



## “Educomp Solutions Limited Q2 FY11 Conference Call”

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**MODERATORS:** Mr. Shantanu Prakash – CEO -- Educomp Solutions Limited  
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**Moderator:** Ladies and gentlemen, good evening and welcome to the Q2 FY 2011 Results Conference Call of Educomp Solutions Limited hosted by Four-S Services Private Limited. As a reminder, for the duration of this conference, all participants' lines will be in the listen-only mode. And there will be an opportunity for you to ask questions at the end of today's presentation. If you should need assistance during this conference, please signal an operator by pressing '\*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Shantanu Prakash. Thank you. And over to you, sir.

**Shantanu Prakash:** Thank you. Good evening everyone. This is Shantanu Prakash; I am the CEO of Educomp Solutions and welcome to the Q2 FY11 earnings call. Joining me on this call are my colleagues Sangeeta Gulati, the Chief Financial Officer of the company, Mr. Sonjoy Mohanty, President, Corporate Affairs and Mr. Raman Bajaj, Vice President, Corporate Affairs.

We are very happy to share with you our numbers and outlook for the second quarter of the financial year FY11 ending on the 30<sup>th</sup> of September. The second quarter for us has been 'business as usual' and we have made good progress across all our businesses as we reach out to thousands of schools and millions of students to address their educational needs. Powered by an extremely enthusiastic and high quality management team, Educomp continues to make deep inroads into the education markets in India across its diverse businesses.

- Our digital content solutions business SmartClass where we continue to dominate the market with a near monopolistic leadership position, now reaches out to 4,585 private schools and 3.6 million students.
- Our K-12 schools business where we have rapidly become the No. 1 corporate player operating brick and mortar K-12 schools in the country with 46 schools operational and a hard visibility of 79 schools.
- Our higher education business where we have recently got the AICTE approval to launch Engineering and MBA programs and where we currently run 7 colleges across the country.
- Our vocational education business where we are fast moving towards leadership status in terms of the size of the network which has now crossed 275 training centers
- And finally, in our online and supplemental education business where we now have the largest e-learning footprint in India with a global scale of 2.5 million users of our various online learning portals.

Indeed, our strategy to emerge as an Education Ecosystem company with an end-to-end spectrum of education products and services is beginning to take very deep roots. We are now the only company in India and perhaps the world with a presence across the entire education life cycle and certainly the largest education company in India. I am happy to share that we are fully on track to meet our stated guidance for FY11 on both revenues as well as profits which is a top line of Rs.1300 to 1350 Crores and a bottom-line of Rs.330 to 335 Crores.

Before I announce the key financials of the business I want to take this opportunity to address some of the key points about our business, the vision, the sustainability of our model, as well as our evolving disclosure practices.

As you know, our new model in our key business SmartClass is a securitization led upfront sale model where we work with a consortium of banks. In the past we have had to provide a corporate guarantee for the entire value of the contract. It gives me great pleasure to share with you that we have now signed securitization contract with a reduction in corporate guarantee from 100% to 20%. This is a major milestone in the journey of SmartClass where we are one more step closer to separating the two key aspects of the SmartClass product which is supply of hardware and the supply of digital content. We are confident of the sustainability of the model as we are seeing high appetite from banks to fund this model. The reduction in corporate guarantee by 80% is a reflection of the robustness of the model. With this reduction we are now fully confident that the recourse to Educomp's balance sheet will **go away fully in due course**.

The other issue that I want to talk about is the concern over debtor days. We have given a detailed disclosure on debtor days in our investor update which should be in your hands where we have split the debtor days across our key businesses to give our investors a better understanding about the working capital requirements of our various businesses. We have given a detailed guidance on debtors, which are likely to happen in Q3 and Q4 of this financial year in the investor update. Broadly, we expect debtors of about 160 to 170 days on a sequential turnover basis which can broadly be divided into 90 to 95 days for SmartClass, 40 to 45 days for ICT, 15 to 20 days for K-12 Schools and 5 to 10 days for other businesses resulting in 160 to 170 days of total debtor days overall. As you would note, SmartClass debtor days are reducing sharply as a result of our securitization-led upfront sale model. In this model we do not receive the entire 75% amount of the contract value upfront but only receive approximately 54% in the first year. And the balance 21% is collected across a five-year period of the contract. The old BOOT contracts, transferred to the new model last year, also contribute to the debtor days because of the deferred second year revenue component. We estimate that by FY13 there will be no debtors because of the transferred contracts and the only debtors will be as a result of the 21% amount of the contract value which is collected across a five-year period and in line with the SmartClass business model.

