Initiating Coverage | 29 March 2017

Sector: Publishing

Navneet Education

Steadfast; growth gaining momentum

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Navneet Education

BSE Sensex	S&P CNX
29,531	9,144

CMP: INR153 TP: INR210 (+37%) Buy

Knowledge is wealth

Stock Info

Bloomberg	NELI IN
Equity Shares (m)	233.5
52-Week Range (INR)	155 / 81
M.Cap. (INR b)	35.3
M.Cap. (USD b)	0.5
1, 6, 12 Rel. Per (%)	4/46/69
Avg Val, (INR m)	17
Free float (%)	-

Financial Snapshot (INR b)

Y/E Mar	2017E	2018E	2019E
Sales	10.9	13.7	16.1
EBITDA	2.5	3.3	4.0
NP	1.6	2.0	2.5
EPS (Rs)	6.6	8.6	10.5
EPS Gr. (%)	53.2	29.3	22.6
BV/Sh. (INR)	26.2	31.0	37.1
RoE (%)	26.0	30.0	30.9
RoCE (%)	21.1	23.7	25.8
P/E (x)	23.0	17.8	14.5
P/BV (x)	5.8	4.9	4.1

Shareholding pattern (%)

As On	Sep-16	Jun-16	Sep-15
Promoter	61.8	61.8	61.8
DII	15.2	15.2	15.2
FII	6.8	6.5	2.5

Navneet Education

Steadfast; growth gaining momentum

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Please click here for Video Link

Navneet Education Limited (NELI), founded by the Gala family, is in the business of (a) publishing – educational, supplementary, children's and general books, (b) stationery products, and (c) digital education. It derives 54% of its revenue from publishing and 43% from stationery. NELI's products are sold under the brand names *Navneet*, *Vikas*, *Gala*, *Grafalco*, *Boss, Youva* and *eSense*. It recently acquired Britannica India's curriculum business for INR880m; this would be synergic to its CBSE curriculum business & did buyback of shares to tune of INR580m.

Steadfast; growth gaining momentum

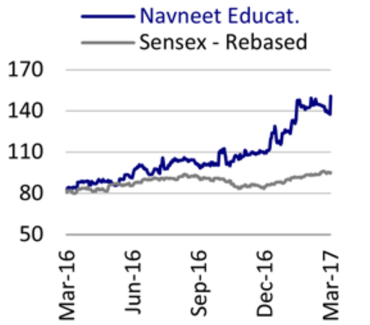
CBSE curriculum opportunity sizable; future-ready with digital offerings

- **NELI dominates the market for supplementary educational material for the Maharashtra and Gujarat State Education Boards. Its domineering position makes it a key beneficiary of the sustained demand for new supplementary material & workbooks, driven by periodical syllabus overhaul by the State Boards.**
- **Change of Syllabus in X and XII in Gujarat in FY18 and X and VII in Maharashtra in FY19 provides strong triggers for growth in next two years.**
- **Common curriculum in Mathematics and Science across India triggers a huge opportunity for NELI to sell textbooks to CBSE-pattern schools across India. With the recent acquisition of Encyclopedia Britannica India (EBI), NELI is well poised to gain meaningful share in the growing CBSE market.**
- **In the stationery business, while competitive intensity in the domestic market is high, NELI's growth would be largely driven by exports. In the exports segment, which constitutes 43% of its stationery business, NELI has begun focusing on value-added products that command premium pricing.**
- **NELI also has various digital content offerings through its subsidiary, eSense. Though this segment hasn't seen rapid growth since its launch in FY09, we believe this will change with increasing thrust on digitization and growing penetration.**
- **We expect 22% revenue CAGR and 26% PAT CAGR over FY17-19. We value the company at 20xFY19E EPS with a target price of INR210 & initiate with a Buy rating.**

Change of Syllabus in standard X in FY18 and FY19, key triggers for growth

State Education Boards (SEBs) change their syllabi for standards I to XII in a phased manner every six years. This provides sustainable demand for supplementary material like guide, workbook and 21 most likely sets as students are compelled to buy material updated as per new syllabi. However, Standard X being critical year for a student, change in syllabi is a big trigger for growth for companies like NELI. Standard X constitutes ~17% of the total revenue for NELI. NELI deals in supplementary books like Guide (40% of revenue), workbook (45%) and 21 most likely sets (15%) and has a strong hold in states of Maharashtra and Gujarat with a market share of ~65%. Students in Xth Standard generally prefer to buy all kinds of supplementary materials and in year of change of syllabus students go for new supplementary materials and not second hand ones. Change of Syllabus in X and XII in Gujarat in FY18 and X and VII in Maharashtra in FY19 provides strong triggers for growth in next two years. Thus, we expect strong revenue CAGR of 18% over FY17-19E vs revenue CAGR of 4% over FY14-16.

Stock Performance (one-year)



Common curriculum, EBI acquisition – huge opportunity in CBSE space

Common curriculum in Mathematics and Science across India triggers a huge opportunity (INR30b market) for NELI to sell textbooks to CBSE schools across India. Unlike schools affiliated to State Boards, CBSE schools use other private publishers' textbooks apart from board-approved textbooks. Currently, NELI operates under the brand *Grafalco*, and besides its two core states, markets textbooks in five regions – NCR, Karnataka, Andhra Pradesh, Kerala and Tamil Nadu. NELI has recently acquired Encyclopedia Britannica India (EBI), which provides curricular material for the CBSE/international boards – has a presence in 6,000+ schools. The acquisition will help NELI to significantly improve market visibility, enhance curriculum offerings, fill title gaps, and deepen penetration in CBSE and international boards. NELI has limited presence in EBI's key markets – Punjab, Rajasthan, Haryana, Andhra Pradesh, Uttar Pradesh and Delhi/NCR. Also, EBI has a well-distributed revenue mix across India, which supports NELI's quest to transition from a regional entity to a pan-India entity. We believe EBI acquisition would be synergic to NELI and grow at 30% CAGR to INR 1,454m over FY17-19. We expect it to garner meaningful market share in this growing segment (market size to expand 3x to INR100b in five years, with many schools opting for conversion from the State Boards to CBSE/CBSE-pattern schools).

High-margin exports to drive growth in stationery business

NELI's stationery business (43% of total revenue) will be largely driven by growth in exports (~44% of stationery revenue). Given the high competitive intensity in the domestic segment, NELI is focusing more on exports. The company has moved from exporting low-margin commoditized products to value-added products like embossed stationery, 3D cover page design, and patented stationery. It has 100% in-house production for export products and margins in the export segment are 300-400bp higher than in the domestic segment. The US is its export hub (NELI being a preferred supplier to Walmart), accounting for 73% of its exports. We expect 12.5% CAGR in the stationery business, led by higher growth of ~19% in the export segment. This is expected to increase contribution of exports business to 50% by FY18 aid margin expansion.

eSense to capture "next gen" digital opportunity

NELI has various offerings in the digital business through its subsidiary, eSense, and is looking to grow in both B2B and B2C segments. Among its digital offerings are an online portal (TopScorer), CD ROMs, tablets, and pen drives containing curricular content. To increase adoption rate, NELI has increased its ad spends to INR80m-100m for FY17 (~INR60m in FY16). This segment hasn't seen a rapid growth since its launch in FY09. However, we believe with increasing thrust on digitization and growing penetration (so far, it has tapped only ~3,500 of 39,000 private schools in Maharashtra and Gujarat), eSense will achieve 20% CAGR over FY17-19.

Valuation and view

In the publication business, we believe NELI is perfectly placed to capture multiple growth triggers like changing syllabus, common curriculum across India, increasing conversion of SEB schools to CBSE. We remain excited about export-led growth in the stationery business and NELI's future-ready eSense platform. We expect 21.7% revenue CAGR and 25.9% PAT CAGR with 120bp margin expansion to 24.5% over FY17-19. Despite EBI acquisition (~INR880m) & equity buyback (INR580m) in FY17E, RoCE is likely to improve from 21.1% in FY17 to 25.8% by FY19. We initiate coverage with a **Buy** – our target price of INR210 (20x FY19E EPS) implies 37% upside.

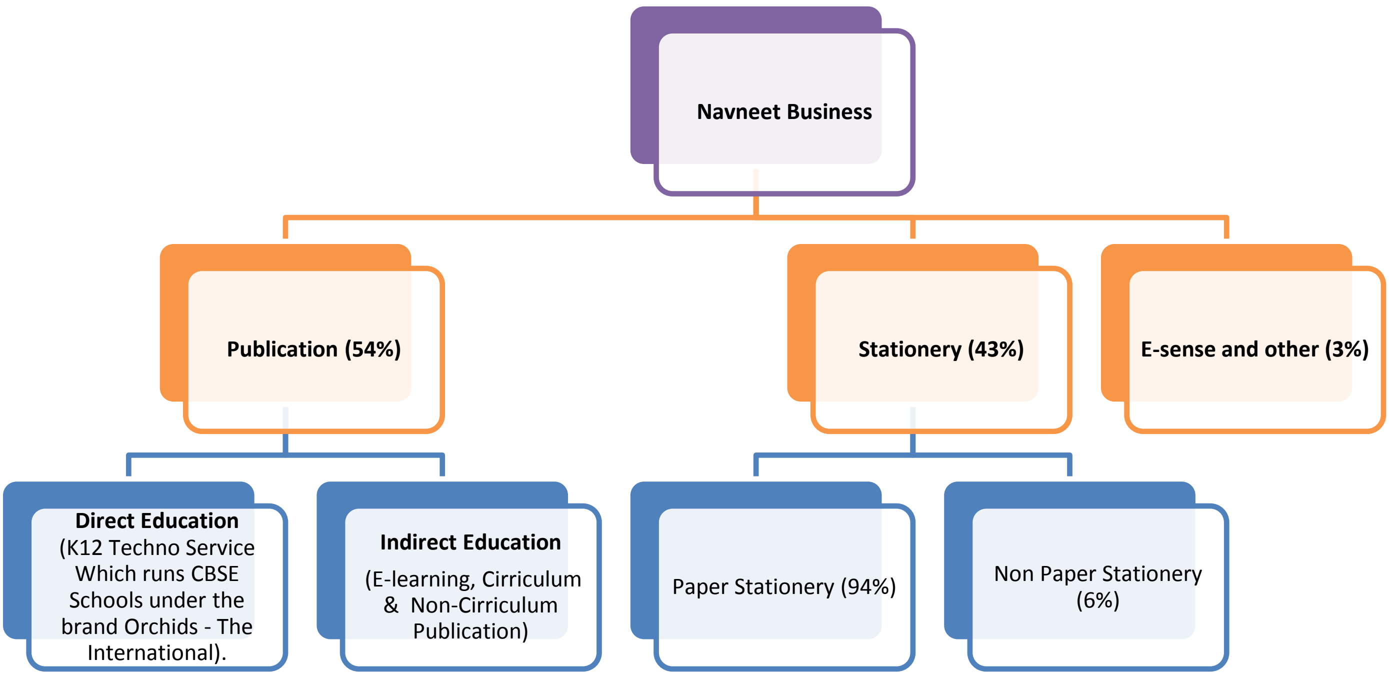
Company description

Navneet Education Limited (NELI; formerly known as Navneet Publications (India) Limited), founded by the Gala family, is in the business of educational, children's and general book publishing, scholastic papers, non-paper stationery products, and digital education. The company has built a strong brand in publications and stationery, and has gained a leadership position. Since 1959, NELI has been a major force in the dissemination of knowledge. It is a dominant player in the field of publishing, with more than 5,000 titles in English, Gujarati, Hindi, Marathi, Tamil, Urdu, and other Indian and foreign Languages.

Over the decades, NELI has emerged as a preferred brand for educational products among teachers and students in India. The company's products are sold under the brand names *Navneet*, *Vikas*, *Gala*, *Grafalco*, *Boss, Youva* and *eSense*. Its portfolio of educational books includes high quality supplementary books like digests (guides), workbooks, and 21 most likely question sets, most of which are published in five languages – English, Gujarati, Hindi, Marathi, and Urdu.

NELI has a dominant market share of about 65% in West India. Also, with the new range of text books targeting students from the CBSE and ICSE boards, its educational products are now available in seven states of India. It also publishes various titles in the children's and general books category, which are not based on syllabus – coloring and activity books, board books, story books, and books on health & hygiene, art & artist, cooking, mehendi, embroidery, etc. These are sold pan India.

Exhibit 1: Navneet's business



Source: Company, MOSL

Evolution over the years

1 **1959** First Digest/Guide published for Std X

2 **1970** Workbook concept introduced to standardize teaching across classes and divisions

3 **1975** Published 21 Most likely Question sets for X & XII

4 **1990** Children Books introduced

5 **1993** Started Stationery division

6 **1994** First and only Educational Publisher to be listed on BSE & NSE

7 **2000** Stationery capacity reached 100tns/day. ISO Certification awarded

8 **2003** Implementation of SAP & KAIZEN

9 **2008** Entered B2B Digital Learning space

10 **2011** Ventured Direct Education space

11 **2014** Entered B2C Digital Learning space

12 **2016** New Stationery brand YOUVA launched

Multiple triggers in print publication

Signs of sustainable growth visible

- **State Education Boards (SEBs) change their syllabi for standards I to XII in a phased manner every six years. This provides sustainable demand for supplementary material, as students are compelled to buy material updated as per new syllabi. Given its domineering position in Maharashtra (~65% market share) and Gujarat (~70% market share), NELI is a major beneficiary.**
- **The next two years should mark a period of high growth for NELI, given the significant changes in standard-X syllabi scheduled over FY17-19 in its two core states (refer exhibit 12).**
- **Its (a) presence in multiple regional languages, and (b) strong pool of ~225 authors, with NELI paying 2-8% royalty (highest in the industry) act as significant entry barriers. Barring NELI, no publisher of educational supplementary books is present in more than two states in India.**
- **Every state has a different regional language and no publisher can be successful without regional language publication as ~80% students study in regional medium (except few southern states where number is ~60%; infringement of IPR risk creates a huge entry barrier due to which no publisher in educational supplementary book except Navneet is present in more than 2 states across India.**
- **After a tepid FY16, the publishing segment has grown 16% in 1HFY17, led by (a) syllabus change, (b) strong growth in the CBSE segment, and (c) enhanced curriculum offerings. We expect this segment to grow at 18.1% over FY17-19, led by significant changes in standard X curriculum in core states.**

Diversified revenue streams to ensure sustained growth

Barring class X, no single class contributes over 10% of revenue

The ~INR135b K-12 (Kindergarten to 12th) print publication market is growing at 12% per year. It is a fragmented industry in India, with a large number of regional players. It consists of textbooks and supplementary books like workbooks, guides/digests and question banks. It is a content-driven business, with publishers/authors developing course material based on latest syllabi prescribed by respective state education boards.

