Prabhudas Lilladher
POWERING YOUR FINANCIAL GROWTH

December 4, 2018

Management Meet Update

■ Change in Estimates | ■ Target | ■ Reco

Change in Estimates

	Current		Previous	
	FY20E	FY21E	FY20E	FY21E
Rating	**BUY**		**-**	
Target Price	**400**		**-**	
Sales (Rs. m)	10,897	12,210	-	-
% Chng.			-	-
EBITDA (Rs. m)	2,703	3,015	-	-
% Chng.			-	-
EPS (Rs.)	40.0	45.1	-	-
% Chng.			-	-

Key Financials

	FY18	FY19E	FY20E	FY21E
Sales (Rs. m)	7,944	9,021	10,897	12,210
EBITDA (Rs. m)	1,927	2,239	2,703	3,015
Margin (%)	*24.3*	*24.8*	*24.8*	*24.7*
PAT (Rs. m)	1,071	1,165	1,398	1,577
EPS (Rs.)	30.6	33.3	40.0	45.1
Gr. (%)	*64.3*	*8.8*	*19.9*	*12.8*
DPS (Rs.)	1.5	2.0	2.5	2.5
Yield (%)	*0.7*	*0.9*	*1.1*	*1.1*
RoE (%)	*13.0*	*11.0*	*11.9*	*12.0*
RoCE (%)	*12.4*	*12.3*	*13.2*	*13.4*
EV/Sales (x)	1.0	1.0	0.8	0.7
EV/EBITDA (x)	4.3	4.1	3.4	2.9
PE (x)	7.2	6.6	5.5	4.9
P/BV (x)	0.8	0.7	0.6	0.6

Key Data	SCHA.NS | SCAND IN
52-W High / Low	Rs.535 / Rs.182
Sensex / Nifty	36,241 / 10,884
Market Cap	Rs.8bn/ $ 110m
Shares Outstanding	35m
3M Avg. Daily Value	Rs.6.98m

Shareholding Pattern (%)

Promoter's	46.67
Foreign	4.72
Domestic Institution	16.13
Public & Others	32.48
Promoter Pledge (Rs bn)	-

Stock Performance (%)

	1M	6M	12M
Absolute	11.5	(40.0)	(53.4)
Relative	7.7	(41.7)	(57.7)

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S Chand and Company (SCAND IN)

Rating: BUY | CMP: Rs221 | TP: Rs400

Valuations provide lucrative entry point

In our recent interaction with S Chand Ltd (S Chand) management highlighted that 1) top-line growth guidance of 13-14% for FY19E remains intact 2) EBITDA margin expansion is on the cards as paper prices are locked in at just 4-5% increase over last sourcing cycle by preponing purchase contracts 3) working capital cycle is expected to ease out by 15-20 days on renegotiation of credit terms for certain best sellers and launch of dealer finance program 4) no incremental investment (Rs~1.43bn so far) in digital space is lined up with break-even expected in 3-4 years 5) collectively the company will have to shell out Rs~1-1.2bn in FY19E for Chetana's acquisition and buying out balance 26% stake in Chhaya Prakashini 6) tax rate will be lower by 100-200bps in FY19E due to lower tax on few subsidiaries (<Rs2.5bn in revenues) and tax break in impending restructuring exercise.

We feel S Chand's aggressive growth strategy (4 acquisitions over last 6 years) is crucial for anyone who wishes to grow in the Indian publishing market and the company has been able to pull it off in a smooth manner till now. Industry-leading position in K-12 publishing space with 12-13% market share, long standing relation with more than 2,400 well-known authors, strong brand equity built over eight decades and management pedigree acts as moat which we believe is difficult to break into. We believe recent correction in stock price (~53% since our last update) and valuations at 6.6x FY19E and 5.5x FY20E EPS make the stock attractive from long term. Maintain BUY with a TP of Rs400 per share (10x FY20E EPS of Rs40).

Growth guidance maintained: Management reiterated its top-line growth guidance of 13-14% along with EBITDA margin expansion in FY19E. Pre-stocking of paper inventory in an environment where paper prices are rising is a key margin lever.

