

Tree House Education & Accessories

Performance Highlights

Y/E March (₹ cr)	2QFY16	2QFY15	% chg (qoq)	1QFY16	% chg (yoy)
Net sales	57	50	15.1	69	(17.1)
EBITDA	30.2	30	1.5	41	(26.4)
EBITDA Margin (%)	52.7	59.7	(700bp)	59.4	(670bp)
Adjusted PAT	13	13	1.2	18	(29.3)

Source: Company, Angel Research

Tree House Education & Accessories (THEAL)' 2QFY2016 results underperformed our estimates on all parameters. The top-line growth was decent mainly due to strong addition of 73 new pre-schools. On the operating profit front, the company reported flattish growth yoy which resulted into lower growth in profitability.

Top-line grew ~15% yoy: The company's top-line grew ~15% yoy to ~₹57cr, mainly due to growth in existing pre-schools and addition of new pre-schools. The company added 73 pre-schools in various cities like Ahmednagar, Goa, Gurgaon, Jalgaon, Noida, and Ratnagiri, during the quarter.

Poor operating performance drags down Net profit growth: The operating profit came in at ~₹30cr, up ~2% yoy. However, operating margins contracted by 700bp yoy to 52.7%, as the company opened 73 new centres during the quarter, which is the highest ever in the history of the company in a single quarter. The reported net profit grew by only ~1% yoy to ~₹13cr, due to the poor operating performance.

Outlook and Valuation: We continue to remain positive on the stock, as we believe THEAL will continue to register robust growth going ahead. The growth would come on the back of consistent expansion of pre-schools and repayment of debt which would boost earnings. We expect the company to report a CAGR of ~23% in the top-line and ~21% in the bottom-line over FY2015-17E. **We recommend a Buy rating on the stock, with a target price of ₹314.**

Key Financials

Y/E March (₹ cr)	FY2013	FY2014E	FY2015	FY2016E	FY2017E
Net Sales	114	158	207	256	315
% chg	48.0	37.9	31.6	23.4	23.2
Net Profit	33	44	61	70	89
% chg	53.9	31.8	38.6	14.7	27.0
EBITDA Margin (%)	54.1	56.6	57.2	57.2	57.5
FDEPS (₹)	7.9	10.4	14.4	16.5	21.0
P/E (x)	31.6	24.0	17.3	15.1	11.9
P/BV (x)	3.1	2.6	1.6	1.5	1.3
RoE (%)	9.7	11.0	9.3	9.6	10.9
RoCE (%)	11.8	14.9	12.0	12.7	14.5
EV/Sales (x)	9.3	7.1	4.8	4.2	3.6

Source: Company, Angel Research; Note: CMP as of November 9, 2015

BUY

CMP	₹249
Target Price	₹314

Investment Period	12 Months
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Stock Info

Sector	Educational Services
Market Cap (₹ cr)	1,052
Net Debt	(66.8)
Beta	0.8
52 Week High / Low	548 / 246
Avg. Daily Volume	10,782
Face Value (₹)	10
BSE Sensex	26,121
Nifty	7,915
Reuters Code	THEA.BO
Bloomberg Code	THEAL.IN

Shareholding Pattern (%)

Promoters	30.0
MF / Banks / Indian FIIs	3.5
FII / NRIs / OCBs	21.3
Indian Public / Others	45.2

