In God we trust. For everybody else, we stand by our QoE analysis.

Here's a follow-up on our previous article on CX & K.

Recently we observed that a company operating in the tours and travels business has plummeted, with stock prices eroding by nearly 80% in the last one year.

If you have been following our blog, we gave a meticulous explanation of this very company's long haul in our article – Lost and Found: The Many Acquisitions of a Travel Company, and identified red flags in advance (August 2018).

In this follow-up article we would like to address some of our previous points and present some new points we have unearthed subsequently, that should have been early warning signs for investors.

1) Acquisition in 2011: Break Holiday (BH)

Here's the management's rational of this acquisition: "*The acquisition of a leading European Education activity and Leisure specialist travel company, has brought along deep synergies in the form of our expanded market reach, cross selling opportunities and a more resilient business model. The acquisition also brings in a unique mix of fast growing & defensive business segments like leisure & education.*"

Here are the events that followed:

Year	Sale of Business	Management Commentary on sale
2013-14	Camping Business	*"Acquisition of camping business, despite its leadership position and high margins was not synergistic to our other group activities and hence was approached from a tactical perspective during our transformation journey"*
2016-17	Adventure	*"While it had been resurrected over the past four years following the Euro crisis, the business was exposed to a high volume of traffic to some of the more politically sensitive regions of the world. Management decided that the brand would be better served in the capable hands of….."*
2017	Hotels	*No specific commentary*
2018	Education	*"Since our successful acquisition in 2011, the business, with the strategic direction of CX & K, has scaled larger heights. Over the years, we have made efforts to maximise shareholder value by divesting some parts of the business, reduce debt and focus on high-growth, asset-light businesses. This is in-line with our stated policy of consistently unlocking value in the company and we shall aggressively continue to follow our stated policy. "*

Truth to the transaction: The management's commentary while acquiring the business vs. at time of their sale reflect poor decision-making. Prior to sale of education business in 2018, the company had effectively sold off 50% of the acquired BH business and written off 47% of the acquisition price. Further, upon sale of education business in 2018, it thus now has effectively disposed most of the originally acquired BH business in 2011.

It sold the education business (part of BH business acquired in 2011) in 2018 for a consideration of INR 43 bn. and booked a gain of INR 13 bn. Proceeds from all the disposal of acquired businesses have been used by the company to repay debt.

2) Rising pledged shares of Promoters and an Associate (T-Hotels)

Pledged shares are at an all-time high with Indian promoters pledging more than 82% of their shareholding.

Particulars	Q1 FY 18	Q4 2018	Q4 2019
% of Indian promoters holdings	79.6%	81.9%	82.4%
% of promoters holding	54.5%	65.6%	63.3%
% of total shares outstanding	27.9%	30.9%	31.5%

An article by 'The Ken' suggests that promoters have been pledging shares to raise funds for company's associate T-Hotels (promoter group entity). We then looked at pledged shares of promoters in T-Hotels:

Particulars	Q1 FY 18	Q4 2018	Q4 2019
% of Promoters Holding	53.4%	53.4%	89.5%
% of Total Holdings	30.4%	30.4%	51.3%

We further analysed the financial statements of T-Hotels for last 3 years and found the following.

The company reported no operations and has been reporting losses (INR -79 mn. for FY 2019) and had negative net worth of INR -176 mn. The company is laden with ~650 mn. worth of debt as at March 2019 (details of debt not available). The debt reported on March 2018 balance sheet was ~ INR 585 mn. (all unsecured but not from CX & K) and as at March 2017 balance sheet, total debt stood at INR 544 mn. (all unsecured), 60% of which was from CX & K.

Interestingly, in the standalone books of CX & K, the investment value reported for T-Hotels (as associate) had not been impaired till FY 2018 and has been carried at cost, despite continuous losses and negative net worth. However in the consolidated financial statements, CX & K has carried T-Hotels at nil.March 2019 consolidated earnings release does report 'impairment in associates' as part of extra-ordinary items but no further details are available.