As far as our corporate disclosures are concerned, I am happy to share that compared to every other listed education company worldwide we have perhaps the highest level of disclosure on all our businesses. The 45-page 2<sup>nd</sup> quarter investor update circulated a while ago, is testimony to our commitment toward best-in-class corporate governance in disclosure practices. We have disclosed various quality metrics about our SmartClass business, our ICT business and published the financial statements and balance sheet of all our key subsidiaries which are available on our web site. This will help our investors understand the various moving parts of the company and how we are performing.

I would like our investors to understand that in the past 18 months the company went through two key transitions. A) Change in the business model from BOOT that is *high CapEx* to a sale model that is *high Cashflow*. And secondly, our transition to becoming a core education infrastructure company which is involved in running pre-schools, high schools, colleges and vocational education centers. Any kind of change is difficult and we are fully cognizant that it might take our shareholders and investors a few quarters to fully understand the implications and the results of these changes. When we transitioned the business model in SmartClass, our objective was to become CapEx light, and Cashflow positive and to move away from providing non-core services such as maintenance and installation of hardware in schools. I am glad to mention that we have achieved all of this. The reduction in bank guarantees of securitization to 20% from 100% earlier is a big achievement and is a step towards bringing it down to zero. We have also become Cashflow positive on an operating basis as well as our focus now is entirely on building and licensing our intellectual property to schools rather than installation of hardware and maintenance of equipment.

If you look at our education infrastructure business, where we have invested over 1,350 Crores of our capital in our schools business, in building core capacity for education in the country, a typical infrastructure business has a gestation period after which it starts generating assured and annuity style cashflows. In our investor update we have provided our investors for their understanding, a detailed chart on how the margins and the return on capital employed of the schools business will look like after an initial gestation period of about two years. After this period of time, the schools will start generating an ROCE as high as 25% to 30%. This infrastructure that we are putting in place, the schools, the colleges, and the vocational training centers is not plain vanilla infrastructure. It is a unique infrastructure. While there maybe a large number of other infrastructure style companies in the power sector, in the road sector, in the real estate sector, etc. what Educomp is building is uniquely differentiative and extremely high value. It is branded as perpetual annuity, it is based on taking small amounts of money from a very large number of customers and has a very high component of intellectual property. We are building it in a scenario of shortages in schools capacity and in higher education capacity in India which may continue for several decades. We are now the No. 1 corporate player in K-12 schools in India with a visibility of 79 schools and multiple established brands in different price points in each segment of school education. This is quite an amazing achievement in a short period of three years. We are building similar value in our higher education and vocational education businesses about which I will talk more later.

Most significantly, while some of these high CapEx sectors of our business will take a few years to show up in our P&L, we are still able to generate a growth of 35% to 40% for our investments, both in profits as well as sales. And this is because of our very strong services side of our business where we continue to have market dominance in terms of product quality and the market penetration.

The value of what Educomp is building cannot simply be assessed by the quarterly results of this quarter simply on a Y-o-Y comparison with the last quarter. It has to be seen in a two years to three years context of what we are creating. Undoubtedly, both the K-12 schools as well as the higher education businesses are 25%+ ROCE businesses. We have put in over 1350 Crores in both these businesses. In a few years, our financials for these businesses are going to look very different compared to the strategic losses that we are incurring in these businesses today.

On a back-of-the-envelope calculation, Educomp will easily double our profits up till date simply with the existing footprints of schools and higher education in the next three years to five years even if we did no further expansion.

Our vision, however, is to become a key market participant in the education sector in India and thus far our management teams have executed flawlessly and we have achieved a leadership status across all sectors in which we operate. With the market where 140 million students still do not go to schools, shortage of over 200,000 schools, shortage of 1500 universities, impending launch of large scale public-private partnership programs driven by new legislation by the government such as the 'Right to Education', one of the lowest gross enrollment ratios in the world for higher education, a non-existent vocational training infrastructure and the creation of a new market coming up for e-learning based on the launch of 3G and wireless broadband, it is unlikely that Educomp is going to run out of customers very soon.

Let me now update you on the key financials of the second quarter. On a standalone basis, reported net income from operations for the quarter is 199.2 Crores compared to 206.9 Crores in the same period last year. On a consolidated basis reported net income from operations is 276.8 Crores compared to 253.5 Crores in the corresponding quarter last year. Since our business model change came into effect from FY10 onwards, these numbers do not reflect a like-to-like comparison and we have provided reconciled numbers in the investor update which is with you, which reflects the actual like-to-like growth in the business.

On a standalone basis, reconciled net income from operations for the quarter is 198.1 Crores, an increase of 43% over the corresponding period last year. While on a consolidated basis, the reconciled net income from operations for the quarter is 275.7 Crores, an increase of 49% over the corresponding period last year.

