

## Educomp Solutions

### Performance Highlights

Educomp reported robust performance recording 37.2% yoy growth in Top-line and a robust 92.3% yoy increase in Bottom-line with EBITDA Margins expanding by 580bp to 52.4% in 3QFY2010. Strong government backing pertaining to higher budgetary spends to spur growth of the Education and Training Sector across the globe, and particularly in India, is a key positive for companies in this space like Educomp, which has been growing aggressively through its strong execution capabilities. We expect Educomp to thrive on the upcoming opportunities in Education space and continue to witness strong growth trajectory backed by ongoing investments for newer initiatives with focus on product and content innovation. **At current levels, the stock is trading at attractive valuations owing to which we upgrade the stock from Neutral to a Buy.**

**Performance driven by strong Operational efficiency in SLS:** Educomp recorded 37.2% yoy growth in Revenues for 3QFY2010 driven by strong growth recorded by its School Learning Solutions (SLS) Business. The SLS Business comprising Smart Class and ICT Solutions (ICT) registered robust 55.3% yoy growth. The company implemented 355 new schools under the Smart Class Business and signed in 363 new schools in ICT during the quarter. EBITDA Margins grew by a strong 580bp yoy following strong improvement in SLS Margins. Strong Margins and Other Income boosted Bottom-line by 92.3% yoy despite higher Depreciation and Interest costs.

**Outlook and Valuation:** In addition to the aggressive expansion plans in the Smart Class Segment, the company is also investing considerable amounts towards newer initiatives in terms of setting up its own K-12 high-schools and has embarked on expansion of its Online, Supplementary business. We expect Educomp to record strong CAGR of 48.5% and 45.4% in Top-line and Bottom-line respectively, over FY2009-12E. At the CMP, the stock is trading at a P/E of 14.2x FY2012E EPS. We upgrade the stock from Neutral to a Buy, with a Target Price of Rs926.

### Key Financials (Consolidated)

Y/E March (Rs cr)	FY2009	FY2010E	FY2011E	FY2012E
<b>Net Sales</b>	<b>637</b>	<b>1,001</b>	<b>1,567</b>	<b>2,085</b>
% chg	122.7	57.1	56.6	33.0
<b>Net Profit</b>	<b>133</b>	<b>270</b>	<b>347</b>	<b>439</b>
% chg	87.6	102.3	28.5	26.7
<b>Diluted EPS (Rs)</b>	<b>15.1</b>	<b>28.4</b>	<b>36.5</b>	<b>46.3</b>
EBITDA Margin (%)	47.8	46.1	45.2	42.0
P/E (x)	43.7	23.2	18.0	14.2
P/BV (x)	11.6	4.6	3.7	2.9
RoE (%)	33.0	29.1	22.9	23.1
RoCE (%)	23.7	24.1	21.7	21.9
EV/Sales (x)	9.4	6.2	4.2	3.1
EV/EBITDA (x)	19.7	13.4	9.3	7.5

Source: Company, Angel Research

## BUY

CMP	Rs657
Target Price	Rs926
Investment Period	15 Months

### Stock Info

Sector	IT
Market Cap (Rs cr)	6,239
Beta	1.0
52 WK High / Low	1,017/280
Avg. Daily Volume	4,99,257
Face Value (Rs)	2
BSE Sensex	15,936
Nifty	4,760
Reuters Code	EDSO.BO
Bloomberg Code	EDSL@IN

