Cox & Kings – BUY

27 November 2017

Management meeting

IIFL Institutional Equities

HBR stake swap sets valuation benchmark

The recent change of hands in the minority stake in Holidaybreak (HBR) sets a benchmark EV of c.£600m for HBR, and implies a significantly higher EV/Ebitda multiple (c13x FY18ii) for HBR than we ascribe (10x) in our SOTP for Cox & Kings (C&K). Furthermore, our estimates project nearly 50% growth in HBR's Ebitda over FY18-20, driven principally by aggressive bed addition at Meininger. If we increased our target EV/Ebitda multiple to 13x, our SOTP valuation would increase by c.Rs60 per share to Rs420. Meanwhile, C&K's other businesses remain steady and leverage is comfortable.

Transaction sets valuation benchmark for HBR: We understand from media reports, that SSG Capital's purchase of a 34.4% stake in HBR from The Rohatyn Group, announced on November 16th, was at an aggregate EV of c.$800m (c.£600m). This implies an EV/Ebitda multiple of c.13x, based on our FY18 estimate of £46m of Ebitda from HBR. It also implies that HBR's EV has been marked up from £512m in 2012 to £600m now despite the divestiture of numerous businesses.

HBR Ebitda set for rapid growth, driven by Meininger: Meininger's expansion plan is expected to ramp up its bed count from c.8,500 currently to c.15,000 by March 2019 and c.25,000 by March 2022. Although Meininger's Ebitda is unlikely to grow in FY18 due to substantial investment in senior management addition, FY19-20 could see Ebitda almost doubling versus FY18 levels. This is the key driver of the nearly 50% growth we project in HBR Ebitda over FY18-20.

Other businesses performing steadily; valuations attractive: The leisure travel business (both in India and overseas) continues to generate steady earnings growth despite competitive pressures. Working capital did increase in 1H FY18 and is a concern; yet, overall net debt-to-Ebitda remains comfortable at c.2.5x. At a 12x FY19ii P/E, valuations are attractive. Our SOTP too suggests a substantial discount to fair value, even at just a 10x EV/Ebitda multiple for HBR (versus the 13x benchmark set by the recent transaction).

Company update

CMP	Rs264
12-mth TP (Rs)	360 (37%)
Market cap (US$m)	719
Enterprise value(US$m)	1,120
Bloomberg	COXK IN
Sector	Travel & Tourism

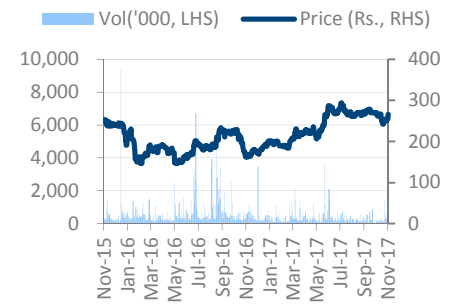
Price performance (%)

	1M	3M	1Y
Absolute (Rs)	(1.3)	0.5	62.4
Absolute (US$)	(0.8)	(0.2)	67.9
Rel. to Sensex	(4.6)	(6.1)	32.2
Cagr (%)		**3 yrs**	**5 yrs**
EPS		(22.3)	NM

Shareholding pattern (%)

Promoter	51.3
FII	33.3
DII	5.5
Others	9.9
52Wk High/Low (Rs)	306/159
Shares o/s (m)	177
Daily volume (US$ m)	1.1
Dividend yield FY18ii (%)	0.4
Free float (%)	48.7

Stock performance



Financial summary (Rs m)

