

## HOTELS

### Sector Impact - Positive

#### Background

- During FY09, the global economic slowdown combined with Mumbai terror attacks adversely affected the hospitality industry leading to a drop in Foreign Tourist Arrivals (FTAs) by 2.5% y-o-y to around 5.1 million. In an attempt to boost occupancy, hotels reduced Average Room Rents (ARRs) considerably in FY09. As per media reports, room rates for the five-star category in Mumbai and Delhi were down by 38% and 44% respectively, in the March 2009 quarter. However, demand remained subdued in H2FY09, which continued for the first half of FY10. This caused Revenue per Available Room (RevPAR) to drop thereby putting pressure on the margins of hotel companies. [*Source- Centre for Monitoring Indian Economy (CMIE)*].
- The second half of a financial year is the prime season for the hospitality sector, and FTAs have shown an improvement in the December 2009 quarter with a decent growth of 7% in the December 2009 quarter, with FTAs touching an all-time high in December. (*Source- CMIE*). The improvement in FTAs is a positive sign for the hotel industry as they dominate the demand in the five-star category covering over 60%. Also, the Delhi Commonwealth Games are expected to stimulate the tourist arrivals in FY11.
- The improvement in FTAs along with revival in domestic corporate travel will help boost occupancy which will enable hotel companies to increase ARR's which in turn will improve RevPAR and profits will grow.
- The hotel industry is expected to stage a recovery in the March 2010 quarter with a sales growth of 15%. Profitability of the industry is also expected to improve. The industry is expected to wrap FY2009-10 with a fall of 6.3% in sales and a contraction of 400 basis points in the PAT margin to 9.8%. The growth momentum in FTAs is expected to continue in the March 2010 quarter, registering a growth of 11.7%, on a y-o-y basis. (*Source- CMIE*).
- The challenges faced by the sector are lack of industry status at the central level has prevented companies from enjoying tax exemptions and other benefits. Other issues faced by the sector are differential state taxes and absence of facilities like visa-on-arrival facility and single-window clearance for tourism projects.

## Budget Proposals

1. Section 35AD of the Income tax Act, which provides for deduction in respect of expenditure of capital nature has been amended to include building and operating a new hotel of two-star or above category as classified by the Central Government should commence its operation on or after 1st April, 2010. This amendment will take effect from 1st April, 2011 and will, accordingly, apply in relation to the assessment year 2011-2012 and subsequent years. The capital expenditure above does not include cost of land, goodwill and financial instruments.
2. The time line for commencing operation under Section 80-ID of the Income tax Act relating to deduction in respect of profits and gains from business of hotels and convention centres in specified areas has been extended from 31<sup>st</sup> March, 2010 to 31<sup>st</sup> July, 2010.

## Duty Structure

(%)	Existing	Proposed
<b>CUSTOMS DUTY</b>		
<ul style="list-style-type: none"> <li>• Under Export Promotion Capital Goods (EPCG)*</li> </ul>	3	3
<ul style="list-style-type: none"> <li>• Under the Served From India Scheme (SFIS), 5% of Forex earnings is granted as credit which is available for set off custom duty on Imported items like liquor, cigarettes etc.</li> </ul>	Set-off available	Set-off available
<b>SERVICE TAX (On 60% of applicable turnover)</b>	10	10

\* subject to an export obligation equivalent to 8 times of duty saved on capital goods imported under EPCG scheme, to be fulfilled in 8 years reckoned from Authorisation issue-date

## Budget Impact: Industry

1. The inclusion of hotel business under specified business under section 35AD is a boon for the hospitality industry and will help them to reduce their direct tax liability, hence, improve margins.
2. The extension of time line under section 80-ID will help operators whose projects have been delayed to take benefit exemption.

**Budget Impact: Companies**

Company	Applicable Proposals	Overall Impact
The Indian Hotels Company Limited	1 and 2	▲▲
Hotel Leela Venture Limited	1 and 2	▲▲
Kamat Hotels (India) Limited	1	▲▲
Jaypee Hotels	1 and 2	▲▲

**Legends:**

▲▲	Highly Positive	▼	Negative	◄►	Neutral
▲	Positive	▼▼	Highly Negative	∅	No Proposals