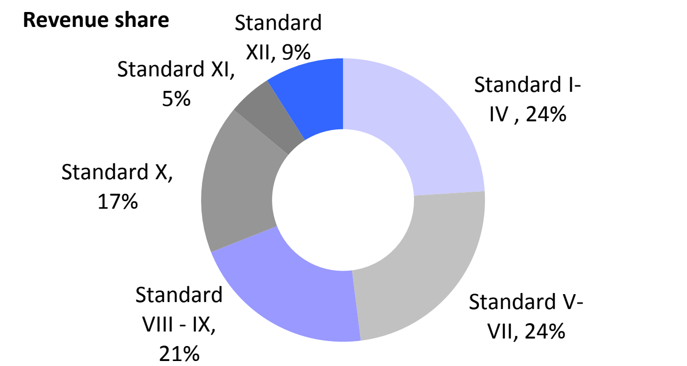
Exhibit 2: Navneet's K-12 print publication portfolio

	Curriculum segment		Non-Curriculum segment
	Supplementary	Textbooks	
Target market	Caters to State board curriculum in Maharashtra and Gujarat	Caters to CBSE curriculum in Maharashtra, Gujarat, Andhra Pradesh, Karnataka, Tamil Nadu, Kerala and NCR region	Presence all over India and overseas
Products	Offers Supplementary Educational Publication(Workbooks, Digest and 21 Most likely questions) for K12 segment	Offers Textbooks for grades kindergarten to VIII	Caters to children and General books
Revenue split	89% of total publication revenue (Workbook: 48%, Digest/Guides: 35%, 21 Most likely questions:17%)	4% of total K12 print content revenue in FY16	7% of total publication revenue in FY16 (Domestic: 69%, Exports: 31%)

Source: Company, MOSL

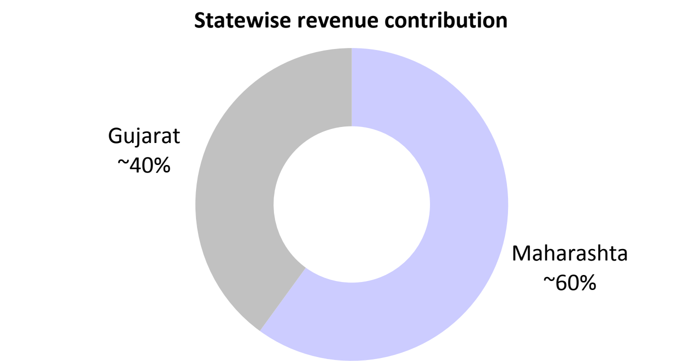
NELI provides workbooks, guides and last minute revision books as supplementary material for students to prepare for their curriculum. Workbooks and guides are available for all standards, while last minute revision books are available only for class X and class XII. NELI's publication revenues are diversified across categories and classes. Barring class X, no single class contributes more than 10% of revenue. Workbooks (48% of publication revenue) are recommended by teachers – 'pull' model. Guides (35% of publication revenue) and last minute revision sets (17% of publication revenue) are demanded by students to assist them in their studies – 'push' model. NELI's revenues are diversified geographically as well, with Maharashtra contributing ~60% and Gujarat contributing ~40%. Its plans to expand to new states will further diversify its revenue streams.

Exhibit 3: Break-up of revenue based on various classes



Source: Company, MOSL

Exhibit 4: Geographical revenue break-up



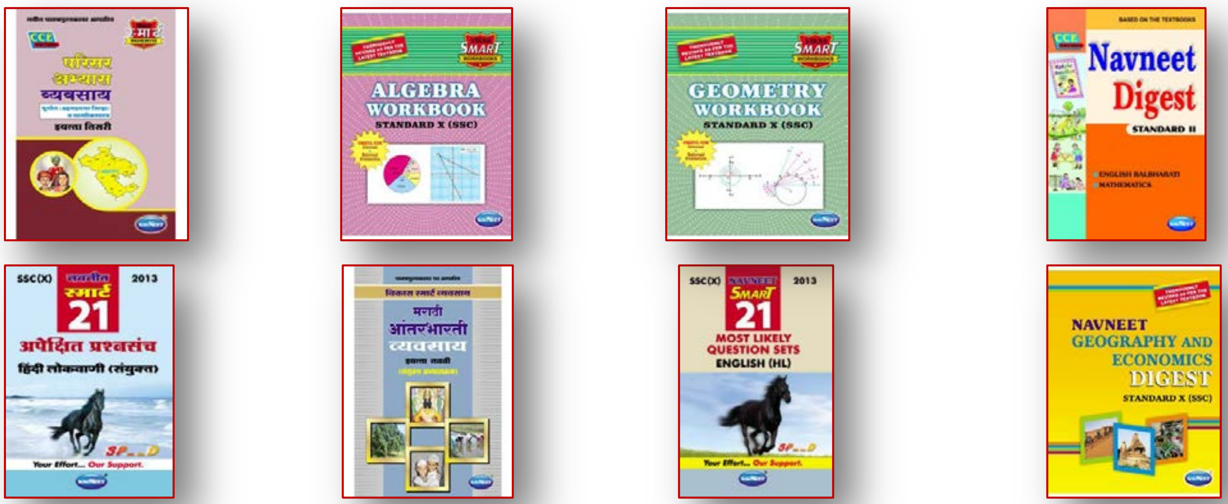
Source: Company, MOSL

Exhibit 5: Supplementary segment split

Particulars	Workbooks	Guides	Last Minute Revision
Classes for which book is available	Class II to X	Class I to XII	Class X & XII
% of Print Publication Revenue	48%	35%	17%
Sales Model	Pull model	Push model	Push model
Recommendation	Schools	Informal suggestion by teachers	Self-study

Source: Company, MOSL

Exhibit 6: Snapshot of product portfolio of syllabus-based books



Source:

Exhibit 7: Snapshot of product portfolio of non-syllabus books

Source: Company, MOSL

The publishing business is seasonal, with April-June (Q1) accounting for 50-55% of sales. However, for sales to happen in Q1, NELI starts its printing activity from November. Paper procurement happens over November-December and manufacturing commences for the next season. Marketing activity starts during the January-March period. Working capital requirement is at its peak in March and at its trough in September.

Exhibit 8: Quarter-wise activity

Quarters	Activities during the quarter	Effect on P&L and Balance Sheet
Oct-Dec	Paper purchase contracts	Huge Manufacturing expenditure
	Start of printing activity	Inventory rises
	Sales ~10-15%	
Jan-Mar	Printing activity continues	Huge Manufacturing expenditure
	Marketing activity starts from next academic year	Inventory at its peak
	Sales ~15%	Short term borrowings from banks
Apr-June	Printing activity continues	Highest revenue amongst all quarters
	Major Sale ~50-55%	Major profits realized
Jul-Sept	Major debtors realized	Thin Balance Sheet
	Sales ~15-20%	Zero debt

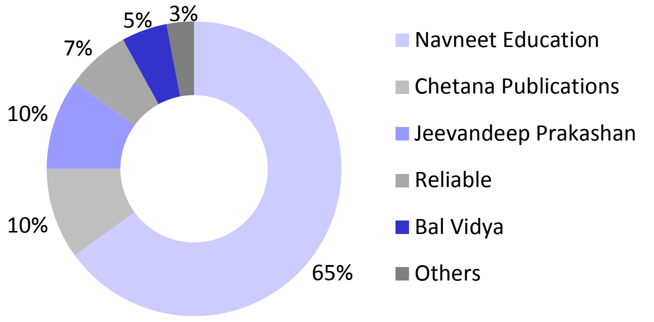
Source: Company, MOSL

Market leader in Maharashtra and Gujarat

Navneet is the market leader in both Maharashtra and Gujarat, with a market share of ~65% and ~70%, respectively

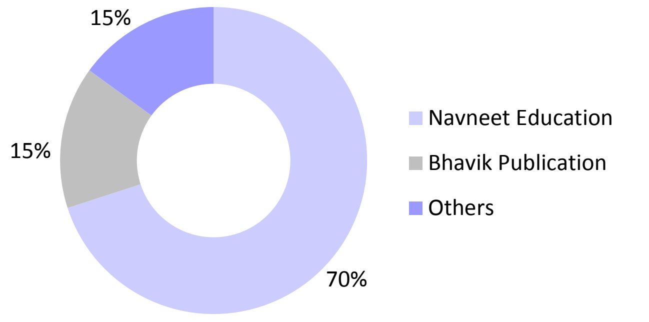
NELI is the leading publisher in both Gujarat and Maharashtra, with rich experience of over 50 years in both regions. It has ~65% market share in Maharashtra; other publishers like Chetana, Jeevandeep, Reliable, and Bal Vidhya Prakashan have single-digit to low double-digit share. Gujarat is dominated by two players – NELI is the leader, with ~70% market share, followed by Bhavik Publisher, with 15% market share. An advantage of being market leader is that authors have an incentive to be associated with large publishers, as their compensation is linked to the number of copies sold. (NELI pays royalty on sales every year unlike other publishers that pay lump sum royalty). We believe NELI will continue to dominate the two states and penetrate more to gain operating leverage.

Exhibit 9: Market share in Maharashtra



Source: Industry, MOSL

Exhibit 10: Market share in Gujarat



Source: Industry, MOSL

Syllabus changes lead to sustainable growth

Complete syllabus change every six years brings sustainability in the business

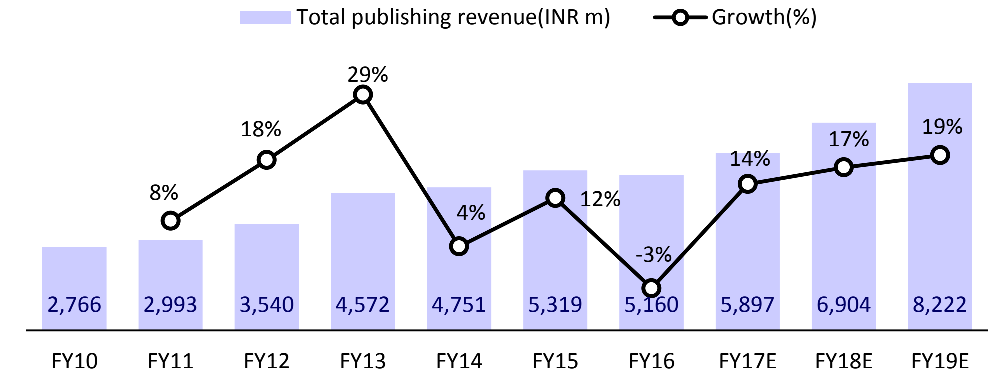
According to the directives of the SSC Board, the syllabus is changed in a phased manner over every 5-6 years for all standards. All text books provided by the state are changed and so is the supplementary material (workbooks, guides and last-minute revision sets). NELI is a preferred brand in supplementary material; it has ~65% market share in Maharashtra and ~70% market share in Gujarat. NELI's supplementary material is updated regularly and its better format makes it the first choice amongst students. Changing syllabus 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 long-term visibility in the business.

Exhibit 11: Syllabus change schedule- Significant changes in Std X curriculum

Academic year	Maharashtra Standards	Subjects	Gujarat Standards	Subjects
2013-14	I	All subjects (All mediums)	VI	All subjects (Eng and Hindi medium)
	II	All subjects (All mediums)	VII	All subjects (Eng and Hindi medium)
	X	All languages	VIII	All subjects (Eng and Hindi medium)
		History and Political science		
		Geography, Economics		
		Science - Environment		
2014-15	III	All subjects (All mediums)	I	All subjects (Gujarati medium)
	IV	All subjects (All mediums)	II	All subjects (Gujarati medium)
			III	All subjects (Gujarati medium)
			IV	All subjects (Gujarati medium)
			V	All subjects (Gujarati medium)
	V	All subjects (All mediums)	I	All subjects (English & Hindi Mediums)
			III	All subjects (English & Hindi Mediums)
2015-16			IV	All subjects (English & Hindi Mediums)
			V	All subjects (English & Hindi Mediums)
2016-17	VI	All subjects (All mediums)	IX	All subjects(Gujarati Medium)
	IX	Marathi & Hindi(Paper Pattern)	XI	All subjects(Gujarati Medium)
	X	Marathi & Hindi(Paper Pattern)		
2017-18	VII	All Subjects(All Medium)	X	All subjects except Maths and Science(All mediums)
	IX	All Subjects(All Medium)	XII	All commerce & Art subjects (All mediums)
2018-19	VIII	All Subjects(All Medium)		Not Yet Announced
	X	All Subjects(All Medium)		

Source: Company, MOSL

Exhibit 12: Publishing revenue to grow at 18.1% CAGR in over FY17-19E



Source: Company, MOSL

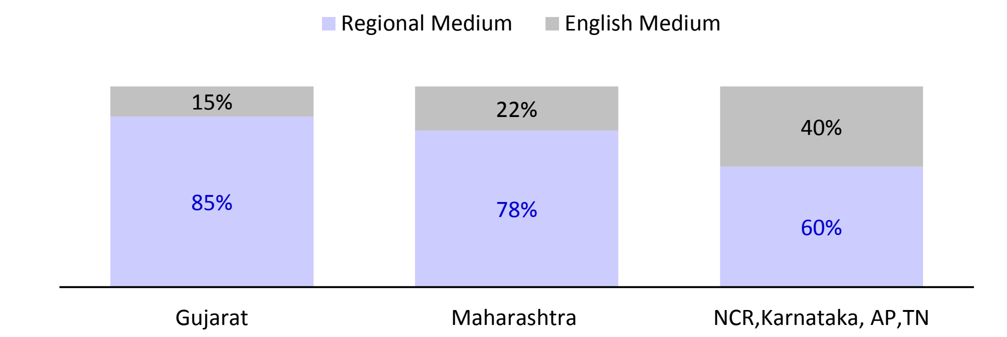
Regional languages, different evaluation patterns an entry barrier

Navneet has ~225 authors, aged 55-85 years, who have published ~5,000 titles

Most schools in India are regional medium schools, which require specialization to develop content and having a panel of authors is a key success factor. With over 50 years of experience in the publication industry, NELI has developed strong relationships with renowned authors. The biggest risk in the business is IPR infringement. If a new author ends up copying material from some other publisher, it leads to a huge liability for the company. Publishers are, therefore, cautious while selecting authors. Given that authors are language specialists, a publication company cannot simply replicate the success a particular author has had in one state in another. In this industry, no publisher in educational supplementary books is present in more than two states, catering to state board supplementary books.

Currently, NELI has ~225 authors, aged 55-85 years, who have published ~5,000 titles (2,700 school publication titles and 2,300 non-school publication titles). Authors are compensated in the form of royalty ranging from 2% to 8% of the revenue generated by their titles (other publishers make a lump sum royalty payment). Royalty for workbooks is usually lower, as these are recommended by teachers (‘pull’ demand). Guides and last minute revision sets are demanded by students based on content (‘push’ demand); royalty on these is higher. For FY16, NELI paid INR170m (3.5% of publication revenue) as royalty. On an average, royalty accounts for ~3.5% of sales.

Exhibit 13: Most schools in India are regional language medium schools



Source: Company, MOSL

Strong marketing team ensures reach even in remote areas

Navneet has a strong marketing team of 350 canvassers that visits schools regularly, promoting the books & ensuring brand visibility

Of the total number of schools in India, 1.45m ~99% follow the SSC format. Of these, ~1.1m schools are government schools. The remaining ~330k are private schools, of which ~80k are English medium schools. The curriculum of these schools is governed by the respective state education boards and the government chooses the textbooks and authors. NELI provides supplementary material for students from class I to class XII in Maharashtra and Gujarat. Of the ~330k private SSC schools in India, ~38k schools (15%) are in Maharashtra and Gujarat. Of these, NELI targets 75% schools – the remaining schools are in the interiors and servicing becomes difficult. NELI has a strong marketing team of 350 canvassers that visit the targeted schools regularly, promoting the books and ensuring brand visibility. The company has a strong fleet of executives, who reach out to schools even in relatively remote areas.