Y/e 31 Mar, Consolidated	FY16A	FY17A	FY18ii	FY19ii	FY20ii
Revenues (Rs m)	20,274	21,790	24,274	26,547	30,404
Ebitda margins (%)	*40.1*	*31.2*	*39.3*	*35.9*	*36.7*
Pre-exceptional PAT (Rs m)	2,441	1,531	3,961	3,721	4,874
Reported PAT (Rs m)	507	1,470	3,863	3,721	4,874
Pre-exceptional EPS (Rs)	13.8	8.7	22.4	21.1	27.6
Growth (%)	*(28.1)*	*(37.3)*	*158.8*	*(6.0)*	*31.0*
IIFL vs consensus (%)			*16.8*	*(12.2)*	*(13.9)*
PER (x)	**19.1**	**30.4**	**11.8**	**12.5**	**9.6**
ROE (%)	*9.6*	*6.1*	*14.2*	*11.8*	*13.7*
Net debt/equity (x)	0.9	0.8	0.6	0.5	0.3
EV/Ebitda (x)	9.3	10.6	7.5	7.3	6.0
Price/book (x)	1.9	1.8	1.6	1.4	1.2

Source: Company, IIFL Research. Priced as on 24 November 2017

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Holidaybreak stake swap sets valuation benchmark

C&K announced on November 16th that SSG Capital has acquired The Rohatyn Group's 34.42% stake in Cox & Kings' subsidiary, Prometheon Holdings (UK), which is the holding company of HBR. According to media reports, the transaction was consummated at an aggregate enterprise value of c.$800m (i.e., c.£600m). We understand that net of outstanding debt at HBR, the equity valuation works out to c.£484m. The implied value of C&K's 65.58% stake in HBR is therefore c.£317m. The Rohatyn Group had acquired the stake through a buyout of PE firm Citigroup Venture Capital International (CVCI) in 2013.

Based on our FY18 Ebitda estimate of c.£46m for HBR, the implied EV/Ebitda multiple is c.13x, which is well above the 8x multiple paid by C&K when it acquired HBR (including Meininger) during the period 2011-14. The main reason for the significant increase in valuation multiple since then is that HBR's two best businesses (Education Travel and Meininger) now represent 100% of its portfolio, whereas in 2011, they contributed less than half of HBR's overall Ebitda, with the remainder coming from lower-multiple businesses such as Camping, Superbreak and Explore. All these other businesses have been divested over the years, and in addition, Ebitda from the Education Travel and Meininger businesses has grown materially since their acquisition.

We currently assign a 10x EV/Ebitda multiple to HBR in our SOTP for C&K. If we increased our target multiple to 13x, our target price for C&K would increase by c.Rs60 to Rs420. Press reports indicate that C&K is exploring an initial public offering (IPO) for HBR's education business, as management believes that C&K's current market cap "does not adequately reflect the potential of the education tour business." Please see figure 1 alongside for further details on transactions involving HBR.

We note that the new benchmark EV of c.£600m is above the EV of c.£512m that was paid by C&K when acquiring HBR and later Meininger. In addition, C&K realized amounts of over £100m via divestitures of Camping and other businesses, even though it took significant goodwill write-downs in the process. In the final analysis, Ebitda growth from Education Travel and Meininger seems to have protected C&K from the value erosion at other businesses bought from HBR.

Figure 1: Transactions involving Holidaybreak

Year	Transaction	Amount	Comments
2011	Holidaybreak acquired by Cox & Kings	c.£312m	100% of Holidaybreak acquired by Cox & Kings at an equity valuation of c.£312m. Enterprise value of c.£460m. Equity infusion by Cox & Kings was £125m in the purchase transaction.
2012/2014	Remaining 50% stake in Meininger acquired by Holidaybreak	c.£50m	With this purchase, enterprise value of Holidaybreak totals c.£512m, implying an EV/Ebitda multiple of 8.1x.
2012	CVCI acquires 34.4% in Holidaybreak	c.£85m	Implied equity valuation of Holidaybreak at £247m, and that of Cox & Kings' share at £162m.
2014	Holidaybreak sells 100% of its stake in the camping business	c.£89m	Camping division sold for £89m to Homair Vacances, with proceeds used to repay debt.
2015	Holidaybreak sells 100% of its stake in Explore Worldwide	c.£26m	Explore, an adventure holidays unit, sold for £26m.
2016	Holidaybreak sells 100% of its stake in LateRooms and Superbreak to Malvern	c.£30m	LateRooms was sold for £20m, while Superbreak sold for £9.3m cash. Cox & Kings acquires 49% stake in Malvern for £6.4m. Goodwill write-off on sale of Superbreak of £71.4m.
2017	SSG Capital acquires Rohatyn's 34.4% stake in Holidaybreak	c.£167m	Enterprise valuation of £600-620m. Implied equity valuation of Holidaybreak at c.£484m, and that of Cox & Kings' share at c.£317m.

