MOTILAL OSWAL

9 August 2018

1QFY19 Results Update | Sector: Publishing

Navneet Education

BSE SENSEX	S&P CNX
38,024	11,471

Motilal Oswal values your support in the Asiamoney Brokers Poll 2018 for India Research, Sales and Trading team. We request your ballot.

Bloomberg	NELI IN
Equity Shares (m)	234
M.Cap.(INRb)/(USDb)	28 / 0.4
52-Week Range (INR)	180 / 109
1, 6, 12 Rel. Per (%)	-9/-26/-44
12M Avg Val (INR M)	15
Free float (%)	38.2

Financials & Valuations (INR b)

Y/E March	2018	2019E	2020E
Net Sales	12.0	14.3	15.7
EBITDA	2.2	3.1	3.5
NP	1.3	1.8	2.1
EPS (INR)	5.4	7.9	8.9
EPS Gr. (%)	-26.1	45.7	12.8
BV/Sh. (INR)	32.2	36.5	40.5
RoE (%)	17.4	22.9	23.1
RoCE (%)	14.4	19.9	22.0
P/E (x)	21.7	14.9	13.2
P/BV (x)	3.6	3.2	2.9

Estimate change	↑
TP change	↑
Rating change	↑

CMP: INR120 TP: INR160 (+33%) Upgrade to Buy

In-line performance; improved visibility; Upgrade to Buy

Revenue up 19%, EBIDTA expands 75bp: Standalone revenue grew 19% YoY to INR6,700m (est. of INR6,453m) in 1QFY19, primarily driven by 58% YoY growth in Stationery revenue. EBITDA rose 22% YoY to INR1,974m (est. of INR1,916m), with the margin expanding 75bp YoY to 29.5% (est. of 30%). Adj. PAT grew 15% YoY to INR1,263m (est. of INR1,245m). PAT margin was flat YoY at 19% (in-line).

Publishing revenue marred by delay in textbook release…: Publishing revenue declined 2% YoY, primarily on account of a delay in government textbook (Balbharti) release (based on which the supplementary material is created) for standards 1, 8 and 10, where syllabus was changed. The delay was due to the introduction of a new policy on licensee fee, which was announced only on 21st June 2018. Consequently, we expect a spillover of ~INR600-700m of revenue to 2QFY19. Moreover, Publishing business visibility has improved further for FY20 based on syllabus change in Gujarat. We expect Publishing business to grow by 12% in FY19 and 9% in FY20.

…impact of which was offset by robust pick-up in Stationery biz: Stationery revenue grew by a robust 58% YoY, primarily driven by high-margin exports. In the domestic market, NELI aims to focus on improving profitability with higher emphasis on premium products, where it has a brand called 'Youva'. This will allow NELI to set itself apart from other players in the mid-premium and economy segments. We expect this segment to grow at 23% in FY19 and 7% in FY20.

New initiatives to place Navneet ahead of competitors, drive sustained growth: In Indiannica, NELI has added seven series for 1st to 8th standards, translating to 56 new titles for the next academic year. The marketing for these products will commence in October 2019, which will translate into sales in 4QFY19. Moreover, NELI will explore the supplementary books business in Indiannica. Further, the company plans to grow inorganically in the traditional supplementary books business in other parts of the country, as management believes that there is a dearth of serious players in other regions. NELI plans to publish only English medium books and believes that south is a good potential market. Also, NELI has its own apps for online learning which are scaling up. Notable initiatives are expected to drive sustained growth for NELI.

Valuation and view: We upgrade to **Buy** in view of:

a. Clarity emerging on the license policy, which is now already in place and applicable. NELI has also fully complied with it (immaterial cost attached with it).
b. Improved visibility on FY20 syllabus change
c. Stationary exports business coming back on track with large orders
d. Steep correction in the stock over the last three months (~19%), making it attractive from a valuation perspective

We expect NELI to deliver sales/PAT CAGR of 14%/28% over FY18-20. We value the stock at 18x (three-year average of one-year forward PE) FY20E earnings of INR8.9/share. Upgrading our rating to **Buy** with a revised TP of INR160/share.

