ANANDRATHI

India I Equities

Education
Result Update
Change in Estimates ☑ Target ☑ Reco ☐

12 November 2012

TreeHouse Education and Accessories

Robust revenue and other income; Buy

Rating: **Buy**
Target Price: ₹260
Share Price: ₹228

TreeHouse Education and Accessories' (Treehouse) 2QFY13 revenue grew 62% yoy. EBITDA margin was down ~600bps yoy and net profit was at ₹99m (+88.4% yoy, +23.8% qoq) led by strong revenues and high other income. It added five new centres during the quarter. We raise our target price to ₹260 and maintain Buy on the stock.

- **2QFY13 result highlights.** Treehouse registered 2QFY13 revenue of ₹283m (+61.6% yoy; +2.7% qoq). EBITDA margin was at 54.9%(-603bps yoy; -248bps qoq), while net profit stood at ₹99m (+88.4% yoy; +23.8% qoq). Other income was ₹32m (+394%yoy; +240%qoq).
- **Centre update.** The company added five new centres this quarter, taking the total to 309. Of these, 243 are own, while 66 are franchised. The company has maintained that it will open 75 own centres by FY13 end.
- **Management guidance.** 1) TreeHouse has already started admission for academic year 2013-14 and is seeing good traction; 2) it has 21 K-12 schools operational and expects to set-up 3 more by 2015, to a total 25.
- **Change in estimates.** While our top-line estimates are intact, we are revising our EBITDA estimates upwards by 19% and 18% for FY13 and FY14, respectively, primarily because margins have sustained above 53% (above our expectations of 46%) owing to good capacity utilization. We also raise our FY13 and FY14 adj. PAT estimates 4.5% and 3.1% respectively.
- **Valuation.** We increase our target price on the stock to ₹260, using the DCF-based method. At this target, the stock would trade at PE of 18x FY14e and 11x FY15e earnings. **Risks. A**vailability of skilled manpower; geographical concentration, regulatory risks for the K-12 segment.

Key data	THEAL IN / THEA.BO
52-week high / low	₹259 / ₹140
Sensex / Nifty	18684 / 5686
3-m average volume	US$0.1m
Market cap	₹7.6bn / US$139.7m
Shares outstanding	33.71m

Shareholding pattern (%)	Sep '12	Jun '12	Mar '12
Promoters	29.60	29.60	29.60
- of which, Pledged	-	-	-
Free Float	70.75	70.40	70.40
- Foreign Institutions	4.88	2.92	2.56
- Domestic Institutions	7.23	7.41	7.30
- Public	58.64	60.07	60.54

Estimates revision (%)	FY13e	FY14e	FY15e
Sales	0.4	1.5	-
EBITDA	18.8	17.7	-
EPS	4.5	3.1	-
Target multiple (x)	-	-	-

Consol. financials (YE Mar)	FY13e	FY14e
Sales (₹m)	1,135	1,732
Net profit (₹m)	318	494
EPS (₹)	9.4	14.6
Growth (%)	46.6	55.5
PE (x)	23.8	15.3
PBV (x)	2.7	2.3
RoE (%)	11.7	16.1
RoCE (%)	16.8	22.6
Dividend yield (%)	0.4	0.4
Net gearing (%)	4.5	(4.2)

Source: Anand Rathi Research

Quarterly results (YE Mar)	2QFY12	2QFY13	% yoy	1HFY12	1HFY13	% yoy
Sales (₹m)	175	283	61.6	338	558	65.3
EBITDA (₹m)	107	155	45.6	201	313	55.8
EBITDA margin (%)	60.9	54.9	(603)bps	59.5	56.1	(344)bps
Interest (₹m)	16.20	16.70	-	28	33	-
Depreciation (₹m)	23	32	42.0	28	63	124.0
Other income (₹m)	14	32	127.3	12	41	235.2
PBT (₹m)	85	138	63.1	157	258	64.5
Tax (₹m)	23	39	65.4	52	79	51.3
Tax rate (%)	27.7	28.0	38bps	33.1	30.4	(267)bps
Consolidated PAT (₹m)	53	99	88.4	105	180	71.1

Source: Company

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Quick Glance – Financials and Valuations

Fig 1 – Income statement (₹m)