Working capital cycle to ease out: Renegotiation of credit for certain bestsellers and initiation of dealer finance program should ease the working capital cycle by 15-20 days.

Digital venture to break-even: S Chand has invested ~Rs1.43bn in digital properties till date and in FY18 total loss was ~Rs70mn. Further investments are unlikely and the digital venture is expected to break even in 3-4 years.

Chetana acquisition to smoothen business volatility: Chetana's acquisition will smoothen business volatility as it is a state board player and derives 85-90% of revenue in 1Q as against revenue accretion of 75-80% in 4Q for S Chand.

Attractive valuations: S Chand is trading at 6.6x FY19E and 5.5x FY20E, in comparison to Navneet which is trading at 15.4x FY19E and 13.2x FY20E. We believe the current valuation gap should narrow given expected improvement in return ratios, margins and working capital cycle. Maintain BUY with a TP of Rs400.

Key takeaways from the meeting

Guidance remains intact: Management reiterated top-line growth guidance of 13-14% in FY19E aided by growth in higher education space due to realignment of portfolio (focus on volumes) and strong growth in the K-12 segment (mix of volume & price). EBITDA margins are likely to expand as paper inventory is stocked well in advance at a marginal hike of 4-5% YoY while paper prices are up by 10-15% as compared to the last sourcing cycle. Further, lower royalty payments due to higher share of in-house titles and consolidation of Chetana (EBITDA margin is in the range of 28-30%) will act as another margin kicker.

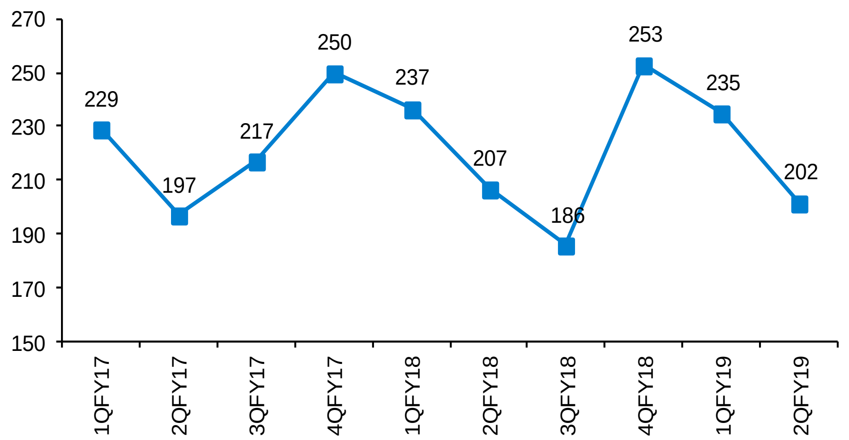
Exhibit 1: K12 segment to grow at a CAGR of 13.4% over FY18-20E

Particulars (Rs mn)	FY18	FY19E	FY20E
K-12	5,164	5,884	6,642
Higher Education	1,403	1,561	1,722
-Test Preparation	681	743	805
-College and University/ Technical and Professional	723	818	917
Early Learning	154	176	202
Miscellaneous Income	32	36	41
Chhaya	1,191	1,363	1,539
Chetana	-	-	750
Total Operating Revenue	**7,944**	**9,021**	**10,897**

Source: Company, PL

Working capital cycle to ease out: While working capital intensity will continue to remain high due to cyclical nature of the business with bulk of the sales happening in 4Q, the overall cycle should ease out by 15-20 days amid conscious efforts to reduce credit for bestselling titles & initiation of dealer finance program. In addition, initiating credit checks and giving preference to dealers with good pay cycle should further reduce working capital requirements.

Exhibit 2: Working capital appears stretched due to seasonality



Source: Company, PL

Digital investments to break even in 3-4 years: S Chand has invested ~Rs1.43bn in digital properties till date and in FY18 total loss was ~Rs70mn. Further investments are unlikely and the digital venture is expected to break even in 3-4 years. DS Digital, the interactive classroom business is already EBITDA positive

(Rs30mn). As volumes increase in the software business, it should break even. Under the Mylestone business (end to end curriculum for schools) the company is expecting tie-up with 300 schools in FY19E and breakeven is expected once 400 schools are empanelled. For test coach, online testing app, and Nuri Nori, pre-school education product, break-even will be achieved once S Chand hits 5,000 users and 100 schools respectively.