Government orders to aid overall growth

In FY14, the government decided that all its orders would be through tenders; Navneet did not receive any government order

Availability of quality teachers is a major problem in India, especially in rural areas. Government school students do not have resources to buy supplementary material. Departments like the Tribal Department, Social Welfare Department, and Women and Child Development Department buy supplementary books and distribute them free of cost to students. In FY14, the government decided that all its orders would be through tenders; NELI did not receive any government order. Later, the government issued a resolution that orders involving intellectual property rights (IPR) would not be through tenders and visibility of government orders returned. Considering government impetus on improved education and digital India, this segment remains a dark horse with significant upside potential. Digital classroom tender in Maharashtra alone has a potential of INR7.5b.

Common curriculum, EBI acquisition – huge opportunity in CBSE space

Scale-up likely with deeper penetration

- **Common curriculum in Mathematics and Science across India triggers a huge opportunity (INR30b market) for NELI to sell textbooks to CBSE schools across India. Unlike schools affiliated to State Boards, CBSE schools use other private publishers' textbooks apart from board-approved textbooks.**
- **NELI operates under the brand Grafalco, and besides its two core states, markets textbooks in five regions – NCR, Karnataka, Andhra Pradesh, Kerala and Tamil Nadu.**
- **NELI has recently acquired Encyclopedia Britannica India (EBI for ~INR880m), which provides curricular material for the CBSE/international boards – has a presence in 6,000+ schools. The acquisition will help NELI to significantly improve market visibility, enhance curriculum offerings, fill title gaps, and deepen penetration in CBSE and international boards.**
- **NELI is making healthy inroads in the CBSE segment, and has grown by 30% in 1HFY17. We expect it to garner meaningful market share in this growing segment (market size to expand 3x from INR30b to INR100b in five years, with many schools opting for conversion from the State Education Boards to CBSE/CBSE-pattern schools).**

Common curriculum in Mathematics and Science across India a big trigger

From FY14, the MHRD made it compulsory to have a common Science and Mathematics curriculum across India

The Ministry of Human Resource Development (MHRD) issued a circular mandating common curriculum for Mathematics and Science across India to offer a level playing field to all students for various competitive examinations for higher education. From FY14, the Ministry made it compulsory to have a common Science and Mathematics curriculum across India. Currently, NELI provides supplementary material like guides and workbooks to SSC school students. This ruling opens an opportunity for it to supply textbooks to CBSE schools across India. International publishers dominate the market for CBSE books. S Chand, the leader with ~17% share in the INR30b CBSE market, is the only Indian player. Oxford, Macmillan, and Pearson share about 10% each. We believe NELI's entry into the CBSE market will drive long-term growth.

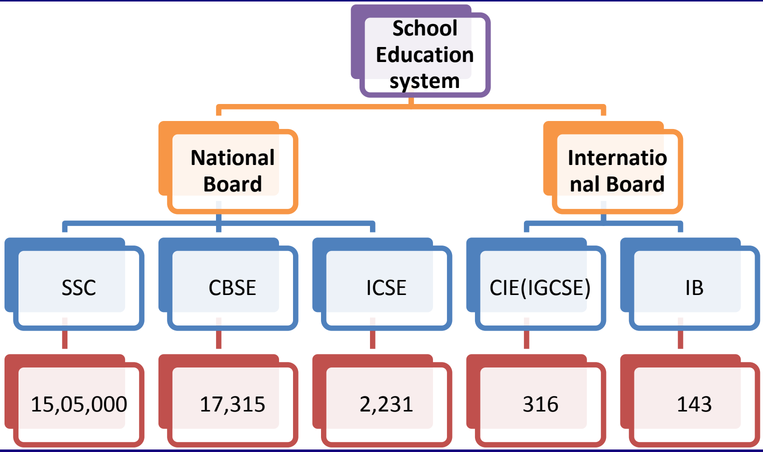
'CBSE affiliated' and 'CBSE pattern' schools provide huge opportunity

Navneet has entered the CBSE space; it provides textbooks in five regions – NCR, Karnataka, Andhra Pradesh, Kerala and Tamil Nadu

About 98% of the schools in India follow the SSC curriculum. However, there is now a trend of private SSC English medium schools (overall ~80,000 in India) converting themselves into CBSE-affiliated or CBSE-pattern schools, where they use private publishers' textbooks up to Grade VIII. To be CBSE-affiliated, schools need to satisfy stringent norms and requirements such as availability of playground, advanced computer laboratories, etc. SSC schools that are unable to meet these norms but still want to follow the CBSE curriculum are doing so by calling themselves CBSE-pattern schools. CBSE-pattern schools can follow a curriculum similar to CBSE up to class VIII, with class IX and class X still governed by the SSC board. There are ~80,000 English medium SSC schools in India, of which Maharashtra and Gujarat have ~11,000 schools.

Unlike SSC schools, CBSE schools also use other private publisher's textbook apart from board-approved textbooks. They have the liberty to choose their own textbooks, subject to their fulfilling certain guidelines. This gives NELI immense opportunity to provide textbooks to CBSE-affiliated and CBSE-pattern schools set by National Council of Educational Research and Training (NCERT). NELI has entered the CBSE space and started marketing textbooks in five regions – NCR, Karnataka, Andhra Pradesh, Kerala and Tamil Nadu apart from Maharashtra and Gujarat.

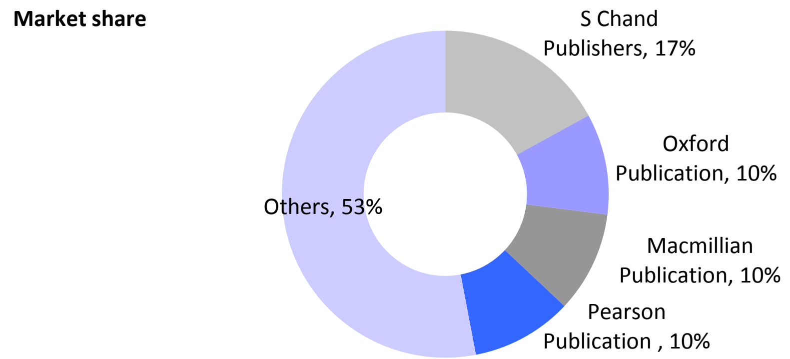
Exhibit 14: Distribution of schools by various boards



Source: Company, MOSL

NELI offers a range of textbooks marketed under brand name Grafalco up to Grade 8 and is looking to build the entire library for CBSE grade in FY17. It is also targeting South India's private schools instead of those in North India due to better literacy, leading to increased market opportunity. This is a new stream for NELI – providing direct textbooks to schools – and is a scalable business. **It has ventured into states like NCR, Andhra Pradesh, Karnataka, Kerala and Tamil Nadu, apart from Maharashtra and Gujarat, to tap CBSE schools in these regions over last two years and has made good inroads.** It has grown by a healthy 30% in 1HFY17 in the CBSE textbook market and we believe this growth will continue over the next few years.

Exhibit 15: Market share in CBSE curriculum publication



Source: Industry, MOSL

Britannica acquisition to enhance market footprint and penetration

NELI announced its acquisition of Britannica's India (EBI) curriculum business on October 26, 2016 (expected to complete in 40 days) for INR850m-INR900m in cash (17m shares amounting to 100% of EBI's share capital). Britannica India's curriculum division designs and develops educational products used by 5m students across schools in India and Indian schools abroad.

Post-acquisition, the Britannica business unit will become an independent company within NELI and realize considerable synergies. It will market its existing India-specific curriculum titles such as *Know for Sure* and *The English Channel*, and also develop new titles under Britannica's brand, editorial supervision and guidelines for seven years (post which the arrangement can be extended by paying fees). The acquisition will help NELI to enhance its footprint and access newer markets, significantly augmenting EBI's intellectual property.

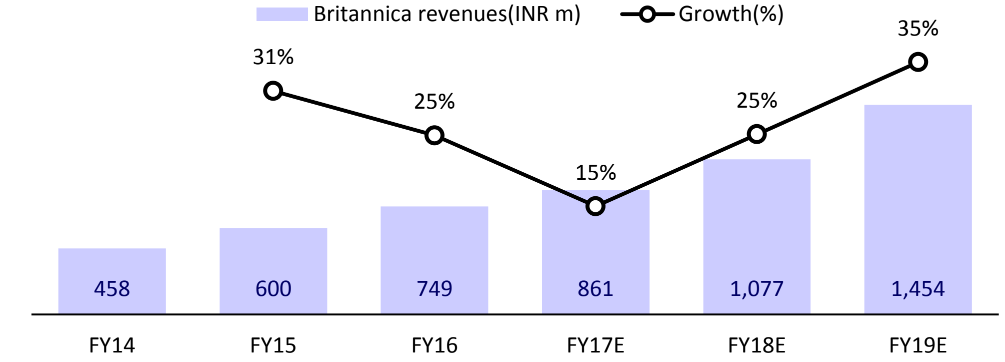
Encyclopedia Britannica India (EBI) is one of India's leading K-12 curricular book publishers. It began publishing operations in India in 2009. It has an extensive product catalogue comprising educational, instructional and information products & technology solutions, and is fast transforming into a major digital player designing products for 21st century classroom and home learning environments. EBI's revenue has grown from INR458m in FY14 to INR600m in FY15 to INR749m in FY16. Revenues for EBI are highly concentrated in December to March season with 80% of revenues from it.

EBI and NELI – significant synergies

EBI & NELI are expected to have synergies in terms of product offerings, school footprint, deepening penetration & filling gaps in title libraries.

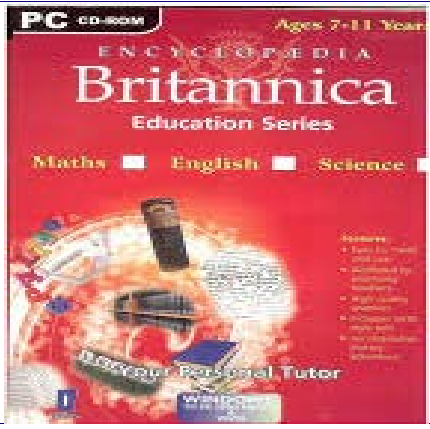
- **Product offerings:** While NELI's product offerings are mainly targeted at students following the Gujarat/Maharashtra SEB syllabi, EBI's product offerings are targeted at students following the CBSE syllabus.
- **School footprint:** EBI has footprints in 6,000+ schools in India, mainly CBSE, ICSE, and international schools, where NELI has limited presence. EBI has negligible presence in the schools NELI has a stronghold in.
- **Scale benefits:** As a larger entity post-acquisition, NELI's bargaining power with both suppliers and the marketing chain improves. Also, the advantage of a common distribution channel helps NELI to gain operating leverage and enhance its brand visibility.
- **Region-wise penetration:** Maharashtra and Gujarat, the two core states for NELI, constitute only ~3% of EBI's revenue. Similarly, NELI has limited presence in EBI's key markets – Punjab, Rajasthan, Haryana, Andhra Pradesh, Uttar Pradesh and Delhi/NCR. Also, EBI has a well-distributed revenue mix across India, which supports NELI's quest to transition from a regional entity to a pan-India entity. The acquisition grants NELI EBI's rights across CBSE schools worldwide (besides India, CBSE schools exist mainly in the Gulf countries), further enhancing brand visibility.
- **Title library:** EBI's acquisition helps NELI to fill gaps in its title library, which otherwise would have taken a considerably long period.
- **Limited follow-on investments:** Apart from the acquisition amount, NELI only needs to invest in incremental working investments. No material follow-on investments are required.

Exhibit 16: Britannica India revenues to grow at 30% CAGR over FY17-19E



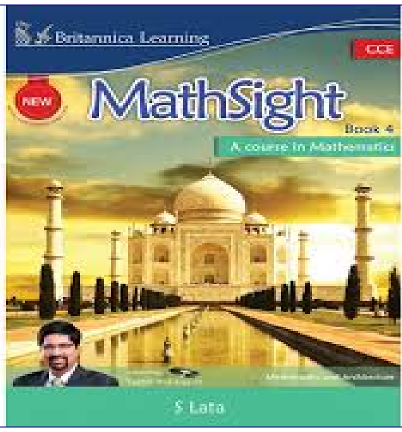
Note: EBI nos would be consolidated with NELI likely from FY18 onwards Source: Company, MOSL

Exhibit 17: Britannica curriculum learning products…



Source: Company, MOSL

Exhibit 18: ..and digital products



Source: Company, MOSL

Exhibit 19: Income Statement for Encyclopedia Britannica India

Income Statement (INR m)	FY14	FY15
Revenue	523	679
COGS	134	153
Employee expense	91	130
Other expense	270	354
Total Expense	494	637
EBITDA	**28**	**41**
EBITDA Margin (%)	5.40%	6.10%
Depreciation	4	4
Interest	0	7
Other Income	5	1
PBT	30	32
Tax	18	9
PAT	**12**	**23**
PAT Margin (%)	2.30%	3.40%

Source: ROC, MOSL

Exhibit 20: Balance Sheet for Encyclopedia Britannica India

Balance Sheet(INR m)	FY14	FY15
Share Capital	35	54
Reserve & Surplus	-6	17
Net Worth	**29**	**70**
Long term provisions	3	6
Short term borrowings	0	100
Short term provisions	79	113
Trade Payables	399	421
Other current Liabilities	14	30
Total Liabilities	**523**	**740**
Tangible Assets	4	4
intangible Assets	1	3
Total Fixed Assets	5	7
Deferred Tax Assets	2	30
Long term loans and advances	5	6
Other non-current assets	0	0
Inventories	68	123
Trade recievables	410	536
Cash& Equivalents	26	25
Short term loans	2	7
Other current Assets	5	7
Total Assets	**523**	**740**

Source: ROC, MOSL

High-margin exports to drive stationery business growth

Export of value-added product to give next leap

- **Indian paper stationery market is largely unorganized with 80-85% of the market dominance. Organized stationery market is highly competitive and largely driven by ITC and Navneet. Non-paper stationary market consists of ~60% dominance of organized players.**
- **NELI's stationery business (43% of total revenue) will be largely driven by growth in exports (44% of stationery revenue). Given the high competitive intensity in the domestic segment, NELI is focusing more on exports.**
- **The company has moved from exporting low-margin commoditized products to value-added products like embossed stationery, 3D cover page design, and patented stationery. It has 100% in-house production for export products and margins in the export segment are 300-400bp higher than in the domestic segment.**
- **The US is its export hub (NELI being a preferred supplier to Walmart), accounting for 73% of its exports, while the balance 27% comes from other countries.**
- **We expect 13.3% CAGR in the stationery business, led by the export segment.**

Synergic to Navneet's product offerings

NELI was the first organized brand to enter the stationery business in India in 1995, offering (1) standardized products with number of pages and MRP (maximum retail prices) printed on them, (2) full-size note books, and (3) shrink-wrapped packets in carton packing. Its stationery business gives NELI higher bargaining power in buying paper, and helps it to build a national brand and target highly-profitable exports.