Year-end: Mar	FY11	FY12	FY13e	FY14e	FY15e
Net revenues	392	772	1,135	1,732	2,518
Revenue growth (%)	83.6	96.8	47.0	52.6	45.4
- Op. expenses	223	352	523	807	1,177
EBIDTA	**169**	**420**	**612**	**925**	**1,341**
EBITDA margin (%)	43.1	54.4	53.9	53.4	53.3
- Interest expenses	12	65	67	60	47
- Depreciation	40	78	121	142	161
+ Other income	19	39	50	14	25
- Tax	44	99	156	243	382
Effective tax rate (%)	32.5	31.4	33.0	33.0	33.0
Reported PAT	92	217	318	494	776
+/- Extraordinary items	-	-	-	-	-
+/- Minority interest	-	-	-	-	-
Adjusted PAT	92	217	318	494	776
Adj. FDEPS (₹/share)	3.8	6.4	9.4	14.6	23.0
Adj. FDEPS growth (%)	156.5	67.9	46.6	55.5	57.2

Source: Company, Anand Rathi Research

Fig 2 – Balance sheet (₹m)

Year-end: Mar	FY11	FY12	FY13e	FY14e	FY15e
Share capital	240	337	337	337	337
Reserves & surplus	986	2,227	2,505	2,959	3,695
Net worth	1,226	2,564	2,842	3,296	4,032
Minority interest	-	-	-	-	-
Total debt	466	515	515	415	315
Def. tax liab. (net)	18	33	33	33	33
Capital employed	**1,711**	**3,112**	**3,390**	**3,744**	**4,380**
Net fixed assets	1,288	1,566	1,669	1,720	1,908
Investments	26	312	250	250	250
- of which, Liquid	26	250	250	250	250
Net working capital	117	757	1,333	1,472	1,749
Cash and bank balance	279	477	138	302	473
Capital deployed	**1,711**	**3,112**	**3,390**	**3,744**	**4,380**
Net debt	161	(212)	127	(137)	(408)
WC days	109	381	429	310	254
Book value (₹/sh)	51.1	76.0	84.3	97.8	119.6

Source: Company, Anand Rathi Research

Fig 3 – Cash-flow statement (₹m)

Year-end: Mar	FY11	FY12	FY13e	FY14e	FY15e
PAT	92	217	318	494	776
+ Non-cash items	54	93	121	142	161
Cash profit	146	309	438	636	936
- Incr./(Decr.) in WC	45	640	577	138	277
Operating cash-flow	101	(330)	(138)	497	659
- Capex	693	356	223	193	348
Free cash-flow	(591)	(686)	(361)	304	311
- Dividend	-	39	39	39	39
+ Equity raised	437	1,160	(0)	0	0
+ Debt raised	346	49	-	(100)	(100)
- Investments	16	285	(62)	-	-
- Misc. items	-	-	-	-	-
Net cash-flow	175	198	(339)	164	171
+ Op. cash & bank bal.	103	279	477	138	302
Cl. cash & bank bal.	279	477	138	302	473

Source: Company, Anand Rathi Research

Fig 4 – Ratio analysis @ ₹224

Year-end: Mar	FY11	FY12	FY13e	FY14e	FY15e
CEPS (₹/share)	5.5	8.7	13.0	18.8	27.8
Cash / (debt) (₹/share)	(6.7)	6.3	(3.8)	4.1	12.1
P/E (x)	58.5	34.9	23.8	15.3	9.7
P/B (x)	4.4	2.9	2.7	2.3	1.9
P/C (x)	40.9	25.6	17.2	11.9	8.1
EV/sales (x)	19.7	9.8	7.0	4.4	2.9
EV/EBITDA (x)	45.8	18.1	13.0	8.3	5.5
EBIT/sales (%)	37.9	49.3	47.7	46.0	47.9
Sales/average CE (x)	0.3	0.3	0.4	0.5	0.6
Adj.RoCE (%)	11.8	16.0	16.8	22.6	29.9
Avg. CE/ avg. eq. (x)	1.3	1.3	1.2	1.2	1.1
PBT/EBIT (x)	0.9	0.8	0.9	0.9	1.0
PAT/PBT (x)	0.7	0.7	0.7	0.7	0.7
Adj.RoE (%)	9.6	11.4	11.7	16.1	21.2
Dividend yield (%)	-	0.4	0.4	0.4	0.4

Source: Company, Anand Rathi Research

Fig 5 – Valuation chart (EV/EBITDA)

Source: Bloomberg, Anand Rathi Research

Fig 6 – Revenue break-up

Source: Company, Anand Rathi Research

Results Review

Treehouse registered 2QFY13 revenue of ₹283m (+61.6% yoy; +2.7% qoq). EBITDA margin came in at 54.9%(-603bps yoy; -248bps qoq). Consolidated net profit, at ₹99m (+88.4% yoy; +23.8% qoq).

