NO. OF HOTELS IN FY12	PROPOSED NEW SUPPLY	MID MARKET (%)
Agra	1,739	650	80
Ahmedabad	1,975	2550	90.2
Bengaluru	7,713	9,716	80
Chennai	4,904	7,547	79.8
Delhi	10,697	5,626	81.6
Goa	3,885	2,422	95.7
Gurgaon	3,782	5,818	76.8
Hyderabad	4,797	5,265	87.6
Jaipur	3,054	3,356	96.7
Kolkata	1,787	3,118	79.4
Mumbai	12,052	10,896	70
Noida	527	5,522	67.5
Pune	5,672	4,645	87.8
Other cities	21,729	26,224	99.3
Total	84,313	93,355	85.5

CONFUSED MIDDLE

Despite this demand demarcation, segmentation is hazy. Internationally, the market is neatly segmented into budget (\$50 to \$75), mid-market (\$75 to \$150), upscale (\$150 to \$300) and luxury (upwards of \$300), but in India it is not that clearly defined. This means that hotel brands can easily get their price-product proposition wrong and err on the side of too little or plenty. Service expectations, a key differentiator in the hospitality industry, differ as well. "Foreign brands are accustomed to differentiating themselves on the basis of service though the product remains more or less the same," says Lemon Tree's Pandit. Premier Inn, for example, is positioned as a budget brand globally and does not offer services like in-room dining and service internationally. But, in India, it has positioned itself as a mid-market chain with an expanded in-room menu and service. Another example, a room at a five-star Ista sells for about ₹6,500

in Bengaluru's MG road while a Lemon Tree Premier also commands the same tariff. Premier Inn India's country head Shwetank Singh says these fuzzy boundaries arise as the Indian market has had only luxury properties or poorly-run hotels in the past. "Quality consciousness is just setting in and most notions of hospitality in India come from five-star or four-star properties. The consumer, hence, is not very clear what mid-market or budget stands for," he says.

In any case, the concept of a "budget hotel" comprising a clean basic stay and minimum service does not seem to be taking off in India. Goenka narrates the example of his property at Pimpri, an industrial hub in Maharashtra where his hotel is next to a Ginger that charges about ₹2,000 compared with a Citrus rate of around ₹4,500. "Almost everyday, you have guests switching over to us. Concepts like Ginger work if you have to stay for a night or two and just

"The increase in demand for mid-market rooms has insulated the segment from price erosion"

—SANJAY SETHI
MD, Berggruen Hotels



TUSHAR MANE

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need a bed to crash, but anything more than that, you need basic services," he says.

Others, too, are experimenting and learning. "We had a lot of discussion around whether we should have room service in Red Fox or not," Pandit recalls. "We tried to do without but there were sharp reactions." Lemon Tree, in fact, first decided not to provide newspapers but had to introduce them after adverse feedback. Consulting firms like HVS India expect the "price-value" expectation to get better defined as international brands arrive and the market matures.

The mid-market proposition only gets more complex when it comes to the line dividing business and leisure tourism. Contrary to expectations, it is not just business travellers that are driving the mid-market segment. "For us, it is a 60:40 mix," says Citrus Hotel's Goenka. Even for Keys Hotels, the focus is equally on the tourist as well as the business travellers. "For a property like Lonavla, which is close to Mumbai, we see that for four days it is business meetings, conventions and seminars that drive traffic. But for the remaining three, we get the leisure traveller," says Sethi, adding that he expects domestic tourists and not business travellers to drive future growth. "But then, if a person is spending money from his own pocket, his expectations do go up. So you will eventually end up adding a pool or a spa. This is not something that you will find in most mid-market hotels abroad," adds Goenka.

Most hotels are beginning to balance customer expectations and their product to ensure that they earn their monies. Keys, for instance, creates a well-lit friendly common area that has pool tables and Xbox games, not to mention well-trained bartenders and staff. "We found that our billings from the bar and F&B have gone



PHOTOS: VISHAL KOUL



“Our aim at Lemon Tree and Red Fox is to have at least an 18% return on capital across properties

—**RAHUL PANDIT**
President, Lemon Tree Hotels

up,” exults Sethi. “Guests also invite friends over to catch up with them.” Similarly, Lemon Tree is paying extra attention to women travellers, who make up 15% of its clientele. It tries to ensure that female guests feel safe and are given extra care and attention when visiting its properties.