Exhibit 21: Stationery segment snapshot (INR m)

	Paper Stationery	Non-paper Stationery
Market Size in India	INR100b	INR50b
Organized players market share	15%	60%
Navneet's market share in organized segment	15%	1.50%
Production	~70% in house(all exports products in-house)	Outsourced
Market	Domestic as well as export	Sold pan India
Products	Notebooks, Drawing books, Writing pads, Index cards etc	Pencils, Erasers, Crayons, Geometric sets, Rulers, Dough, Colour Pastels etc
Revenue share(FY16)	94% of segment(55% Domestic, 45% Exports)	6% of segment

Source: Company, MOSL

NELI has two centralized offices in Mumbai and Ahmedabad, and two manufacturing locations at Silvassa (Union Territory) and Khaniwade (Maharashtra), with a capacity to produce 150tpd (blended capacity utilization of ~70%). It also outsources manufacturing from Vapi, Vasai, Kanpur and Bangalore for its domestically-sold stationery, but manufactures all export items in-house. Its 14 branch offices, 1,200+ distributors, 16 C&F agents, three mother depots and 450+ sales personnel ensure NELI's presence across all major markets in India. Its stationery products reach over 85,000 retail outlets in more than 600 towns across 23 states and three union territories in India.

Value-added products to drive high-margin exports

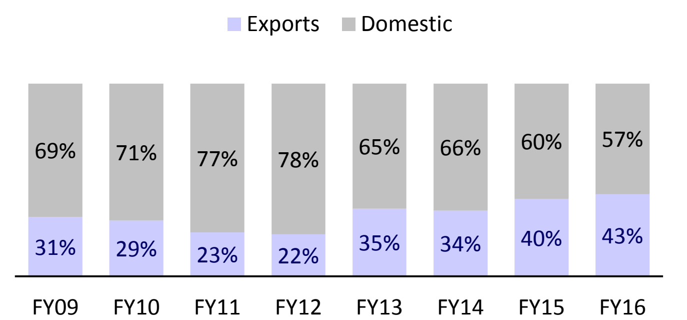
The US, which accounts for 73% of its exports, is the export hub for Navneet

NELI's stationery business posted a revenue of INR4,077m (43% of total revenue) in FY16, of which exports constituted 43%. It has been in the international stationery business for 18 years and has grown at a healthy pace. The US alone accounted for 73% of its exports in FY16. NELI is a "preferred supplier" to Walmart (white label brand), which is a testimony to its brand quality. It is moving from a commodity business, where competition is huge and margins are lower, to various value-added products like embossed stationery, 3D cover page design and patented stationery, which will command premium and drive up margins. Apart from supplying white label goods, it has also launched its own brand, *American Scholar*.

NELI's international products are marketed under the brand names, *Navneet*, *Grafalco* and *American Scholar*, and are exported to various territories across the globe, specifically the US, Europe, Africa, and Central and Latin America. It has three dedicated factories in and around Mumbai to cater to the stationery division. The presence of in-house printing and finishing equipment, supported by in-house product development and design team helps create tailor-made products for the fashion range, with premium effects like glitter, metallic, flocking and embossing.

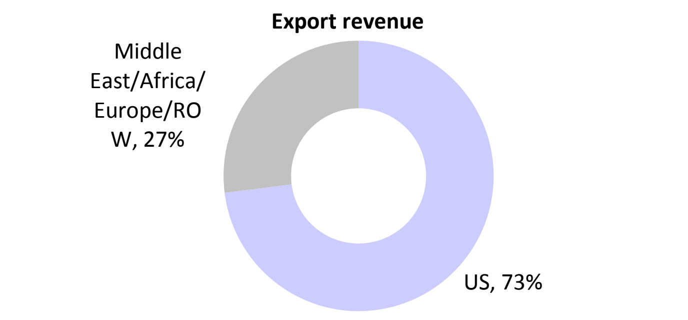
We believe that growth in the stationery business will be driven largely by exports, going forward, with NELI expanding its footprint in the Middle East, Africa, and Europe. The company will be able to achieve 20% CAGR growth over FY17-19E in the high-margin (300-400bp higher margin than domestic segment) export segment, largely driven by value-added products and its own brand.

Exhibit 22: Exhibit 25: Stationery revenue break-up



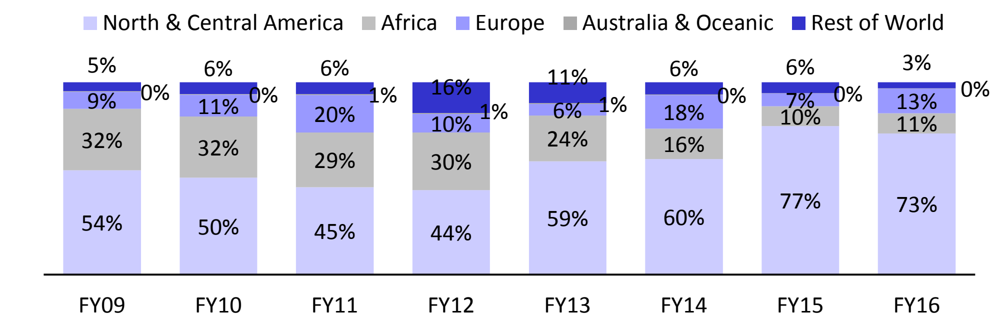
Source: Company, MOSL

Exhibit 23: US is the major market for exports



Source: Company, MOSL

Exhibit 24: Region-wise export distribution



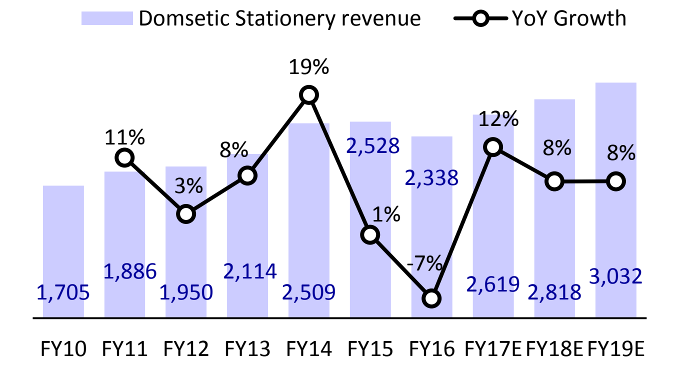
Source: Company, MOSL

High competitive intensity in domestic market

The Indian stationery market is largely unorganized; organized players account for just 15-20% of the market

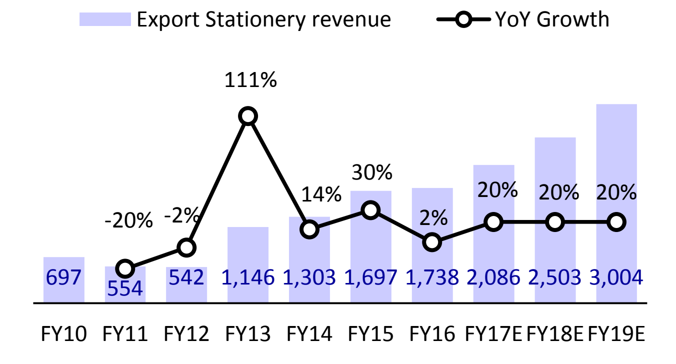
The Indian stationery market is largely unorganized; organized players account for just 15-20% of the market. The organized stationery market is highly competitive and dominated by two large players – ITC and NELI (ITC has ~20% market share, while NELI has ~7%). Over the last few years, ITC (paperboard, paper and packaging revenue of INR9b in FY16) is increasingly focusing on the stationery segment due to reduction of import duties under free trade agreements, especially with ASEAN (effective January 2014) – increased competition from imports has impacted the profitability of the domestic paper and paper board industry. Recently, ITC has been gaining market share due to the following: (1) higher advertisement spend, (2) higher dealer margins, encouraging dealers to push ITC products, and (3) higher credit period to dealers. The domestic market accounts for 51% of NELI's overall stationery revenue. Given the mounting pressure from ITC, we expect NELI to achieve modest 8% growth over FY17-19E.

Exhibit 25: Domestic stationery revenue CAGR at 8% for FY17-19E vs 5% for FY11-FY16



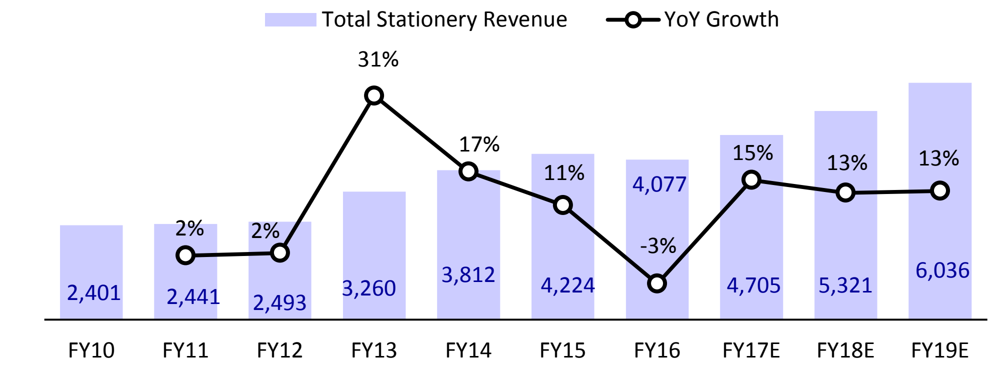
Source: Company, MOSL

Exhibit 26: Export stationery revenue CAGR at 20% for FY17-19E



Source: Company, MOSL

Exhibit 27: Total stationery revenue CAGR at 13.3% over FY17-19E



Source: Company, MOSL

eSense to capture "next gen" digital opportunity

Increasing thrust on digitization to bolster eSense growth

- **NELI has developed a brand "eSense" which has 4 products to offer to next generation student viz Top Class, Top Assessment, UTOP and Top Scorer across B2B & B2C segments; has installed its products in ~3,500 schools and over 20,000 classrooms.**
- **To increase adoption rate among customers, Navneet has increased its ad-spends to INR80-100m for FY17 (~INR60m in FY16).**
- **This segment hasn't seen a rapid growth since its launch in FY09. However, we believe with increasing thrust on digitization and growing penetration (so far, it has tapped only ~3,500 of 39,000 private schools in Maharashtra and Gujarat), eSense will achieve 13.7% CAGR over FY16-19.**
- **Navneet has entered direct education in collaboration with K12 Techno Services and manages 12 Orchid's International School" (CBSE Board). Current, occupancy rate in Orchid international across all schools stands at ~50-55%(despite increase in students from 6,500 to 9,500+ in a year), margins can go to ~30% at full occupancy levels.**

eSense – product to cater to next generation

NELI is evolving from a pure play publisher to a content developer. eSense is a content-based product, developed to meet the needs of the next generation student, who will be technology savvy and will have access to multiple sources of information. NELI launched eSense, which equips children with syllabus-based multimedia animations, in 2009. Students get practical visuals relating to the content they learned from traditional textbooks, which makes learning fun.

Navneet has installed eSense in ~3,500 schools and over 20,000 classrooms

Top-Class (~80% of revenues for eSense): NELI has installed the product in ~3,500 schools and over 20,000 classrooms in Maharashtra and Gujarat. It charges INR15-20/student/month for the content it provides. It had revenue of INR198m and loss of INR47.1m at PBT level in FY16. We believe e-learning is a huge opportunity and NELI will be able to scale up quickly as eSense becomes more popular. We expect eSense to grow at ~20% over the next two years; this would drive profitability.

Exhibit 28: E-learning product details

Product	Description
TOPClass	eSense TOPClass is a complete digital education solution. It consists of interesting and attractive animated content for every chapter. This, making teaching and learning easier and faster
TOPAssessment	eSense TOPAssessment is a assessment solution provider. It provides artificial intelligence based assessment engine
UTOP	UTOP is smart digital educational tool for children and communicational tablet for parents. With smart audiovisual learning it engages children and separate password for parents delivers full value for parents.
TOPScorer	Top Scorer is first of its kind educational tool designed only for CBSE students. Top Scorer smartly transforms the widest NCERT syllabus, into more involving audiovisual content. It helps student learn better, understand faster and remember more.

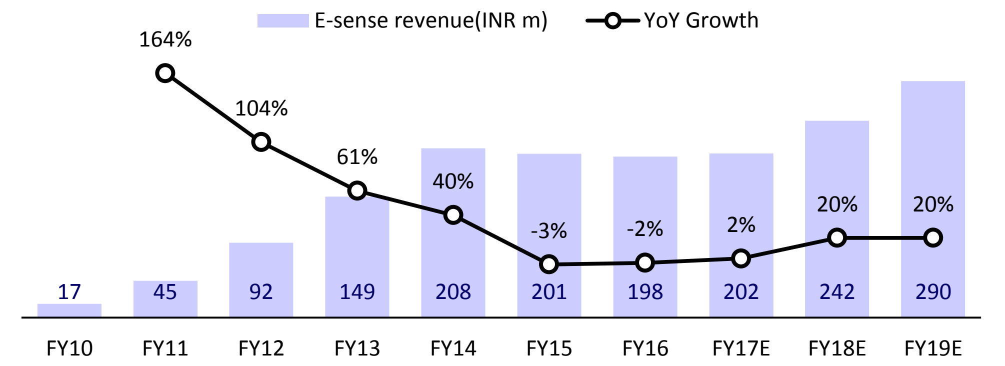
Source: Company, MOSL

Exhibit 29: Growth drivers for e-learning segment

Product	Description
Huge Untapped B2B market	Out of 39,000 private schools, only 3,500 have been tapped till 1HFY17, creating a huge potential market only in the two states of Maharashtra and Gujarat
B2C Market	B2C market has started flourishing in India. Navneet is ready with B2C retail offerings like Online portal, CDs, Tablets and Pen Drives for State Boards curriculum of Maharashtra and Gujarat. Also has Pen drives for CBSE curriculum for grades I-X
Acceptability	Acceptability by teacher and students due to ease of use

Source: Company, MOSL

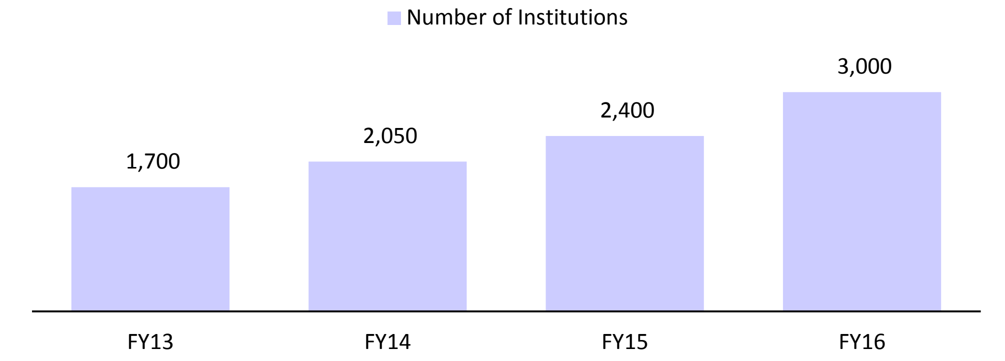
Exhibit 30: eSense revenue to grow 20% over FY17-19E



Source: Company, MOSL

Being a digital representation of a textbook, Top-Class is syllabus-focused, and is preferred and recommended by teachers in Maharashtra and Gujarat. It has already developed over 65,000 minutes of content library for the education boards of these two states and the CBSE curriculum. Its strong brand name, especially in West India, creates a strong platform to launch products and penetrate new markets.

