

April 21, 2017

# Subscribe For Listing Gains

## S Chand & Company

IPO Note

**LKP**  
Since 1948

S Chand & Company (S Chand) is one of India's leading Indian education content companies and has nearly 7 decades of experience in delivering content, solution & services throughout the K-12, higher education & early learning segments. It is a leading K - 12 education content provider in terms of revenue and has a strong presence in the CBSE / ICSE affiliated schools & increasing presence in state board affiliated schools across India. With over 55 consumer brands across knowledge products & services including *S Chand*, *Vikas*, *Madhubun*, *Saraswati*, *Destination Success* & *Ignitor*, it sold over 35.5 mn copies over 11,147 titles in FY16. While it has a contractual relationship with over 1,958 authors (including co-authors) for over the last 5 financial years, its top 10 best-selling titles accounted for 3.0 mn copies, with over 15 authors having each sold over a million copies of their titles during the last 5 fiscals. Such high volumes of sales has been possible because of the company's strong distribution & sales network of over 4,932 distributors & dealers and an in-house sales team of 838 professionals working from 82 branches & marketing offices across India. It also went ahead with the acquisition of 74 % stake in Chhaya Prakashan which gave an access to 4 brands, 9.9 mn FY16 sales volumes of 433 titles from 24 authors and an additional reach of 771 distributors & dealers.

### Indian Education Sector - A Structural Growth Story

The education sector which comprises of formal, informal (test prep, tutoring, early education & vocational training) & ancillary (content / publishing, digital content & services) segments is estimated to be US\$ 90 bn as on 2015 and is expected to reach US\$ 188 bn by 2020. India has a large population in the education age bracket, consisting of students aged 5-24, which stood at approximately 520 mn as on 2016. This is expected to grow to approximately 534 mn in 2020. In addition to the growing population, the reduction in drop-out rates is also expected to contribute to the increase in market size.

The K-12 education system in India is one of the largest in the world, with a market size of US\$49.5 bn, comprising 1.1 mn government schools and 0.4 mn private schools. During 2011-2015, enrolment in K-12 schools has grown from 248 mn to 259 mn students, adding an average of approximately 3 mn students per annum. While historically government schools accounted for the majority of schools and enrolments, the private unaided schools have significantly added to the growth in enrollment. As a result, the share of private unaided schools recorded the highest growth rate among other types of schools from 14.2% to 19% during 2011- 2014. Most schools in India are affiliated to one of 3 main governing bodies for K-12 schools: state level board, CBSE & ICSE. CBSE is the most common curriculum in secondary school and is governed by the central government and its standards for syllabus & examinations for classes 9 - 12. CBSE schools have grown at the fastest CAGR of 8.9% during 2011-2015, in comparison to ICSE (7.2%) & state boards (2.6%). Currently estimated at US\$ 15 bn, India has also one of the largest higher education systems globally, with 34.2 mn students enrolled across 777 universities, 38,498 colleges & 12,276 stand-alone institutions. The informal education (US\$ 19.6 bn) & ancillary segments (US\$ 6.2 bn) are significant markets as well.

### Issue Details

<b>Promoter</b>	Dinesh Kumar Jhunjhnuwala Neerja Jhunjhnuwala Himanshu Gupta
<b>Issue Type</b>	Book Built Issue
<b>Anchor</b>	Tuesday, April 25, 2017
<b>Opens on</b>	Wednesday, April 26, 2017
<b>Closes on</b>	Friday, April 28, 2017
<b>Face Value</b>	₹ 5 per share
<b>Price Band</b>	₹ 660 - ₹ 670
<b>Bid Lot</b>	22 Equity Shares
<b>Issue Size</b>	₹ 7.3 bn
<b>Listed Peers</b>	Navneet Education
<b>Listing</b>	BSE & NSE
<b>Mode of Payment</b>	Mandatory ASBA (No cheques will be accepted)
<b>Registrar</b>	Link Intime India Private Limited

