

# Thomas Cook (India)

14 August 2018

Reuters: THOM.NS; Bloomberg: TC IN

## Tailwinds in Travel; DMS Improves; Fx Steady; Risk-Reward Favourable

We interacted with the management of Thomas Cook India or TCIL at the Institutional Equities Conference hosted by us last week. The active participation of TCIL's management was encouraging. Overall, the conversation was positive and a few investors also appreciated the simplified financial reporting for 1QFY19. The management highlighted key measures undertaken in the recent past which are now beginning to show results in terms of rising margins. Value unlocking with respect to Qness spin-off took centre stage as the growth outlook looks convincing. According to the current market value, TCIL's 49% stake in Qness is valued at Rs195/share. Also, TCIL holds nearly Rs8,000mn or Rs21.6/share in net cash. This grossly undervalues the core travel, forex and vacation ownership businesses. Travel and forex business continues to grow at 15% and 9%, respectively. We remain positive on TCIL's business scalability as well as strong financial health. We have retained Buy rating on TCIL with an unchanged target price of Rs350, representing 36% upside from the current stock price.

**DMS business improves:** The B2B inbound business is spread over more than 17 countries in Europe, Africa, Middle East and North America. During 1QFY19, this unit performed extremely well. It increased sales by 5% YoY while net revenues rose 24% YoY, indicating spectacular improvement in gross margin. The management believes that this gross margin improvement is sustainable and largely comes from cost savings and technology upgradation. 1Q is a seasonally slow quarter for major contributing countries like the US, Kenya and Dubai. The unit has reduced its losses to Rs 90mn in 1QFY19 as compared to Rs 240mn YoY.

**Domestic & online travel grows:** This business unit continues to grow well, but is currently loss-making. During 1QFY19, it delivered revenues of Rs1,300mn and EBIT loss of Rs200mn. TCIL is a distant No. 2 player in the industry with makemytrip.com at the top. Over the next three years, the management expects annual revenue run-rate of Rs3,000mn with EBIT of Rs450mn from the segment. Interestingly, the operations team of this unit largely comprises ex-makemytrip employees. The management also highlighted that 65% of its holiday packages are now sold online or via call-centres.

**Forex – the focus shifts to retail trade:** The management has identified retail as the new growth area for the forex segment in the next few years. Within the forex segment, retail trade contributes one-third volume, but two-third EBIT contribution. This is because of the fact that the company enjoys approximately 200bps spread in this trade. The retail business continues to grow at more than 15% tracking inbound & outbound tourism growth. Nearly 78% of TCIL's outbound and MICE customers exchange forex from TCIL only. Under the retail business, TCIL has 300 points of sales including high-street shops, corporate relationships, airport kiosks and the forex website. The company is targeting Tier 2 cities to open more airport kiosks. The online/website business mostly comprises pre-paid forex card which also reduces TCIL's inventory requirement substantially. As of now, the company holds approximately Rs4,000mn float in the forex business. For other points of sale, the company maintains anywhere between Rs1,500mn to Rs1,800mn cash inventory. This amount is enough to meet 1.5 days of sales and has improved from three days in the past few years.

*NBIE Values your patronage- Vote for The Team in the Asia Money poll 2018. [Click Here](#)*

## BUY

**Sector:** Travel & Tourism

**CMP:** Rs258

**Target Price:** Rs350

**Upside:** 36%

**Mohit Khanna**

Research Analyst

mohit.khanna@nirmalbang.com

+91-22-6273 8089

### Key Data

Current Shares O/S (mn)	370.4
Mkt Cap (Rsbn/US\$bn)	96.5/1.4
52 Wk H / L (Rs)	303/211
Daily Vol. (3M NSE Avg.)	496,519