### Shareholding Pattern (%)

Promoters	46.4
MF/Banks/Indian FIIs	5.0
FII/NRIs/OCBs	50.1
Indian Public	5.5

Abs. (%)	3m	1yr	3yr
Sensex	(1.4)	71.3	8.8
Educomp	(19.7)	134.6	260.0

### Hitesh Agrawal

Tel: 022 – 4040 3800 Ext: 341

E-mail: hitesh.agrawal@angeltrade.com

### Vibha Salvi

Tel: 022 – 4040 3800 Ext: 329

E-mail: vibhas.salvi@angeltrade.com

## Top-line driven by SLS and K-12 Segments

Educomp Solutions recorded 37.2% yoy growth in Revenues in 3QFY2010 driven by strong growth recorded by its SLS and K-12 Segments. The SLS Business comprising Smart Class and ICT Solutions (ICT) recorded strong 55.3% yoy growth in consolidated Revenues. The company implemented 355 new schools under the Smart Class Business, where the total number of schools touched 2,574 in 3QFY2010. In the ICT Business, Educomp signed in 363 new schools during the quarter taking the total to 14,826 schools in 3QFY2010. K-12 business comprising Educomp's owned and Eurokids High Schools, Pre-schools of Eurokids and Roots to Wings, grew 26.8% yoy on a consolidated basis on a lower base.

The Higher Learning Solutions (HLS) Segment however, de-grew by 12.7% yoy on a consolidated basis mainly on account of the 47% yoy fall in total teachers being trained during the quarter, which stood at 55,828 in 3QFY2010, and the new joint ventures (JVs), viz. Raffles and Pearson, which are under investment mode and yet not contributing strongly to Revenues.

The Online, Supplementary and Global Segments (comprises Online Supplementary products from its subsidiaries, viz. Learning.Com USA, Ask n Learn Singapore, AuthorGen, Learnhub.com and Learninghour.com, which provide career and work related counseling initiatives) de-grew 13.4% yoy as most of these products are currently in investment mode.

### Exhibit 1: Segment-wise Revenue Break-up

Segments	Revenues (Rs cr)		chg (%)	Contribution (%)	
	3QFY09	3QFY10		3QFY09	3QFY10
School Learning Solutions	127.9	198.7	55.3	67.5	76.4
Higher Learning Solutions	8.9	7.8	(12.7)	4.7	3.0
K-12 Schools	19.8	25.1	26.8	10.4	9.6
Online, Supplementary & Global	32.9	28.5	(13.4)	17.4	11.0
<b>Net Revenues</b>	<b>189.6</b>	<b>260.1</b>	<b>37.2</b>	<b>100.0</b>	<b>100.0</b>

Source: Company, Angel Research

## Outstanding Margins expansion due to reduction in Cost of Goods

Educomp's EBITDA Margins registered expansion of 580bp yoy during 3QFY2010 to 52.4% on the back of the 1,088bp yoy reduction in the Cost of Goods sold. However, SG&A and Staff costs increased by 440bp and 68bp yoy, respectively. The company's newer initiatives in HLS and Online, Supplement businesses, which are currently in investment mode, impacted overall Margins. However, strong improvement in SLS Margins cushioned the pressure on overall Margins.

### Exhibit 2: Segment-wise EBIT Break-up

Segment	EBIT (Rs cr)		chg (%)	Margin (%)	
	3QFY09	3QFY10		3QFY09	3QFY10
School Learning Solutions	61.4	121.6	98.2	48.0	61.2
Higher Learning Solutions	1.9	(4.1)	(315.4)	21.4	(52.7)
K-12 Schools	9.0	10.3	15.0	45.4	41.1
Online, Supplementary & Global	3.7	(4.7)	(227.6)	11.2	(16.5)
<b>Total</b>	<b>76.0</b>	<b>123.1</b>	<b>62.1</b>	<b>40.1</b>	<b>47.3</b>

Source: Company, Angel Research

### Strong Margins boost PAT despite higher Depreciation and Interest costs

Bottom-line grew by a robust 92.3% yoy in 3QFY2010 despite the 61% and 185% yoy increase in Depreciation and Interest costs respectively. This was mainly due to the strong Operational efficiency registered during the quarter and Other Income of Rs13.1cr (Loss of Rs15cr in 3QFY2009).

