



“Educomp Solutions Limited”

November 09, 2012



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Moderator: Ladies and gentlemen, good day and welcome to the Educomp Solution's Q2 FY'13 earnings conference call, hosted by IDFC Securities. 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. Should you need assistance during this conference call, please signal an operator by pressing "*" followed by "0" on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Nikhil Vora from IDFC Securities. Thank you and over to you Sir.

Nikhil Vora: Thanks Melissa. Welcome everyone to this Q2 FY'13 earnings conference call for Educomp Solutions. We have with us the senior management team of Educomp, represented by Shantanu Prakash, Chairman and Managing Director, Sanjay Jain, Group CEO, Abhinav Dhar, Executive Director and Ashish Gupta, Senior VP Finance. I will hand it over to Shantanu and Sanjay to make the opening remarks and then open the floor for Q&A. Over to you Shantanu.

Shantanu Prakash: Thank you Nikhil. Good evening everyone. Welcome to Educomp's Q2 Earning Call of the financial year FY'13. We are very happy to share with you our numbers for the second quarter FY'13 ending September 30, 2012. As you are aware, this is a year of consolidation for us and we have embarked upon several important initiatives to streamline our operations, increase efficiency and productivity with a very clear focus on strengthening our balance sheet and becoming free cash flow faster.

I am happy to share with you, that we have started off very well and are already making good progress on all fronts. The key message that I want to share with you for today's call is that over the next few quarters just as we have been working over the past few quarters, we will continue to work tirelessly on internal operations, processes, controls, improve our IT systems backbone and develop a sharper focus on our bottomline rather than focusing primarily on topline and last but not the least improve our working capital management.

This quarter we are also witnessing some very interesting positive trends in our flagship SmartClass business, which augers well for the business in the future especially the rise in average price per classroom, increase in the number of classrooms per school and the impending launch of two new products from Educomp; that is our language lab and the tablet PC.

I will come back and talk more about this in detail and the future outlook for the company, but first, I will request Sanjay Jain, to share with you the detailed financial highlights of the quarter.

Sanjay Jain: Thank you Shantanu. Good evening everyone. Good morning to our investors in North America. I am happy to share with you the detailed performance of the Company in the Q2 of financial year 2012-13. I am sure; you would have all received the Q2 investor update. This had been circulated about two hours back and I would request your attention to the PPT file and I will start with the consolidated results on slide #3.



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On a consolidated basis the revenue for the quarter is Rs.3021 million compared to Rs.3198 million during the same period last year. The EBITDA for the quarter is Rs.714 million as compared to Rs.694 million last year and as a result, there has been an improvement in EBITDA margin at 24% as compared to 22% in the corresponding period last quarter.

The EBIT for this quarter is at Rs.543 million as compared to Rs.512 million last year. Post that there is a profit of Rs.36 million compared to a PAT of Rs.128 million last year.

Coming now to the quarterly standalone results on slide #4, the operational revenue was Rs.1761 million down 20% on a year-on-year basis. The EBITDA is Rs.473 million compared to Rs.612 million last year. The EBITDA margin was at about 27% as compared to 28% in the last financial year for the same period. The EBIT for the quarter is Rs.380 million down 27% on a year-over-year basis whereas the net profit after tax for the quarter is Rs.93 million.

The earnings per share for Q2 are 0.27 basic and 0.27 diluted on a consolidated basis. On a standalone basis the EPS for the quarter is 0.77 basic, and 0.77 diluted.

I want to take a moment here and talk about the detailed performance this quarter. As you are aware our strategic priorities as also mentioned by Shantanu in the opening remarks, this year is consolidation, operational efficiency and internal process optimization. It was very important for us to focus inward and spend our energies on all these areas to become lean, efficient and ready for long-term growth and value creation.

Being the market leader in the digital content business we have taken steps to arrest the continuous price erosion. The SmartClass average price this quarter came in at Rs.3.46 lakhs approximately 9% higher than the last quarter Q1 of this financial year. But the stabilization of price came in at our conscious thought process of focusing on price rather than actually focusing on growing the numbers. Our business has a large fixed-cost base, and since the Company has already built in cost for Q3 and Q4, any reduction in revenue has a marked impact on our margins. As a result our margin in SmartClass business has seen a downward movement this quarter.