Source: Company, IIFL Research

Meininger's aggressive expansion will drive HBR Ebitda growth

Meininger has an aggressive expansion plan for the next few years, involving a ramp-up in bed count from c.8,500 currently to over 15,000 by March 2019 and over 25,000 by March 2022 (see figure 2). The company has aggressively added headcount to support this expansion plan, and has added 32 people (including a CFO) over the past year,

mostly at the senior management level. Consequently, while margins took a beating in 1H FY18 (35.2% vs. 48.6% YoY), they should recover substantially over the next few years driven by operating leverage. According to management, occupancies for the newly-added beds have been strong, and this should continue for future bed additions. In 2Q FY18, bed occupancy stood at 81.7% (vs. 83.6% YoY), while the average bed rate was €32.3/bed night (vs. €29.7 YoY). This is despite the aggressive bed addition over the past year. We expect Meininger's Ebitda to nearly double over the period FY18-20, driving nearly a 50% increase in HBR's Ebitda over that same period. Meininger has also shifted its head-office from Germany to London, which should help it benefit from a lower tax rate in London.

Figure 2: Aggressive bed addition plans at Meininger

Timeline	Bed capacity
Dec-16	7,000
Mar-17	8,150
Sep-17	8,555
Dec-17	+ 830 (Berlin)
Dec-17	+ 270 (Milan)
Feb-18	+ 375 (Rome)
Mar-18	+ 805 (Amsterdam)
Mar-18	10,840
Jun-18	+ 855 (Berlin)
Aug-18	+ 825 (Munich)
Aug-18	+ 490 (Milan)
Aug-18	+ 750 (Budapest)
Jan-19	+ 335 (Heidelberg)
Jan-19	+ 670 (Brussels)
Jan-19	+ 410 (Amsterdam)
Mar-19	15,175
Mar-22	25,000

Source: Company, IIFL Research

Earnings from leisure travel business remain steady

In 1H FY18, Ebitda from the India as well as international leisure travel business grew c.6% YoY increase. The India business has so far successfully withstood intense competition from online travel agents, although working capital has increased considerably in 1H FY18. However, the working capital increase may be partly due to seasonality and implementation of the Goods and Services Tax (GST). The international leisure travel business too is growing, albeit at a modest single-digit pace, driven especially by strong growth from the Dubai business.

Working capital a concern, but leverage remains comfortable

India business debt levels jumped sharply to c.Rs18b at September 2017, but are seen winding down partially by year-end. Meanwhile, C&K has repaid $11m out of its $191m debt at Prometheon (which was mainly taken to fund the acquisition of Holidaybreak in 2011) in 1H FY18. The company also has debts of £141m at its UK operations. Net debt-to-Ebitda remains fairly comfortable at a little over 2.5x (based on net debt as of September 2017). We assume that this falls to c.Rs18b by March 2018 (vs. Rs20b as of March 2017), driven by a seasonal wind-down in working capital, normalization of GST-related challenges, and demerger of the forex business.

2Q FY18 Ebitda broadly along expected lines

Meininger Ebitda missed estimates due to the sharp increase in employee costs, as mentioned earlier, but Ebitda from all other business divisions was broadly in line with expectations. Although Education Travel Ebitda was under pressure, this was due to the weaker GBP and pressure on NST (the tours business), whereas PGL (the main growth driver) continues to perform solidly. However, the increase in debt was a negative surprise. Consequently, the main drivers of the changes to our estimates are: 1) an assumption of lower margins at Meininger going forward; and 2) an assumption of higher debt and interest expense.