3) Increasing debtors as % of Sales

TTM	Sept -17	Mar- 18	Sept- 18	Mar- 19
As % of revenue	39%	39%	41%	39%
Competitor-Thomas Cook				
As % of revenue	24.3%	13.0%	11.4%	54.9%

As the CX & K's investment in B2B has increased, receivables have piled up over time. In Q3 FY 2019, the company had said that it will be reducing the focus on the B2B segment and will focus on the B2C segment.

Its competitor, Thomas Cook had receivables which accounted for ~12-25% of revenue. This was a large discrepancy we observed in the receivables t/o (possibly due to different business models also).

4) Downgrading of the rating by Care & Brickwork

The credit rating agency CARE, in its report on 11th June 2019 downgraded company's Long term bank facilities and certain NCDs (55% of the total debt) by one notch to 'AA-', Stable. Prior to this CX & K's all debt had 'AA'; Stable ratings. The rating agency has cited the following reasons for downgrading the ratings:

Lower than envisaged reduction in debt as on March 31st 2019,
Continued high level of pledged shares by promoters
Reduced financial flexibility as a result of decline in CX & K's market capitalization
Interest coverage deteriorated from 3.25x in FY18 to 2.81x in FY 19. (unadjusted for forex)
Account of increase in debtors CX & K's cash flow from operations continues to remain negative
On 24th June 2019, another rating agency, Brickworks, assigned one notch downgrading to the company's NCD (1% of the total debt) citing similar reasons as mentioned above.

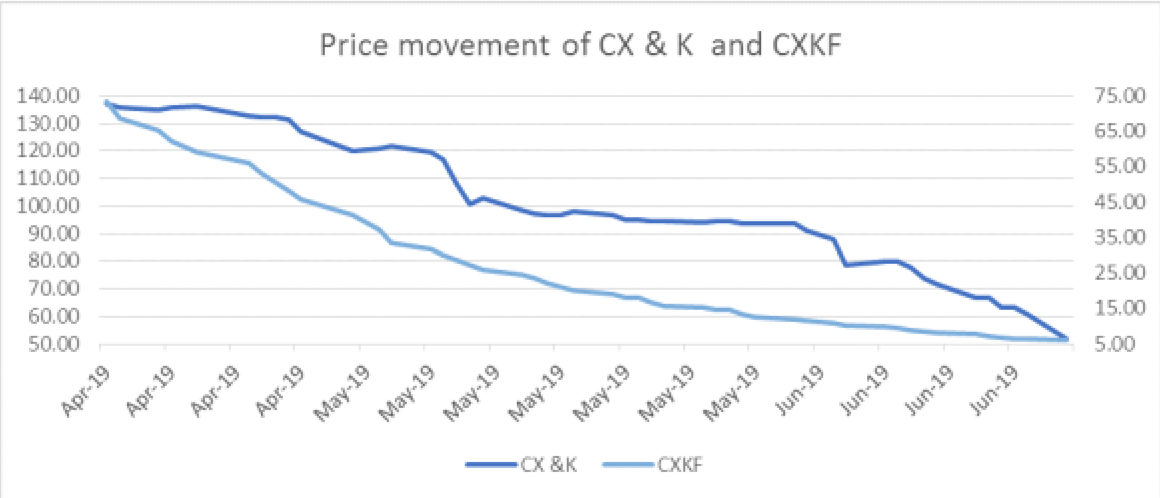
Conclusion:

All the above mentioned warning signs and factors were visible much in advance and were blatantly evident in the numbers and the management's commentary but were ignored by the market participants.

Timely cognizance of the same could have prevented significant investment losses here.

Additional Observations:

Share price of demerged entity- CXKF
The company's demerged financial services was listed in April 2019 at INR 70/share has also declined in value by over 90% and is currently trading at INR 6/share. Following chart shows the movement of prices of CX & K and CXKF.



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