### Issue Structure

Category	Allocation	Amt (₹)
QIB	50%	3.7 bn
NIB	15%	1.1 bn
Retail	35%	2.5 bn

### Financial Snapshot

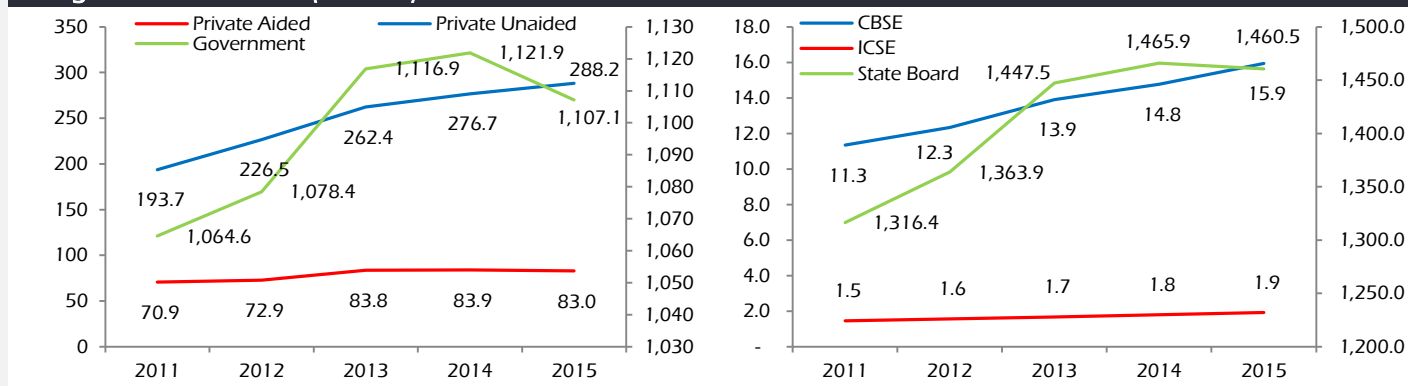
YE Mar	FY13	FY14	FY15	FY16
Op. Revenue(mn)	2,790	3,700	4,767	5,378
Revenue Growth	61.2%	32.6%	28.8%	12.8%
EBITDA(mn)	573	788	1,022	1,253
EBITDA Growth	124.9%	37.5%	29.6%	22.6%
EBITDA Margins	20.5%	21.3%	21.4%	23.3%
PAT(mn)	320	426	327	466
PAT Growth	117.8%	33.0%	-23.0%	42.4%
PAT Margins	11.4%	11.5%	6.8%	8.6%
EPS	16.7	17.6	10.5	17.1
ROCE	14.8%	17.3%	15.5%	14.9%
ROE	11.0%	11.6%	8.3%	7.8%

Yashas Bhat

yashas\_bhat@lkipsec.com

+91 22 6635 1220

## Strength of K-12 Schools (in '000s)



Source, Company, LKP Research

The test preparation market comprises of technical / professional course entry exams and employment related exams and is currently estimated that over 26 mn students take these exams each year in order to gain admission into professional & post graduate courses and also for public sector jobs. This market is estimated at US\$5 bn, as of 2015 – 2016. The digital test preparation segment is estimated to be US\$50 mn and is expected to grow at a CAGR of 30% over 2016-2020. The early learning segment, catering to the age group less than 5 years, is a largely untapped market as well, with revenue from this segment currently estimated at US\$2 bn in India, growing at a healthy CAGR of 15%.

The ancillary segment comprises of the industries related and supplementary to both formal & informal education segments and is therefore a direct beneficiary of the growth in both education segments. This segment is estimated to be worth approximately US\$6.2 bn in 2015, and is expected to grow at a CAGR of 21% to US\$15.4 bn by 2020. It is believed that the ancillary segment is taking an increasingly central role in education given the increasing participation of the private sector in Indian education. This includes participation from content providers, digital and other service providers. Content providers develop a repository of education content by leveraging their editorial capabilities and author relationships which is delivered either in print medium (textbooks, reference books or supplementary books) or a digital medium (online education, e-books etc.). Digital providers use the digital medium of delivering education solutions (including content, hands-on learning tools & assessment) where the content is developed in-house or sourced from a content provider. Other services include innovative offerings (curriculum management, etc.) that aid & improve K-12 learning.