Figure 3: Summary of estimate changes

Rs m, except per share	New	Old	% Change
FY18ii			
Revenues	24,274	23,957	1%
EBITDA	9,533	8,771	9%
Net profit	3,961	3,380	17%
EPS	22.43	19.14	17%
FY19ii			
Revenues	26,547	26,863	-1%
EBITDA	9,540	9,939	-4%
Net profit	3,721	4,477	-17%
EPS	21.08	25.35	-17%
FY20ii			
Revenues	30,404	31,150	-2%
EBITDA	11,163	11,782	-5%
Net profit	*4,874*	5,783	-16%
EPS	27.60	32.75	-16%

Source: Company, IIFL Research

Our FY18ii EPS estimate is revised upwards by 17%, primarily to take into account the foreign currency gain of c.Rs840m during 1H FY18. We cut FY19/20ii EPS estimate by 17/16%, mainly to reflect lower margins at Meininger and higher interest expense.

Figure 4: SOTP Valuation

Division	EV/EBITDA (x)	Sep-19ii EBITDA	% stake	Sep-18 Valuation
Education Travel + Meininger	10	5,249	67%	35,166
Leisure Travel - India	10	3,153		31,526
Leisure Travel - RoW	6	1,877		11,259
Forex business (CKFSL)	15	963	19%	2,744
Total				**80,696**
Less: Net debt				(17,013)
= Equity valuation				**63,683**
Implied value per share				361
Rounded target price				**360**
Vs. Current share price				264
% Upside/downside				36%

Source: Company, IIFL Research

- We assign a 10x EV/Ebitda multiple to the education division, consistent with the multiple paid by C&K for this division at the time of the Holidaybreak acquisition. We believe that the relatively defensive nature of the education business (making it more recession-resistant), its healthy growth profile, and potential for operating leverage as well as significant base of fixed assets all justify at least a 10x multiple. We note that the recent stake swap by SSG Partners implies a multiple of c.13x for this business. If we used a 13x multiple, our target price per share would increase by c.Rs60.
- For India leisure travel too, we assign a 10x EV/Ebitda multiple. This is consistent with the multiple at which C&K's shares traded for a period of time before the Holidaybreak acquisition and is also justified by historical valuations of Thomas Cook India, whose core business is a close comparable for C&K. We think the growth potential of the India business justifies a 10x multiple.
- For the international leisure travel division, we assign a 6x EV/Ebitda multiple, consistent with the multiples paid by C&K and later by CVCI when acquiring Holidaybreak.

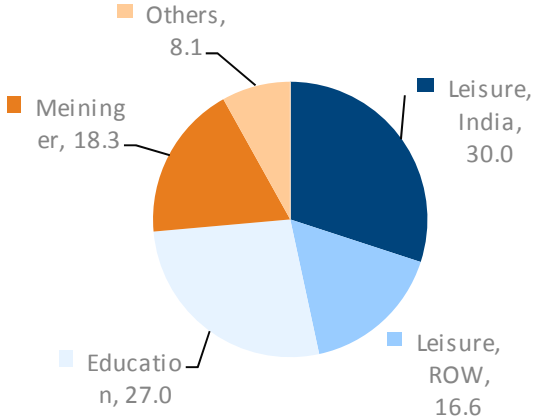
- For the forex business, we assign a 15x EV/Ebitda multiple, which is at a discount at which Weizmann Forex, its closest listed competitor, trades.
- Our SOTP suggests substantial room for upside in C&K's share price predicated on continued healthy growth in revenue and Ebitda and continued de-leveraging. Our SOTP-based target price for Sep-2018 falls to Rs360 (Rs390 previously).