Exhibit 31: Navneet's reach via e-learning content



Source: Company, MOSL

Exhibit 32: Prominent online vendors

Name	Promoted by	Based out of	Target segment	Year
TopperLearning	Educomp and Network 18	Mumbai	K-12,ICSE/CBSE, State Boards	NA
Meritnation	Pavan Chauhan	Delhi	K-12,ICSE/CBSE, State Boards	2009
Extramarks	Atul Kulshrestha	Noida	K-12,ICSE/CBSE	2007
Learn Next	IIT Alumni	Hyderabad	K-12,ICSE/CBSE, State Boards	2013
Byju's	Byju Raveendran funded by Sequoia Capital	Banglore	K-12,Test preparation	2008
Edurite	Pearson Group	Banglore	CBSE/ICSE/General worksheets	NA
Toppr	Zishaan Hayath and Hemanth Goteti	Mumbai	IIT JEE, Pre medical and Foundation	2013
Esense	Navneet	Mumbai	K-12,ICSE/CBSE, State boards	2009
Khan Academy	Salman Khan, MIT and Harvard Graduate	US	Free content/Non-Profit organization	2005
100 percentile	NA	Gurgaon	Engineering, Medical, MBA entrance	2012

Source: Company, MOSL

Top Scorer platform to pick up with increasing digitization

NELI has created Top Scorer, an online knowledge platform that provides smart learning packs for Grade 1-10 students across CBSE, Gujarat and Maharashtra state boards. It is looking to target the retail segment through pen-drives and CDs across its distribution network in Maharashtra and Gujarat in the next one year. The product is sold at INR3,000-4,000 at retail level (offline) while online subscription is priced lower. Currently, there is not much traction in this segment, but we believe that with increasing thrust on digitization, and given the current under-penetration in the market, this segment has huge growth potential. The company is investing in advertisements and content creation in FY17 to grow its B2C revenue. We understand NELI is looking to increase its investments in marketing and distribution for its digital segment to INR80m-100m in FY17 from an average of INR60m-80m per year for the past five years.

Exhibit 33: Top Scorer products…

Source: Company, MOSL

Exhibit 34: ...in a variety of forms

Source: Company, MOSL

Small investment in direct education business can pay off

Navneet has entered into direct education in collaboration with K12 Techno Services

NELI has entered direct education in collaboration with K12 Techno Services. It had invested INR480m for its 25% stake in the venture. At the end of 1QFY17, Sequoia Capital held 58%, Navneet learning LLP held 32%, while the management (ESOP) held 10% in Techno Services Private Limited. The company now manages 12 Orchid International Schools (CBSE Board). Of these 12 schools, five are in Bangalore, four in Mumbai, and one each in Navi Mumbai, Pune and Hyderabad. All these businesses are asset light and operate under a 30-year lease agreement.

As the Indian education sector evolves and there is greater need for schools with better facilities, this investment should pay off handsomely for NELI. In FY16, Orchid International School had 6,500 students across 12 schools; this year, the number has increased to more than 9,500 students (despite that, occupancy is 50-55%). CBSE generally gets higher fees, as its offerings are more. In this business, margins depend on occupancy rate – operating leverage kicks in as occupancy rises. NELI is open to holding its investment or exiting, depending on economics. Until FY16, it also had 52 SSC schools in Andhra Pradesh, under the brand Gowtham Model School, which it sold back to the promoter.

Exhibit 35: Orchid International School

Source: Company, MOSL

SWOT Analysis

- ☑ Strong market share of ~65% in Maharashtra and ~70% in Gujarat in publication segment
- ☑ Over 50+ year strong legacy brand in India in SSC board syllabus for K12 segment
- ☑ Strong sales team of 450+ with 1,200 distributors,16C&F & 3 Mother depots

- ☑ Relatively less aggressive in marketing its e-learning products compared to few others
- ☑ Late entrant in highly scalable CBSE market in India

- ☑ Huge untapped opportunity with only 3,500 of 39,000 private schools tapped in ELearning segment in Maharashtra & Gujarat
- ☑ Britannica India curriculum acquisition will aid in penetration in CBSE schools across different states
- ☑ Increasing exports of value add products in stationery segment

- ☑ Competitive intensity in publication segment with market leader Classmate(ITC) having aggressive pricing
- ☑ Increase in paper prices can impact operating margins
- ☑ Any defamation suits related to IPR may have an adverse impact on company financials

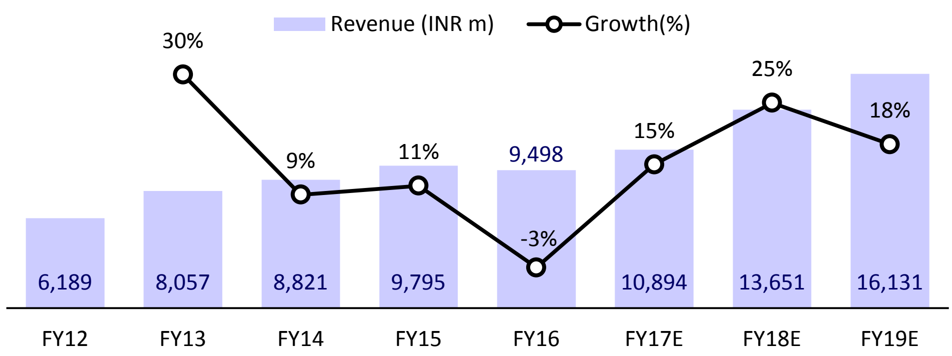
Financial Overview

- **We expect 21.7% revenue CAGR over FY17-19E driven by syllabus change, CBSE school penetration (aided by Britannica India curriculum acquisition), digital content business and growth in exports of stationery.**
- **We expect EBITDA to post 24.8% CAGR and PAT to post 25.9% CAGR over FY17-19E with a margin expansion of 120bp over FY17-19E to 24.5%.**
- **We expect return ratios to improve over the period; RoCE is expected to improve from 21.1% in FY17 to 25.8% in FY19E primarily due to operational efficiencies & expect Net D/E to decline from 0.3x to 0.2x despite acquisition cost of ~INR880m for EBI & buyback of ~INR580m in FY17E.**
- **We expect steady improvement in operating cash flow.**

Expect 21.7% revenue CAGR over FY17-19E

Syllabus change across SSC schools in a phased manner every six years (significant changes in Std X curriculum in two core states in FY18 & 19), would drive growth in publication revenue by 18.1% CAGR over FY17-19E while Encyclopedia Britannica acquisition is expected to grow at 30% CAGR over FY17-19E aided scale-up in five new states (apart from its two core states). Led by growth in stationery exports, we expect stationery segment to grow at 13.3% CAGR over FY17-19E; with increasing thrust on digitization also expect a spurt in eSense with revenue CAGR of 20% over FY17-19E. Overall revenue is likely to grow at a CAGR of 21.7% over FY17-19.

Exhibit 36: Revenue expected to grow at 21.7% CAGR over FY17-19E

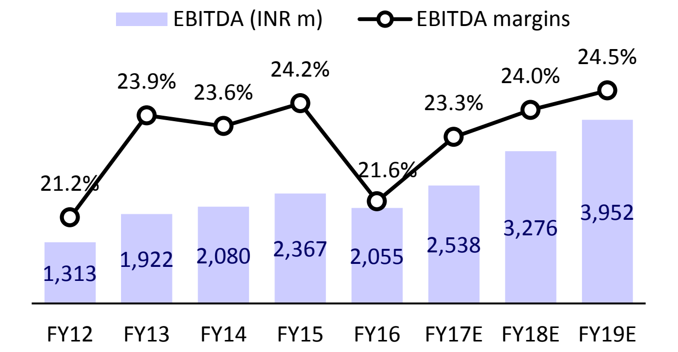


Source: Company, MOSL

EBITDA margin to expand 120bp; expect 25.9% PAT CAGR over FY17-19E

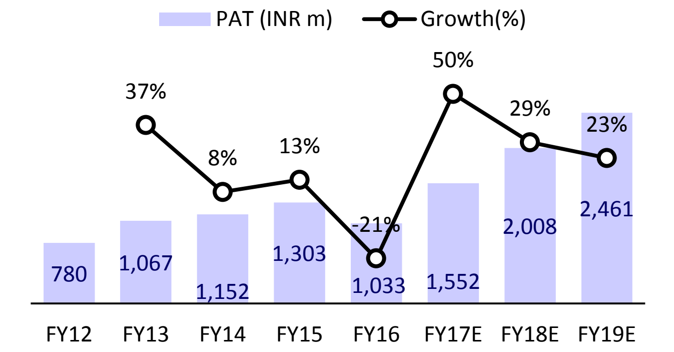
Encyclopedia Britannica India made margins of 5.4%/6.1% in FY14/FY15 respectively, lower in comparison to Navneet's current consolidated which stood at 21.6% in FY16. Post consolidation, we expect NELI's EBITDA margin to expand by 120bp from 23.3% in FY17 to 24.5% in FY19, driven by operational efficiencies and improvement in EBI margins with synergies driving both business. PAT is likely to grow at a CAGR of 25.9% over FY17-19E.

Exhibit 37: EBITDA margin to expand 120bp over FY17-19E



Source: Company, MOSL

Exhibit 38: PAT to grow at 25.9% CAGR over FY17-19E

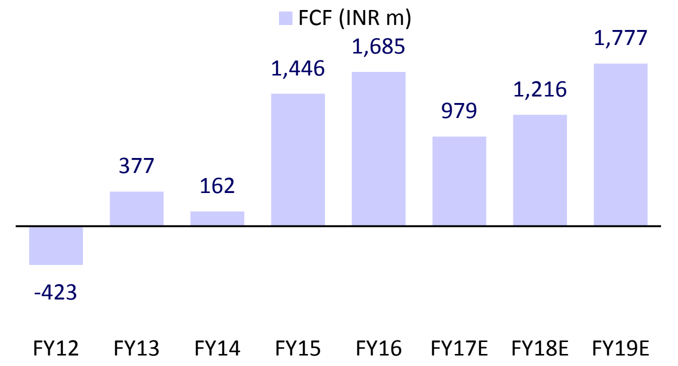


Source: Company, MOSL

Cash flows to improve significantly

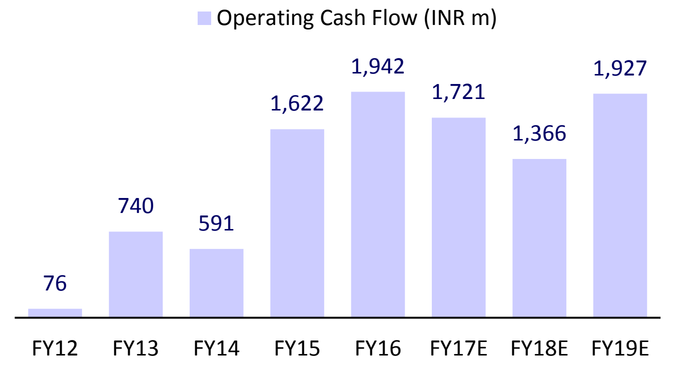
We expect Navneet's free cash flows (FCF) to improve significantly over the years. Navneet is acquiring Encyclopedia Britannica India business for ~INR880m (transaction completed in Dec 2016) & has also gone for a buyback of ~INR580m (2% share capital). The company does not expect to incur significant capex; over FY16-19, its INR200m capex (except for acquisition cost of INR 880m to acquire EBI in FY17E) would be largely in the nature of maintenance capex. Operating cash flows would remain robust over FY17-19E.

Exhibit 39: FCF to remain robust



Source: Company, MOSL

Exhibit 40: Steady improvement in operating cash flow

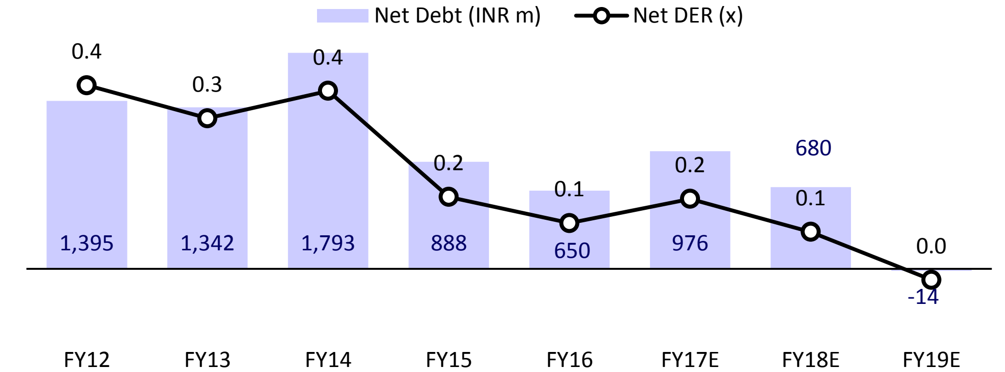


Source: Company, MOSL

Net debt-equity to decline & Return ratios to improve

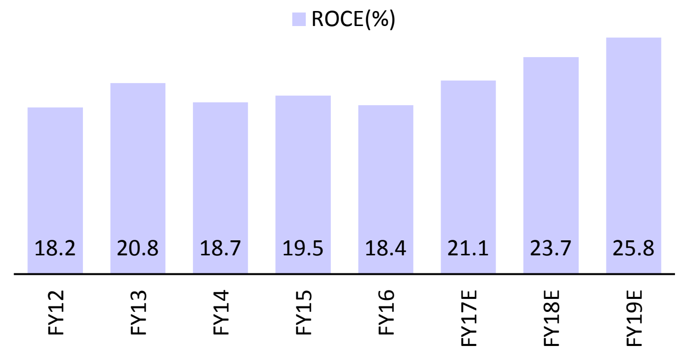
During the year end Navneet has high working capital requirement as ~50% of its annual sales happen in 1Q. However, by the end of the 2nd quarter, company recovers its working capital and becomes cash positive. We believe that with growing business year end debt requirement will continue to remain high which will be liquidated by the end of 2nd quarter. Despite acquisition cost of ~INR880m for Encyclopedia Britannica India curriculum acquisition and buyback of share to tune of ~INR580m (~46.57lakh share of face value INR2 each at INR125) in FY17, we believe net debt free in FY19 after increase in FY17 .Working capital days are expected to improve from 179 days to 147days post acquisition of EBI over FY16-19E.