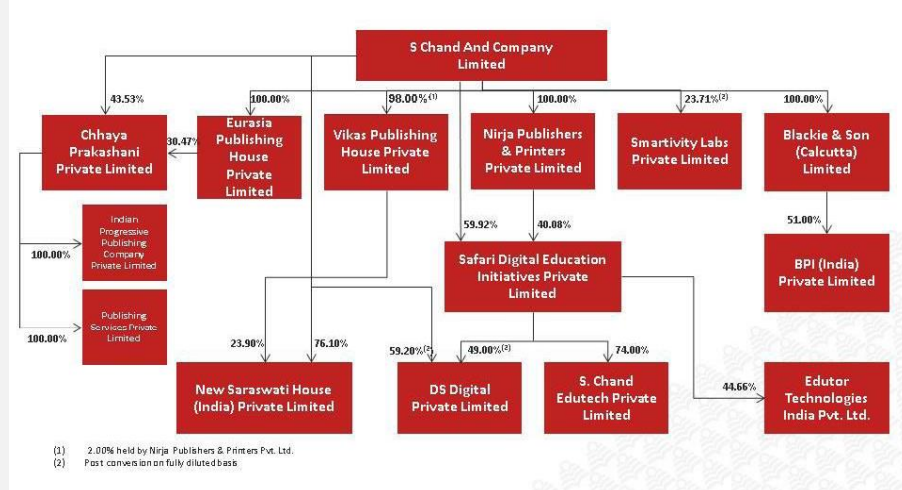
The market size of education content in India, the space S Chand mainly operates in, is estimated to be US\$4.5 bn, with the K-12 education content market estimated at US\$ 3.4 bn thereby clocking a 19.3% CAGR from 2011-2015. Central board affiliated schools (i.e. CBSE/ICSE schools) have exhibited the faster growth at 21.7% CAGR from 2011 - 2015, aided by the participation of the private sector.

## Competitive Landscape of K-12 Content Providers

Company	S Chand	Navneet	Orient Blackswan	Ratna Sagar	Macmillan Publishers	Holy Faith International	Cambridge University Press India	Rachna Sagar	HarperCollins Publishers India
Listed	Y	Y	N	N	N	N	N	N	N
Period	Mar-16	Mar-16	Mar-15	Mar-15	Dec-15	Mar-14	Mar-15	Mar-15	Mar-14
Revenues	537.8 Cr	534.6 Cr	183.9 Cr	183.2 Cr	168.6 Cr	131.3 Cr	111.1 Cr	80.9 Cr	45.3 Cr
% Growth	12.8%	-3.1%	12.5%	7.2%	10.1%	-5.6%	6.8%	7.9%	1.1%

\*Pearson and OUP are been excluded from above table as their revenue figures from direct publishing were not available.

## Organization Structure of S Chand



Source: Company, LKP Research

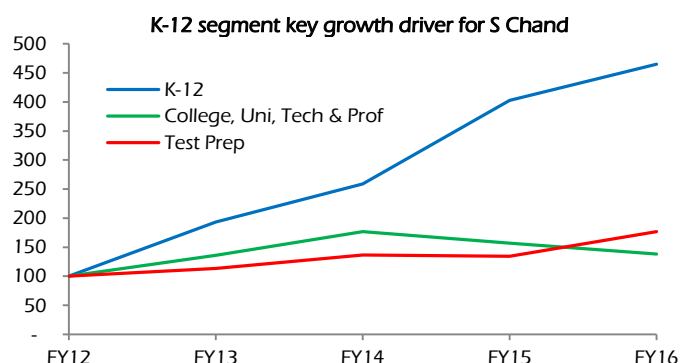
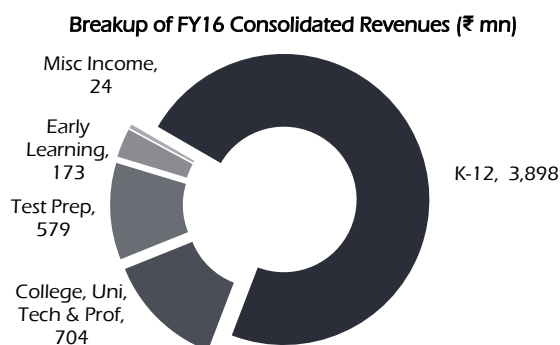
### Strong brand equity & high customer recall with leader position in K-12.