Background: Cox & Kings (C&K) is an international travel and tours company with operations in 26 countries around the world. Its operations spread across India, Europe, Australia, the USA, Dubai, Japan and Singapore, where it sells packaged holidays for leisure travel. In addition, following the acquisition of Holidaybreak plc in 2011, C&K entered education travel in the UK and acquired Meininger, a European budget hotel chain.

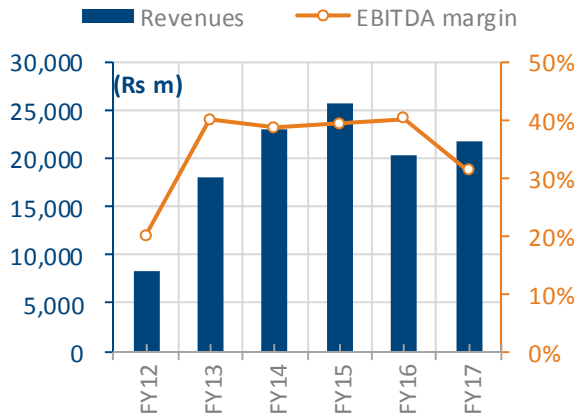
Management

Name	Designation
Peter Kerkar	Promoter & Non-Executive Director
Urrshila Kerkar	Promoter & Whole Time Director
Anil Khandelwal	Chief Financial Officer

Revenue break-up (%) - FY17



Rev. & Ebitda margin, FY12-17

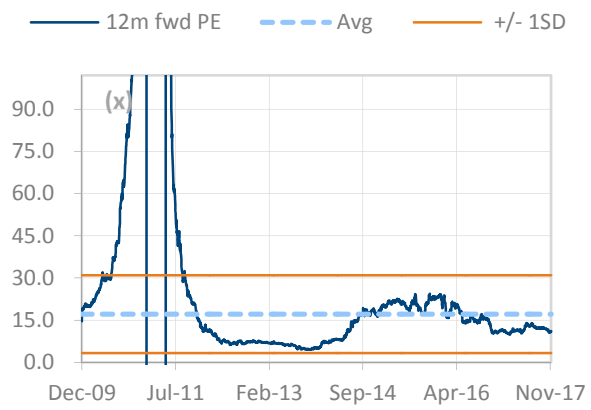


Assumptions

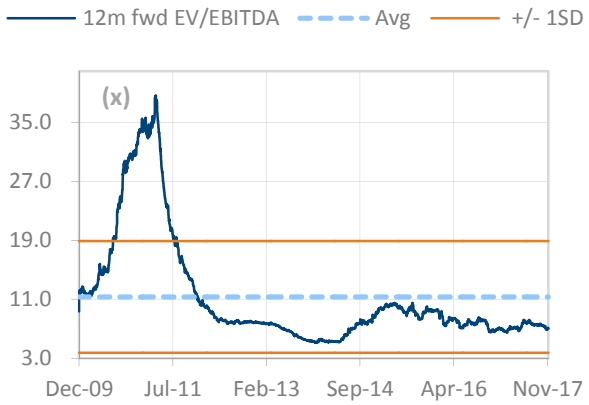
Y/e 31 Mar, Consolidated	FY16A	FY17A	FY18ii	FY19ii	FY20ii
Revenue					
Leisure	9,520	10,140	10,878	10,978	12,235
Education	6,650	5,890	5,884	6,473	7,120
Meininger	3,640	3,990	5,564	6,955	8,694
Ebitda					
Leisure	4,410	4,510	4,778	4,754	5,304
Education	2,860	2,640	2,471	2,783	3,133
Meininger	1,340	1,460	1,444	1,949	2,632

Source: Company data, IIFL Research

PE Chart



EV/Ebitda



Financial summary

Income statement summary (Rs m)