So, in a sense, there was a higher ARPU realization, but lower volume while there is some improvement, slight improvement in fixed cost but fixed cost is largely same as built for a larger quarter Q3, Q4. And this has resulted into low margins. But as we work towards better quarters with higher volumes the margin should see some improvement.

Let me explain our rationale behind taking this conscious move of focusing on price realization rather than focusing a lot on the volume growth. We have recently completed an engagement with one of the top three global consulting firms focused on a five-year strategy roadmap for the company and our market intelligence study thereof. I would like to share some of their findings with all of you. Based on their analysis, the addressable market opportunity for the digital



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content business in India is as high as 194,000 schools, which translates into an opportunity of 1.8 million classrooms. Now these, over 1 million are classrooms in English Medium Schools, which are clearly the low hanging fruit for us. Given we have over 90% headroom available for us to grow, we believe our price war at this nascent stage of the market evolution is unhealthy and as an industry leader, we are taking steps to work towards stabilizing the prices and prevent any further price erosion and our steps seems to be bearing fruit as are visible in the price trends in Q2.

The competitive environment this quarter is also substantially subdued as compared to past two quarters. We believe we have taken the right steps in attempting the curb the fall in prices, as we believe this is the right direction for us and will help us improving our margin in the long run. In the interim, we shall also be focusing on improving our back-end systems to improve operational efficiencies mainly effecting deployment, inventory, collections and cost efficiencies. At the same time, we will also continue to work on access to long-term capital to strengthen our balance sheet. As you all know that the SmartClass sale that we make leads to recovery of our money in 20 equal quarterly installments. We want to be conscious towards how do we contract our liabilities for procurement of hardware, which is what we have to invest upfront, so, that we can minimize any asset liability mismatch as we continue to ramp up.

Apart from working to normalize SmartClass pricing, we have made all progress on these initiatives and I will share some more details a little later. Let me now go into the segmental overview starting with our school learning solution segment that comprises of SmartClass and ICT business.

In the SLS segment, our quarterly operating revenue came in at Rs.1671 million as compared to Rs.2187 million during the same period last year. The decline in the revenue is a phenomena which is what I explained earlier that as part of our structured plan to arrest the prices, there have been lower volumes and thus there is lower operating revenue. In the SmartClass part of the business, out of the SLS segment we added 5,112 Classroom during this quarter. In terms of new schools, we added 787 new schools to the SmartClass portfolio.

What is critical here is the fact that average pricing for this quarter was 3.46 lakhs. As I explained earlier, this is part of our conscious definitive strategic move to not reduce pricing any further even at the cost of temporarily decline in classroom numbers. We would rather focus on more healthy strong business. Our business commensurate by a sufficient and a proper tie up of long-term capital than actually just running after booking the numbers. There is ample opportunity for us to clog these numbers even a little later post we have a back end systems well in place.

With the addition of 787 schools in this quarter, we now reach a total of 14,292 schools across the country serving 6.6 million students. As I had shared with you, in our last interaction, the future strategy for SmartClass is taking a concrete shape. We know there is ample opportunity in



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the market, which is already validated by our consulting firm. We know we have a market leader position, a first-mover advantage; and very importantly a very high quality product unmatched by the competition. This, though, is a self-assessment as well, but is also strongly being validated by the third party evaluation that today our quality product is unmatched by the competition. So clearly, part of the strategy is to continue to grow SmartClass. We should see a healthy growth over the next foreseeable future of five to ten years, but more important part of the strategy is to leverage the existing sales, distribution and customer base to sell additional products and become digital technology partners to the schools and thereby accessing larger customer wallet share and improving our margins in the long-term.

While, yes, it is important to count the number of classrooms sold in a given school, but increasingly what we really want to focus on is what is my revenue per school, so that I can amortize my fixed cost over a larger base. In line with this strategy we are transforming the way we are structured and training our sales force to think in terms of revenue per school and not SmartClasses per school. We are also preparing and testing new products like English Language Lab Product and our Tablets Solution, which will be launched soon in the latter part of this financial year.