S Chand is the leading K-12 education content company in terms of revenue from operations in FY16, according to Nielsen, with a strong presence in the CBSE / ICSE affiliated schools and increasing presence in the state board affiliated schools across India. Forming 72.5 % of FY16 revenues, the company sold a total of 5,253 titles in the K-12 business segment, thereby clocking a CAGR of 46.8 % in consolidated K-12 business revenues, which includes organic growth of 20.5%. Print content represents the largest portion of its consolidated operating revenue in the K-12 segment (55.6%), with hybrid offering which couples print content with digital & interactive methods of learning contributing 38.8% of consolidated K-12 revenues. It also offered an aggregate of 7,722 hours of e-content as on FY16, for delivery through digital platforms which constituted 5.6 % of K-12 consolidated revenues.

S Chand's higher education segment is its second largest segment comprising 23.9 % of its consolidated revenues. The seasonality of the higher education segment is lower than K-12 segment which clocks 75 - 80 % of its sales in its 4<sup>th</sup> quarter. While it sold 2.0 mn copies of 109 titles in test preparation in FY16, 2.9 mn copies of 2,920 titles in college & university/technical & professional segment were also sold during the same period. Its test prep & college & university / technical & professional segment has been growing at a decent pace, clocking a 5 year CAGR of 15.3 % & 8.4 % respectively. Its early learning business which caters to age group 0 - 4 years is currently a small part of S Chand's revenues comprising only 3.2 % of its top-line as on FY16.

S Chand has a contractual relationship with at least 1,958 authors for over 5 years as on March 31, 2016 whereby the authors are compensated through royalties linked to content sales & editorial support. Royalties are paid on an average of 7.5 % of revenues with minimum royalties usually not guaranteed.

### Impressive growth on the back of organic & inorganic expansion



Source: Company, LKP Research

An important point to consider with its mainstay K-12 business is that print content from K-1 to K-8 are prescribed by the school and students buy this print content from retailers. In K-9 to K-12 segment schools recommend print content and students have the option of choosing from several options available in the market. Content providers like S Chand regularly interact with schools, educators & retailers as their primary aim is to get these 'adoptions' or prescriptions' of print content by schools, so that print content becomes a core resource used by students on a particular course or in a particular class. This results in multiple sales of that title as every student on that course needs access to it. This is where the brand equity & recall as a quality educational content provider becomes of paramount importance.

We believe that its business would be a key beneficiary of the increasing share of education within the discretionary expenditure of the Indian consumer as its presence across the student lifecycle would allow the company to generate recurring revenue throughout student's lives. We like S Chand's brand appeal developed over 7 decades of experience in delivering quality education content as two thirds of the 18,000 plus CBSE & ICSE schools are prescribing / recommending at least one book from one of their many brands to their students. It has demonstrated the ability to attract & retain leading authors considering its healthy track record in progressing authors' careers. We also believe there is a lot of scope for consolidation in the industry, apparent by S Chand's focus on inorganic growth such as acquisition of *Madhuban* & *Vikas* brands in FY13 for Hindi language titles, *Saraswati* for French, languages, arts & crafts titles and *Chhaya Prakashan* in FY17 for eastern state board markets.

#### Principal brands of S Chand

Brand	K-12	Test Prep	College & Uni / Tech & Prof
S Chand	✓	✓	✓
Vikas			✓
Madhuban	✓		
Saraswati	✓		
Blackie	✓		
Chhaya	✓		
IPP	✓		
<b>Brands specializing in e-content &amp; services</b>			
Mystudygear	✓		
Flipclass*	✓		
Destination Success	✓		
Ignitor*	✓	✓	✓
Testbook*		✓	
OnlineTyari*		✓	

*\*Revenue not consolidated for these companies*

#### Pan-India sales & distribution network and strong integrated in-house printing & logistics a significant moat

S Chand has a strong distribution & sales network of over 4,932 distributors & dealers and an in-house sales team of 838 professionals working from 82 branches & marketing offices across India. It maintains separate sales teams focused on each brand which serve two distinct purposes: (a) working to achieve healthy growth for each brand & better overall sales and (b) catering to the end consumer preference of selecting from a wider product catalogue of authors & titles. An additional long term benefit from separate brand-focused sales teams is that each team is able to develop deep product expertise, which allows for better brand positioning and increased brand recall.