The reported profits before tax on a standalone basis is Rs. 80.9 Crores compared to 76.1 Crores in the same quarter last year. On a consolidated basis, the reported PBT is 72.3 Crores compared to 143.9 Crores in the same period last year. While the reconciled PBT on a standalone basis shows an increase of 49% over the corresponding quarter last year and the reconciled PBT on a consolidated basis shows an increase of again a 49% on a Y-o-Y basis.

Similarly, the reported PAT for the quarter on a standalone basis is 75.2 Crores, an increase of 49% over the same period last year. On a consolidated basis, the reported PAT is 57.8 Crores,

down from last quarter; this is due to the result of one-time profit recognition of Rs. 73 Crores as a result of sale of investment in vocational business to Pearson in Q2 of FY10.

Our earnings per share for the quarter is 7.88 basic and 7.15 diluted on a standalone basis, an increase of 47 and 40% respectively.

As you are seeing we have given a detailed note to arrive at a like-to-like comparison for the quarter in the investor update.

I will now go into the segmental overview. In the School Learning Solutions segment, our key business SmartClass continues to grow rapidly across private schools in the country across all tiers and locations. We have implemented a total of 5,309 classrooms across 664 schools this quarter taking the coverage to 4,585 schools and 3.6 million students. Q2 generally is a leaner quarter for us since the bulk of SmartClass orders come in the second half of the financial year in Q3 and Q4. Even in an otherwise lean quarter, we are happy to have added 5309 classrooms which takes the cumulative number of classrooms added in FY11 year-to-date to 12,069. With the inherent seasonality in this business, we are very comfortable to reach our stated guidance for the year which is 25,000 to 30,000 classrooms. The growth in SmartClass therefore continues unabated.

SmartClass had reported quarterly revenue of 150.05 Crores and an EBIT of 81.61 Crores. On a like-to-like basis, SmartClass revenue is up by 46% from 115.9 Crores in the second quarter of FY10 to 169.2 Crores in this quarter.

I am also happy to report that SmartClass pricing remains robust. With the average selling price per classroom for the quarter clocking in at Rs. 4.04 lakh though we estimate that the normal pricing for the product should stay in the range of about 3.9 lakh. We also do not see any material delinquency risk as we believe all receivables of SmartClass will be collected.

As far as margins are concerned, SmartClass has margins ranging from 37% to 45% for revenue recognized in year one and 82% to 91% for revenue recognized in year two, leaving a blended margin of 51% to 59% after taking into consideration sale, marketing and general administrative cost.

Let me now turn to our second business in the Schools Learning Solutions segment, the ICT business. In this business as you are aware, we are no longer gunning for market share, but we are more focused on profitability. Going by the fact that historically this business has had lower margins, delayed payments from government, and longer receivable cycles, we are continuing our strategy of only bidding for contracts where we can make good enough margins. As a result, we did not add any new school contracts to our ICT schools kitty in this quarter.

Our Preschools business is gradually becoming more and more mature. We are still the largest preschool company in the country with over 750 Preschools in our portfolio across two brands, Roots-to-Wings and Eurokids. Together we are addressing over 40,000 students in our preschools business.

The key business within our K-12 segment of course is the Educomp Infrastructure and School Management subsidiary. In a short period of time we have become the No. 1 corporate player in India operating a chain of brick and mortar K-12 schools with 46 operational schools and a visibility of 79 schools in the near future

Our K12 strategy is to cover the entire spectrum of customer segments at different price points and this strategy is evolving as planned. We now have an international curriculum school brand added to our portfolio called Le Mont High School which will be a premier IB curriculum school coming up in Lavasa in Maharashtra. This is geared to open up for the next academic term and will be one of the finest international schools in the country. In our K-12 business there is a 54% growth in revenue on a Y-o-Y basis.

In our Higher Education part of business which is a joint venture with Raffles Education Corporation of Singapore, while we continue our focus on design courses and where we have market leadership, I am happy to share that we have now received AICTE approval. AICTE is the regulator for technical education in India and we have received their approval to launch Engineering and PGDM programs starting from the next academic year at our Greater Noida campus which is fully up and running.

With the rapid opening up of the higher education space we are now gearing up to become a mainstream higher education player with the presence across all disciplines like engineering, management, design and commerce. .

Moving on now to the Vocational Education part of our business. IndiaCan, our joint venture with Pearson has been on a most phenomenal growth track. Indeed, one of the most exciting stories across the entire spectrum of products at Educomp. Since the joint venture was signed about five quarters back we now have over 275 points of presence across the country. Again, this is a unique business that spreads across customer segments and programs that cover a wide variety of vocations and employability skill sets. Our ETEN CA program is a leading such program for CA that is Chartered Accountancy coaching, in the country that uses Educomp's proprietary cutting edge VSAT technology to broadcast live lectures from the top faculty of the country to towns and cities all over. ETEN now has 115 operational centers and over 25,000 enrollments making us a clear market leader in this market in India. We have also launched pilots for civil services exams and the banking service exams. This business has a target of 40,000 enrollments overall by the year end.