Y/e 31 Mar, Consolidated	FY16A	FY17A	FY18ii	FY19ii	FY20ii
Revenues	**20,274**	**21,790**	**24,274**	**26,547**	**30,404**
Ebitda	8,127	6,809	9,533	9,540	11,163
Depreciation and amortisation	(1,485)	(953)	(953)	(1,020)	(1,092)
Ebit	6,642	5,856	8,580	8,520	10,072
Non-operating income	814	465	450	450	450
Financial expense	(2,563)	(2,255)	(2,278)	(2,301)	(1,978)
PBT	4,893	4,065	6,752	6,669	8,544
Exceptionals	(3,406)	(109)	(139)	0	0
Reported PBT	1,487	3,956	6,613	6,669	8,544
Tax expense	(1,567)	(1,722)	(1,984)	(2,001)	(2,563)
PAT	(80)	2,234	4,629	4,668	5,980
Minorities, Associates etc.	587	(764)	(766)	(947)	(1,107)
Attributable PAT	**507**	**1,470**	**3,863**	**3,721**	**4,874**

Ratio analysis

Y/e 31 Mar, Consolidated	FY16A	FY17A	FY18ii	FY19ii	FY20ii
Per share data (Rs)					
Pre-exceptional EPS	13.8	8.7	22.4	21.1	27.6
DPS	1.0	1.0	1.0	1.0	1.0
BVPS	139.3	147.2	167.9	187.8	214.3
Growth ratios (%)					
Revenues	(21.1)	7.5	11.4	9.4	14.5
Ebitda	(19.6)	(16.2)	40.0	0.1	17.0
EPS	(28.1)	(37.3)	158.8	(6.0)	31.0
Profitability ratios (%)					
Ebitda margin	40.1	31.2	39.3	35.9	36.7
Ebit margin	32.8	26.9	35.3	32.1	33.1
Tax rate	105.4	43.5	30.0	30.0	30.0
Net profit margin	(0.4)	10.3	19.1	17.6	19.7
Return ratios (%)					
ROE	9.6	6.1	14.2	11.8	13.7
ROCE	10.2	8.7	12.6	12.4	14.3
Solvency ratios (x)					
Net debt-equity	0.9	0.8	0.6	0.5	0.3
Net debt to Ebitda	2.8	2.9	1.9	1.6	1.1
Interest coverage	2.6	2.6	3.8	3.7	5.1

Source: Company data, IIFL Research

Balance sheet summary (Rs m)

Y/e 31 Mar, Consolidated	FY16A	FY17A	FY18ii	FY19ii	FY20ii
Cash & cash equivalents	18,442	16,926	16,871	13,943	15,199
Inventories	292	199	221	242	277
Receivables	13,983	18,201	19,286	21,092	24,157
Other current assets	11,896	11,467	10,967	10,967	10,967
Creditors	1,251	1,225	1,320	1,395	1,541
Other current liabilities	18,202	18,192	20,373	21,415	23,459
Net current assets	**25,159**	**27,376**	**25,652**	**23,434**	**25,599**
Fixed assets	21,437	20,062	22,308	23,488	24,597
Intangibles	26,249	22,028	23,658	23,658	23,658
Investments	1,202	1,088	1,588	1,388	1,238
Other long-term assets	0	0	0	0	0
Total net assets	**74,047**	**70,553**	**73,207**	**71,968**	**75,092**
Borrowings	41,009	36,739	35,170	29,670	27,170
Other long-term liabilities	8,437	7,819	8,385	9,132	10,089
Shareholders' equity	**24,601**	**25,995**	**29,652**	**33,166**	**37,833**
Total liabilities	**74,047**	**70,553**	**73,207**	**71,968**	**75,092**

Cash flow summary (Rs m)