S Chand has also built a robust supply chain and has fully integrated its printing needs & capabilities, such that in FY16, over 85 % of its printing requirements were met by its Sahibabad & Rudrapur facilities. The company has incurred a capex of ₹453.5 mn to set up its Sahibabad facility which enhanced its printing capacity from 15 tons of paper per day in FY14 to 55 tons of paper per day in FY16, taking its printing capacity to 64.2 mn pages per day. Its print facilities & distribution networks are supported by a strong logistics network which comprised of 42 warehouses located in 19 states as on Q1FY17 to allow coverage across India. Additionally, Chhaya has 2 warehouses located in West Bengal as well.

We believe that the company has a significant moat with its wide distribution reach & in-house printing capabilities as it is able to meet peak season demand by reducing dependence on printers that may charge higher rates in light of the demand while its market reach along with customer touch points give it a competitive advantage to grow existing brands as well as build new brands.

### **Healthy growth at the cost of poor capital efficiency**

S Chand has managed to grow pretty impressively on the back of consistent organic growth & acquisitions, evident by its impressive 32.8 % & 33.4 % CAGR on its top-line & bottom-line respectively between FY12 - FY16. It also managed to improve its EBITDA by 860 basis points from 14.7 % in FY12 to 23.3 % in FY16. This margin expansion was offset by a rise in depreciation & finance costs on account of the expansion of its printing facilities as well as inorganic expansion, thereby keeping its PAT margins at around an 8 % clip.

This inorganic growth has come on the back of private equity funding where it raised ₹1.4 bn & ₹1.7 bn from Everstone Capital & IFC in equity along with a rise in equity share capital to the extent of ₹ 350 mn on conversion of convertible debentures & ₹ 249 mn as consideration for acquisition of shareholdings of promoters in a few companies engaged in related businesses. So while S Chand managed to grow its revenues & profits at an impressive pace, this came at the cost of dilution in returns on equity which experienced ~ 840 basis fall from 16.2 % in FY12 to 7.8 % in FY16. The ₹ 3.3 bn fresh issue which would be used to repay debt raised for the Chhaya Prakashan acquisition as well as other borrowings poses the risk of further diluting its returns on equity on expansion of its equity base despite the increasing revenues & profits from its latest acquisition.

### **Recommendation**

We like the brand equity enjoyed by S Chand in the education content space and distribution & marketing depth it has developed over nearly 7 decades of experience in this industry. We expect this company to continue to grow at a robust pace on the back of rising share of education across all segments in discretionary spends and strategic acquisitions. While we like the margin profile of the company and potential upside on its bottom-line through prudent debt management and consequent savings in finance costs, we believe that there is limited scope of improvement for its return on equity in the medium term. The seasonality of S Chand's business does not help in allaying these fears as it earns more than 3/4<sup>th</sup> of its business in the fourth quarter.

We believe that its 7 decade legacy, leadership in K-12 education content market, strong margin & growth prospects have been captured well at the valuations of ₹ 660-670 per share where the scrip would trade at 39X FY16 earnings. We recommend a **SUBSCRIBE** on the S Chand IPO for **listing gains**.