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Standalone - Quarterly Earning Model (INR Million)

Y/E March	FY18				FY19				FY18	FY19E	FY19	Var
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE			1QE	%
Net Sales	5,652	1,834	1,744	2,126	6,700	2,890	1,906	1,694	12,040	14,294	6,453	4
YoY Change (%)	0.9	6.3	11.4	1.3	18.5	57.6	9.3	-20.3	1.9	18.7	14.2	
Total Expenditure	4,028	1,553	1,540	1,888	4,726	2,167	1,639	1,525	9,816	11,207	4,536	
EBITDA	1,624	281	205	238	1,974	722	267	169	2,225	3,088	1,916	3
Margins (%)	28.7	15.3	11.7	11.2	29.5	25.0	14.0	10.0	18.5	21.6	29.7	
Depreciation	53	56	62	64	57	67	69	70	307	349	65	
Interest	26	16	1	17	42	30	10	20	77	88	30	
Other Income	123	47	44	79	71	45	45	45	260	209	50	
PBT before EO expense	1,668	256	186	236	1,946	670	233	124	2,100	2,860	1,871	4
Extra-Ord expense	0	0	0	0	0	0	0	0	0	0	0	
PBT	1,668	256	186	236	1,946	670	233	124	2,100	2,860	1,871	4
Tax	572	89	67	84	683	228	79	42	825	972	636	
Rate (%)	34.3	34.9	36.1	35.8	35.1	34.0	34.0	34.0	39.3	34.0	34.0	
Minority Interest & Profit/Loss of Asso. Cos.	0	0	0	0	0	-10	-10	-10	14	50	-10	
Reported PAT	1,097	166	119	151	1,263	452	164	92	1,261	1,838	1,245	1
Adj PAT	1,097	166	119	151	1,263	452	164	92	1,261	1,838	1,245	1
YoY Change (%)	-3.4	-10.5	-6.1	-10.3	15.2	172.1	37.9	-39.1	-30.4	45.7	13.6	
Margins (%)	19.4	9.1	6.8	7.1	18.9	15.7	8.6	5.4	10.5	12.9	19.3	

E: MOSL Estimates

Improved visibility on account of FY20 syllabus change in Gujarat and Maharashtra

- Sustainable growth in publishing revenues is expected on the back of significant change in syllabus, especially Gujarat, where syllabus change is expected across 1st to 10th standards (refer exhibit).
- A change in syllabus typically does away with old and second hand books from trade and students buy new books (as per revised syllabus), which leads to sustainable growth; NELI being the preferred choice, there is good visibility in the business.

Exhibit 1: Syllabus change schedule- Significant changes in Gujarat curriculum

Academic year	Maharashtra		Gujarat	
	Standards	Subjects	Standards	Subjects
2019-20	II	All Subjects(All Medium)	I to VIII	Math
	III	All Subjects(All Medium)	VI to VIII	Science
	XI	All Subjects(All Medium)	X	Math and Science
			XII	Physics, Chemistry, Biology, Math

Source: Company, MOSL

EBIT margin expands 200bp in publishing biz: Publishing segment EBIT margins expanded 200bps YoY to 42% in 1QFY19 on account of price hikes taken on increased paper prices and efficiencies due to economies of scale. Stationery EBIT margins expanded 300 bps YoY to 18% in 1QFY19 due to substantial growth in high margin exports. On a blended basis, EBIT margins expanded only 82bp on account of relatively higher proportion of stationary revenues (lower margins than publishing segment) in the revenues mix, compared to previous year.

Clarity emerges over license policy, publishers to pay a license fee; negligible impact on margins for NELI

The Balbharti Board, which publishes textbooks for the state board of Maharashtra, had issued an advertisement/information in newspapers in March 2018 stating that all publishers in Maharashtra (including coaching classes) will have to procure a license before publishing any title. As a result of this none of the publishers had released any supplementary books for standard X (a key revenue driver) until June 20, 2018 when the regulatory clarity came in. Policy clarity has now been obtained and as per the new regulations, publishers are expected to pay a license fee for using the government textbooks. NELI incurred a one-time expense of INR2.5m-3m for full year FY19 for standards 1^{st}, 8^{th} and 10^{th}. In FY20 this is expected to increase to INR150m for standards 1^{st} to 10^{th} and is expected to be a recurring expense from hereon. In our view, this policy clarity provides comfort on business visibility, sustained continuity and is expected to have a negligible impact on margins for a large player like NELI.