Revenue analysis

- 2QFY13 revenue was ₹283m +61.6%yoy; +2.7% qoq.
- Company saw addition of 5 centres (3 owned and 2 franchised), taking the total number of centres to 309, of which, 243 (79%) are owned.
- Management has retained its guidance of setting up 75 new centres in FY13 and expects to setup the same in 2HFY13.

EBITDA margin

EBITDA was ₹155m (+45.6% yoy; -1.7% qoq), while margin was at 54.9%(-603bps yoy; -248bps qoq), chiefly due to higher SG&A (204bps qoq) and operating costs (437bps qoq). However, the same was partially compensated by lower personal cost (37bps yoy).

Non-operating items

Other income – Other income was ₹32m (+394%yoy; +240%qoq).

Effective tax rate – The tax rate was 28%.

Net profit growth

Consolidated net profit came in at ₹99m, +88.4% yoy and +23.8% qoq.

Fig 7 – Quarterly details

(₹m)	2Q12	3Q12	4Q12	1Q13	2Q13
Net Sales	163	175	213	221	275
Growth % – yoy	-	-	-	-	69.3
Growth % – qoq	-	7.6	21.7	3.9	24.3
EBITDA	94	107	110	109	158
EBITDA margin (%)	58.1	60.9	51.7	49.2	57.4
Growth % – yoy	-	-	-	-	67.3
Growth % – qoq	-	12.9	3.3	(1.0)	44.9
PBT	77	80	85	74	120
Taxes	25	27	23	24	40
Consolidated PAT	-	-	-	-	53.6
Growth % – yoy	-	1.0	16.1	(17.3)	58.5
Growth % – qoq	2.1	1.6	1.8	1.5	2.4
EPS (₹)	163	175	213	221	275

Source: Company

Other points

- Total staff strength is at 1,450 (+130), of which, teaching staff is 1,379.
- Due diligence of MT Educare's six pre-school centres is done and the transaction will be completed by 3QFY13.
- Company has started admission for academic year 2013-14.
- Company currently operates 21 K-12 schools in 3 states and wants to expand the same to 25 in next 2-3 years.

Change in estimates

We raise our FY13e and FY14e EPS 4.5% and 3.1% to ₹9.4 and ₹14.6, respectively. We increase our target price to ₹260 and retain Buy.

Major estimate changes

While our top-line estimates are intact, we are revising our EBITDA estimates 19% and 18% for FY13 and FY14, respectively, primarily because margins have sustained above 53% (above our expectations of 46%). Management is able to achieve the same due to better capacity utilization. We also raise our FY13 and FY14 adjusted PAT estimates 4.5% and 3.1%, respectively.

Fig 8 – Change in estimates

	FY13e			FY14e		
(₹m)	Previous	Revised	% chg	Previous	Revised	% chg
Sales	1,130	1,135	0.4	1,706	1,732	1.5
EBITDA	515	612	18.8	786	925	17.7
EBITDA margin (%)	45.6	53.9	835bps	46.1	53.4	735bps
Consolidated PAT	304	318	4.5	479	494	3.1
FDEPS (₹)	9.0	9.4	4.5	14.2	14.6	3.1

Source: Anand Rathi Research

Valuation

We increase our target price on the stock to ₹260, using DCF-based method. At this target, the stock would trade at PE of 18x FY14e and 11x FY15e earnings (fig 9).

Risks

- **Geographical concentration.** Most of the company's operations are centered in Mumbai (over 115 of the centers it runs are in the city). Hence, any disruption in operations or competition would significantly cut into its overall operations. The company is aware of this and has entered new markets: Kolkata (20 centers), Nagpur, Ranchi and Guwahati.
- **Attrition.** Attrition in the senior management/content/teaching team could hit the business. While senior members of the team are already holding shares, management is keen in issuing ESOPs to employees at lower levels as well.
- **Regulatory risk for formal education.** Any changes in regulatory norms for formal education (K-12) may significantly impact earnings.