## Consolidated Financials

### Income Statement

Particulars	FY12	FY13	FY14	FY15	FY16	9MFY17
<b>Op. Revenues</b>	<b>1,730</b>	<b>2,790</b>	<b>3,700</b>	<b>4,767</b>	<b>5,378</b>	<b>1,495</b>
Raw Materials & Components Cost	891	1,005	1,492	1,782	1,757	987
Purchase & Implementation Costs	5	7	3	17	49	37
Publication Expenses	176	300	423	482	503	223
Changes in FG, WIP & Traded Goods	(90)	78	(138)	(243)	(279)	(680)
Selling & Distribution Expenses	181	221	344	456	527	406
Employee Benefits	200	353	527	803	942	836
Other Expenses	112	252	262	447	626	535
<b>Op. Expenses</b>	<b>1,475</b>	<b>2,217</b>	<b>2,912</b>	<b>3,745</b>	<b>4,124</b>	<b>2,344</b>
<b>EBITDA</b>	<b>255</b>	<b>573</b>	<b>788</b>	<b>1,022</b>	<b>1,253</b>	<b>(849)</b>
<b>EBITDA Margins</b>	<b>14.7%</b>	<b>20.5%</b>	<b>21.3%</b>	<b>21.4%</b>	<b>23.3%</b>	<b>-56.8%</b>
Depreciation & Amortization	39	75	123	225	259	203
<b>EBIT</b>	<b>216</b>	<b>498</b>	<b>665</b>	<b>797</b>	<b>994</b>	<b>(1,052)</b>
<b>EBIT Margins</b>	<b>12.5%</b>	<b>17.8%</b>	<b>18.0%</b>	<b>16.7%</b>	<b>18.5%</b>	<b>-70.3%</b>
Finance Costs	59	88	95	283	306	227
Interest Income	1	3	6	4	9	2
Other Income	16	25	9	18	29	13
<b>PBT</b>	<b>174</b>	<b>439</b>	<b>586</b>	<b>537</b>	<b>727</b>	<b>(1,263)</b>
Tax	28	119	160	195	233	(395)
Share in Associate Companies	(1)	-	-	14	27	17
<b>PAT</b>	<b>147</b>	<b>320</b>	<b>426</b>	<b>328</b>	<b>466</b>	<b>(885)</b>
<b>PAT Margins</b>	<b>8.4%</b>	<b>11.4%</b>	<b>11.5%</b>	<b>6.8%</b>	<b>8.6%</b>	<b>-58.6%</b>

### Balance Sheet

Particulars	FY12	FY13	FY14	FY15	FY16	9MFY17
Share Capital	1	2	2	2	2	149
Reserves & Surplus	907	2,906	3,675	3,941	5,990	4,942
<b>Shareholders' Funds</b>	<b>908</b>	<b>2,909</b>	<b>3,677</b>	<b>3,944</b>	<b>5,992</b>	<b>5,092</b>
Share Application money pending allotment	15	-	-	-	-	-
Minority Interest	-	28	30	215	31	88
Long Term Borrowings	78	466	160	1,185	679	595
Other Non-Current Liabilities	2	3	3	5	10	13
Non-Current Provisions	1	17	21	46	50	70
<b>Sources of Funds</b>	<b>1,004</b>	<b>3,422</b>	<b>3,891</b>	<b>5,395</b>	<b>6,762</b>	<b>5,857</b>
Tangible Fixed Assets	157	425	600	1,097	1,025	986
Intangible Assets	113	1,275	1,263	1,643	2,282	3,834
Capital WIP	16	18	99	12	32	9
Intangible Assets Under Development	32	9	13	36	35	100
Non-Current Investments	86	68	74	130	254	254
Deferred Tax Assets	30	42	54	104	124	563
Loans & Advances	90	122	159	187	178	258
Other Non-Current Assets	0	12	17	40	62	12
<b>Current Assets</b>						
Current Investments	7	8	6	47	164	43
Inventories	424	600	839	1,197	1,398	2,506
Trade Receivables	712	1,737	2,309	3,417	3,951	1,956
Cash & Bank Balances	30	137	176	213	244	244
Current Loans & Advances	470	441	160	132	185	624
Other Current Assets	2	1	1	3	2	8
<b>Current Liabilities &amp; Provisions</b>						
Short Term Borrowings	421	638	695	965	1,258	1,831
Trade Payables	639	669	992	1,358	1,511	1,401
Other Current Liabilities	71	137	149	409	232	2,000
Short Term Provisions	34	28	43	133	172	310
<b>Net Current Assets</b>	<b>480</b>	<b>1,452</b>	<b>1,613</b>	<b>2,145</b>	<b>2,771</b>	<b>(160)</b>
<b>Application of Funds</b>	<b>1,004</b>	<b>3,422</b>	<b>3,891</b>	<b>5,395</b>	<b>6,762</b>	<b>5,857</b>

### Cash Flow Statement

Particulars	FY12	FY13	FY14	FY15	FY16	9MFY17
CF from Operating Activities	(310)	(674)	427	(175)	381	(340)
CF from Investing Activities	1,611	(1,346)	(395)	(1,016)	(1,115)	(1,594)
CF from Financing Activities	(1,346)	2,132	5	1,227	1,009	1,907
Inc / (Dec) in Cash & CE	(45)	112	37	36	276	(27)
<b>Closing Cash &amp; CE</b>	<b>25</b>	<b>136</b>	<b>174</b>	<b>209</b>	<b>238</b>	<b>212</b>

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