Capex plans of INR1.1b in Publishing and Stationery to support growth

The company has planned a capex of INR300-350m in publication – for up gradation of machinery. It also plans to undertake capex INR800m in stationery business with INR400m to be invested in FY19 towards warehouse needs due to significant increase in export orders and another INR400m in FY20 to be invested towards storage and dispatch requirements especially critical during the peak season of sales from April to June (production from Jan to March). Funding for all capex will be done through internal accruals. This capex is expected to enhance operational efficiencies and create additional capacities required to support growth.

Indiannica transitioned; expect 58% growth in revenues

This year, the company has added 7 series for 1^{st} to 8^{th} standard translating to 56 new titles for the next academic year. The marketing for these products will commence in October 2019 which will translate to sales for 4QFY19. These titles will be marketed across India and across addressable markets. We expect these new 7 series introduction to drive 58% growth in revenues to INR900m in FY19 from INR570m in FY18; it is expected to break-even at EBITDA level this year in FY19.

Plans to grow supplementary books business inorganically

- NELI plans to grow inorganically in the supplementary books business in other parts of the country. It believes that it is very difficult to grow organically by starting from the scratch whereas it is easier to acquire an established player and scale that up. Also, no single publisher in any other state does more than INR1000m in revenue. Management believes there is a dearth of serious players in other regions. NELI plans to publish only English medium books and believes that the demand in South India is high as English as a medium of instruction is more commonly used in south India – around 45-50% students in south study in English medium versus 15-25% in Maharashtra and 15% in Gujarat.

Online learning scope expanding; to include B2B and now B2C

- In ESense, the company undertook B2B (business to business - sold to schools) business, now it has also commenced focusing on B2C (business to consumer) where content is sold to consumers who download the app at a nominal cost. It already has about 1,00,000 paid registrations. The app covers all subjects from grade 1 to 10 - across mediums. The apps have English and Marathi medium for Maharashtra and English and Guajarati medium for Gujarat grades 1-10. The management believes that there is huge scope - No. of students appearing for

10th std is ~1.7m/year and 1st to 10th is 22m/year (this includes government schools where parents do not have phones + if we exclude kids from 1st to 4th std; there is a visible market size of 10m/year). For this business, NELI has increased the no. of marketers from 150 last year to 200 this year.

Valuation and view

We upgrade to Buy in view of

- Clarity emerging on the license policy, which is now already in place and applicable. NELI has also fully complied with it (immaterial cost attached with it).
- Improved visibility on FY20 syllabus change
- Stationary exports business coming back on track with large orders
- Steep correction in the stock over the last three months (~19%), making it attractive from a valuation perspective

With pushback of some revenues to 2QFY19 in Publishing, combined with strong traction in high-margin Stationery exports, we expect NELI to deliver sales/PAT CAGR of 14%/28% over FY18-20. We value the stock at 18x (three-year average of one-year forward PE) FY20E earnings of INR8.9/share and upgrade our rating to Buy with a revised target price of INR160/share.