The Purple Leap part of our Vocational Education business now has a network of 107 colleges, up from 95 in the last quarter and plans to reach 180 colleges this year targeting 14,000 students enrolled. Purple Leap has programs for Engineering and MBA students in place which makes them workplace-ready while they are still continuing their college degrees.

Our retail vocational centers business, the third part of our Vocational business now has a network of 55 centers, with courses in English language training, Sales, Retail as well as Media courses in partnership with NDTV in place.

Our partnership with Pearson who are world leaders in Vocational Education with strong IP across several vocations is growing very well and we believe we are building a unique Vocational business unlike any other in the country. As guided earlier, this business as well as the Raffles Higher Education business will continue to remain in investment mode for sometime. We also believe that the losses that we are incurring in these businesses are extremely low compared to the value that we are creating for our shareholders in these businesses for the future. The Higher Learning Solutions segment had quarterly revenues of 13.7 Crores, an increase of 123% over the corresponding quarter last year.

Finally, let me come to our last segment, Online Supplemental and Global which comprises of all our investments in the Online and Supplemental space as well as our two global subsidiaries. Our Supplemental Education strategy is to cater to all supplemental education needs of our customers as they continue to evolve. With the addition of Vidya Mandir Classes to our portfolio of investments, we now have a strong Test Prep franchise and along with LEAP, we plan to become India's largest VSAT-based IIT JEE coaching platform.

WizIQ.com, our portal for student-teacher exchange now has over 900,000 registered users. It is poised to cross ONE MILLION registered users in the current quarter. WizIQ now gets more than a million visits a month generating more than 3 million in monthly page views and is the world leader in its market segment. Learnhub now has over 450,000 registered users and Studyplaces, our other admissions advisory portal now has over 645,000 registered users. Learnhub and Studyplaces together have over an additional million registered users.

Educomp Online, our e-learning platform offering multimedia content, assessments and learning management systems for students, teachers, parents and schools, now has 52,000 students actively using the portal as well as 12,000 parents and 6,000 active teachers.

I am happy to share that we are now the largest e-learning footprint in India with over 2.5 million users of our various online educational properties and we are best placed in the country by far to take advantage of the rollout of 3G and wireless broadband solutions that our likely to come in over the next 12 to 18 months.

Finally, in our Global business, I am happy to share that Ask n Learn, our fully-owned subsidiary in Singapore has signed an exclusive licensing agreement with China Distance Education Holdings Limited, a leading provider of online education in China to distribute Educomp's SmartClass products in China. China represents a large and growing market opportunity for Educomp and we are very excited to partner in this important market with CDEL, the leading online education company in China.

I would like to end by summarizing where we have reached so far. We are India's largest education company reaching out to over 3.6 million students and over 4,500 private schools in SmartClass, 7.4 million students and almost 14,000 schools in ICT. We run 750 pre-schools, 46 high schools, 7 colleges and 275 vocational training centers with over 2.5 million users of our online education properties. Having achieved all of that, what excites our team the most is the belief that we are only getting started.

With that I will pause now and we will open for questions and answers.

**Moderator:** Thank you very much sir. The first question is from Sunil Tirumalai from Credit Suisse. Please go ahead.

**Sunil Tirumalai:** I have a few questions around the securitization. So you mentioned in the presentation about having securitized the receivables by 5<sup>th</sup> of October bringing down your DSO and also the 20% limit on the recourse due, I just want to understand does this hold for all the future contracts, and can we expect it go down to zero per cent at sometime?

**Shantanu Prakash:** Well, if you go back to what we have been saying for a long time. When we started off the securitization we had said that we need to give banks sometime to become comfortable with our model and once they do that the corporate guarantees will be brought down. We have met our promise to investors, they have come down from 100% to 20%, that is a reduction of 80%. We have several term sheets with us at the 20% level so we are generally confident that we will be able to maintain this as well as in the future we stand committed to the fact that eventually the corporate guarantees will go away entirely.

**Sangeeta Gulati:** Sunil, I just want to add one more thing. The reduction in the corporate guarantee is applicable on the new term sheet. So whatever term sheet we have already signed, that still stands at 100%, for example, the term sheet of Axis Bank. We might be talking to the bank for a review, that now, there is another bank who is giving us a 20% but as of now we have both term sheets, one with 100% corporate guarantee and the second one with 20% corporate guarantee.

**Shantanu Prakash:** And I have to state that we have availed our substantial amount of funding at 20% which is Rs. 3 billion.