### Price Performance (%)

	1 M	6 M	1 Yr
Thomas Cook (India)	(5.5)	6.0	17.6
Nifty Index	3.9	9.0	16.8

Source: Bloomberg

Y/E March (Rsmn): consolidated	FY17	FY18	FY19E	FY20E	FY21E
Net sales	87,624	112,484	66,177	76,375	87,430
EBITDA	3,378	3,712	2,455	2,818	3,147
Core net profit	(101)	1,426	1,662	1,787	1,953
Core EPS (Rs)	(0.28)	3.87	4.47	4.80	5.25
EPS growth (%)	NA	NA	15	8	9
EBITDA margin (%)	3.9	3.3	3.7	3.7	3.6
P/E (x)	NA	1.7	30.9	27.1	23.6
Net cash (incl. Qness)/mkt cap (%)	6.7	86.9	100.4	104.9	109.9
Capital employed in core business	NA	17,158	18,712	20,400	22,246
Core Pre-tax RoIC (%)	21.3	21.9	22.1	23.3	28.6

Note: FY19E onwards Qness is recorded as an associate

Source: Company, Nirmal Bang Institutional Equities Research

## DMS acquisition for diversification and expansion

The management's strategic motive to acquire DMS business was to mitigate seasonality in legacy operations, diversify geographically and build a bigger integrated travel business. TCIL acquired the DMS business (also referred as international inbound business) from Kuoni last year for Rs13,000mn (US\$19.8mn). At the time of acquisition, all DMS entities cumulatively held Rs 9,000mn (US\$14mn) net cash which means that the effective cost of acquisition to TCIL was only Rs 4,000mn (US\$5.8mn). Even as these entities are still loss making, they continue to add free cash. At the end of the June quarter, net cash in the DMS business was Rs 10,990mn (US\$15.7mn). Pre-acquisition, these entities generated Rs.275mn (US\$3.5mn) EBITDA. The management is hopeful of generating Rs350mn (US\$5-7mn) EBITDA from the business in the coming years.

## Wholesale forex becomes unattractive

Wholesale forex business includes dealing with other money changers and banks. The average transaction in the segment is around US\$50,000 and carries a spread of 30bps-50bps. The spreads in the business are constantly under pressure as banks are undercutting to gain more share. The division contributes two-thirds of the total forex volume, but only one-third of EBIT.

## Prepaid forex card is the new growth driver

The management is now focusing to build US\$1bn p.a. prepaid solutions portfolio (CAGR of 30%). TCIL's online forex business to the overall retail portfolio is expected to grow from 3% to 5% (with last mile delivery fulfilled offline). There is a growing industry preference to buy FX online; currently ~95% offline. There is a thrust on outbound remittances to drive the share of retail business; 31% in 2017 to 36% by 2021.

## Sterling - the IndAS 115 issue & margin of safety:

Following the IndAS115 implementation, Sterling is facing revenue recognition problem even as the cash flow of the business remains the same. The accounting standard has hit the vacation ownership business, which is 50% of the segment's revenues. The remaining 50% is received from normal hotel operations which has no such impact. Previously, the company recorded all the upfront payment (60% of the 25-year vacation ownership product fee) as revenues and the remaining 40% was recorded as and when received in EMLs over the next two to four years. Under the new standard, revenue recognition has to be spread over the product lifecycle. While the floating costs should be amortised over the same time period, fixed costs relating to customer acquisition has to be recorded upfront. This has prompted the management to aggressively push the shorter duration (10-year) product. Marketing costs are also being adjusted with inclination towards more variable components. We expect revenues from non-members to increase as a percentage of overall Sterling's revenues as new vacation ownership member addition has already slowed in the past two years.

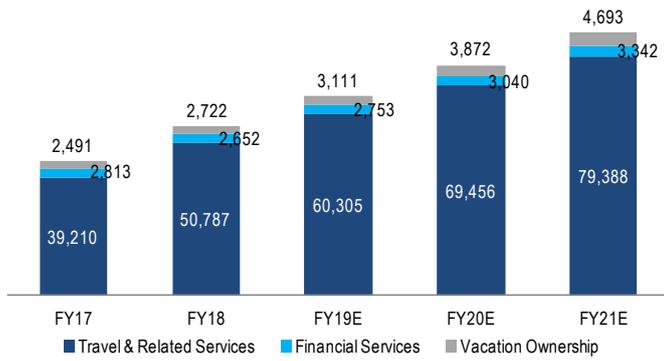
The company hoards Rs 5,500mn of land bank, most of which is surplus. Additionally, it owns 17 out of 33 operational resorts, providing a margin of safety to the Rs 10,000mn capital employed in the business. The management intends to monetise the land bank opportunistically. There is no incremental capex requirement at Sterling and future expansion will be modeled on revenue-sharing basis with the resort owners. Occupancy rate during 1QFY19 stood at 78%.