Exhibit 2: Youva long book and project books

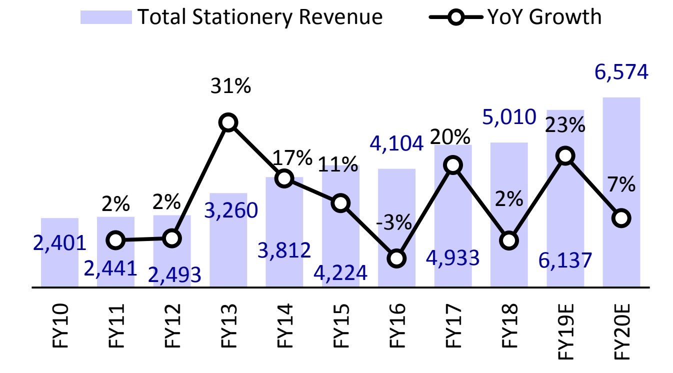
Source: MOSL, Company

Exhibit 3: Youva regular note book

Source: MOSL, Company

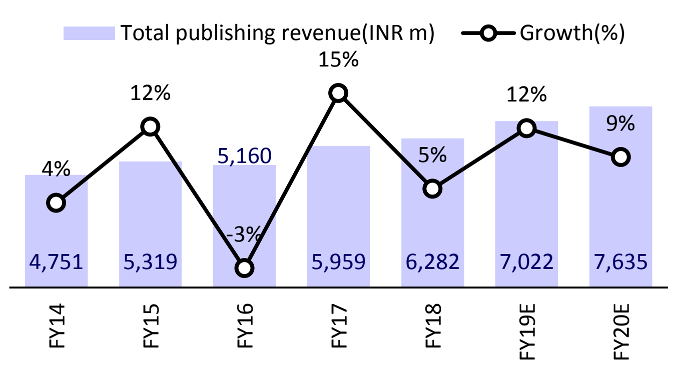
Story in charts

Exhibit 4: Stationary to grow at 15% CAGR over FY18-20



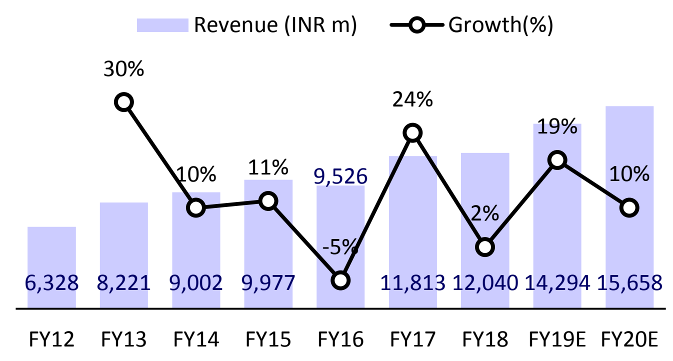
Source: MOSL, Company

Exhibit 5: Publishing to grow at 10% CAGR over FY18-20



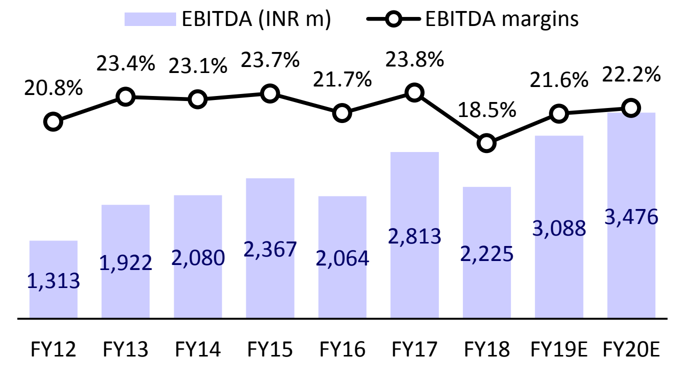
Source: MOSL, Company

Exhibit 6: 14% CAGR expected in revenues in FY18-20



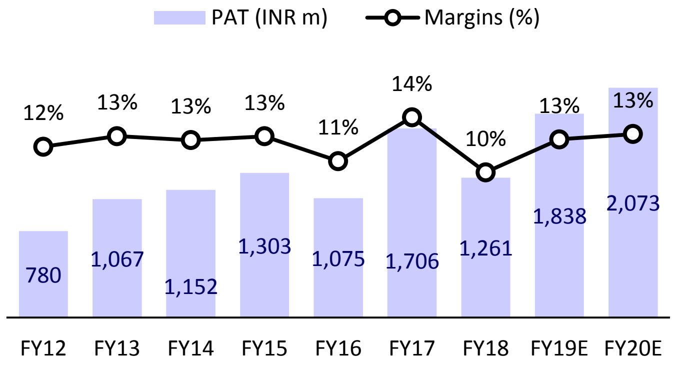
Source: MOSL, Company

Exhibit 7: EBIDTA margins trend



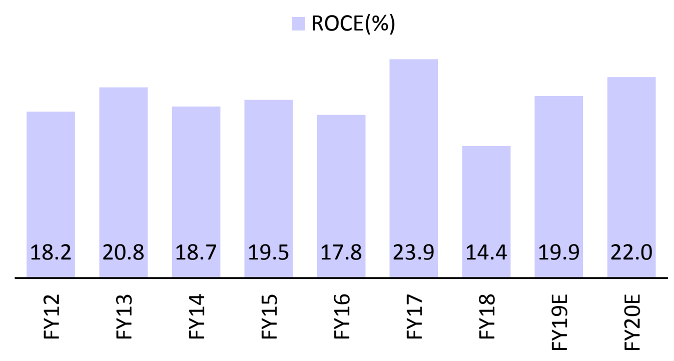
Source: MOSL, Company

Exhibit 8: PAT margins to improve



Source: MOSL, Company

Exhibit 9: ROCE trend



Source: MOSL, Company

Financials and Valuations

Consolidated - Income Statement **(INR Million)**

Y/E March	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Total Income from Operations	**5,599**	**6,328**	**8,221**	**9,002**	**9,977**	**9,526**	**11,813**	**12,040**	**14,294**	**15,658**
Change (%)	5.3	13.0	29.9	9.5	10.8	-4.5	24.0	1.9	18.7	9.5
Cost of Materials Consumed	2,687	3,003	3,870	4,337	4,640	4,597	5,447	5,849	6,647	7,250
% of Sales	48.0	47.5	47.1	48.2	46.5	48.3	46.1	48.6	46.5	46.3
Personnel Expenses	540	611	687	736	875	994	1,187	1,468	1,701	1,816
% of Sales	9.6	9.7	8.4	8.2	8.8	10.4	10.0	12.2	11.9	11.6
Other Expenses	1,102	1,262	1,577	1,668	1,912	1,871	2,368	2,499	2,859	3,116
% of Sales	19.7	20.0	19.2	18.5	19.2	19.6	20.0	20.8	20.0	19.9
