

Multi-year growth prospects in Smart Class

Management meeting reinforces potential for Smart Class

We met up with President-Smart Class to understand Educomp's market potential and opportunities in private school content business in India. Management highlighted that it has identified ~28,000 schools with a fee structure of Rs400pm-4,000pm as targets in the initial phase. Of these, Educomp has already had initial contacts with 18,000 schools and is actively in touch with 11,000. With ~1,700 Smart Class schools, Educomp's market share is over 97% as per management. Smart Class contributes 50% to revenues.

Strong visibility: 900 schools in the pipeline currently

Management highlighted that its pipeline stood at 900 schools. Educomp has already demonstrated its product to these prospective schools and could be negotiating for a sign-up. The strong pipeline gives credence to management guidance of adding 1,060-1,160 schools in FY10e. We expect Smart Class's school base to double over the next two years.

Scaleable model; strong backend team to support growth

Management reiterated that it has a strong operations team, which supports Smart Class implementation in class rooms. The company's 120-strong academic support group primarily interacts with teachers and school principals to improve satisfaction levels among schools.

Retain Buy; after near doubling, stock likely to consolidate

Reiterate Buy with PO of Rs3400 at PEG of 0.9 (FY09/FY09-11e), attractive to us given the 54% earnings growth over FY09-11e. Though we do not rule out near term consolidation post near doubling in last 3months, see triggers in strong Smart Class additions during 1Q. Key risk: delays in building K-12 brick- and-mortar schools.

Estimates (Mar)

(Rs)	2007A	2008A	2009E	2010E	2011E
Net Income (Adjusted - mn)	287	707	1,327	2,145	3,151
EPS	15.43	38.01	71.37	115.32	169.44
EPS Change (YoY)	115.0%	146.3%	87.8%	61.6%	46.9%
Dividend / Share	2.42	2.93	3.00	3.00	3.00
Free Cash Flow / Share	(31.92)	(99.66)	(201.95)	(126.65)	(92.64)

Valuation (Mar)

	2007A	2008A	2009E	2010E	2011E
P/E	195.24x	79.26x	42.21x	26.12x	17.78x
Dividend Yield	0.080%	0.097%	0.100%	0.100%	0.100%
EV / EBITDA*	105.31x	42.07x	21.21x	11.69x	8.07x
Free Cash Flow Yield*	-0.982%	-3.31%	-7.19%	-4.53%	-3.33%

* For full definitions of *iQmethod*SM measures, see page 4.

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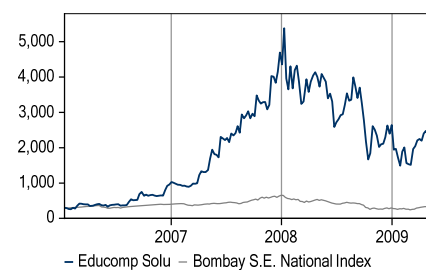


RESEARCH

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Stock Data

Price	Rs3,013
Price Objective	Rs3,400
Date Established	27-Jan-2009
Investment Opinion	C-1-7
Volatility Risk	HIGH
52-Week Range	Rs1,331-Rs4,029
Mrkt Val / Shares Out (mn)	US\$1,104 / 17.2
Average Daily Volume	1,161,990
ML Symbol / Exchange	EUSOF / BSE
Bloomberg / Reuters	EDSL IN / EDSO.BO
ROE (2009E)	26.3%
Net Dbt to Eqty (Mar-2008A)	28.0%
Est. 5-Yr EPS / DPS Growth	35.0% / 35.0%
Free Float	35.0%



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Refer to important disclosures on page 5 to 7. Analyst Certification on Page 3. Price Objective Basis/Risk on page 3.

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iQprofileSM Educomp Solutions Ltd.

Key Income Statement Data (Mar)	2007A	2008A	2009E	2010E	2011E
(Rs Millions)					
Sales	1,100	2,861	6,342	9,403	12,880
Gross Profit	670	1,575	4,549	7,411	10,119
Sell General & Admin Expense	(164)	(301)	(409)	(995)	(1,466)
Operating Profit	410	935	1,708	3,621	5,284
Net Interest & Other Income	45	129	323	(169)	(202)
Associates	NA	NA	NA	NA	NA
Pretax Income	455	1,065	2,031	3,452	5,082
Tax (expense) / Benefit	(170)	(351)	(704)	(1,139)	(1,728)
Net Income (Adjusted)	287	707	1,327	2,145	3,151
Average Fully Diluted Shares Outstanding	19	19	19	19	19