## Exhibit 1: Key Indicators – Sterling (vacation ownership)

Key Indicators	FY 14	FY 15	FY 16	FY 17	FY 18
VO new members	3,651	5,481	6,233	5,295	4,065
Average unit realization (Rs lacs)	2.21	2.38	2.52	2.88	2.92
Resort Occupancy	49%	56%	57%	63%	64%
ARR (Rs)	2,291	2,730	2,982	3,123	3,529

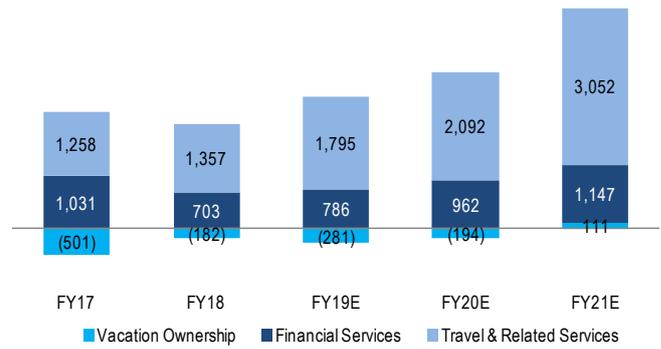
Source: Company reports

**Exhibit 2: TCIL's revenue break-up**



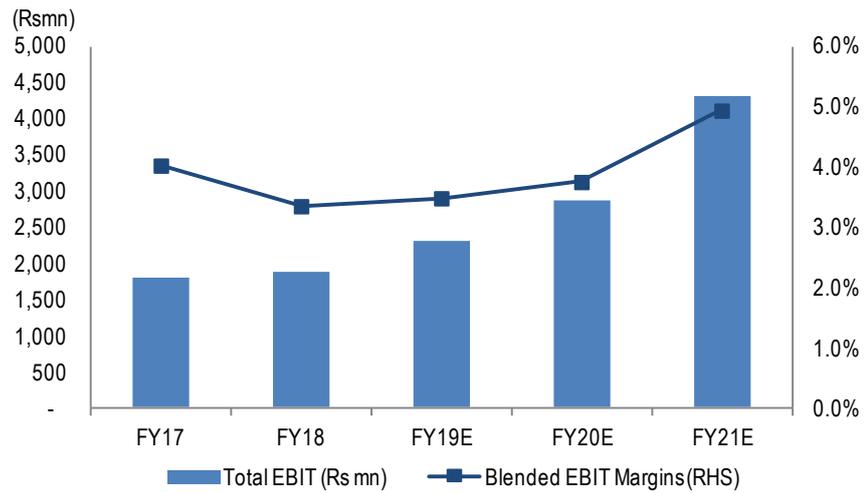
Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 3: TCIL's EBIT break-up**



Source: Company, Nirmal Bang Institutional Equities Research

**Exhibit 4: TCIL's EBIT and margins**



Source: Company, Nirmal Bang Institutional Equities Research

## TCIL's consolidated financials (Deconsolidating Quesq Corp starting FY19)

### Exhibit 5: Income statement

Y/E March (Rsmn)	FY18	FY19E	FY20E	FY21E
Net sales	112,484	66,177	76,375	87,430
% growth	28.4	(41.2)	15.4	14.5
Cost of sales & service	(43,987)	(52,293)	(60,413)	(69,157)
Staff, general & admin costs	(53,022)	(5,294)	(6,118)	(7,082)
Other expenditure	(11,763)	(6,135)	(7,027)	(8,044)
EBITDA	3,712	2,455	2,818	3,147
% growth	9.9	(33.9)	14.8	11.7
EBITDA margin (%)	3.3	3.7	3.7	3.6
Depreciation	(1,367)	(397)	(611)	(699)
<b>EBIT</b>	<b>2,345</b>	<b>2,058</b>	<b>2,207</b>	<b>2,448</b>
% growth	(5)	(12)	7	11
EBIT margin (%)	2.1	3.1	2.9	2.8
Interest cost	(1,490)	(357)	(327)	(372)
Interest/other recurring income	309	386	421	424
Non-recurring & Exceptional items	58,255	-	-	-
Profit before tax	60,909	2,444	2,628	2,872
% growth	NA	(96.0)	7.5	9.3
Tax	406	(782)	(841)	(919)
Effective tax rate (%)	(0.7)	32.0	32.0	32.0
Minority interest	(1,634)	-	-	-
Net profit	59,680	3,091	3,531	4,045
% growth	NA	16.6	7.5	9.3
Diluted EPS (Rs)	162.10	8.31	9.49	10.87
% growth	NA	(94.9)	14.2	14.6