Let me now turn to the other part of the school learning solution segment, which is the ICT business. We did not bid any major contracts in this business in this quarter, which is in line with the conscious move. We still serve 10,771 schools and over 5.9 million students, which is one of the largest presence in the space of ICT education in the government schools. The focus is that whatever orders we have in hand, really want to do a good execution of that and make sure that it emerges relatively more channelized in collecting whatever we have built. Once again, there is an ample opportunity to pause for a while and then actually run for growth.

Next, let me turn to our K12 schools business. In the K12 part of our business, our total number of operational school at the end of Q2 is at 66 schools, out of which the Greenfield and acquired schools are 37 while the total number of asset-like schools is about 29. One of our schools in Bangalore got transferred to Euro Kids as it met both of our operational goals and two JV schools under the brand Chranjiv Bharti and their management thereof have been transferred back to the original trust with our strategy to focus only on our own schools and brands thereof. That is why you see a number of 69 schools coming to 66. We also terminated the contract with one franchise school in Jalandhar as we were not happy with the performance of this franchise partner and that explains the number of 66. We are happy at where we are placed in this business vis-à-vis the market opportunity.

Similar to SmartClass, the global consulting firm's efforts, were also focused on assessing the potential in the K-12 segment. And as part of this five years strategic assessment, some of the conclusions are that India has a severe shortage of K-12 schools, and will see 25,000 new English medium private sector schools being set up by 2016. Education is the fastest growing sector in India and it is estimated to have market size of \$100 billion in 2010. On an average over



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10,000 schools have been set up in India in the period from FY'06 to FY'11 and that is what we are saying would actually lead to 25,000 more schools by 2016.

Asset-light JV model is the best model to scale this business, and will allow us to focus on our core competencies and internally ESML is aiming at opening 200 to 250 schools over the next three to five years. While we have this aspiration to scale up, given the ample opportunity, we would also be very consciously working on contracting the capital, which though would be small because it is a JV model but we will be conscious to contract capital in line with the gestation period of a given school.

So, we will be growing this business in an asset-light model and right now we are also busy generating leads and identifying partners with whom we can tie up long-term contracts. And as we are moving toward JV model our capex in this quarter is only 546 million and this also is part of our conscious move to conserve cash and keep the capex as low as possible. The total number of students enrolled in our school put together stands at 37,480 students and there is headroom to ramp up the students which are studying in our given schools and as a result assuming the ramp up say 7,000 to 10,000 students in the coming financial year that largely goes to the EBITDA generation for our given school because the cost structure does not go as linear as you are adding actually more students in our given classroom.

The school business is structured in our subsidiary Educomp Infrastructure & School Management Limited, which had the revenue of 332 million in this quarter, a growth of healthy 23% from the same quarter last year. EBIT for the quarter came in at 224 million within EBIT margin of 67% as compared to 162 million and the margin of 60% during the same period last year.

Clearly the K-12 business is at the core of our strategy going forward as we have deployed a significant amount of our capital towards this business. We are mindful of the fact that on one hand we have a large capital employed in the business and at the current stage the return metrics are not very high. But from a long-term point of view every single school in a portfolio can and will generate return as high as 25% and above. Already, there is a millennium school that generates 38% margin. There is another millennium school rather two of them down south generating 45% to 50% margin. There is a millennium school in NCR generating 39% margin. There is a Takshila school in the west generating 27% margin. There is a Universal Academy school making 10% margin. So, you can see there are schools in our portfolio depending on the brand category, depending on the numbers of years of life that the school has lived since it has commenced the operations, that one could actually take the margins to as high as 50% and returns to as high as 52%.

The proof of concept has already been established. The need of the hour is to scale the business through our JV model. But, at the cost of repetition the entire Educomp Group wants to make sure that we get our backend systems well in place and the proper tie-up of capital and learning



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takes place and then we actually start looking for growth. The K-12 segment as a whole which includes our pre-school business as well had a total revenue of 482 million, an increase of 9% over the same period last year. The quarterly EBIT was 214 million, an increase of 57% on year-over-year basis. The EBIT margin therefore was 44% this quarter compared to 31% in the same quarter last year.