**Sunil Tirumalai:** Okay. It is good that we have it for the Rs. 3 billion. I believe that is with respect to the securitization you did on 5<sup>th</sup> of October, but going forward would the new contracts be at 20%?

**Shantanu Prakash:** So the trend has already started. I mentioned, we have several other term sheets at 20%, I do not think that should be a problem as we go forward.

**Sunil Tirumalai:** Okay. My second question was regarding the overall model where Edusmart is involved. A year ago when we got into this model, you guys have said that you will develop an ecosystem of similar such players. But over the last one year we have not seen any other partner other than Edusmart coming up. They are a very important integral part of this business, their execution and their quality needs to be really good if in future we do not have any quality concerns and all that. So my worry is we are relying on one partner and I see that as a risk.

**Shantanu Prakash:** Sunil, if you recall we said that let this model be validated and we will have other vendors, we are in active discussions with few, watch us carefully and you will hear some news on that front also shortly.

**Sunil Tirumalai:** Okay. You made a note on the K-12 schools business about the variable rent of 4.5% will start from the fourth year, you mentioned it because of good corporate governance, I did not understand what you were trying to say?

**Shantanu Prakash:** No, that is a part of our model. Our model is that Educomp Infrastructure charges 14.5% on the capital it has deployed to build schools as well as in addition to that charges 4.5% of revenue which we charge from the fourth year onwards.

**Sunil Tirumalai:** Has it always been from the fourth year or is it a change that you have brought in now

**Shantanu Prakash:** Yes, it is always been like that. That is our standard model. So we have simply stated our model.

**Sunil Tirumalai:** Okay, sure. Thank you. I will come back for questions later.

**Moderator:** Thank you. The next question is from Mohit Jain from Alchemy. Please go ahead.

**Mohit Jain:** Hi, I have three questions; first on SLS, which sector contributed to SLS pricing improvement or margin improvement, although you mentioned that it is non-recurring in nature, but just wanted to understand that? Second, on the seasonality. Last year we did not see a dip in number of classrooms implemented in the second quarter, so what could be the potential sustainable level for classroom additions on a quarterly basis? And third, is it fair to assume that your FY12 margins for SmartClass could be around 60%?

**Shantanu Prakash:** Let me answer these questions. I will take the first question on classroom additions. If you look at our business historically, you can clearly see that Q1 and Q2 are generally leaner quarters, Q3

and Q4 are stronger quarters. This is a normal seasonality of our business. However, if we sign a very large number of contracts in Q4, and it is not possible for us to finish the implementation of these contracts in Q4, that spills over to Q1. So if we have a bumper Q4, our Q1 also looks better because all the contracts cannot be physically implemented in Q4 which is the reason that Q1 of this year we did 6,750 installations which is actually a spillover from Q4 of last year where we did 4,038 installations and typically we have noted that Q3 and Q4 will typically lead to about 60% to 65% of the entire sales of the year. So there is a distinct seasonality in our business. Again, in my speech just now I have reiterated that our guidance for 25,000 to 30,000 classrooms this year will be completely met because we have already achieved over 40% of our guidance of this year just in Q1 and Q2. Coming over to your other question on the SLS margins, could you explain that question, I was not able to understand what you meant by your first question on SLS?

**Mohit Jain:** Yeah, there was a pricing improvement which you mentioned that the sustainable level is 3.9 and not 4.03, so just wanted to understand which sector contributed to pricing improvement in this quarter?

**Shantanu Prakash:** Yeah, the pricing improvement is in SmartClass and this quarter the average selling price per classroom has improved over the last quarter, however, we have simply said as a word of caution that we expect the pricing in the future to remain in range so that investor expectations of price increase are not built in, this quarter the pricing was better than expected. In the next quarter it could be the same. It could be as much as it was in Q2, however, we are essentially saying that do not expect that this price increase is permanent, it should be normal, it should be 3.9, but this quarter we had a great quarter, our price was better.

**Mohit Jain:** Okay sure. And sir on FY12 margins for SmartClass?

**Shantanu Prakash:** We have not given any guidance for FY12 margins so far.

**Mohit Jain:** No, there is no guidance, but as per the note you ....

**Shantanu Prakash:** We do not see any reason why margins should deteriorate. Margins are a function of the selling price. Our selling price continues to be extremely robust. As I have just spoken, this quarter we had much better pricing so I think the customer is willing to pay us. We are increasing our pricing power in the market and margins are a function of price, so we see no real reason why FY12 margins would be any worse than FY11 margins in SmartClass.