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 7: Balance sheet

Y/E March (Rsmn): Consolidated	FY18	FY19E	FY20E	FY21E
Equity	367	370	370	370
Reserves	86,344	87,898	89,586	91,432
<b>Net worth</b>	<b>86,714</b>	<b>88,268</b>	<b>89,957</b>	<b>91,802</b>
Accounts payables	14,840	22,207	25,655	29,368
Other ST liabilities	12,649	12,649	12,649	12,649
Short-term loans	664	664	664	664
<b>Total current liabilities</b>	<b>28,153</b>	<b>35,519</b>	<b>38,967</b>	<b>42,681</b>
Long-term loans	2,310	2,310	2,310	2,310
Other LT liabilities	4,735	4,735	4,735	4,735
Minority interest	131	131	131	131
<b>Total equity &amp; liabilities</b>	<b>122,042</b>	<b>130,963</b>	<b>136,099</b>	<b>141,658</b>
Gross block	10,000	10,662	11,273	11,885
Depreciation	(2,601)	(2,998)	(3,609)	(4,308)
Net block	7,399	7,664	7,664	7,576
Other LT assets + WIP	3,358	3,358	3,358	3,358
Long-term investments (Quesq)	72,530	72,530	72,530	72,530
Inventories	11	57	66	76
Debtors	8,574	5,439	6,277	7,186
Cash & ST Investments	12,378	24,123	28,412	33,140
Other current assets	7,962	7,962	7,962	7,962
Total current assets	28,926	37,581	42,718	48,364
Net current assets	773	2,062	3,751	5,684
<b>Total assets</b>	<b>122,042</b>	<b>130,963</b>	<b>136,099</b>	<b>141,658</b>

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 6: Cash flow

Y/E March (Rsmn): Consolidated	FY18	FY19E	FY20E	FY21E
PBT	2,654	2,444	2,628	2,872
(Inc./dec. in working capital)	3,337	10,455	2,601	2,795
Depreciation	1,125	397	611	699
Other non-cash adjustments	406	(782)	(841)	(919)
<b>Net cash from operations</b>	<b>7,521</b>	<b>12,514</b>	<b>4,999</b>	<b>5,447</b>
Disposal of fixed assets	-	-	-	-
Capital expenditure (-)	(1,125)	(662)	(611)	(612)
<b>Net cash after capex (FCF)</b>	<b>6,396</b>	<b>11,852</b>	<b>4,388</b>	<b>4,835</b>
Other investing activities	682	-	-	-
<b>Cash from investing activities</b>	<b>(443)</b>	<b>(662)</b>	<b>(611)</b>	<b>(612)</b>
Inc./(dec.) in short-term borrowing	(5,030)	-	-	-
Inc./(dec.) in long-term borrowing	(5,066)	-	-	-
Inc./(dec.) in preference capital	-	-	-	-
Dividends paid	(150)	(108)	(98)	(107)
Equity issue/(buyback)	-	-	-	-
Other financing activities	-	-	-	-
<b>Cash from financial activities</b>	<b>(10,246)</b>	<b>(108)</b>	<b>(98)</b>	<b>(107)</b>