#### Exhibit 3: 3QFY2010 Performance (Consolidated)

Y/E March (Rs cr)	3QFY10	3QFY09	% chg	9MFY10	9MFY09	% chg
<b>Net Revenue</b>	<b>260.1</b>	<b>189.6</b>	<b>37.2</b>	<b>707.4</b>	<b>407.7</b>	<b>73.5</b>
Operating Costs	123.9	101.3	22.3	380.5	201.7	88.7
<b>EBITDA</b>	<b>136.2</b>	<b>88.3</b>	<b>54.3</b>	<b>326.9</b>	<b>206.1</b>	<b>58.6</b>
Depreciation & Amortisation	33.8	21.0	60.9	93.7	52.0	80.3
Finance Charges	13.9	4.9	185.2	36.0	10.4	247.8
Prior Period Items						
Other Income	13.1	(15.0)	(187.3)	106.3	(16.8)	(731.8)
<b>Income before Income Taxes</b>	<b>101.6</b>	<b>47.5</b>	<b>114.0</b>	<b>303.5</b>	<b>126.9</b>	<b>139.2</b>
Income Taxes	37.5	17.9	109.8	87.0	43.5	100.1
Net Income	64.1	29.6	116.6	216.5	83.4	159.5
Minority Interest	(3.0)	2.2		(5.7)	(5.5)	
Share in Associates						
Profit/Loss	0.1	0.0		0.1	(0.8)	
<b>Net Income after Min. Int. &amp; share in associates</b>	<b>61.2</b>	<b>31.8</b>	<b>92.3</b>	<b>210.9</b>	<b>77.2</b>	<b>173.3</b>
<b>Diluted EPS (Rs)</b>	<b>6.1</b>	<b>3.6</b>	<b>69.8</b>	<b>21.0</b>	<b>8.7</b>	<b>141.4</b>
EBITDA Margin (%)	52.4	46.6		46.2	50.5	
Net Profit Margin (%)	23.5	16.8		29.8	18.9	
Effective Tax Rate (%)	36.9	37.6		28.7	34.3	

Source: Company, Angel Research

### Outlook and Valuation

Educomp has been growing aggressively backed by strong expansion plans and execution capabilities. The company's total schools in Smart Class business currently stands at 2,574, with plans to take the same to 20,000 over the next 5-6 years, with shift in focus of expansion from Tier I to Tier II and III cities. This would also reduce the company's Sales cycle and improve Working Capital efficiency going forward in the Smart Class business. In 4QFY2010E, Educomp plans to add another 500 schools under the Smart Class umbrella, while in FY2011E it has guided to add totally 2,500 Smart Class schools.

The company plans to continue investing in Advertisements and Branding, to reach out faster to customers specifically in Tier I cities, which take longer conversion time. It has also strengthened its Sales team, which currently stands at around 230 personnel. Moreover, the School business being capital intensive, the company will require funding to facilitate planned expansion. Currently, it has received loan sanctions totaling Rs415cr (includes Term loan of Rs250cr from ICICI Bank, Rs100cr from Standard Chartered Bank and Rs75cr from Punjab National Bank). Further, additional Rs200-300cr Securitisation proposals are under sanction from State Bank of India, Axis Bank, IndusInd Bank and Canara Bank. Thus, as on date, the company has Rs720cr of debt sanctions to fund its expansion plans.

In the ICT Segment, the company plans to reduce focus on the low-Margin and long pay cycle projects, which would improve its Operational growth going forward.

In addition to its aggressive expansion plans in Smart Class, the company is also investing considerable amounts towards newer initiatives in terms of setting up its own K-12 high schools and colleges in JV with Raffles in the HLS Business Segment. Currently, two colleges are operational and going ahead another four colleges are expected to get operational across various cities in India. The company is also growing operations of newly acquired subsidiaries in the Online Supplementary businesses, which are under investment phase (capex incurred in Supplement business this far stands at Rs25cr, while another Rs40-50cr is expected to be incurred on small acquisitions and product launches by the company over the next 12-18 months) and hence witnessing losses. The company expects these newer initiatives particularly in the Supplementary business to deliver strong Revenue inflow over the next few years as it expects consumer spending in this area of Education to be 2x than on the school and college education spend.

The company's pre-school initiatives, viz. *Eurokids* and *Roots To Wings* are also witnessing strong traction.