**Sangeeta Gulati:** I just want to add few lines for you. We have actually explained our model on Slide #16 wherein the guidance is actually given for SmartClass. We have said that whenever we sign any new classroom under the securitization led sale model then in the first year there would be an EBIT of about 37% to 45% and the second year because of the deferment there will be an EBIT of 82% to 91%, so that means over a two year period, the blended margin will be 51 to 59%. And this is

what we have actually explained. So to calculate the profit for SmartClass for FY12, you can simply calculate the margins based on how many additions are there in FY12, take an average of anything between 37 to 45% then just add whatever is the deferment amount, take a margin of 90%, and you will be able to calculate your EBIT margins.

**Mohit Jain:** Okay. I simply take the weighted average which in my case comes closer to 60%.

**Sangeeta Gulati:** We definitely did around 58% to 60%; it will be coming to that you can take that average.

**Mohit Jain:** Okay sure. And one question on K-12, you have not given operational schools guidance but is it possible to give any indicative fees charged in operational schools so far and the average number of students in these schools?

**Shantanu Prakash:** As you can see we have many different brands of schools. We have listed out five different school brands. The pricing is different in each of these brands. It also varies from location to location. But by and large the pricing for a Millennium school is in the range of (depending on location) Rs. 3,500 to Rs. 5,000 a month, the co-branded schools again depending on location, and depending on the brand, could be between Rs. 4,000 to Rs. 8,000 a month, the Takshila pricing is between Rs. 1600 to Rs. 1800 a month per student, Universal Academy is between Rs. 800 to Rs. 1000 per student, the international school pricing is approximately 3.5 lakhs to 4 lakhs per annum.

**Mohit Jain:** Thanks, thanks a lot.

**Moderator:** Thank you. The next question is from Himanshu Gandhi from Hansberger. Please go ahead.

**Himanshu Gandhi:** Just wanted to understand a little bit on the K-12 schools, what is your strategy going forward, a lot of revenue stream coming out from them in the future years, so when you are saying 79 schools visibility, can you help us understand how many schools are going to be coming up in the next year or two, and how is the progress there?

**Shantanu Prakash:** When we say visibility it means that these schools are either currently under construction or the lands for these have already been acquired, in an earlier investor update we have said that we should achieve 60 plus Schools including Euro Schools getting into the next academic year and the balance schools will come up later. We continue to expand our schools portfolio. Our broader guidance is for doing 150 schools by FY13, so that is where we are really headed. Now, we have also launched our joint venture school model where the ROCE can be as high as 70% and going forward the joint venture schools, which are a more CapEx-light model, may also expand, thereby adding to the number of schools. But 79 is our hard visibility at this stage.

**Himanshu Gandhi:** Okay. And typically after removing the Edu Infra part of it, what is going to be the margins that we could look for probably three years after the school is opened?

- Shantanu Prakash:** So that has been provided in the investor update, let me draw your attention to Slide #21 of the investor update. I assume that when you say that you remove Educomp Infrastructure you are talking of the school at a trust level – the school level.
- Himanshu Gandhi:** Right.
- Shantanu Prakash:** School level, the EBITDA margins from year three onwards is in the range of approximately 50% to 60%, we have given that range for different models of schools, for instance, Millennium is 44% to 64% EBITDA, co-branded is 54% to 68% and so on. So those are the typical margins you should expect from the third year onwards. Broadly speaking, schools will lose money in the first year, they will achieve breakeven in the second year and from the third year onwards they will start generating profit, and at the EISML that is at the Educomp Infrastructure level, from third year onwards, the ROCE of the school will start at the level of 13% to 14% and over the years will go all the way up to 25% to 30% as the case maybe.
- Himanshu Gandhi:** Thank you sir. That is it from my side.
- Moderator:** Thank you. The next question is from Subhashini Gurumurthi from Ambit Capital. Please go ahead.
- Subhashini Gurumurthi:** I just had a couple of questions regarding SmartClass. Firstly, with regards to securitization I just wanted to know whether all the banks under the consortium have agreed to the new funding of 20%?
- Shantanu Prakash:** As Sangeeta has just explained to you our new funding is at 20%, the existing funding limit which have been taken earlier are still at 100%, in future attempt will be to do all funding at 20%, we have several other term sheets at 20% level which are under discussions, apart from the funding that we have just taken.
- Subhashini Gurumurthi:** So is this agreement restricted to a single bank right now and you expect that probably later on other banks will take it?
- Shantanu Prakash:** Indeed. The current funding of Rs. 3 billion is from a single bank but we expect other banks to also follow suit for which we are already discussing term sheets from other banks.
- Subhashini Gurumurthi:** Sure. Right now, what is the kind of funding we have tied up for and how much of it has been availed, if you can give us those figures?
- Sangeeta Gulati:** If you recall that we informed in Q4 of last year that we already have got a term sheet for 500 Crores. That 500 Crores has not been availed in full and we have only availed 250-odd Crores, and the remainder 250 Crores is still pending. That means whenever we give more contracts to the bank, the bank will securitize and we will be able to receive our 250 Crores. This is one and

secondly, this 3 billion funding, which is separate, this is in addition to the previous limit. We are also talking to the consortium of bankers and even independent bankers for giving us similar facilities on a debt of 500 Crores to 1000 Crores. Because we are estimating only for a year. For example, next year whatever guidance will be there, we will be having the limit at the start of the year to the amount of maybe 700 to 800 Crores so that as and when we sign new contracts we have the bank funding in place.