Exhibit 41: Turning debt free in FY19



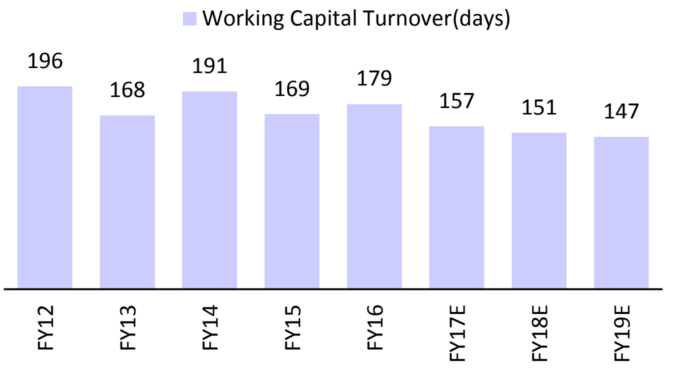
Source: Company, MOSL

Exhibit 42: ROCE ratio to improve



Source: Company, MOSL

Exhibit 43: Improvement in working capital cycle



Source: Company, MOSL

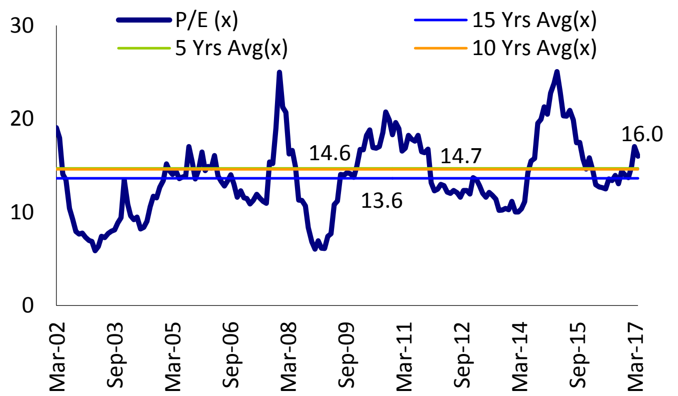
Valuation and view

Initiate with a Buy

Compelling story of India's education sector demand

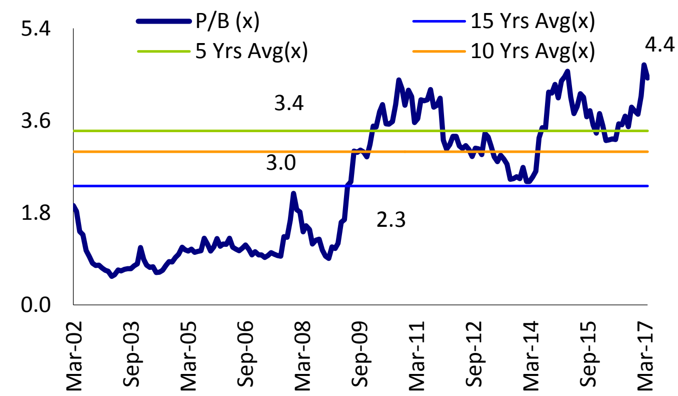
- NELI is a dominant player in publishing business in Maharashtra (~65% market share) and Gujarat (~70% market share). It has over five decades of experience in developing content with an asset base of over ~225 authors who create content and update the same timely. With long standing relationship with state boards & schools and a strong distribution channel, we believe it is well posed to capture the growth opportunity.
- The current gradual transition of SSC syllabus schools towards CBSE pattern has opened up CBSE text books market for Navneet (potential market of INR30b).
- With the addition of Britannica, Navneet would provide higher offerings in the Indian curriculum segment and would be able to tap newer markets in India, especially CBSE and international board schools. We believe the acquisition would be synergic to its core operations & lead to improvement in margins for EBI going ahead (6.1% in FY15 as per ROC filings).
- We view Navneet as a value stock with steady growth & dividend payout (61% in FY16) over the years. We believe Navneet is well posed to achieve 21.7% CAGR in revenues & PAT CAGR of 25.9% with a 120bp expansion in margins led by major changes in SSC curriculum in its two core states over FY17-19E, increasing penetration in CBSE schools & other international boards due to Britannica India (EBI) acquisition, spurt in exports (mainly led by Walmart) and improvement in e-sense revenues with increasing adoption of digitization.
- Despite EBI acquisition to tune of INR880m (completed in Dec 2016) and buyback of shares of INR580m in FY17, we expect RoCE to improve from 21.1% to 25.8%, working capital cycle to improve from 157 days to 157days and company to turn net debt free from net debt equity levels of 0.2x in 19E.
- Strong management bandwidth with proven track record, high visibility on operating cash-flows, superior return ratios and strong balance sheet, makes Navneet a preferred 'BUY' in the Education space. Initiate with a **'Buy'** and TP of INR210 (20x FY19E), upside of 40%.

Exhibit 44: P/E trend



Source: Company, MOSL

Exhibit 45: P/B trend



Source: Company, MOSL

Exhibit 46: Assumption sheet

Navneet Education Ltd	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17E	FY18E	FY19E
Revenues(INR m)	**5,239**	**5,530**	**6,189**	**8,057**	**8,821**	**9,795**	**9,509**	**10,894**	**13,651**	**16,131**
Educational Books	2,517	2,734	3,266	4,190	4,425	4,932	4,830	5,555	6,555	7,865
Children's and General Books	157	164	191	246	205	267	226	235	240	244
Children's and General Books Export	93	96	83	136	121	120	103	108	110	112
Exports (including incentives)	697	554	542	1,146	1,303	1,697	1,738	2,086	2,503	3,004
Paper Stationery (Domestic)	1,449	1,609	1,650	1,813	2,207	2,213	2,099	2,351	2,539	2,742
Non Paper Stationery (Domestic)	255	278	301	301	303	315	239	268	279	290
E-Sense	17	45	92	149	208	201	198	202	242	290
Britannica	-	-	-	-	458	600	749	861	1,077	1,454
Others	55	51	64	77	50	51	75	90	108	130
Growth (%)		**6%**	**12%**	**30%**	**9%**	**11%**	**-3%**	**15%**	**25%**	**18%**
Educational Books		9%	19%	28%	6%	11%	-2%	15%	18%	20%
Children's and General Books		4%	17%	28%	-17%	31%	-15%	4%	2%	2%
Children's and General Books Export		3%	-13%	64%	-11%	-1%	-14%	4%	2%	2%
Exports (including incentives)		-20%	-2%	111%	14%	30%	2%	20%	20%	20%
Paper Stationery (Domestic)		11%	3%	10%	22%	0%	-5%	12%	8%	8%
Non Paper Stationery (Domestic)		9%	8%	0%	0%	4%	-24%	12%	4%	4%
E-Sense		164%	104%	61%	40%	-3%	-2%	2%	20%	20%
Britannica		-	-	-	-	-	-	-	25%	35%
Revenue Mix (%)										
Publishing Division	53%	54%	57%	57%	54%	54%	54%	54%	51%	51%
Stationery Division	46%	44%	40%	40%	43%	43%	43%	43%	39%	37%
E-sense and Others	1%	2%	3%	3%	3%	3%	3%	3%	3%	3%
Britannica Cirriculum	0%	0%	0%	0%	-	-	-	0%	8%	9%

Source: Company, MOSL

Exhibit 47: Peer valuation

Company Name	PE			EV/EBITDA			RoE %			EV/Sales			Sales CAGR	PAT CAGR
	FY17E	FY18E	FY19E	FY17E	FY18E	FY19E	FY17E	FY18E	FY19E	FY17E	FY18E	FY19E	FY17-19E	FY17-19E
Navneet Education*	23	18	14	14	11	9	26	30	31	3	3	2	22	26
MPS	17	15	14	10	9	8	23	23	22	4	3	3	14	13

*MOSL Estimates Source: Company, MOSL

Bull & Bear case

Bull case

- In our bull case we assume higher than expected revenue growth in publishing segment (over base case) due to Std X syllabus change over FY17-19E, higher exports with traction from Walmart, larger revenue growth in e-Sense with increasing level of digitization & higher growth in EBI due to synergies with Navneet. Additionally, we assume prices of critical raw material like paper & ink decrease for FY18E and FY19E.
- Instead of assuming a 120bp EBITDA margin increase over FY17-19E in the base case due to operational efficiencies, we are assuming 170bps YoY improvement over FY17-19E with improvement in Britannica margins due to synergies with Navneet & also in Navneet's core business.
- In the bull case we are assuming that company will not pass on benefit on lower raw material prices and thus enjoy higher margins.
- There is an increase 7% in FY18E EPS and 10% in FY19E EPS over the base case EPS to INR9.2 and INR11.6 respectively.
- Assuming higher PE of 24x (vs 20x in base case) target multiple, we get a bull case target price of INR278 (upside of 84% to CMP) based on FY19 EPS instead of the base case target price of INR210, upside of 40%.

Exhibit 48: Bull case scenario

	FY16	FY17E	FY18E	FY19E
Sales (INR m)	9,498	11,148	14,382	17,239
Sales growth (%)	-3.0	17.4	29.0	19.9
EBITDA (INR m)	2,055	2,597	3,495	4,310
EBITDA Margin (%)	21.6	23.3	24.3	25.0
EBITDA growth (%)	-13.2	26.4	34.5	23.3
PAT (INR m)	1,033	1,594	2,157	2,701
PAT Margin (%)	10.9	14.3	15.0	15.7
PAT growth (%)	-20.7	54.3	35.3	25.2
EPS (INR)	4.3	6.8	9.2	11.6
Target multiple (x)				24
Target price (INR)				278
Upside/downside (%)				84

Source: Company, MOSL

Bear case

- Our bear case assumptions mainly have a negative impact on both sales growth and operating margins for FY17E, FY18E and FY19E compared to our base case.
- We are assuming a 310bp EBITDA margin decline over FY17-19E in the bear case compared to 120bp expansion in base case and sales growth of 10.8%/16.1%/8% in FY17E/FY18E/FY19E over our base case.
- In our bear case, we assume that exports will see higher competition, lower growth in publishing segment due to slower economic growth, flattish e-Sense revenue & single digit EBI growth with synergic benefit not occurring. Additionally, we assume the company is unable to pass on the increase in raw material prices and the benefits of operating leverage will also get delayed.
- This will lead to decrease of 26% in FY18E EPS and 37% decrease in FY19E EPS over the base case to INR6.3 and INR6.6 respectively.
- Assuming the target multiple as 16x vs 20x that we have taken for the base case, we get a bear case target price of INR106 (downside of 30% to CMP) based on FY19 EPS instead of the base case target price of INR210, upside of 40%.

Exhibit 49: Bear case scenario

	FY16	FY17E	FY18E	FY19E
Sales (INR m)	9,498	10,528	12,225	13,188
Sales growth (%)	-3.0	10.8	16.1	7.9
EBITDA (INR m)	2,055	2,348	2,457	2,532
EBITDA Margin (%)	21.6	22.3	20.1	19.2
EBITDA growth (%)	-13.2	14.2	4.7	3.0
PAT (INR m)	1,033	1,432	1,481	1,542
PAT Margin (%)	10.9	13.6	12.1	11.7
PAT growth (%)	-20.7	38.6	3.4	4.1
EPS (INR)	4.3	6.1	6.3	6.6
Target multiple (x)				16
Target price (INR)				106
Upside/downside (%)				-30

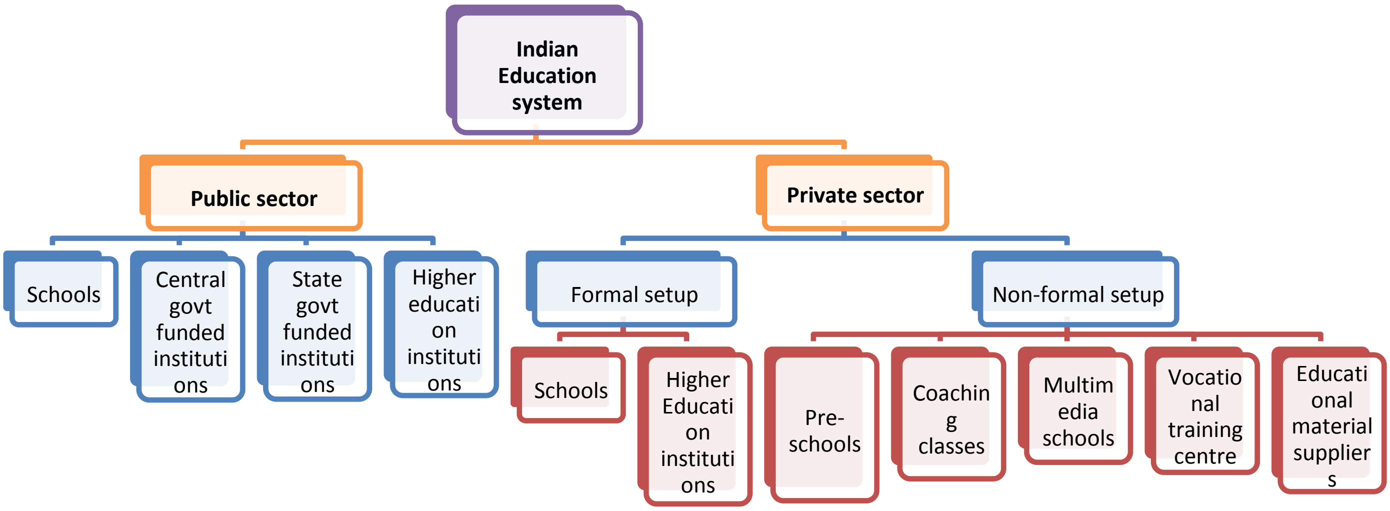
Source: Company, MOSL

Industry overview

Industry structure in India

The Indian education system in the private sector can be divided into the formal and informal segments. The formal education segment broadly comprises of schools and higher education institutions. Schools, often classified as K-12 (Kindergarten to 12th grade) cater to the 3-17 years age group. Higher education, which includes graduate, diploma, professional and post-graduation courses, caters to the 18 years and above age group. The informal education segment includes pre-schools, multimedia, vocational training, books and coaching classes. This segment is free from price regulation as opposed to the highly regulated formal education segment.

Exhibit 50: Education landscape in India

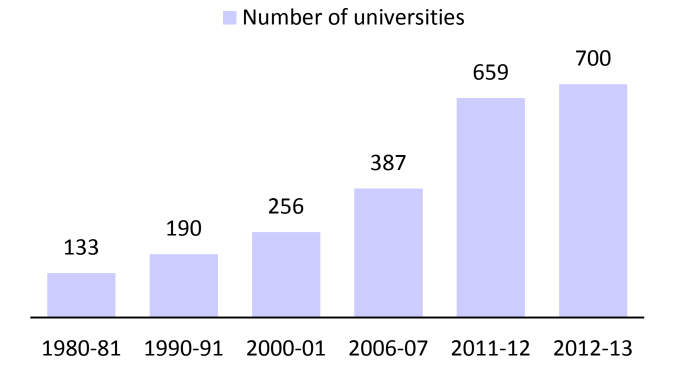


Source: DISE, MOSL

India is one of the largest education systems in the world

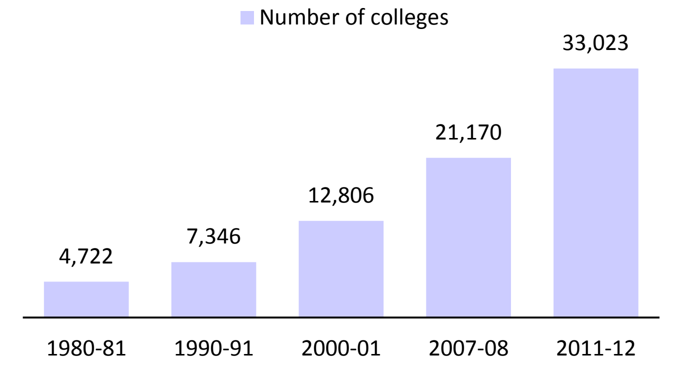
India has one of the largest higher education systems in the world, with 25.9m students enrolled in more than 45,000 degree and diploma institutions. In the last decade, the growth rate has been particularly high. Private institutions are playing a major role in the growth and account for 64% of the total number of institutions and 59% of the enrollment as against 43% and 33%, respectively, a decade ago. The government has passed various bills during the last decade – the Higher Education and Research Bill, the Educational Tribunal Bill, and the Foreign Educational Institutions Bill to improve transparency in the system.