Exhibit 3: Digital business to turnaround in 3-4 years

Particulars (Rs mn) (FY18)	Sales	PBT	Tax	PAT
S Chand Edutech Pvt Ltd	0.55	(1.16)	-	(1.16)
Safari Digital Education initiatives Pvt Ltd	127.6	(41.2)	(26.2)	(15.0)
DS Digital Pvt Ltd	218.3	(59.1)	(29.7)	(29.4)

Source: Company, PL

Chetana acquisition to smoothen volatility and aid margins: In Aug 2018, S Chand entered into an agreement with Chetana publications to buy 51% stake in the latter for a consideration of ~Rs590mn. The balance 49% stake will be acquired over a period of time provided certain earning benchmarks are achieved in the interim. Transaction is expected to culminate by end of FY19 and will smoothen the business volatility as Chetana (state board player) derives 85-90% of revenue in 1Q as against revenue accretion of 75-80% in 4Q for S Chand. In addition, Chetana's acquisition will also drive profits as it has superior margin profile (EBITDA margin of 28-30% as compared to 24-25% for S Chand).

Attractive valuations: Post the recent correction in stock price (~53% since our last update) S Chand is trading at 6.6x FY19E and 5.5x FY20E, in comparison to Navneet which is trading at 15.4x FY19E and 13.2x FY20E. Overall, Navneet trades at 123% premium to S Chand on FY20E basis. We believe Navneet deserves to trade at a premium given 1) superior return profile 2) better working capital cycle 3) diversified business (~42% of the business is from stationery which lowers seasonality) 4) lesser regulatory hurdle/government interference. In the past, CBSE had come out with circulars emphasizing the use of NCERT textbooks as against private publishers' textbooks which can hurt players like S Chand unlike Navneet which is into state board supplementary books.

Exhibit 4: Comparative Valuation: S Chand trades at 57% discount to Navneet Education

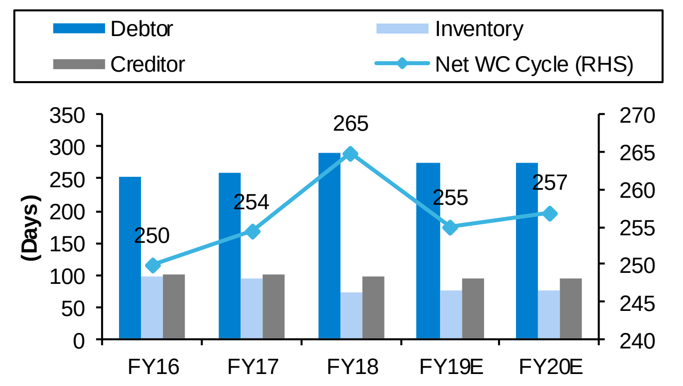
Company	Sales (Rs mn)			RoE (%)			RoCE (%)			Working capital cycle (days)			P/E (x)		
	FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E	FY18	FY19E	FY20E
S Chand	7,944	9,021	10,897	13.0	11.0	11.9	12.4	12.3	13.2	265	255	257	7.5	6.6	5.5
Navneet	12,040	13,690	15,278	17.6	20.8	21.6	23.8	25.1	25.9	203	190	188	20.3	15.4	13.2

Source: Company, PL

However, we believe that the current premium is unjustified and should narrow as return ratios of S Chand are likely to improve since the last two acquisitions (Chhaya & Chetana) are margin accretive. Further, return ratios in the past appeared muted due to goodwill creation (Rs3.3bn on acquisitions) and cash burning digital ventures (expected to break even soon). With improved cash generation, return ratios are expected to improve gradually. Even the working capital cycle and margins are likely to improve. We thus assign a P/E multiple of 10x to S Chand (we are valuing Navneet at 18x) and arrive at a TP of Rs400 per share. Maintain BUY.