**Shantanu Prakash:** So the short answer to your question is that we anticipate no problem in the bank funding, the bankers are very enthusiastic about the market.

**Subhashini Gurumurthi:** Sure. Just one more question, with regards to the restatement on BOOT basis that you explained in Slide #8, just wanted to understand how is the 127 Crores revenue derived, how is the addition derived, if you can just explain it to me?

**Shantanu Prakash:** We will prefer to explain that on a one-on-one call because there are about 200 investors in this call and that would take a little time to explain.

**Subhashini Gurumurthi:** Sure, just one last question. What was the export revenues which were booked in SmartClass this quarter?

**Shantanu Prakash:** Nil.

**Subhashini Gurumurthi:** Okay. Sure. Thanks, that is all from my side.

**Moderator:** Thank you. The next question is from Pratish Krishnan from Bank of America Merrill Lynch. Please go ahead.

**Pratish Krishnan:** My question is on the K-12 business, just wanted to understand the management view in terms of the overall share of the dry management business. It seems like your capital deployment continues to be very high, whereas the intent was to have nearly 50% of these schools in the dry management side.

**Shantanu Prakash:** Pratish, we are moving rapidly on the JV and dry management side as well. And between now and June of next year you will see a large number of dry management deals that we will put into place. We like the joint venture and dry management model a lot. But we also are not shy of investing our own capital in setting up the schools. It is a great business to be in, given the financial characteristics of the business, so we will continue both these models. The joint venture/ dry management model is also linked to how many of our own schools are in place and how famous our brands are and you will be happy to know that some of our brands like Millennium in their respective towns and cities are already counted as one of the top three or top five schools in most of these places. And these brands are becoming famous because we have taken the proactive steps of having invested in the brands at the right period of time so the

answer is yes, we are continuing on joint venture model, we are getting a good traction there. But we are also continuing to build these schools on our own and given the large potential of opening schools in India and the response that we have got, some of the schools that we opened three years back are running to over 100% capacity for us and every single seat is sold out. So given our experience in running these schools and the good experience that we have had we believe that the scale that we have achieved is just a very small fraction of what is possible to achieve in this particular business so we will continue to invest for some period of time but simultaneously our joint ventures will also start kicking in.

- Pratish Krishnan:** Sure, and the balance sheet during the first half the CapEx was around 300 Crores. Is this substantially towards the K-12 side or are there other businesses also which you are funding?
- Shantanu Prakash:** No, its substantially for K-12.
- Pratish Krishnan:** So the 33 schools guidance, you have given the number, are those different, I am not able to correlate both of them?
- Shantanu Prakash:** I am not able to understand your question?
- Pratish Krishnan:** If you look at the CapEx last year in terms of the K-12 business, it was around 400 Crores and there is probably additional 300 Crores in this first half?
- Shantanu Prakash:** Yes, capital gets spent in the first half and the schools open up in Q3 and Q4 so the capital is generally front-loaded in the first half of the year and as far as the number of the school visibility is concerned, that has also gone up from last quarter. Now we have 79 schools visible.
- Pratish Krishnan:** Okay sure, we will take this offline.
- Shantanu Prakash:** We are investing in either acquiring land or additional construction and so on.
- Pratish Krishnan:** And second, any reasons for the loans and advances to have doubled since the start of the year?
- Sangeeta Gulati:** Are you talking about the loans and advances which we have given?
- Pratish Krishnan:** Yeah. I mean if you look at the March 2010 number which was I think 180 Crores it's moved to more than 350 Crores?
- Sangeeta Gulati:** Yeah, let me bring up the detail right away in front of me.
- Pratish Krishnan:** Yeah, fine, and lastly in terms of the supplemental business, in which we did see a profit this quarter, is this one-off or I mean should we assume that probably lots of spill will come back?