Excise Duty	116	138	164	181	182	0	0	0	0	0
% of Sales	2.1	2.2	2.0	2.0	1.8	0.0	0.0	0.0	0.0	0.0
Total Expenditure	**4,445**	**5,014**	**6,298**	**6,922**	**7,610**	**7,462**	**9,001**	**9,816**	**11,207**	**12,182**
% of Sales	79.4	79.2	76.6	76.9	76.3	78.3	76.2	81.5	78.4	77.8
EBITDA	**1,154**	**1,313**	**1,922**	**2,080**	**2,367**	**2,064**	**2,813**	**2,225**	**3,088**	**3,476**
Margin (%)	20.6	20.8	23.4	23.1	23.7	21.7	23.8	18.5	21.6	22.2
Depreciation	136	171	235	258	308	297	284	307	349	386
EBIT	**1,018**	**1,142**	**1,688**	**1,822**	**2,060**	**1,768**	**2,529**	**1,918**	**2,739**	**3,090**
Int. and Finance Charges	32	58	88	100	91	36	43	77	88	48
Other Income	82	112	37	35	28	167	152	260	209	219
PBT bef. EO Exp.	**1,068**	**1,197**	**1,637**	**1,757**	**1,996**	**1,899**	**2,638**	**2,100**	**2,860**	**3,261**
EO Items	0	0	-13	0	0	0	0	0	0	0
PBT after EO Exp.	**1,068**	**1,197**	**1,623**	**1,757**	**1,996**	**1,899**	**2,638**	**2,100**	**2,860**	**3,261**
Current Tax	394	408	547	594	699	694	865	825	972	1,109
Deferred Tax	10	12	3	11	-7	4	-39	0	0	0
Tax Rate (%)	37.8	35.1	33.9	34.4	34.7	36.7	31.3	39.3	34.0	34.0
Less: Minority Interest	-3	-3	6	1	1	127	104.7	14	50	80
Reported PAT	**668**	**780**	**1,067**	**1,152**	**1,303**	**1,075**	**1,706**	**1,261**	**1,838**	**2,073**
Adjusted PAT	**668**	**780**	**1,076**	**1,152**	**1,303**	**1,075**	**1,706**	**1,261**	**1,838**	**2,073**
Change (%)	4.4	16.8	37.9	7.1	13.2	-17.5	58.7	-26.1	45.7	12.8
Margin (%)	11.9	12.3	13.1	12.8	13.1	11.3	14.4	10.5	12.9	13.2