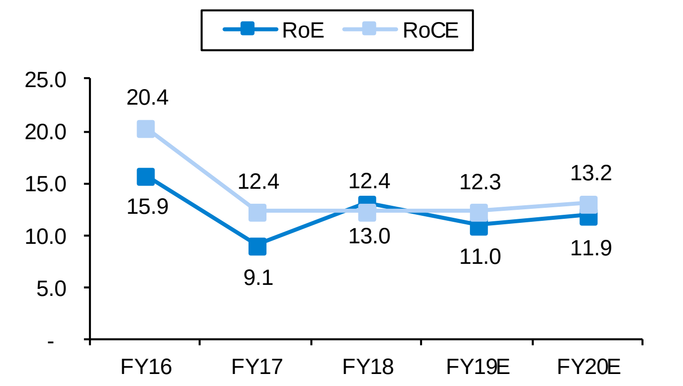
Story in Charts

Exhibit 5: High debtor day's stretches WC cycle



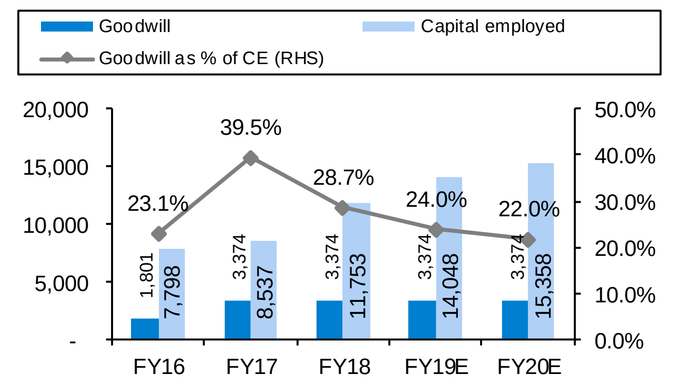
Source: Company, PL

Exhibit 6: Goodwill & digital losses dampen return ratios



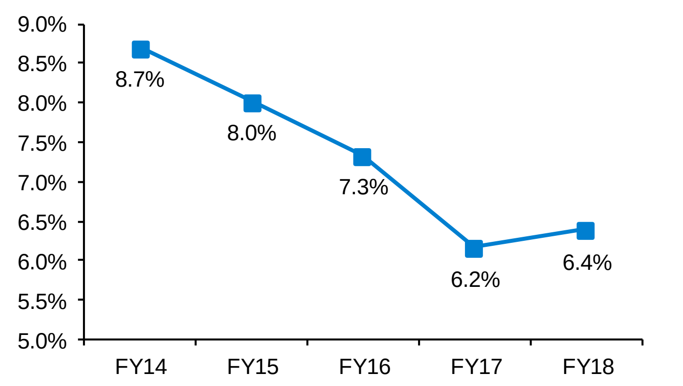
Source: Company, PL

Exhibit 7: Inorganic growth has led to creation of goodwill



Source: Company, PL

Exhibit 8: Royalty cost declines due to in-house title creation



Source: Company, PL

Financials

Income Statement (Rs m)

Y/e Mar	FY18	FY19E	FY20E	FY21E
Net Revenues	**7,944**	**9,021**	**10,897**	**12,210**
YoY gr. (%)	*20.5*	*13.5*	*20.8*	*12.1*
Cost of Goods Sold	3,245	3,613	4,347	4,867
Gross Profit	4,699	5,408	6,549	7,344
Margin (%)	*59.2*	*59.9*	*60.1*	*60.1*
Employee Cost	1,386	1,559	1,902	2,149
Other Expenses	650	767	926	1,038
EBITDA	**1,927**	**2,239**	**2,703**	**3,015**
YoY gr. (%)	*16.2*	*16.2*	*20.7*	*11.6*
Margin (%)	*24.3*	*24.8*	*24.8*	*24.7*
Depreciation and Amortization	193	224	263	289
EBIT	**1,734**	**2,015**	**2,440**	**2,726**
Margin (%)	*21.8*	*22.3*	*22.4*	*22.3*
Net Interest	240	291	364	379
Other Income	127	60	60	60
Profit Before Tax	**1,622**	**1,784**	**2,136**	**2,408**
Margin (%)	*20.4*	*19.8*	*19.6*	*19.7*
Total Tax	539	606	726	819
Effective tax rate (%)	*33.2*	*34.0*	*34.0*	*34.0*
Profit after tax	**1,083**	**1,177**	**1,410**	**1,589**
Minority interest	0	-	-	-
Share Profit from Associate	(12)	(12)	(12)	(12)
Adjusted PAT	**1,071**	**1,165**	**1,398**	**1,577**
YoY gr. (%)	*92.6*	*8.8*	*19.9*	*12.8*
Margin (%)	*13.5*	*12.9*	*12.8*	*12.9*
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	**1,071**	**1,165**	**1,398**	**1,577**
YoY gr. (%)	*92.6*	*8.8*	*19.9*	*12.8*
Margin (%)	*13.5*	*12.9*	*12.8*	*12.9*
Other Comprehensive Income	1	-	-	-
Total Comprehensive Income	1,072	1,165	1,398	1,577
Equity Shares O/s (m)	**35**	**35**	**35**	**35**
EPS (Rs)	**30.6**	**33.3**	**40.0**	**45.1**

