# Everonn: Unpredictable and unvaluable, reiterate SELL (EEDU IN, mcap US$150mn, SELL)

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**Event: CBI arrests Everonn MD on allegations of bribery and tax evasion for undisclosed income of Rs1.2bn**

The CBI, (Central Bureau of Intelligence, a govt investigation agency) released a press release on 30 August 2011 stating that it arrested Everonn's MD, Mr. P Kishore on Tuesday on charges that he had concealed taxable income and bribed a Income Tax commissioner. The CBI press release also stated that an Additional Commissioner of Income Tax was also arrested for accepting the bribe. The case details so far highlighted include that the premises of Everonn were raided on 4 August 2011 (before the 1QFY12 results) by the above mentioned tax commissioner and the MD was found to have concealed ~Rs1.2bn. The MD negotiated a bribe of Rs.5mn to reduce his taxable income by Rs600mn. Greater details are available at http://www.cbi.nic.in/pressreleases/pr_2011-08-30-1.html.

**Corporate Updates since:** Subsequently, on 2 September 2011, the company appointed Ms. Susha John as the CEO, while the recently appointed Chairman Mr. J.J. Irani resigned. The company has further appointed Independent Directors, Mr. R.Sankaran and Mr.Joe Thomas to advice the CEO and look into the company's tax assessment. The outgoing Chairman, who has an impeccable corporate track record, has commented that although he did not want to comment on the case and Everonn was a well managed firm, he did not want to be associated with a firm so maligned.

**Other updates:** Rating agency Fitch Ratings has migrated India-based Everonn Education Limited's (EEL) 'Fitch A-(ind)' National Long-Term rating to the "Non-Monitored" category. Fitch will no longer provide ratings or analytical coverage of EEL. The ratings will remain in the "Non-Monitored" category for a period of six months and be withdrawn at the end of that period.

**Our View**: Our SELL stance on Everonn (since December 2011) was primarily based on the structural issues with the long term sustainability of Everonn's business model that is clearly accentuated by present circumstances. Our primary concerns have been – a) the working capital intensity of the business remains high with ICT remaining 25-30% of revenues, b) aggressive revenue recognition in its Classroom software business (ViTELS iSchools) has resulted in lengthening of debtor days and c) like Educomp, Everonn's cash burn from capex has risen substantially which has begun to meaningfully impact PAT as interest costs almost tripled in the last quarter- also Everonn burnt ~Rs.1.1bn in 1QFY12 due to difficult to understand reasons- primarily around rising debtor days and fixed capital investments. Besides, we have also found over the course of FY11 that Everonn's reported numbers were substantially ahead of our estimates despite weaker than expected KPIs in terms of number of schools, colleges and Retail centres added. The lack of information in several of its businesses such as enrollments in colleges had made analysis difficult. Given that the previous MD, Mr. Kishore, was the primary driver at the helm of the firm, despite having brought in a replacement fairly quickly, we don't think anyone else will be able to manage the multitude of business areas Everonn entered into over the last couple of years. Thus irrespective of the outcome of the tax investigation, Mr. Kishore's absence will still be quite meaningfully felt despite the new CEO stepping in. As highlighted earlier Everonn's business mix continues to drift towards lower quality businesses with less sustainable business models and predictability. The recent arrest of the MD further reduces the predictability of the business and make our previous estimates and valuation unreliable. **Heretofore we will not publish any estimates and valuation and reiterate our SELL stance.**

**Substantial pledged shares by insiders:** The table below highlights shareholding and pledged share data of insiders, as we understand, including Mr. Kishore's interests (in Red) and Mr. Nikhil Gandhi's firm SKIL (in grey) that made an investment in Everonn via an open offer in 2010. SKIL's shares are locked in for two-three years under the clauses of its share acquisition agreement. We note the high proportion of pledged shares by each party.

**Exhibit 1: Promoter Shareholding Details as on 30th June 2011**

| Name | Total Shares | % Holding | Pledged shares | Pledged shares as % of owned shares | Pledged shares as % of Total Shares |
|---|---|---|---|---|---|
| P Kishore | 1,635,764 | 8.5 | - | - | - |
| P K Padmanabhan | 1,170,784 | 6.1 | 293,784 | 25.1 | 1.5 |
| Jayalakshmi Padmanabhan | 652,205 | 3.4 | 520,205 | 79.8 | 2.7 |
| P Sarvotham | 125,050 | 0.7 | - | - | - |
| Susha John | 419,985 | 2.2 | - | - | - |
| Jansi Kishore | 50 | - | - | - | - |
| Keerthi K | 60 | - | - | - | - |
| SKIL Infrastructure Ltd | 4,000,000 | 20.8 | 4,000,000 | 100.0 | 20.8 |
| Celebrate India Tourism Ltd | 116,500 | 0.6 | 116,500 | 100.0 | 0.6 |
| **Total** | **8,120,398** | **42.3** | **4,930,489** | **60.7** | **25.7** |

Source: Company Filings

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## Explanation of Investment Rating

| Investment Rating | Expected return (over 12-month period from date of initial rating) |
|---|---|
| Buy | >5% |
| Sell | ≤5% |

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