Fig 9 – DCF-based valuation

Year-end: Mar	FY12	FY13e	FY14e	FY15e	FY16e	FY17e	FY18e	FY19e	FY20e	FY21e	FY22e	FY23e
FCFF												
Revenues (₹m)	772	1,135	1,732	2,518	3,471	4,699	6,244	8,140	10,409	13,050	16,034	19,301
Growth (%)	96.8	47.0	52.6	45.4	37.9	35.4	32.9	30.4	27.9	25.4	22.9	20.4
EBITDA (₹m)	420	612	925	1,341	1,814	2,409	3,138	3,969	4,919	5,939	7,017	8,108
Margins (%)	54.4	53.9	53.4	53.3	52.3	51.3	50.3	48.8	47.3	45.5	43.8	42.0
Depreciation/amortisation (₹m)	78	121	142	161	141	162	187	219	257	301	351	405
Interest expenses (₹m)	65	67	60	47	38	38	38	38	38	38	38	38
Other income (₹m)	39	50	14	25	25	25	25	25	25	25	25	25
PBT (₹m)	316	474	737	1,158	1,660	2,234	2,938	3,737	4,650	5,625	6,653	7,691
Tax (₹m)	99	156	243	382	548	737	970	1,233	1,534	1,856	2,196	2,538
PAT (before MI) (₹m)	**217**	**318**	**494**	**776**	**1,112**	**1,497**	**1,968**	**2,504**	**3,115**	**3,769**	**4,458**	**5,153**
Add: depreciation (₹m)	78	121	142	161	141	162	187	219	257	301	351	405
Add: interest*(1-tax rate) (₹m)												
Cash profit (₹m)	45	45	40	32	25	25	25	25	25	25	25	25
Increase/decrease in working capital (₹m)	**339**	**483**	**676**	**968**	**1,279**	**1,684**	**2,181**	**2,748**	**3,397**	**4,095**	**4,834**	**5,583**
Operating cash flow (₹m)	640	577	138	277	-1,559	67	85	104	124	145	164	179
Capex (₹m)	-300	-93	538	691	2,838	1,617	2,096	2,644	3,273	3,950	4,670	5,404
FCFF (₹m)	356	223	193	348	318	409	515	632	756	880	995	1,089
Less: interest*(1-tax rate) (₹m)	**-656**	**-317**	**344**	**343**	**2,520**	**1,207**	**1,582**	**2,012**	**2,517**	**3,070**	**3,675**	**4,315**
FCFE (₹m)	45	45	40	32	25	25	25	25	25	25	25	25
Year of discounting (no.)	**-701**	**-361**	**304**	**311**	**2,495**	**1,182**	**1,556**	**1,987**	**2,491**	**3,045**	**3,650**	**4,290**
Discounted FCFF (₹m)			1	2	3	4	5	6	7	8	9	10
Discounted FCFE (₹m)	**-656**	**-317**	**302**	**264**	**1,701**	**715**	**822**	**917**	**1,006**	**1,077**	**1,131**	**1,165**

Calculation WACC	
CMP (₹)	224
Equity (market cap) (₹m)	7,552
Debt (FY13e) (₹m)	515
Risk-free rate - Rf (%)	9.0
Rm - market return (%)	15.0
Beta (B)	0.9
Cost of equity (ke) (%)	14.4
Cost of debt (kd) (%)	12.0
Wd (%)	6.4
We (%)	93.6
WACC (%)	**14.0**
Growth rate (g) (%)	5.0
FCFF in 2023e (₹m)	4,315
Terminal value of firm (₹m)	2,879
Present value of terminal value(₹m)	777
NPV of FCFF (₹m)	7,704
Net debt (₹m)	-274
Intrinsic value (₹m)	8,755
Outstanding shares (no. m)	33.7
Value per share (₹)	**260**

Terminal growth (%) \ Cost of equity (%)	260	12.4	13.4	14.4	15.4	16.4
	3	284	266	249	234	220
	4	292	272	254	238	223
	5	301	279	260	243	227
	6	313	288	267	248	232
	7	330	301	276	255	237

Source: Company, Anand Rathi Research

Appendix

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	Date	Rating	TP (₹)	Share Price (₹)
1	29-Dec-11	Buy	225	168

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