Source: Company Data, PL Research

Balance Sheet Abstract (Rs m)

Y/e Mar	FY18	FY19E	FY20E	FY21E
Non-Current Assets				
Gross Block	**2,204**	**2,554**	**2,904**	**3,254**
Tangibles	1,307	1,657	2,007	2,357
Intangibles	897	897	897	897
Acc: Dep / Amortization	**436**	**659**	**922**	**1,211**
Tangibles	233	349	500	676
Intangibles	202	310	422	534
Net fixed assets	**1,768**	**1,895**	**1,982**	**2,043**
Tangibles	1,074	1,308	1,507	1,680
Intangibles	695	587	475	363
Capital Work In Progress	68	68	68	68
Goodwill	3,374	3,374	3,374	3,374
Non-Current Investments	338	1,543	1,548	1,553
Net Deferred tax assets	220	220	220	220
Other Non-Current Assets	135	135	135	135
Current Assets				
Investments	468	468	468	468
Inventories	1,562	1,854	2,239	2,509
Trade receivables	6,312	6,796	8,210	9,200
Cash & Bank Balance	665	1,084	925	1,383
Other Current Assets	134	134	134	134
Total Assets	**15,162**	**17,687**	**19,419**	**21,204**
Equity				
Equity Share Capital	175	175	175	175
Other Equity	9,822	10,918	12,228	13,718
Total Networth	**9,997**	**11,093**	**12,403**	**13,892**
Non-Current Liabilities				
Long Term borrowings	266	1,466	1,466	1,466
Provisions	-	-	-	-
Other non current liabilities	84	88	91	95
Current Liabilities				
ST Debt / Current of LT Debt	1,448	1,448	1,448	1,448
Trade payables	2,110	2,348	2,776	3,078
Other current liabilities	1,211	1,200	1,190	1,180
Total Equity & Liabilities	**15,162**	**17,687**	**19,419**	**21,204**

Source: Company Data, PL Research

Cash Flow (Rs m)

Y/e Mar	FY18	FY19E	FY20E	FY21E
PBT	1,622	1,784	2,136	2,408
Add. Depreciation	193	224	263	289
Add. Interest	225	291	364	379
Less Financial Other Income	127	60	60	60
Add. Other	(30)	(8)	(8)	(8)
Op. profit before WC changes	2,009	2,290	2,754	3,067
Net Changes-WC	(1,117)	(549)	(1,381)	(969)
Direct tax	(502)	(606)	(726)	(819)
Net cash from Op. activities	**389**	**1,135**	**647**	**1,280**
Capital expenditures	(397)	(350)	(350)	(350)
Interest / Dividend Income	-	-	-	-
Others	(214)	(1,205)	(5)	(5)
Net Cash from Invt. activities	**(610)**	**(1,555)**	**(355)**	**(355)**
Issue of share cap. / premium	3,318	-	-	-
Debt changes	(2,235)	1,200	-	-
Dividend paid	(44)	(70)	(87)	(87)
Interest paid	(225)	(291)	(364)	(379)
Others	(264)	-	-	-
Net cash from Fin. activities	**551**	**839**	**(452)**	**(466)**
Net change in cash	**329**	**419**	**(159)**	**459**
Free Cash Flow	(37)	785	297	930