Moving to our higher learning solutions segment, this segment comprises of our two joint ventures in the area of higher education and vocational education respectively. In the higher education part of the business our JV with Raffles, which is our Engineering and MBA campus, is operating well and it is gradually moving towards full capacity utilization of the available capacity. The similar phenomena are also being witnessed in our design colleges which are being run as part of this JV. We are conscious of any particular asset if it is not ramping up as per the plan or it is not showing any promise then we are closing it down. For example, we took a conscious call on the Chandigarh Design College and we actually closed it down. As a result, we have now six Design Colleges operational and we have 960 students enrollment in the system.

Our vocational training business IndiaCan had a positive quarter where the number of enrollments went up to 55,000 from 34,500 last quarter. The total number of centers operational at the end of Q2 was 327. IndiaCan had revenue of 320 million this quarter, an increase of 106% from the same period last year. I am very pleased to inform you that as compared to last year's corresponding quarter there is a 50% reduction in EBITDA loss which was at 21 million in Q2 and given the performance of the business over the last few quarters wherein there is a constant decline in losses, we believe the business is heading fast to be EBITDA positive in the next one or two quarters. The HLS segment had revenues of 227 million compared to 89 million during the same period last year. The EBIT loss for the quarter is 66 million down from a loss of 107 million in the corresponding quarter last year.

Coming now to our fourth and last segment Online Supplemental & Global; this segment as you know primarily include Test-Prep businesses like Vidya Mandir, Gateforum and our online businesses and global subsidiaries. Our Test-Prep business VMC continued with another solid quarter ending with 10,100 students compared with 5,200 students at the end of Q2 last year. The company had revenue of 135 million, a jump of 100% on a year-over-year basis. Similarly, the performance of other Test-Prep business Gateforum was equally impressive. Gateforum revenue was 66 million, a jump of 61% over the same period last year.

The number of students enrolled with Gateforum is 17,343 compared to 12,865 enrollments last year. You all might be aware of the recent development that for a job application or for seeking a job in PSU sector, the Gate exam has actually been made mandatory and therefore there is a big opportunity that has suddenly got opened up for the Gateforum business. Hence we believe there should be more and more traction in revenue and EBIT margin in this business going forward.



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The Online Supplemental & Global segment had quarterly revenues of 642 million, growing 34% over the corresponding quarter last year and had an EBIT loss of 95 million. While we just gave you a brief about profits in the Gateforum and Vidya Mandir businesses there is also a profit in our ASKnLearn Singapore business. The loss making entities include our US Company that we acquired a few years ago. We have recently taken some drastic changes including the leadership at the US Company level and we believe the consistent efforts of the next three to four quarters should see the business coming back to profit. We are taking a very critical view of the online platform based businesses and we know they have been losing money for a while and as part of the consolidation focus, we may not be averse to consolidating whatever investments we have made in those businesses. So that, on the whole whatever remains behind is actually a healthy robust segment.

Let me now give you an update on the key management focus areas. As you are aware, our core strategic priority this year is to strengthen our balance sheet and improve the asset-liability profile with the world class institution like IFC and PROPARCO having taken a long-term view of the business with a nine-year exposure on the balance sheet. Post this deal from IFC and PROPARCO, we have some renewed interest from several development institutions and we are engaged with them for long-term capital discussions to replace our short-term debt and improve the asset liability mismatch. However, such an engagement typically tends to get spanned into about two quarters. So that is the timeframe that it might take, but the engagement is going in the right direction.

Now I want to bring your attention to the slide #16, which focuses on inventory days ratio of our various businesses. You would note that our efforts to tighten the working capital management on the inventory side are beginning to show some early signs of fruit. The inventory days in the SmartClass business has come down from 64 days at the beginning of the financial year to 41 days at the end of Q2. This has to be seen in light of the fact that since Q3 is typically a stronger quarter the current inventory also has somewhat build up of the orders to be implemented in Q3. Our efforts will continue in this direction.

Continuing with the consolidation focus theme, we have started to look at our manpower resources as billable and non-billable. What we call as billable resources are the SmartClass coordinator whose cost is embedded into the pricing that we charge from the customer, and an ICT faculty, which is what we provide as part of the government contracts whose cost is being recovered as part of the invoicing that we make to the customer. Balance all is non-billable resources. As part of the conscious move, the non-billable personal expense has seen a decrease of 2% over the last quarter and a decrease of 13% as compared to the last quarter of financial year 2012. This has to be seen in light of our consolidation efforts to streamline our operations and become leaner and more efficient as we prepare for the next year of growth ahead.