Key Cash Flow Statement Data

Net Income	284	711	1,327	2,145	3,151
Depreciation & Amortization	96	331	804	939	1,319
Change in Working Capital	(225)	(730)	(815)	(1,014)	(1,137)
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	10	193	0	169	203
Cash Flow from Operations	165	505	1,317	2,238	3,536
Capital Expenditure	(675)	(2,224)	(5,052)	(4,594)	(5,268)
(Acquisition) / Disposal of Investments	(101)	85	0	0	0
Other Cash Inflow / (Outflow)	38	141	0	0	0
Cash Flow from Investing	(739)	(1,998)	(5,052)	(4,594)	(5,268)
Shares Issue / (Repurchase)	0	0	1	2	3
Cost of Dividends Paid	(27)	(40)	(55)	(56)	(56)
Cash Flow from Financing	1,127	3,461	3,122	1,400	1,588
Free Cash Flow	(510)	(1,719)	(3,736)	(2,355)	(1,732)
Net Debt	150	862	1,508	3,917	5,702
Change in Net Debt	(482)	(1,634)	3,790	2,409	1,785

Key Balance Sheet Data

Property, Plant & Equipment	831	2,714	6,962	10,617	14,566
Other Non-Current Assets	240	318	318	318	318
Trade Receivables	496	1,157	1,885	2,767	3,931
Cash & Equivalents	1,106	2,912	2,291	1,335	1,192
Other Current Assets	159	570	582	697	866
Total Assets	2,832	7,671	12,038	15,734	20,873
Long-Term Debt	1,255	3,773	3,798	5,252	6,894
Other Non-Current Liabilities	59	210	210	210	210
Short-Term Debt	NA	NA	NA	NA	NA
Other Current Liabilities	242	586	607	591	790
Total Liabilities	1,556	4,569	4,615	6,053	7,893
Total Equity	1,276	3,078	7,399	9,658	12,957
Total Equity & Liabilities	2,832	7,647	12,015	15,711	20,850

iQmethodSM - Bus Performance*

Return On Capital Employed	16.9%	16.1%	13.4%	19.0%	20.4%
Return On Equity	28.1%	35.1%	26.3%	26.0%	29.1%
Operating Margin	37.3%	32.7%	26.9%	38.5%	41.0%
EBITDA Margin	46.0%	44.3%	39.6%	48.5%	51.3%

iQmethodSM - Quality of Earnings*

Cash Realization Ratio	0.6x	0.7x	1.0x	1.0x	1.1x
Asset Replacement Ratio	7.0x	6.7x	6.3x	4.9x	4.0x
Tax Rate (Reported)	37.3%	33.0%	34.7%	33.0%	34.0%
Net Debt-to-Equity Ratio	11.7%	28.0%	20.4%	40.6%	44.0%
Interest Cover	28.5x	19.5x	9.3x	15.8x	20.2x

Key Metrics

* For full definitions of iQmethodSM measures, see page 4.

Company Description

Set up in 1994, Educomp is India's largest provider of technology driven education solutions co. It provides end to end solutions for K12 through licensing of digital content to enhance the teaching process. It aims to be a comprehensive provider of solutions in India's school education economy and has expanded its offerings to cater to pre schools, online tutoring, professional development for teachers etc.

Investment Thesis

We expect Educomp to be one of the fastest growing companies in our universe. Key positives include growing adoption of technology based education amongst K-12 (Kindergarten to Class12) private schools, low market penetration of under 5 percent amongst private schools in India and increased spending by state governments on technology adoption in public schools. Besides revenue visibility is high as company enters in to 5 year contracts with private schools.

Stock Data

Price to Book Value 7.2x

Price objective basis & risk Educomp Solu (EUSOF)

Our PO of Rs3400 is at PEG of 0.9 (FY09/FY09-11e), lower than historical PEG of 1.2, and implies a PE of 29x FY10e. We believe premium valuations are fair considering the high 54 percent earnings growth expected over FY09-11E and derisked revenue model given focus on non-discretionary education spend and high exposure to the domestic economy.

Risks to our valuation are delays in execution of contracts in government schools, acquisition related risks and managing multiple growth initiatives.