- Shantanu Prakash:** Well supplemental education is being built and I think generally speaking in each quarter the performance should be better than the performance in the last quarter. I don't see any major one-off events this quarter that have resulted in a profit.
- Sangeeta Gulati:** Okay, I think you are talking about the increase in loans and advances by 146 Crores?
- Pratish Krishnan:** Yeah, that is right.
- Sangeeta Gulati:** On 31<sup>st</sup> March 2010 it was 181 crores, on 31<sup>st</sup> mar 2009 it was 27 crores thereby leading to a jump of 146 crores. Advances have been given to the vendors in Edu Infra for land buying and for construction
- Pratish Krishnan:** Sorry, you mean to the trust?
- Shantanu Prakash:** Yeah. It's only to the trust; the advances are being given by Edu Infra to various vendors.
- Pratish Krishnan:** Okay, fine yeah, thanks a lot.
- Moderator:** Thank you. The next question is from Mohit Jain from Alchemy, please go ahead.
- Mohit Jain:** Thanks for taking my question again. I have two more questions. First is in Edu Reach. Any guidance for Edu Reach would be helpful. What should we expect going forward? In terms of the revenue or the marginal growth and then anything on the margin would be helpful. The second is the online and supplemental business, in this what is the customer profile and how do you plan to charge the customers?
- Shantanu Prakash:** Well let me first talk about the online and supplemental business. Our online and supplemental business consists of many different products. All are focused on extracting the supplement part of the value from the customer **wallet**. For instance, we own Vidya Mandir Classes which is one of the premier IIT JEE Test Prep company. We own Learnhub and Studyplaces which is our Admissions Advisory business. Then in the supplemental space we have LEAP which is a VSAT delivered program. Then we have a career counseling, we have EduIgnite. And so on. So we have many different parts of the supplemental business and they all have different business models of their own so there is no one single model. What we aim to do is since Educomp has a very large base amongst schools we are reaching to almost 4 million students just in the smartclass schools and we have great influence in these schools. We hope to use some of that to get students for our online and supplemental business. So that is one part of the answer now coming back to you're the other question sir, could you repeat the other question again please?
- Mohit Jain:** Any guidance on Edu Reach would be helpful. You mentioned that you will go towards higher margin or better margins business.

**Shantanu Prakash:** No, we are being very picky and choosy about the ICT contracts, which is why in this quarter we have not picked up any fresh government contracts. We believe that we have better avenues for deploying our capital now in other parts of our business which have much better ROCE and build more lasting value. Having said that, we have still remained a strategic participant in this space. We will participate in contracts, which give us margins in excess of 30% EBIT, but this will be something that will be difficult to predict as to how many new contracts we will be able to achieve during the year. Hence, for the ICT revenues you should take the base of where we are today and probably add marginal or modest growth in the business. However, if we manage to get a big one-off contract from any of the state governments that could pull up the revenue of ICT but as such we don't have any robust scientific guidance on ICT because it really depends on how some of the tenders work out for us.

**Mohit Jain:** So lumpiness will continue?

**Shantanu Prakash:** Yeah, lumpiness should be expected in that business.

**Mohit Jain:** And coming back to the online and supplemental business, if I have to include online initiatives do you charge your customers or do they get to access your website free once they are into the smartclass platform or any other product?

**Shantanu Prakash:** Yeah, if you take Educomp Online for instance, that is presently free. We are building the base and once we launch the 3G and the wireless broadband products, we will start charging for it. In websites such as WizIQ, where we have close to a million registered users, we do have a revenue model in place there where some of the users who want to avail a more premium service, pay for it but by and large from our online services our revenues currently are non material.

**Mohit Jain:** Okay, and once 3G comes are you planning to charge for mobile applications?

**Shantanu Prakash:** We have a very interesting strategy for 3G and wireless broadband which we would like to share with you in the next earnings call.

**Mohit Jain:** Sure, thanks a lot and all the best.

**Moderator:** Thank you, the next question is from Swati Nangalia from IDFC Securities please go ahead

**Nikhil Vora:** Hi, this is Nikhil Vora just one clarification on the Edu Smart part of the business. Is it likely that the redeemable NCPS will also get ready in the near term or it will continue? What's the tenure of the instrument in that?

**Shantanu Prakash:** Yeah, it will be typically redeemed after five years. That will stay for five years.

**Nikhil Vora:** Okay.

**Shantanu Prakash:** As you see this is as part of the terms of the initial securitization and it is a pretty small amount it is a non-material amount.

**Nikhil Vora:** So now Edu Smart can pretty much fund itself out?

**Shantanu Prakash:** Yeah, that is the way it is.

**Nikhil Vora:** Okay, cool, my other questions are answered, so thanks so much.

**Moderator:** Thank you. Ladies and gentlemen that was the last question. I would now like to hand over the conference back to Mr. Shantanu Prakash for closing comments.

**Shantanu Prakash:** Thank you. We would like to thank everyone who attended our earnings call tonight. Thank you very much and good night.

**Moderator:** Thank you very much. On behalf of Four-S Services Private Limited that concludes this conference call. Thank you for joining us and you may now disconnect your lines. Thank you.