We are aware that our receivable days are high. This is a combination of slow progress on securitization and a combination of need to further strengthen our operational efficiencies. As



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part of the operational efficiency initiatives, we have made progress over the last few months but it has still got a lot of headroom to further improve our operational efficiencies on billing and collections. We positively believe that the next few months should start seeing the tractions wherein we would actually cross the line that we actually collect more than what we bill that means there is also recovery from the past. But on the securitization front, while there is no reflection of that in the quarter ended September 30, 2012, I am happy to inform you that in the last three days, we just received a fresh securitization sanction of 100 Crores from one PSU Bank and this will also have a positive impact on debtor days going forward. Apart from it post the end of the quarter we also got 80 Crore line of credit against the government contract from a private sector bank in India. So, combination of working on operational efficiencies and a combination of our pursuit for securitization should also see the trend that you are witnessing in inventory and our manpower cost, similar trends are also slowly beginning to see in the receivables as well.

I am also happy to share that we are working with one of the leading technology players to leverage technology to optimize our cost across the entire business. You might have seen that bulk of my manpower cost is billable resources. There seems to be linearity in the equation that as we are selling more our current manpower cost is going up. We want to see a technology interface and, thus, we have signed an MOU with a large global technology player to help us reduce this linearity and help us bring efficiency into our operations. Not only this effort has the potential of streamlining our costs, it could also help us take ourselves to the next level of after sale servicing and a better customer relationship management.

So, over the next few quarters our primary area of focus would be to continue working hard to improve our working capital situation, train our sales force to migrate the change management process of selling solutions instead of products, launch new products, improve our internal processes to boost efficiency and finally have a better asset-liability profile of our balance sheet. This five/six agenda items are very, very key strategic priority for us and any decision that we are taking internally is actually being largely driven by these five/six aspirations of ours. These were some of the operating and financial highlights of the second quarter of financial year 2012-13. I would now like to hand it back to Shantanu to make the closing comments.

Shantanu Prakash:

Thank you Sanjay. I want to start by saying that we are very pleased with the progress that we have made on all of our strategic initiatives in this quarter and that all the initiatives are on track. The SmartClass price erosion seems to have stopped. Our working capital management has shown improvement, which is evident in the movement of our inventory days. Consolidation and asset monetization initiatives are well on track. Capex continues to see a downward trend helping us improve our cash flow and so on. Overall, our business transformation agenda is on track. What has perhaps been a little subdued is the fact that we are in a tough credit environment and high interest rates.

Securitization funding is getting more expensive and as a result our debtor days are high. We continue to look for long-term alternative sources of funding to fully launch SmartClass business.



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We are also very excited about impending launch of our Tablet product which I believe to be game changing opportunity for Educomp. The Tablet products will offer a one of its kind learning environment, which will create a seamless connect between the school and the home. We hope to leverage our massive installed base of about 14,000 schools and almost 7 million customers for the Educomp SmartClass business. The initial market response to the Tablet amongst Educomp customers is indeed very positive and therefore I am confident that Educomp's best days lie ahead of us. It is a fact that we operate in a world of infinite opportunities yet some definite finite challenges.

The path that we have defined for ourselves is of creating a stronger, leaner and fitter business to ensure that we are well positioned to take advantage of the large opportunity in the education sector in India in the near future. Thank you. With that I will now pause and we will open for questions and answers.

Moderator: Thank you. Ladies and gentlemen, we will now begin with the question and answer session. Mr. Vora would you like to go ahead with questions.

Nikhil Vora: Shantanu, just a couple of things. Firstly, with this recapitalization that we have had does it put us financially now in a lot more comfortable position or we would still require some more capitalization before going back to our capex more or you think we will remain where we are?

Shantanu Prakash: Well, certainly additional capital especially long-term capital from IFC, PROPARCO has certainly helped us and improves the balance sheet profile and so on, but in terms of a more detailed answer may I request Sanjay if you want to add a few comments.