Source: Company, Nirmal Bang Institutional Equities Research

### Exhibit 8: Key ratios

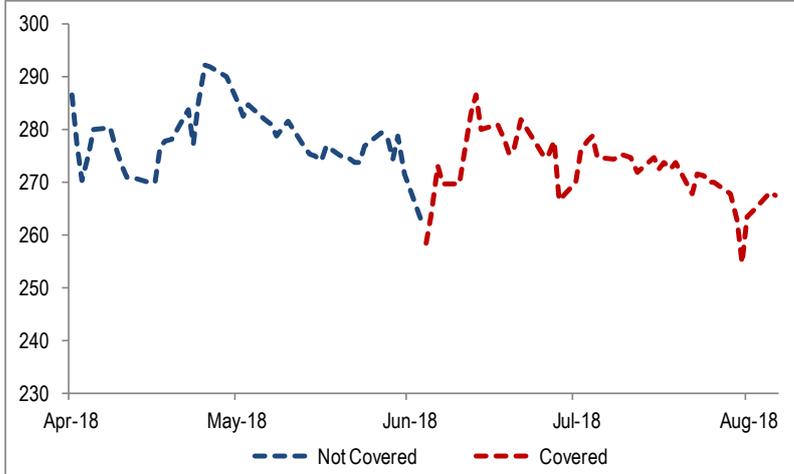
Y/E March (Rsmn): Consolidated	FY18	FY19E	FY20E	FY21E
<b>Profitability &amp; return ratios</b>				
EBITDA margin (%)	3.3	3.7	3.7	3.6
EBIT margin (%)	2.1	3.1	2.9	2.8
Core Net profit margin (%)	1.3	2.5	2.3	2.2
Core RoE (%)	2.7	11.1	10.8	10.6
Core RoCE (%)	3.8	11.5	11.3	11.5
Core Pre-tax RoIC (%)	21.9	22.1	23.3	28.6
Cash conversion cycle	(82)	(125)	(125)	(125)
<b>Leverage and FCF ratios</b>				
Net Cash (Rsmn)	9,404	21,149	25,438	30,166
Net Cash Incl. Quesq @ Mkt. price (Rsmn)	81,935	94,649	98,938	103,666
Net cash (Incl. Quesq) as % of Mkt. Cap	86.9	100.4	104.9	109.9
Total debt/Equity (%)	0.03	0.03	0.03	0.03
FCF Yield (%)	6.8	12.4	4.6	5.1
FCF/Sales (%)	5.7	17.9	5.7	5.5
<b>Valuation ratios</b>				
Core EV/sales (x)	0.20	0.17	0.15	0.13
Core EV/EBITDA (x)	6.0	4.7	4.1	3.7
Core EBIT/EV (Earnings Yield)	16.6	21.3	24.4	27.3
P/E (x)	1.7	30.9	27.1	23.6
P/BV (x)	1.20	1.08	1.06	1.04

Source: Company, Nirmal Bang Institutional Equities Research

## Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
4 June 2018	Buy	271.60	350
9 August 2018	Buy	261	350

## Rating track graph



## DISCLOSURES

This Report is published by Nirmal Bang Equities Private Limited (hereinafter referred to as “NBEPL”) for private circulation. NBEPL is a registered Research Analyst under SEBI (Research Analyst) Regulations, 2014 having Registration no. INH000001436. NBEPL is also a registered Stock Broker with National Stock Exchange of India Limited and BSE Limited in cash and derivatives segments.

NBEPL has other business divisions with independent research teams separated by Chinese walls, and therefore may, at times, have different or contrary views on stocks and markets.

NBEPL or its associates have not been debarred / suspended by SEBI or any other regulatory authority for accessing / dealing in securities Market. NBEPL, its associates or analyst or his relatives do not hold any financial interest in the subject company. NBEPL or its associates or Analyst do not have any conflict or material conflict of interest at the time of publication of the research report with the subject company. NBEPL or its associates or Analyst or his relatives do not hold beneficial ownership of 1% or more in the subject company at the end of the month immediately preceding the date of publication of this research report.

NBEPL or its associates / analyst has not received any compensation / managed or co-managed public offering of securities of the company covered by Analyst during the past twelve months. NBEPL or its associates have not received any compensation or other benefits from the company covered by Analyst or third party in connection with the research report. Analyst has not served as an officer, director or employee of Subject Company and NBEPL / analyst has not been engaged in market making activity of the subject company.