TRUBLE IN PARADISE

All that calculated optimism does not eliminate ground realities. Al-

ready, some hotel groups are struggling under high debt because of heavy expenditure incurred on acquiring land. Kamat Hotels, which owns the Orchid brand, is now trying to sell three land parcels in Coimbatore, Nagpur and Raipur to pay off debts of ₹435 crore. It is also revamping its operations to focus on franchisees. The rest of the players, too, are proceeding with caution and an asset-light model where existing operators teaming up with landowners is in vogue. Sethi says, “It’s prohibitive to buy land in places like Gurgaon. Initially, we followed an asset-heavy policy for Keys. But now, we intend to make selective acquisitions.”

Declining ARRs, at least in the short term, will be another factor

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affecting profitability. There is no denying that mid-market hotels are coming up at a time when supply of rooms is already high, and occupancy rates and ARRs are falling. HVS India notes that while the supply of rooms was up by 18% over last fiscal, the average occupancy rate was down to 59.1% in FY12 as compared to 60.6% in FY11 and 68.8% in FY08. ARRs, too, declined from ₹7,989 in FY08 and ₹6,513 in FY11 to ₹6,257 in FY12. Rating agency Iera expects hotel industry demand to shrink by 5-6% in FY13 even as room supply is expected to increase about 13-15% across key markets. The end result could be a further erosion of 5% in ARRs.

But HVS India counters that, saying recent reports are overplaying a doomsday scenario. It says that while the major cities witnessed a 15% increase in supply in FY12, demand too increased by 12%. "Even when average occupancy declined in FY12, it is important to note that it was owing to supply increasing faster than demand, and not due to an absolute decline in demand," says Kaushik Vardharajan, MD, consulting and valuation practice, HVS India.

Moreover, hotel developers are quite accustomed to the long gestation of the sector and are not



BHUPINDER SINGH

worrying about over-supply. Patu Keswani, founder of Lemon Tree, is planning 35 more hotels in a partnership with Dutch group APG over the next five years. Others like Uttam Dave, president and CEO, InterGlobe Hotels, is currently developing 19 Ibis hotels with 3,600 rooms to be opened across India by 2015. He says, "Our decision to ramp up development is based on the rapid economic growth that we are seeing across the country, combined with the acute shortage of quality hotel accommodation at value-for-money prices."

Much of the hotel industry's optimism is also based on the reversal

"This segment of hotels has become popular as it appeals to both — the investors as well as the guests"

—SURESH KUMAR
CEO, Fortune Park Hotels

of the hotel industry cycle, typically a seven-year one. "I think 2013 will not be very good, but post 2014, I expect good years," says Citrus' Goenka. His optimism is also based on markets like Whitefield outside Bengaluru, where demand is growing minus fresh supply. A market like Pune, on the other hand, will worsen before it improves, he adds. Compared with other major cities around the world, metros and mini-metro cities in India have a far lower supply of affordable quality rooms. "Even with the estimated addition of around 60,000 rooms across India in the next five years, there will still be a shortfall, providing a huge opportunity to investors and operators across all segments," says ITC's Kumar. Like all things Indian, the potential might be immense, but only those operators with the right business model, a keen eye on costs and customer expectations will survive to reap the benefits. ☺

The masterplan

Luxury hotels see the mid-sized market as the new cash cow

HOTEL GROUP	BRANDS	NO. OF HOTELS IN INDIA	TARGET SIZE
Choice Hotels	Comfort, Quality, Sleep Inn, Clarion	25	2,000 rooms by end 2012
Marrriott Hotels	Courtyard by Marriott	1	24 hotels, 8,000 rooms
Carlson	Park Plaza, Country Inn, Park Inn	6 Park Plaza and 2 Park Inn	Park Plaza: 672 rooms, Park Inn: 391 rooms, Country Inn: 15 rooms
Indian Hotels	Gateway Hotels, Ginger	Gateway: 15, Ginger: 26	Gateway: 30 hotels by 2015, Ginger: 80 hotels by 2015
IHG	Holiday Inns and Resorts	11	31 hotels by 2015
Sarovar Hotels	Park Plaza, Sarovar Portico, Homitel, Park Inn	35	100 hotels by 2020
Fleur Hotels	Lemon Tree Premiere, Lemon Tree, Red Fox	16	35 hotels by 2017 with APG
Berggruen Hotel	Keys Hotels	27	50 hotels by 2016