Sanjay Jain: I think the first response is yes it has been quite helpful to strengthen the balance sheet, but we need to continue working towards capital, which improves the existing liability profile of the company number one. Number two, we need to have long-term capital to put into growth with the business. Thirdly apart from the SmartClass and ICT business, all rest of the businesses are being done through special purpose vehicles and given that some of the businesses, which were making losses, like the HLS segment are now heading towards a turnaround. We would not be averse to part monetization of these SPVs. So, that we can unlock some value and use it for deleveraging. So, these would be the paths that we would be pursuing going forward with respect to balance sheet.

Nikhil Vora: Sanjay, what has been the status with regards to some of the businesses that we are planning to exit out or have partnership into those businesses any progress in that?

Sanjay Jain: Well, we are pursuing that agenda. The discussions are on and as you know these things pan over some timeframe but the process is on and as I have mentioned when something definitive crystallizes we would comeback to you and apprise you of that, but there is a meaningful progress being made on that front.



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- Nikhil Vora:** I will comeback if I have more. Thanks for this.
- Moderator:** Thank you. We have the next question from the line of Soumitra Chatterjee from Espirito Santo. Please go ahead.
- Soumitra Chatterjee:** Thanks for taking my question. If I see the number of school and the classroom additions, I think this is the first time since Educomp got listed; you have recorded a year-on-year decline in the classrooms. Now I heard the comment that you would not enter into a price war, but my concern is that if you start to give away market share to the competitors then it will be very difficult to get that share back. I would like your sense on that.
- Shantanu Prakash:** I hear your point of view and we actually have deliberated this, a lot internally. I think given the fact that we have far more deeper understanding of the dynamics of this business than some of our other competitors purely because of the ten odd years that Educomp has been in this business I think in our world view it is not a valid assumption that we are actually giving up market share because even though we have done lower classrooms each of these classrooms has gone to a very high quality school that has passed some of the most stringent test that we have of prequalification that we have put on our sales team so this is more high quality sales firstly. Secondly, we are also seeing a rapid shift in competition dynamics. I believe that there is a consensus amongst the competition as well that there should be more robust pricing that is healthy for the industry. Otherwise the 9% price increase on a quarter-on-quarter basis would not have actually been possible so and if you look at the difference between what we sold last year same quarter and this year, the differences is pretty marginal. So, I think conscious decision to sell as lesser numbers, B) I do not think we are sacrificing market share given the fact that there is 10X headroom in this industry to grow. Industry is at a very nascent stage and if we get the business metrics and business parameters right at this stage I think it will serve us well for the next ten years because you see it is to the same customer that tomorrow we are going to be going around in selling tablet PCs, we are going to be around selling other products, so it is very important to establish the rules of the game initially and yes there was a spurt of competition but you must have also noticed that in the past almost two years no new competition has entered the market and I think the realization has already set in within the industry that everybody wants to do a healthy business, everybody wants to do careful business, everybody wants to do very cautious business and I think collectively the industry is sending out a very strong signal to schools that look we will focus on quality, we will focus on customer value the only thing we will not focus on is price and I think it is the beginning to yield results for Educomp and certainly if you do your own channel checks you will find that our story will be validated by rest of the competition as well.
- Soumitra Chatterjee:** So in light of this then I was just wondering on the guidance that you gave. Last year, we did somewhere around 40,000 classrooms. I think this year the target was somewhere around 50,000 or probably more than that. In the first half we have done only some 11,000 odd classrooms so is

our guidance still valid or should we assume that probably last year what you did is probably what we are going to achieve this year?

Sanjay Jain: On guidance it has to be seen in two scenarios. Scenario one, given that there is 10X headroom one needs to press the accelerator to at least start selling more so therefore on aspiration to reach 50000 classrooms is very much doable. So, therefore that opportunity is not lost. It is very much there but I think as we as said earlier as well, we would be conscious on two fronts a) the quality of business in terms of price and b) appropriate choice of capital to fund the growth. The focus is held to make sure that we make more and more cash going forward and a robust balance sheet. So, hence very specifically in scenario one there is opportunity but in scenario two if you really go conscious then we may at least see the numbers of revenue which are comparable to last year but with a better balance sheet in terms of cash generation for the entire year.

Soumitra Chatterjee: So, coming to the cash point if I see in the first half of this year, the cash that has been blocked in working capital till now is around 3.3 billion close to 330 Crores and for the full year in FY'12 it was only 480 Crores. So, if I were to annualize that probably the requirement of cash in the working capital would be higher so does that mean that probably in the second half, we will have to take further debt because our cash and gross debt level has not materially changed on a sequential basis so despite diluting equity?