Source: Company Data, PL Research

Quarterly Financials (Rs m)

Y/e Mar	Q3FY18	Q4FY18	Q1FY19	Q2FY19
Net Revenue	**461**	**2,511**	**189**	**131**
YoY gr. (%)	*7.4*	*22.0*	*(35.8)*	*(24.7)*
Raw Material Expenses	319	1,111	169	102
Gross Profit	143	1,401	20	29
Margin (%)	*30.9*	*55.8*	*10.5*	*22.0*
EBITDA	**(124)**	**1,084**	**(226)**	**(295)**
YoY gr. (%)	*(37.0)*	*(977.2)*	*(120.8)*	-
Margin (%)	*(26.8)*	*43.2*	*(119.7)*	*(226.1)*
Depreciation / Depletion	8	8	9	9
EBIT	**(132)**	**1,076**	**(235)**	**(305)**
Margin (%)	*(28.5)*	*42.8*	*(124.6)*	*(233.1)*
Net Interest	16	24	21	19
Other Income	56	109	46	41
Profit before Tax	**(92)**	**1,162**	**(209)**	**(283)**
Margin (%)	*(20.0)*	*46.3*	*(111.0)*	*(216.4)*
Total Tax	(35)	415	(69)	(103)
Effective tax rate (%)	*37.6*	*35.8*	*32.8*	*36.5*
Profit after Tax	**(58)**	**746**	**(141)**	**(180)**
Minority interest	-	-	-	-
Share Profit from Associates	-	-	-	-
Adjusted PAT	**(58)**	**746**	**(141)**	**(180)**
YoY gr. (%)	*(29.4)*	*29.4*	*78.0*	*76.2*
Margin (%)	*(12.5)*	*29.7*	*(74.6)*	*(137.4)*
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	**(58)**	**746**	**(141)**	**(180)**
YoY gr. (%)	*(29.4)*	*29.4*	*78.0*	*76.2*
Margin (%)	*(12.5)*	*29.7*	*(74.6)*	*(137.4)*
Other Comprehensive Income	2	1	-	2
Total Comprehensive Income	**(56)**	**747**	**(140)**	**(178)**
Avg. Shares O/s (m)	35	35	35	35
EPS (Rs)	**(1.7)**	**21.4**	**(4.0)**	**(5.1)**

Source: Company Data, PL Research

Key Financial Metrics

Y/e Mar	FY18	FY19E	FY20E	FY21E
Per Share(Rs)				
EPS	30.6	33.3	40.0	45.1
CEPS	36.1	39.7	47.5	53.3
BVPS	285.8	317.1	354.6	397.2
FCF	(1.1)	22.4	8.5	26.6
DPS	1.5	2.0	2.5	2.5
Return Ratio(%)				
RoCE	12.4	12.3	13.2	13.4
ROIC	9.0	8.9	9.4	9.7
RoE	13.0	11.0	11.9	12.0
Balance Sheet				
Net Debt : Equity (x)	0.1	0.1	0.1	0.1
Net Working Capital (Days)	193	180	182	183
Valuation(x)				
PER	7.2	6.6	5.5	4.9
P/B	0.8	0.7	0.6	0.6
P/CEPS	33.9	37.2	44.5	50.0
EV/EBITDA	4.3	4.1	3.4	2.9
EV/Sales	1.0	1.0	0.8	0.7
Dividend Yield (%)	0.7	0.9	1.1	1.1

Source: Company Data, PL Research

Analyst Coverage Universe

Sr. No.	CompanyName	Rating	TP (Rs)	Share Price (Rs)
1	Dish TV India	NR	-	74
2	Entertainment Network (India)	BUY	836	635
3	Music Broadcast	BUY	394	328
4	Navneet Education	BUY	150	111
5	Zee Media Corporation	BUY	39	26

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Buy : > 15%
Accumulate : 5% to 15%
Hold : +5% to -5%
Reduce : -5% to -15%
Sell : < -15%
Not Rated (NR) : No specific call on the stock
Under Review (UR) : Rating likely to change shortly

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