Exhibit 51: The number of universities has grown …



Source:

Exhibit 52: …and so has the number of colleges

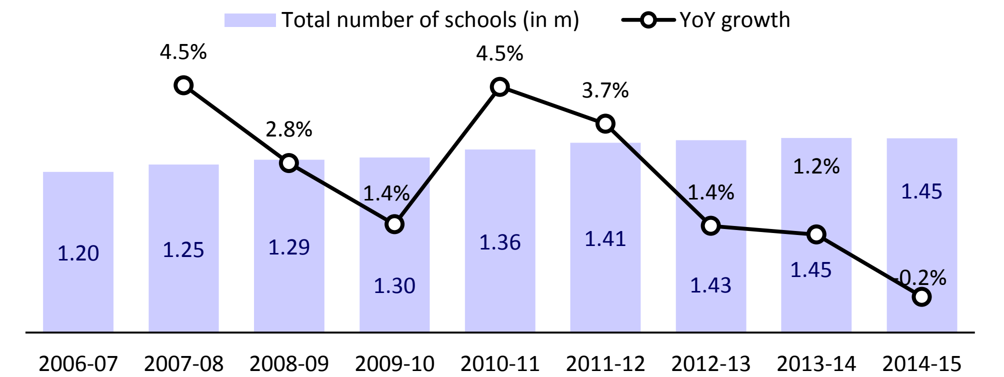


Source:

Number of private schools is increasing

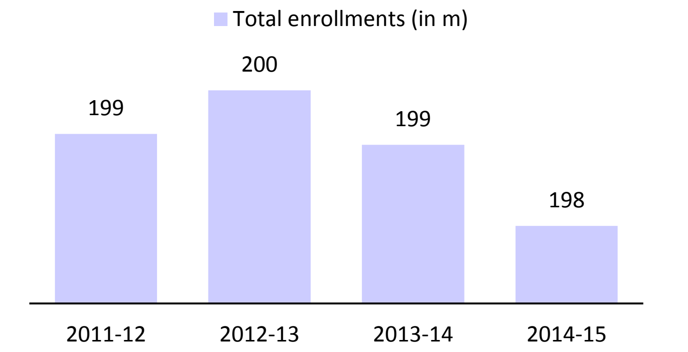
The total number of schools in India has increased from 1,196,663 in 2006-07 to 1,445,807 in 2014-15 – a CAGR of 3%. The government has been promoting education though Sarva Sikhsha Abhiyan since 2000-2001. This initiative provides for a variety of interventions like opening of new schools and alternate schooling facilities (special training), construction of schools and additional classrooms, toilets and drinking water, provisioning for teachers, regular teacher in service training and academic resource support, free textbooks and uniforms, and support for improving learning achievement levels/outcome. The number of private schools is increasing as a percentage of total number of schools in India due to increasing awareness of better quality education. Private schools, which constituted 19% of total schools in India in 2008-09, accounted for 23% in 2014-15.

Exhibit 53: Growth in number of schools in India



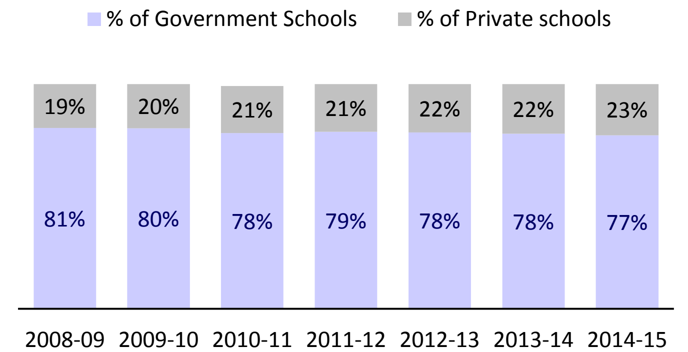
Source: DISE, MOSL

Exhibit 54: Total enrollments in India



Source: DISE, MOSL

Exhibit 55: Private schools increasing



Source: DISE, MOSL

Exhibit 56: Total number of schools in Maharashtra and Gujarat (category-wise; 2014-15)

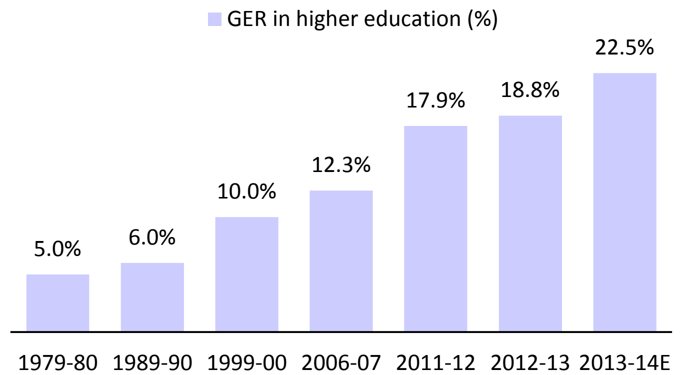
	Primary only	Primary with Upper Primary	Primary with U. Primary & Sec. &Higher Sec.	Upper Primary Only	Upper Primary With Sec. & Higher Sec.	Primary with U. Primary & Sec.	U. Primary with Sec.	All Schools
Total schools in India	847,118	277,706	37,460	147,388	38,734	45,143	52,231	**1,445,807**
Total schools in Maharashtra and Gujarat	64,932	57,343	2,148	876	4,947	2,461	8,016	**140,722**

Source: DISE, MOSL

Improvement in gross enrollment ratio (GER) a big positive

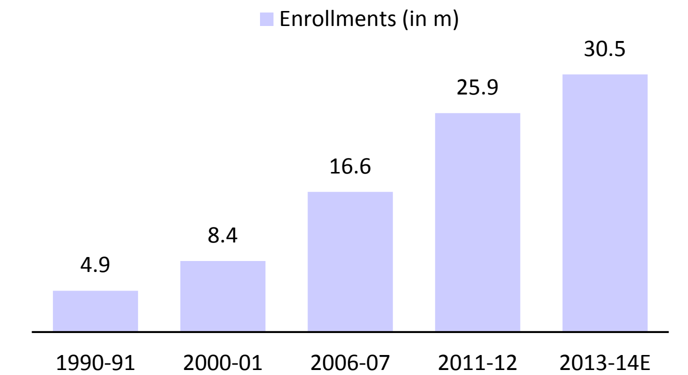
The government has taken various measures in the Eleventh Five Year Plan (2007-2012) to improve the gross enrollment ratio (GER). India reached a GER of 17.9% in 2007, up from 12.3% in 2012. The government has set a target of enrollment of 35.9m students by the end of the Plan period. Enrollments and GER are expected to register an annual growth rate of ~7% during the Plan period. As per the target of the Twelfth Five Year Plan, central higher education institutions are expected to show the highest annual growth of 14.9% in student enrollments as compared to private institutions (7.6%), state institutions (5.6%), and open and distance learning institutions (4.4%).

Exhibit 57: GER has improved over the years



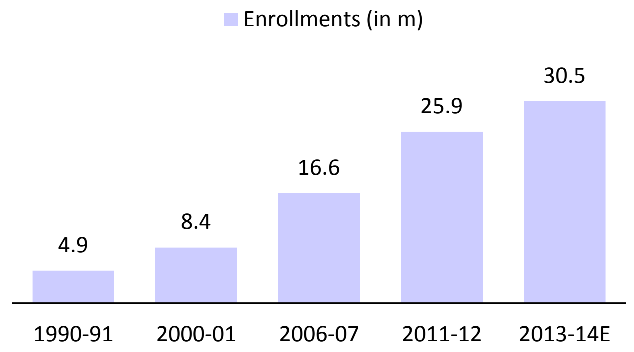
Source: E&Y Report, MOSL

Exhibit 58: Total enrollments trend



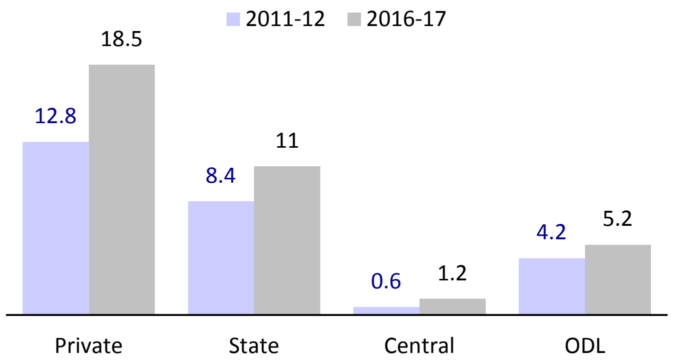
Source: E&Y Report, MOSL

Exhibit 59: Enrollments to grow at 6.7% CAGR



Source: E&Y Report, MOSL

Exhibit 60: Enrollments to improve across categories

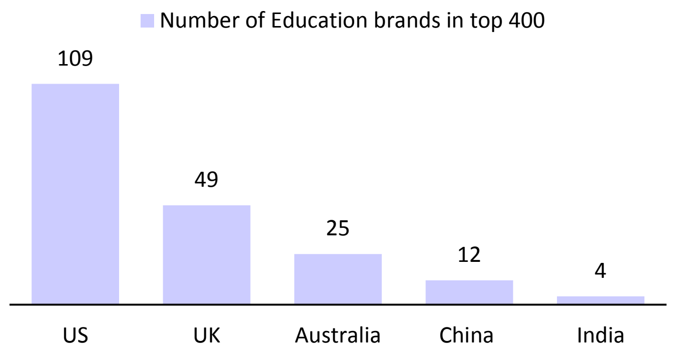


Source: E&Y Report, MOSL

India lags in terms of quality of education and research

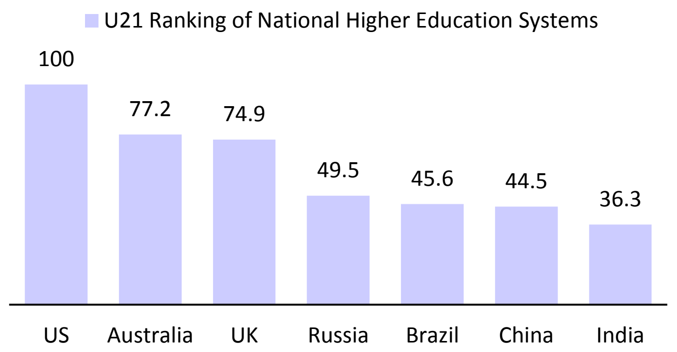
Only four Indian higher education brands featured in the Times Higher Education World University Rankings 2013-14 of the top 400 global universities. This depicts that the quality of education is low in India. Out of the 48 countries studied, India ranks second-last in the U21 rankings of national higher education systems. India featured lowest amongst BRIC nations. Academicians in China authored almost five times more research papers than India's academicians in 2011. Even the relative impact of citations for India is half that of the world average. These statistics call for education sector reforms in India.

Exhibit 61: Times Higher Education world ranking



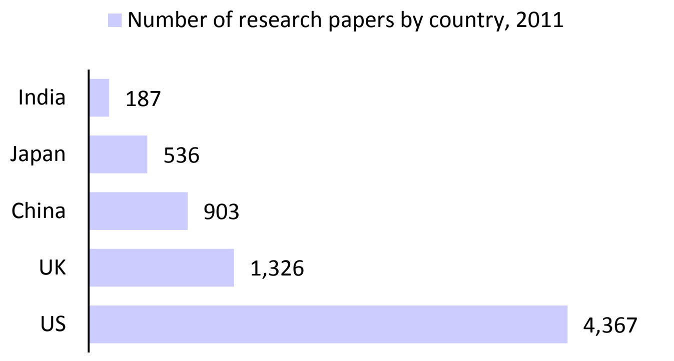
Source: E&Y Report, MOSL

Exhibit 62: India features last amongst BRIC nations



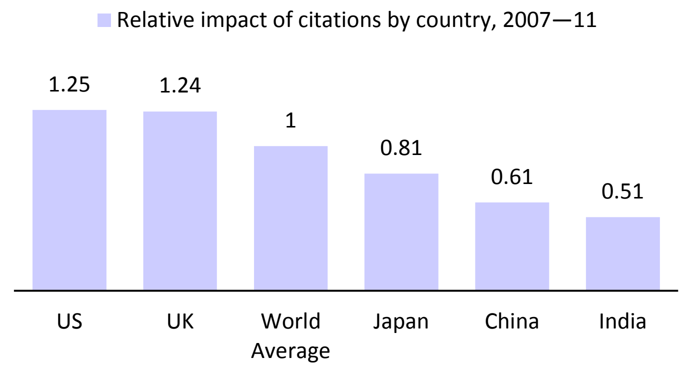
Source: E&Y Report, MOSL

Exhibit 63: Number of research papers released



Source: E&Y Report, MOSL

Exhibit 64: Relative impact of Indian citations lowest

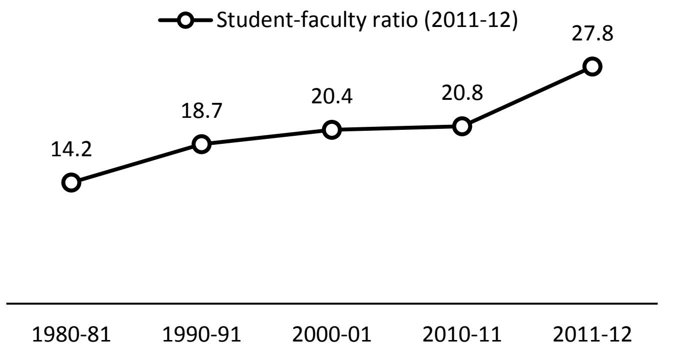


Source: E&Y Report, MOSL

Rise in student-faculty ratio in higher education is concerning

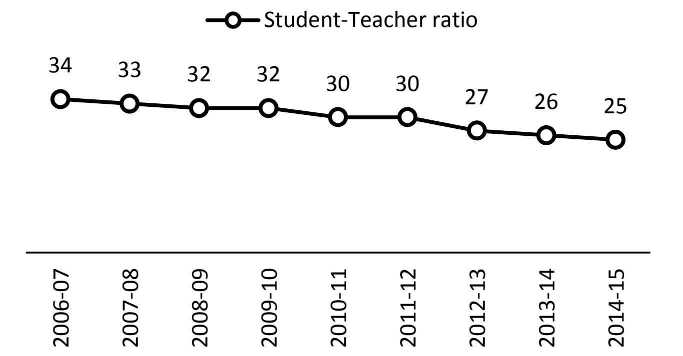
Student-faculty ratio in higher education has almost doubled in the past two decades. However, there has been improvement in student-teacher ratio in schools. Around 35% of faculty positions in state universities and 40% in central universities are lying vacant. There is no mandatory formal teacher training program to develop effective teaching skills, which hampers the quality of the education imparted. While enrollment in higher education has grown six times in the last 30 years, faculty strength has only grown four times, as reflected in the increasing student-faculty ratio. Lower the student-teacher ratio, higher the quality of education, as teachers can focus more on students.