Consolidated - Balance Sheet **(INR Million)**

Y/E March	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Equity Share Capital	476	476	476	476	476	476	467	467	467	467
Preference Capital	0	0	3	3	0	0	0	0	0	0
Total Reserves	2,750	3,138	3,712	4,307	4,956	5,354	6,471	7,053	8,047	8,995
Net Worth	**3,226**	**3,615**	**4,192**	**4,787**	**5,433**	**5,831**	**6,938**	**7,520**	**8,514**	**9,462**
Minority Interest	-3	-6	1	1	1	1	1	2	2	2
Deferred Liabilities	44	57	64	73	41	41	-1	0	0	0
Total Loans	663	1,452	1,687	2,337	1,436	1,035	1,594	2,253	1,253	653
Capital Employed	**3,930**	**5,118**	**5,943**	**7,197**	**6,909**	**6,907**	**8,532**	**9,775**	**9,769**	**10,118**
Gross Block	2,411	2,973	3,316	3,673	3,741	4,147	5,145	5,018	5,718	6,168
Less: Accum. Deprn.	1,222	1,362	1,574	1,798	2,042	2,338	2,622	2,929	3,277	3,664
Net Fixed Assets	**1,189**	**1,611**	**1,742**	**1,874**	**1,699**	**1,809**	**2,523**	**2,089**	**2,440**	**2,504**
Goodwill on Consolidation	0	0	0	0	0	0	0	457	457	457
Capital WIP	98	36	57	45	40	8	28	41	0	0
Total Investments	**1**	**6**	**310**	**475**	**492**	**451**	**360**	**458**	**458**	**458**
Curr. Assets, Loans&Adv.	**3,156**	**4,128**	**4,982**	**6,042**	**5,995**	**5,426**	**7,297**	**8,490**	**8,379**	**8,852**
Inventory	1,771	2,176	2,752	3,337	3,484	3,074	3,843	4,282	4,386	4,633
Account Receivables	868	1,164	1,659	1,961	1,886	1,868	2,781	3,181	2,859	3,046
Cash and Bank Balance	113	51	35	69	55	59	97	68	79	13
Loans and Advances	404	737	536	675	571	425	576	959	1,055	1,161
Curr. Liability & Prov.	**525**	**675**	**1,163**	**1,253**	**1,317**	**788**	**1,676**	**1,761**	**1,965**	**2,154**
Account Payables	271	406	585	643	586	683	760	753	856	934
Provisions	254	268	577	610	731	105	916	1,008	1,109	1,220
Net Current Assets	**2,631**	**3,454**	**3,819**	**4,789**	**4,678**	**4,639**	**5,621**	**6,729**	**6,414**	**6,699**
Appl. of Funds	**3,930**	**5,118**	**5,943**	**7,197**	**6,909**	**6,907**	**8,532**	**9,775**	**9,769**	**10,118**