Sanjay Jain: I think prima facie, your observation is valid that yes there is a significant change in working capital in this quarter, but that is a result of inventory receivables and payables movement and as we explained that the inventory we are bringing under control and I also acknowledge and mentioned earlier in the initial part of the speech that we need to further focus on receivables which we are focusing. There is improvement but I think to answer now specifically your question are very, very close focus on receivables would keep any further increasing working capital under check. Of course the phenomena cannot be reversed just in one more quarter but gradually over the next couple of quarters there would be a reversal trend which we want to aim to set up. Number two, we just mentioned about the securitization line of 100 Crores that we have just got so as a result of securitization and focus on receivables, I do not anticipate that you should actually multiply it four times going forward to arrive at the annualized cash flow. These conscious efforts should actually see the working capital under check.

Soumitra Chatterjee: Sir, last year was 480 Crores this year now we have done 330 Crores will it be higher than last year or will it be lower than last year how should I look at this?

Sanjay Jain: The overall objective that we would be working would be to try and contain the working capital well within what went in incremental over the last year so therefore the chances that it may actually go up beyond the last years working capital increase are low at the stage.

Soumitra Chatterjee: Thanks a lot.



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Moderator: Thank you. The next question is from the line of Zaharah Sheriff from Fedwinteg Knowledge Services. Please go ahead.

Zaharah Sheriff: Thanks for taking the call. I have a question on the tablet solution that you all are talking about. Could you give some more details on that in terms of I know you have talked about the 15 million equivalent revenue potential per school in the last quarter but what was the revenue model be like and what is your sort of capital investment that going to be?

Shantanu Prakash: I will give you some details. The product is, likely to be launched within the next 45-odd days. Educomp plans to sell the tablet. Educomp is really an IP and knowledge services company. So when we speak about the tablet, we are really speaking about an education solution that we are selling.

Just as today's schools mandate that students have to pay for SmartClass. We are essentially pushing the solution in which the school mandates the fact that students will now have to have tablets as a part of their enrollment in the school, as a part of the school bag and the school. I think there has been extensive research that we have done in our field testing and trials there has been a lot of acceptance and this whole idea resonates with them. So, our game is a game of IP, it is a game of content, it is a game of providing the tablet solution that links the student to the classroom that brings all the stakeholders in the education system, which is one the school, second the teacher, third the student and fourth the parent interconnected together and why we think this is a very disruptive solution is because some of the things that we can do with having an electronic device like a tablet with you are things that has not been possible to do earlier. For example, the content that you see inside the classroom you can go back home and revise the same content. Today it is not possible. I think this is the teachers provide to the student can now be done online and the teacher can give the instant feedback to the student. That we are learning that was more of a concept till now become reality with our tablet base. We will sell the tablet and make a small margin on the tablet but we will really make more meaningful margin on the IP and the content that we provide. Educomp has taken a very meaningful and a very differentiated approach to educational content. In our tablet solution when a student of grade five buys the solution all the content of grade five that is the key books that he is using, the entire content, the assessments, the worksheets of all of the material that he needs for the whole year is provided to the student. For example, today when you start a new year in the school you spend Rs.2000 to Rs.4000 buying a set of books and then when you go to the next grade you buy another set of books. It is really the same analogy that if you buy the Educomp tablet you pay about Rs.2700 for the content then you go to the next grade you again pay Rs.2700 for the content.

Zaharah Sheriff: But just what about the actual equipment? Are not you sort of exposing yourself to use the experience that will also be a function of the equipment and given that the student would be using it for longer and also there are lot of students and already a lot of schools are already having tablets and students have IPADS, so just how will that play out?