Exhibit 65: Student-faculty ratio in higher education



Source:

Exhibit 66: Student-faculty ratio in schools

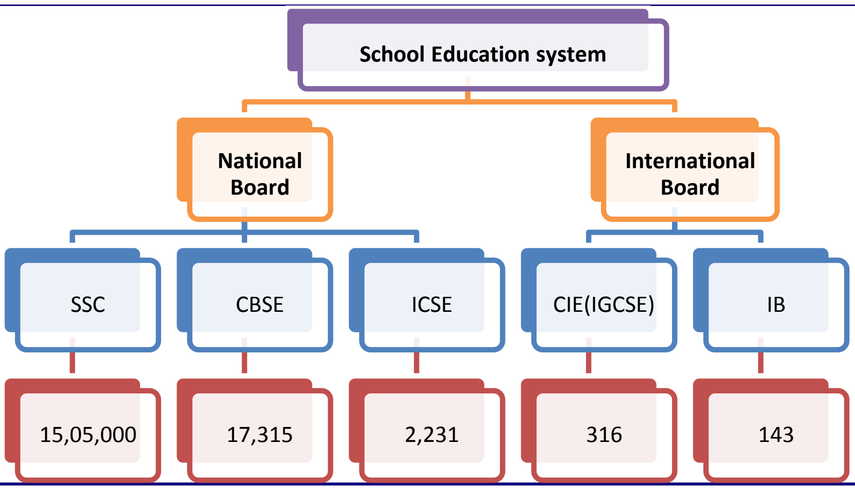


Source:

Highly fragmented industry with dominant regional players

The educational book market in India has been growing rapidly over the past 6-8 years. According to media reports, the K–12 market (school books) has grown from INR63b in FY08 to INR186b in FY14, implying a CAGR of 19.7%. Higher education book sales have grown in this period from INR16b to INR56b.

Exhibit 67: School education system in India



Source: Company Presentation, MOSL

Exhibit 68: Navneet's focus regions for syllabus-based print content

Particulars	Maharashtra	Gujarat
Number of Government schools	67,382	33,755
Number of private schools	29,126	9,880
Total Schools	**97,084**	**43,635**
Number of students*		
a) Standard 1-5	10,125,716	5,764,682
b) Standard 6-8	6,046,718	3,377,769
c) Standard 9-10	3,665,059	1,746,385
d) Standard 11-12	2,515,481	985,972
Total Students	**22,293,964**	**11,874,808**

Source: DISE, MOSL

While the market is highly fragmented, it is also experiencing consolidation, in part as a result of involvement of foreign multinationals. The government allows 100% foreign direct investment. Consolidation is happening not only in trade publishing – merger of Penguin and Random House, and HarperCollins' acquisition of Harlequin (all companies with substantial presence in India) – but also in educational books – S Chand's acquisition of Madhuban, Vikas Publishing House and Saraswati Book House, and Laxmi Publications' acquisition of Macmillan Higher Education.

Key risks

IPR infringement: Infringement of IPRs is a big concern, as it can lead to massive liability on the company. It is difficult for a company to prevent this, as authors may copy material from a source unknown to the company. However, NELI has strong panels of authors with high integrity. It has had long-standing relationships with these authors and the author churn rate is extremely low.

Concentration of revenues in two states: NELI's operations are currently mainly concentrated in its two core states Gujarat & Maharashtra. However, with common syllabus, NELI has expanded into new states like Karnataka, NCR, Tamil Nadu, Kerala and AP for penetrating into CBSE syllabus, diversifying its revenue base.

Stationery segment could face intense competition from ITC: Over the past five years, ITC has become aggressive in the value-added paper space, where NELI is also present. Any predatory pricing by ITC to expand its market share can dent the profitability of NELI's stationery business. However, over the last four years, NELI has increased its exports three-fold to diversify risk in the domestic stationery segment.

Rise in paper costs Paper, the key raw material, accounts for almost ~45-50% of total cost. Sharp rise in paper prices can hit profitability of the publishing as well as domestic stationery businesses.

Management overview

Exhibit 69:

Sr no	Name	Designation	Role
1	Mr. Gnanesh (Sunil) Gala	Managing Director	■ Promoter with an experience of over 30 years in Finance & Corporate Affairs ■ Key person in Developing & Execution of Business Strategies
2	Mr. Anil Gala – Director	Director	■ Promoter with an experience of over 37 years in Content creation & Marketing ■ Key person in hiring right authors and quality check of content
3	Mr Bipin Gala	Wholetime Director	■ Promoter with an experience of over 30 years in operations ■ Key person in Labour Management
4	Mr Raju Gala	Jt Managing Director	■ Promoter with an experience of over 30 years in Printing & Marketing ■ Key person in procuring raw materials and controls manufacturing activities
5	Mr Shailendra Gala	Director	■ Promoter with an experience of over 25 years in Stationery business ■ Key person in stationery marketing, distribution & sales
6	Mr Atul Shethia	Director	■ Cost Accountant with an experience of more than 20 years in Manufacturing and Logistics. ■ Introduced ISO SAP & KAIZEN
7	Mr Mohinder Pal Bansal	Director	■ Chartered Accountant by profession and has over 23 years of experience in M & A Strategic Advisory, Capital Markets, Post Acquisition performance management in India, Asia and Europe
8	Mr Amit Gala	CEO eSense	■ Chartered Accountant by profession, has worked in each activity related to publishing and is keenly involved in e- learning initiatives ■ Key person in product development, marketing and sales of digital products

Source:

Financials and Valuation

Consolidated - Income Statement							(INR Million)
Y/E March	**FY13**	**FY14**	**FY15**	**FY16**	**FY17E**	**FY18E**	**FY19E**
Income from Operations	8,221	9,002	9,977	9,657	11,275	14,127	16,702
Less: Excise Duty	164	181	182	159	381	476	571
Total Income from Operations	**8,057**	**8,821**	**9,795**	**9,498**	**10,894**	**13,651**	**16,131**
Change (%)	30.2	9.5	11.0	-3.0	14.7	25.3	18.2
EBITDA	**1,922**	**2,080**	**2,367**	**2,055**	**2,538**	**3,276**	**3,952**
Margin (%)	23.9	23.6	24.2	21.6	23.3	24.0	24.5
Depreciation	235	258	308	288	266	298	307
EBIT	**1,688**	**1,822**	**2,060**	**1,768**	**2,273**	**2,979**	**3,645**
Int. and Finance Charges	88	100	91	36	34	48	42
Other Income	37	35	28	176	147	154	178
PBT bef. EO Exp.	**1,637**	**1,757**	**1,996**	**1,908**	**2,386**	**3,085**	**3,781**
EO Items	-13	0	0	0	0	0	0
PBT after EO Exp.	**1,623**	**1,757**	**1,996**	**1,908**	**2,386**	**3,085**	**3,781**
Current Tax	547	594	699	694	833	1,077	1,320
Deferred Tax	3	11	-7	-28	0	0	0
Tax Rate (%)	33.9	34.4	34.7	34.9	34.9	34.9	34.9
Less: Minority Interest	6	1	1	209	0.5	0.5	0.5
Reported PAT	**1,067**	**1,152**	**1,303**	**1,033**	**1,552**	**2,008**	**2,461**
Adjusted PAT	**1,076**	**1,152**	**1,303**	**1,033**	**1,552**	**2,008**	**2,461**
Change (%)	37.9	7.1	13.2	-20.7	50.2	29.3	22.6
Margin (%)	13.4	13.1	13.3	10.9	14.3	14.7	15.3

Consolidated - Balance Sheet							(INR Million)
Y/E March	**FY13**	**FY14**	**FY15**	**FY16**	**FY17E**	**FY18E**	**FY19E**
Equity Share Capital	476	476	476	476	467	467	467
Preference Capital	3	3	0	0	0	0	0
Total Reserves	3,712	4,307	4,956	5,356	5,648	6,784	8,205
Net Worth	**4,192**	**4,787**	**5,433**	**5,833**	**6,115**	**7,251**	**8,672**
Minority Interest	1	1	1	1	1	1	1
Deferred Liabilities	64	73	41	13	13	13	13
Total Loans	1,687	2,337	1,436	1,035	1,935	1,935	1,435
Capital Employed	**5,943**	**7,197**	**6,909**	**6,881**	**8,063**	**9,199**	**10,120**
Gross Block	3,316	3,673	3,741	4,053	4,803	4,953	5,103
Less: Accum. Deprn.	1,574	1,798	2,042	2,298	2,564	2,861	3,168
Net Fixed Assets	**1,742**	**1,874**	**1,699**	**1,755**	**2,239**	**2,092**	**1,935**
Goodwill on Consolidation	0	0	0	0	0	0	0
Capital WIP	57	45	40	8	0	0	0
Total Investments	**310**	**475**	**492**	**326**	**326**	**326**	**326**
Curr. Assets, Loans&Adv.	**4,982**	**6,042**	**5,995**	**5,579**	**7,076**	**8,758**	**10,208**
Inventory	2,752	3,337	3,484	3,064	3,432	4,301	5,060
Account Receivables	1,659	1,961	1,886	1,889	2,388	2,842	3,270
Cash and Bank Balance	35	69	55	59	633	929	1,123
Loans and Advances	536	675	571	567	624	686	755
Curr. Liability & Prov.	**1,163**	**1,253**	**1,317**	**787**	**1,579**	**1,977**	**2,349**
Account Payables	585	643	586	683	766	955	1,129
Provisions	577	610	731	104	813	1,021	1,220
Net Current Assets	**3,819**	**4,789**	**4,678**	**4,793**	**5,498**	**6,782**	**7,859**
Appl. of Funds	**5,943**	**7,197**	**6,909**	**6,881**	**8,063**	**9,199**	**10,120**

E: MOSL Estimates

Financials and Valuation

Ratios

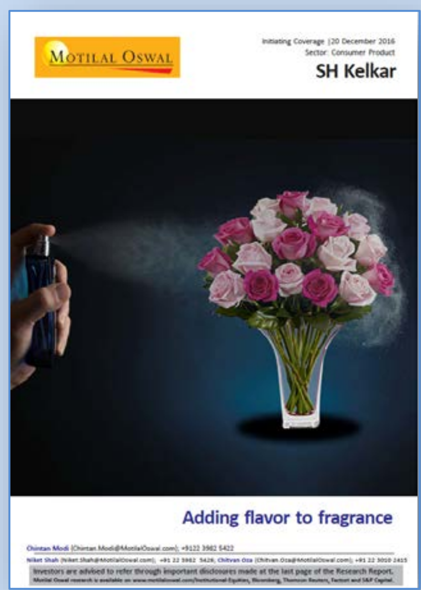
Y/E March	FY13	FY14	FY15	FY16	FY17E	FY18E	FY19E
Basic (INR)							
EPS	**4.5**	**4.8**	**5.5**	**4.3**	**6.6**	**8.6**	**10.5**
Cash EPS	5.5	5.9	6.8	5.5	7.8	9.9	11.9
BV/Share	17.6	20.1	22.8	24.5	26.2	31.0	37.1
DPS	1.8	2.0	2.2	2.2	2.4	3.1	3.7
Payout (%)	47.0	48.4	48.4	61.0	44.3	43.4	42.3
Valuation (x)							
P/E		31.6	28.0	35.3	23.0	17.8	14.5
Cash P/E		25.9	22.6	27.6	19.7	15.5	12.9
P/BV		7.6	6.7	6.2	5.8	4.9	4.1
EV/Sales		4.3	3.8	3.9	3.4	2.7	2.2
EV/EBITDA		18.3	15.7	17.9	14.6	11.2	9.1
Dividend Yield (%)	1.2	1.3	1.4	1.4	1.6	2.0	2.4
Return Ratios (%)							
RoE	27.6	25.7	25.5	18.3	26.0	30.0	30.9
RoCE	20.8	18.7	19.5	18.4	21.1	23.7	25.8
RoIC	21.1	19.7	20.8	18.0	21.8	25.8	28.6
Working Capital Ratios							
Inventory (Days)	122	135	127	116	111	111	111
Debtor (Days)	74	80	69	71	77	73	71
Creditor (Days)	26	26	21	26	25	25	25
Working Cap. Turnover (Days)	168	191	169	179	157	151	147
Leverage Ratio (x)							
Current Ratio	4.3	4.8	4.6	7.1	4.5	4.4	4.3
Debt/Equity	0.4	0.5	0.3	0.2	0.3	0.3	0.2

Consolidated - Cash Flow Statement **(INR Million)**

Y/E March	FY13	FY14	FY15	FY16	FY17E	FY18E	FY19E
OP/(Loss) before Tax	1,636	1,757	1,996	1,909	2,386	3,085	3,781
Depreciation	235	258	308	288	266	298	307
Interest & Finance Charges	-1	0	0	-3	0	0	0
Direct Taxes Paid	-520	-607	-651	-743	-833	-1,077	-1,320
(Inc)/Dec in WC	-658	-889	-100	542	-132	-988	-884
CF from Operations	**692**	**519**	**1,553**	**1,993**	**1,687**	**1,318**	**1,885**
Others	48	72	69	-50	34	48	42
CF from Operating incl EO	**740**	**591**	**1,622**	**1,942**	**1,721**	**1,366**	**1,927**
(inc)/dec in FA	-363	-430	-176	-258	-742	-150	-150
Free Cash Flow	**377**	**162**	**1,446**	**1,685**	**979**	**1,216**	**1,777**
(Pur)/Sale of Investments	-315	-163	-11	-6	0	0	0
Others	-21	-24	106	10	0	0	0
CF from Investments	**-699**	**-617**	**-81**	**-253**	**-742**	**-150**	**-150**
Issue of Shares	12	-1	-3	0	-582	0	0
(Inc)/Dec in Debt	240	658	-901	-401	900	0	-500
Interest Paid	-86	-97	-93	-37	-34	-48	-42
Dividend Paid	-221	-501	-557	-1,247	-688	-871	-1,040
Others	0	0	0	0	-1	-1	-1
CF from Fin. Activity	**-56**	**59**	**-1,555**	**-1,685**	**-405**	**-920**	**-1,583**
Inc/Dec of Cash	**-15**	**34**	**-14**	**4**	**574**	**296**	**194**
Opening Balance	50	35	69	55	59	633	929
Closing Balance	**35**	**69**	**55**	**59**	**633**	**929**	**1,123**

REPORT GALLERY

RECENT INITIATING COVERAGE REPORTS



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