We expect Educomp to record strong CAGR of 48.5% and 45.4% in Top-line and Bottom-line respectively, over FY2009-12E. **At the CMP, the stock is trading at 14.2x FY2012E EPS. We upgrade the stock from Neutral to a Buy, with Target Price of Rs926.**

Research Team Tel: 022-4040 3800

 E-mail: [research@angeltrade.com](mailto:research@angeltrade.com)

 Website: [www.angeltrade.com](http://www.angeltrade.com)
**DISCLAIMER**

This document is not for public distribution and has been furnished to you solely for your information and must not be reproduced or redistributed to any other person. Persons into whose possession this document may come are required to observe these restrictions.

Opinion expressed is our current opinion as of the date appearing on this material only. While we endeavor to update on a reasonable basis the information discussed in this material, there may be regulatory, compliance, or other reasons that prevent us from doing so. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice. Our proprietary trading and investment businesses may make investment decisions that are inconsistent with the recommendations expressed herein.

The information in this document has been printed on the basis of publicly available information, internal data and other reliable sources believed to be true and are for general guidance only. While every effort is made to ensure the accuracy and completeness of information contained, the company takes no guarantee and assumes no liability for any errors or omissions of the information. No one can use the information as the basis for any claim, demand or cause of action.

Recipients of this material should rely on their own investigations and take their own professional advice. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult their own advisors to determine the merits and risks of such an investment. Price and value of the investments referred to in this material may go up or down. Past performance is not a guide for future performance. Certain transactions - futures, options and other derivatives as well as non-investment grade securities - involve substantial risks and are not suitable for all investors. Reports based on technical analysis centers on studying charts of a stock's price movement and trading volume, as opposed to focusing on a company's fundamentals and as such, may not match with a report on a company's fundamentals.

We do not undertake to advise you as to any change of our views expressed in this document. While we would endeavor to update the information herein on a reasonable basis, Angel Securities, its subsidiaries and associated companies, their directors and employees are under no obligation to update or keep the information current. Also there may be regulatory, compliance, or other reasons that may prevent Angel Securities and affiliates from doing so. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice. Angel Securities Limited and affiliates, including the analyst who has issued this report, may, on the date of this report, and from time to time, have long or short positions in, and buy or sell the securities of the companies mentioned herein or engage in any other transaction involving such securities and earn brokerage or compensation or act as advisor or have other potential conflict of interest with respect to company/ies mentioned herein or inconsistent with any recommendation and related information and opinions.

Angel Securities Limited and affiliates may seek to provide or have engaged in providing corporate finance, investment banking or other advisory services in a merger or specific transaction to the companies referred to in this report, as on the date of this report or in the past.

**Note: Please refer important 'Stock Holding Disclosure' report on Angel web-site (Research Section).**

Disclosure of Interest Statement	Educomp
1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

*Note: We have not considered any Exposure below Rs 5 lakh for Angel, its Group companies and Directors.*

<b>Ratings (Returns) :</b>	Buy (> 15%) Reduce (-5% to -15%)	Accumulate (5% to 15%) Sell (< -15%)	Neutral (-5 to 5%)
----------------------------	-------------------------------------	---	--------------------

**Address: Acme Plaza, 'A' Wing, 3rd Floor, M.V. Road, Opp. Sangam Cinema, Andheri (E), Mumbai - 400 059.  
Tel : (022) 3952 4568 / 4040 3800**

Angel Broking Ltd: BSE Sebi Regn No : INB 010996539 / CDSL Regn No: IN - DP - CDSL - 234 - 2004 / PMS Regn Code: PM/INP000001546 Angel Securities Ltd: BSE: INB010994639/INF010994639 NSE: INB230994635/INF230994635 Membership numbers: BSE 028/NSE:09946  
 Angel Capital & Debt Market Ltd: INB 231279838 / NSE FNO: INF 231279838 / NSE Member code -12798 Angel Commodities Broking (P) Ltd: MCX Member ID: 12685 / FMC Regn No: MCX / TCM / CORP / 0037 NCDEX : Member ID 00220 / FMC Regn No: NCDEX / TCM / CORP / 0302