E: MOSL Estimates

Financials and Valuations

Ratios

Y/E March	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Basic (INR)										
EPS	**2.8**	**3.3**	**4.5**	**4.8**	**5.5**	**4.5**	**7.3**	**5.4**	**7.9**	**8.9**
Cash EPS	3.4	4.0	5.5	5.9	6.8	5.8	8.5	6.7	9.4	10.5
BV/Share	13.5	15.2	17.6	20.1	22.8	24.5	29.7	32.2	36.5	40.5
DPS	1.4	1.4	1.8	2.0	2.2	2.2	2.5	1.4	3.0	4.0
Payout (%)	58.1	49.7	47.0	48.4	48.4	58.7	41.2	31.2	45.9	54.3
Valuation (x)										
P/E				24.2	21.4	25.9	16.0	21.7	14.9	13.2
Cash P/E				19.8	17.3	20.3	13.7	17.4	12.5	11.1
P/BV				5.8	5.1	4.8	3.9	3.6	3.2	2.9
EV/Sales				3.3	2.9	3.0	2.4	2.5	2.0	1.8
EV/EBITDA				14.2	12.1	13.7	10.2	13.3	9.2	8.0
Dividend Yield (%)	1.2	1.2	1.5	1.7	1.9	1.9	2.1	1.2	2.6	3.4
Return Ratios (%)										
RoE	21.7	22.8	27.6	25.7	25.5	19.1	26.7	17.4	22.9	23.1
RoCE	18.1	18.2	20.8	18.7	19.5	17.8	23.9	14.4	19.9	22.0
RoIC	17.5	17.0	21.1	19.7	20.8	17.6	24.1	13.5	19.6	21.6
Working Capital Ratios										
Inventory (Days)	115	126	122	135	127	118	119	130	112	108
Debtor (Days)	57	67	74	80	69	72	86	96	73	71
Creditor (Days)	18	23	26	26	21	26	23	23	22	47
Working Cap. Turnover (Days)	164	196	168	191	169	175	171	202	162	156
Leverage Ratio (x)										
Current Ratio	6.0	6.1	4.3	4.8	4.6	6.9	4.4	4.8	4.3	4.1
Debt/Equity	0.2	0.4	0.4	0.5	0.3	0.2	0.2	0.3	0.1	0.1

Consolidated - Cash Flow Statement

(INR Million)

Y/E March	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
OP/(Loss) before Tax	1,068	1,197	1,636	1,757	1,996	1,899	2,638	2,100	2,860	3,261
Depreciation	136	171	235	258	308	297	284	307	349	386
Interest & Finance Charges	8	4	-1	0	0	-19	-12	0	0	0
Direct Taxes Paid	-396	-411	-520	-607	-651	-743	-766	-825	-972	-1,109
(Inc)/Dec in WC	-193	-891	-658	-889	-100	511	-1,140	-1,137	326	-351
CF from Operations	**624**	**70**	**692**	**519**	**1,553**	**1,945**	**1,004**	**445**	**2,562**	**2,188**
Others	-23	6	48	72	69	-140	-126	77	88	48
CF from Operating incl EO	**601**	**76**	**740**	**591**	**1,622**	**1,806**	**878**	**522**	**2,650**	**2,236**
(inc)/dec in FA	-406	-499	-363	-430	-176	-264	-553	113	-659	-450
Free Cash Flow	**195**	**-423**	**377**	**162**	**1,446**	**1,542**	**325**	**636**	**1,991**	**1,786**
(Pur)/Sale of Investments	1	-2	-315	-163	-11	37	37	-99	0	0
Others	52	37	-21	-24	106	188	-256	-741	0	0
CF from Investments	**-353**	**-464**	**-699**	**-617**	**-81**	**-40**	**-771**	**-726**	**-659**	**-450**
Issue of Shares	0	0	12	-1	-3	0	-582	0	0	0
(Inc)/Dec in Debt	-46	769	240	658	-901	-401	562	659	-1,000	-600
Interest Paid	-32	-58	-86	-97	-93	-36	-43	-77	-88	-48
Dividend Paid	-168	-386	-221	-501	-557	-1,262	0	-394	-843	-1,124
Others	0	0	0	0	0	-63	-5	-13	-50	-80
CF from Fin. Activity	**-246**	**325**	**-56**	**59**	**-1,555**	**-1,762**	**-68**	**175**	**-1,981**	**-1,852**
Inc/Dec of Cash	**2**	**-63**	**-15**	**34**	**-14**	**4**	**38**	**-29**	**10**	**-66**
Opening Balance	111	113	50	35	69	55	59	97	69	79
Closing Balance	**113**	**50**	**35**	**69**	**55**	**59**	**97**	**69**	**79**	**13**

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	> - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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