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- Shantanu Prakash:** You know we have thought all of these things as well and on this call we cannot reveal our entire business strategy on the call. Suffice it to say that these are all valid points. A solution like a tablet is essentially a new disruptive solution and therein lies the opportunity because this can fundamentally transform classroom learning. Yes there are several questions but there are answers to those and answers based on technology-based and pedagogy based solutions.
- Zaharah Sheriff:** So, just one last thing on this topic what would be the incremental capital deployed in this business to be extent of the equipment sourcing, because I am assuming that is going to be the largest part in everything else?
- Sanjay Jain:** We are going to sell to the students but it is a capital light model.
- Zaharah Sheriff:** Sorry.
- Sanjay Jain:** Because students will buy the equipment, there is no capital model.
- Zaharah Sheriff:** But you would be carrying the inventory?
- Sanjay Jain:** Yes and no. So like I said it this is not the right forum to go into the very detailed discussion on which warehouse will keep it and who will carry the inventory but we have worked out full ecosystem that is going to support this business.
- Zaharah Sheriff:** Alright fair enough. Just separately on this call you consistently talked about this is a year of consolidation and you want to put the backend in place together before a sort of go for the phase of growth. How much time do you think it will take for you to get to the point where you are deploying or utilizing the capital more efficiently and you feel like at a point where you can start looking at faster growth again especially in the K-12 segment?
- Sanjay Jain:** I think it may take us around one year actually to put this agenda. You have to wait for one year to see the results, some early results are visible in the non-billable resources and inventory every quarter. We should make a meaningful progress but after one year we should have put a substantial part of this behind us.
- Zaharah Sheriff:** That is all from me. Thank you. Good luck.
- Moderator:** Thank you. The next question is from Priyanka. Please go ahead.
- Priyanka:** I had a couple of questions in the K-12 business. Now as I read the presentation you mentioned that you are trending towards an asset-light JV model. I wanted to get a sense on what is the expansion plan here because in the first half we have only seen a reduction in the number of K-12 schools, so going forward what is the outlook on the segment?

- Sanjay Jain:** The game plan of the growth forward is to sign up JV schools and at the current juncture there is strong interest that we have been receiving and we are engaged with the partners. We are going slow in converting those leads into actually definitive agreements. A) They are very, very cautious of the partners selection process and B) is that while we are ramping up these schools to higher revenue and higher EBITDA margin, we are also going to tie up long-term capital to make sure that we have to meet up both ends meaningfully.
- Shantanu Prakash:** Lastly school open in Q4 of the year. So you will basically see the jump shift in the number of schools only Q4 and Q1. So, that is April and July.
- Priyanka:** Also out of the current portfolio of 66-odd schools how many are at the breakeven levels currently?
- Sanjay Jain:** I would say broadly speaking on an average there are about 35% schools which are below breakeven level and beyond 35% they are either at a breakeven or making as high as 50% plus operating margins. Any schools that is more than two years of age and you can see that on the fact sheet is actually breakeven and above.
- Priyanka:** A followup to what you mentioned, Shantanu is that the schools open in the second half, why is it that in the earlier in the same quarters, in the earlier years there was an increase in schools in the first half and was it something different during that?
- Shantanu Prakash:** Not really. Like I said, schools will open in Q4 and Q1. So you will see the change in the delta shift in the number of schools only starting from March, April, May, June, and July. So, that is Q1 in that sense. If you look at the number of schools that Educomp had in FY'11 for Q1 that number will be the same.
- Priyanka:** Just lastly one question on our SmartClass business. Now we have seen some bit of competitive pressure... On the SmartClass business I wanted a sense on how is the competitive intensity in this space because over the last few quarters we had seen yields depression, so just wanted your outlook that is content differentiation very limited in this space that yields play the biggest factor?
- Abhinav Dhar:** We have seen a considerable decline in the competitive aggression. I am saying it is significant because if you look at Q1 and Q2 there has been at least almost near zero activity from one or two competitors who were extremely aggressive earlier part of the year. All others seem to have really, really kind of slowed down in these two quarters. I think it links back to something that's Sanjay and Shantanu said earlier in their note is that realization in the industry that you have to do this business at a certain cost, on certain terms to ensure that you have quality customers, you have less receivable challenges, and you are actually setting up a foothold for customers where you can leverage better revenue in future with other products and so on and so forth. Put simply, I see a significant decline in competitor activity for the last two quarters.



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Priyanka: Thank you.

Moderator: Thank you.

Shantanu Prakash: If there are no more questions, I would like to thank the participants on today's call. Good evening and good night to everyone.

Moderator: Thank you gentlemen of the management. That ends your conference call today. Thank you for joining us and you may disconnect your lines. Thank you.