**Analyst Certification:** I/We, Mohit Khanna, the research analysts are the authors of this report, hereby certify that the views expressed in this research report accurately reflects my/our personal views about the subject securities, issuers, products, sectors or industries. It is also certified that no part of the compensation of the analyst(s) was, is, or will be directly or indirectly related to the inclusion of specific recommendations or views in this research. The analyst(s) principally responsible for the preparation of this research report and has taken reasonable care to achieve and maintain independence and objectivity in making any recommendations.

## Disclaimer

### Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

This report is for the personal information of the authorized recipient and does not constitute to be any investment, legal or taxation advice to you. NBEPL is not soliciting any action based upon it. Nothing in this research shall be construed as a solicitation to buy or sell any security or product, or to engage in or refrain from engaging in any such transaction. In preparing this research, we did not take into account the investment objectives, financial situation and particular needs of the reader.

This research has been prepared for the general use of the clients of NBEPL and must not be copied, either in whole or in part, or distributed or redistributed to any other person in any form. If you are not the intended recipient you must not use or disclose the information in this research in any way. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. NBEPL will not treat recipients as customers by virtue of their receiving this report. This report is not directed or intended for distribution to or use by any person or entity resident in a state, country or any jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject NBEPL & its group companies to registration or licensing requirements within such jurisdictions.

The report is based on the information obtained from sources believed to be reliable, but we do not make any representation or warranty that it is accurate, complete or up-to-date and it should not be relied upon as such. We accept no obligation to correct or update the information or opinions in it. NBEPL or any of its affiliates or employees shall not be in any way responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. NBEPL or any of its affiliates or employees do not provide, at any time, any express or implied warranty of any kind, regarding any matter pertaining to this report, including without limitation the implied warranties of merchantability, fitness for a particular purpose, and non-infringement. The recipients of this report should rely on their own investigations.

This information is subject to change without any prior notice. NBEPL reserves its absolute discretion and right to make or refrain from making modifications and alterations to this statement from time to time. Nevertheless, NBEPL is committed to providing independent and transparent recommendations to its clients, and would be happy to provide information in response to specific client queries.

Before making an investment decision on the basis of this research, the reader needs to consider, with or without the assistance of an adviser, whether the advice is appropriate in light of their particular investment needs, objectives and financial circumstances. There are risks involved in securities trading. The price of securities can and does fluctuate, and an individual security may even become valueless. International investors are reminded of the additional risks inherent in international investments, such as currency fluctuations and international stock market or economic conditions, which may adversely affect the value of the investment. Opinions expressed are subject to change without any notice. Neither the company nor the director or the employees of NBEPL accept any liability whatsoever for any direct, indirect, consequential or other loss arising from any use of this research and/or further communication in relation to this research. Here it may be noted that neither NBEPL, nor its directors, employees, agents or representatives shall be liable for any damages whether direct or indirect, incidental, special or consequential including lost revenue or lost profit that may arise from or in connection with the use of the information contained in this report.

Copyright of this document vests exclusively with NBEPL.

Our reports are also available on our website [www.nirmalbang.com](http://www.nirmalbang.com)

**Access all our reports on Bloomberg, Thomson Reuters and Factset.**

Team Details:			
Name		Email Id	Direct Line
Rahul Arora	CEO	rahul.arora@nirmalbang.com	-
Girish Pai	Head of Research	girish.pai@nirmalbang.com	+91 22 6273 8017 / 18
Dealing			
Ravi Jagtiani	Dealing Desk	ravi.jagtiani@nirmalbang.com	+91 22 6273 8230, +91 22 6636 8833
Pradeep Kasat	Dealing Desk	pradeep.kasat@nirmalbang.com	+91 22 6273 8100/8101, +91 22 6636 8831
Michael Pillai	Dealing Desk	michael.pillai@nirmalbang.com	+91 22 6273 8102/8103, +91 22 6636 8830

## Nirmal Bang Equities Pvt. Ltd.

### Correspondence Address

B-2, 301/302, Marathon Innova,  
 Nr. Peninsula Corporate Park,  
 Lower Parel (W), Mumbai-400013.

Board No. : 91 22 6273 8000/1; Fax. : 022 6273 8010