Analyst Certification

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India - Software & IT Services Coverage Cluster

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	Mphasis Ltd	MPSSF	MPHL IN	Pratish Krishnan
	Patni	PATIF	PATNI IN	Mitali Ghosh
	Patni Computer	PTI	PTI US	Mitali Ghosh
	Tech Mahindra	TMHAF	TECHM IN	Pratish Krishnan
	WNS (Holdings) L	WNS	WNS US	Mitali Ghosh
NEUTRAL				
	Genpact Ltd	G	G US	Mitali Ghosh

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India - Software & IT Services Coverage Cluster

Investment rating	Company	ML ticker	Bloomberg symbol	Analyst
UNDERPERFORM				
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	Firstsource	FSSOF	FSOL IN	Mitali Ghosh
	HCL	XHCLF	HCLT IN	Mitali Ghosh
	Hexaware Tech	XFTCF	HEXW IN	Pratish Krishnan
	Infosys Tech	INFYF	INFO IN	Mitali Ghosh
	Infosys Tech - A	INFY	INFY US	Mitali Ghosh
	Infotech Enterprises Ltd	IFKFF	INFTC IN	Pratish Krishnan
	Mastek	MSKDF	MAST IN	Pratish Krishnan
	Rollta India	RLTAF	RLTA IN	Pratish Krishnan
	Rollta India-GDR	XLROF	RTI LI	Pratish Krishnan
	Tata Consultancy	TACSF	TCS IN	Mitali Ghosh
	Wipro	WIPRF	WPRO IN	Mitali Ghosh
	Wipro	WIT	WIT US	Mitali Ghosh

*iQmethod*SM Measures Definitions

Business Performance	Numerator	Denominator
Return On Capital Employed	$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) * (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$	Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Return On Equity	Net Income	Shareholders' Equity
Operating Margin	Operating Profit	Sales
Earnings Growth	Expected 5-Year CAGR From Latest Actual	N/A
Free Cash Flow	Cash Flow From Operations – Total Capex	N/A
Quality of Earnings		
Cash Realization Ratio	Cash Flow From Operations	Net Income
Asset Replacement Ratio	Capex	Depreciation
Tax Rate	Tax Charge	Pre-Tax Income
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents	Total Equity
Interest Cover	EBIT	Interest Expense
Valuation Toolkit		
Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	$\text{EV} = \text{Current Share Price} * \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Other LT Liabilities}$	Sales
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

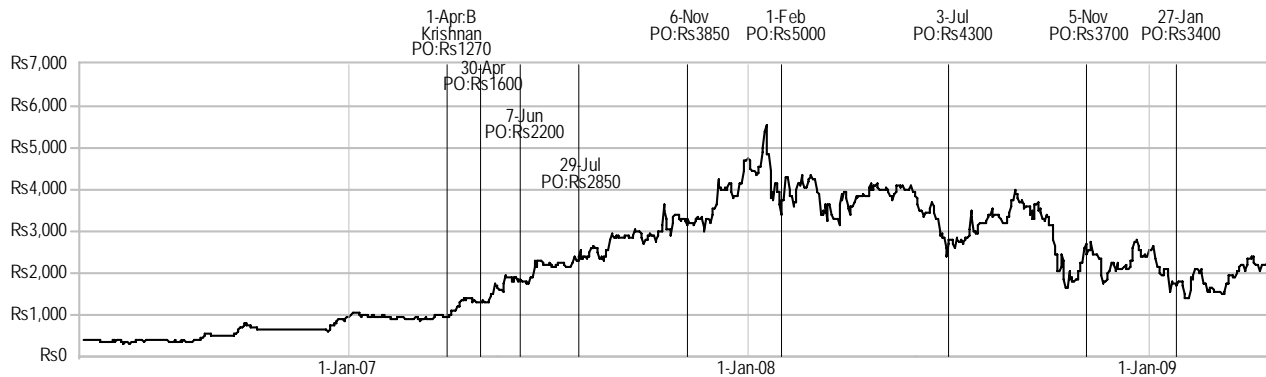
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EUSOF Price Chart



EUSOF _____

B : Buy, N : Neutral, S : Sell, U : Underperform, PO : Price objective, NA : No longer valid

*Prior to May 31, 2008, the investment opinion system included Buy, Neutral and Sell. As of May 31, 2008, the investment opinion system includes Buy, Neutral and Underperform. Dark Grey shading indicates that a security is restricted with the opinion suspended. Light grey shading indicates that a security is under review with the opinion withdrawn. The current investment opinion key is contained at the end of the report. Chart is current as of April 30, 2009 or such later date as indicated. BAS-ML price charts do not reflect analysts' coverage of the stock at prior firms. Historical price charts relating to companies covered as of April 30, 2009 by former Banc of America Securities LLC (BAS) analysts are available to BAS clients on the BAS website."

Investment Rating Distribution: Education & Training Services Group (as of 01 Apr 2009)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	14	77.78%	Buy	8	57.14%
Neutral	3	16.67%	Neutral	2	66.67%
Sell	1	5.56%	Sell	1	100.00%

Investment Rating Distribution: Global Group (as of 01 Apr 2009)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1243	38.21%	Buy	520	46.39%
Neutral	841	25.85%	Neutral	349	47.04%
Sell	1169	35.94%	Sell	388	36.30%

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