Y/e 31 Mar, Consolidated	FY16A	FY17A	FY18ii	FY19ii	FY20ii
Ebit	6,642	5,856	8,580	8,520	10,072
Tax paid	(1,424)	(1,322)	(1,984)	(2,001)	(2,563)
Depreciation and amortization	1,485	953	953	1,020	1,092
Net working capital change	594	(4,405)	1,669	(710)	(910)
Other operating items	179	1,545	311	450	450
Operating cash flow before interest	7,477	2,627	9,529	7,279	8,140
Financial expense	(2,537)	(2,255)	(2,278)	(2,301)	(1,978)
Non-operating income	203	465	0	0	0
Operating cash flow after interest	**5,144**	**836**	**7,251**	**4,978**	**6,162**
Capital expenditure	**(3,202)**	**(2,072)**	**(3,200)**	**(2,200)**	**(2,200)**
Long-term investments	4,833	0	(700)	0	0
Others	(3,959)	64	(1,631)	0	0
Free cash flow	**2,816**	**(1,172)**	**1,721**	**2,778**	**3,962**
Equity raising	(125)	1,648	0	0	0
Borrowings	1,900	(1,782)	(1,569)	(5,500)	(2,500)
Dividend	(205)	(211)	(207)	(207)	(207)
Net chg in cash and equivalents	4,385	(1,516)	(55)	(2,928)	1,256

Source: Company data, IIFL Research

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A graph of daily closing prices of securities is available at http://www.nseindia.com/ChartApp/install/charts/mainpage.jsp, www.bseindia.com and http://economictimes.indiatimes.com/markets/stocks/stock-quotes. (Choose a company from the list on the browser and select the "three years" period in the price chart).

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Key to our recommendation structure

BUY - Stock expected to give a return 10%+ more than average return on a debt instrument over a 1-year horizon.

SELL - Stock expected to give a return 10%+ below the average return on a debt instrument over a 1-year horizon.

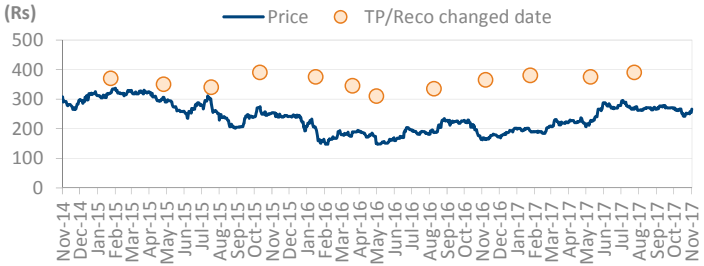
Add - Stock expected to give a return 0-10% over the average return on a debt instrument over a 1-year horizon.

Reduce - Stock expected to give a return 0-10% below the average return on a debt instrument over a 1-year horizon.

Distribution of Ratings: Out of 204 stocks rated in the IIFL coverage universe, 106 have BUY ratings, 6 have SELL ratings, 67 have ADD ratings and 25 have REDUCE ratings

Price Target: Unless otherwise stated in the text of this report, target prices in this report are based on either a discounted cash flow valuation or comparison of valuation ratios with companies seen by the analyst as comparable or a combination of the two methods. The result of this fundamental valuation is adjusted to reflect the analyst's views on the likely course of investor sentiment. Whichever valuation method is used there is a significant risk that the target price will not be achieved within the expected timeframe. Risk factors include unforeseen changes in competitive pressures or in the level of demand for the company's products. Such demand variations may result from changes in technology, in the overall level of economic activity or, in some cases, in fashion. Valuations may also be affected by changes in taxation, in exchange rates and, in certain industries, in regulations. Investment in overseas markets and instruments such as ADRs can result in increased risk from factors such as exchange rates, exchange controls, taxation, and political and social conditions. This discussion of valuation methods and risk factors is not comprehensive – further information is available upon request.

Cox & Kings: 3 year price and rating history



Date	Close price (Rs)	Target price (Rs)	Rating
17 Nov 2014	309	375	BUY
16 Feb 2015	319	370	BUY
19 May 2015	306	350	BUY
10 Aug 2015	301	340	BUY
03 Nov 2015	271	390	BUY
08 Feb 2016	206	375	BUY
12 Apr 2016	183	345	BUY
24 May 2016	150	310	BUY
01 Sep 2016	187	335	BUY
30 Nov 2016	163	365	BUY
16 Feb 2017	194	380	BUY
01 Jun 2017	223	375	BUY
16 Aug 2017	270	390	BUY