Abs.(%)	3m	1yr	3yr
Sensex	(7.5)	(6.3)	39.8
THEAL	(37.5)	(44.7)	10.7

3 year daily price chart



Source: Company, Angel Research

Amarjeet S Maurya

+91 22 39357800 Ext: 6831

amarjeet.maurya@angelbroking.com

Exhibit 1: 2QFY2016 performance highlights

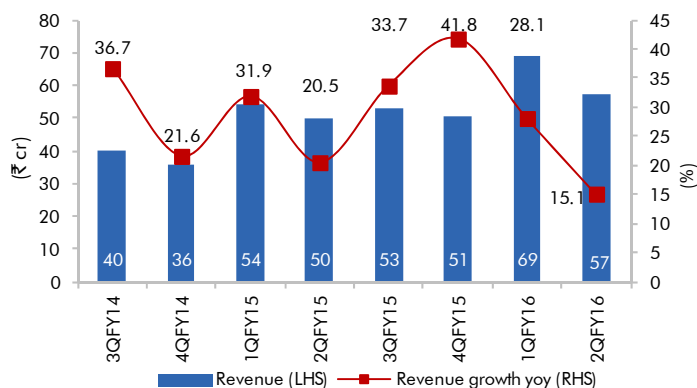
Y/E March (₹ cr)	2QFY16	2QFY15	% yoy	1QFY16	% qoq	1HFY16	1HFY15	% chg
Net Sales	57	50	15.1	69	(17.1)	126	104	21.8
Staff Costs	8	6	28.0	6	20.6	14	11	27.4
(% of Sales)	13.4	12.1		9.2		11.1	10.6	
Operating Expense	19	14	38.0	22	(10.4)	41	30	38.5
(% of Sales)	33.9	28.3		31.4		32.5	28.6	
Total Expenditure	27	20	35.0	28	(3.4)	55	41	35.5
Operating Profit	30	30	2	41	(26.4)	71	63	13.0
OPM (%)	52.7	59.7		59.4		56.3	60.7	
Interest	5	4	3.7	4	22.5	8	8	
Depreciation	10	6	58.4	10	4.0	20	12	59.7
Other Income	3	0	826.5	3	5.0	6	0	1,155.1
PBT	19	19	(3.1)	31	(38.8)	49	44	13.3
(% of Sales)	32.7	38.8		44.4		39.1	42.0	
Provision for Taxation	6	7	(11.0)	13	(52.5)	19	15	24.7
(% of PBT)	32.0	34.9		41.2		37.7	34.3	
Minority Interest								
Recurring PAT	13	13	1.2	18	(29.3)	31	29	7.4
PATM	22.3	25.3		26.1		24.4	27.6	
Extra-ordinary Items (Income)				2		2		
Adj. PAT	13	13	1.2	20	(36.0)	33	29	14.0

Source: Company, Angel Research

Healthy top-line growth led by addition of pre-schools

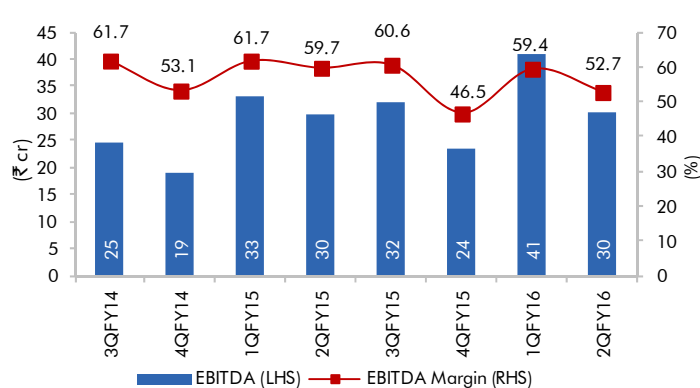
The company's top-line grew ~15% yoy to ~₹57cr, mainly due to growth in existing pre-schools and addition of new pre-schools. The company added 73 pre-schools in various cities like Ahmednagar, Goa, Gurgaon, Jalgaon, Noida, and Ratnagiri, during the quarter.

Exhibit 2: Steady expansion aids growth momentum



Source: Company, Angel Research

Exhibit 3: EBIDTA and EBIDTA margin tend



Source: Company, Angel Research

Operating margin contraction by 700bp yoy

The operating profit came in at ~₹30cr, up ~2% yoy. However, the operating margin contracted by 700bp yoy to 52.7%, as the company opened 73 new centres during the quarter, which is the highest ever in the history of the company in a single quarter.

Poor operating performance drags down Net profit growth

For the quarter, the reported net profit grew by only ~1% yoy to ~₹13cr, due to the poor operating performance.

Investment Arguments

Expansion plan for pre-schools to drive growth

THEAL is expected to continue to post revenue growth on the back of its growing geographic presence. In the past few years, the company has increased its number of pre-school branches at a rapid pace, ie from 302 in FY2012 to 720 in 2QFY2016 (self-operated branches + franchisees). At present, the company's branches are concentrated in Maharashtra, with the region accounting for ~40% of its branches. THEAL is now looking at expansion of pre-schools on a large scale and across different regions, with particular focus on the Delhi & NCR region. The company would be adding 150 pre-schools in FY2016. This move, we believe, is a positive step in terms of mitigating the risk of geographic concentration.

Day care centers to trigger growth & profitability

THEAL has expanded its day-care foot print to 190 centers, with it receiving an encouraging response in this segment. The Management believes that this service will contribute significantly to the company's top-line and bottom-line, going ahead. THEAL has entered into tie-ups with large corporates in the IT, ITES, banking and consulting space to provide day-care services for their employees.

Focus on monetization of K-12 School assets

The company is providing school management services to 24 K-12 schools in 3 states in India. The company is now focusing on monetizing its investments in K-12 school premises and moving towards an asset-light model while it would continue to provide educational services in this segment. The company owns 5 set-ups (land & building) including 1 in collaboration with a joint venture (JV) partner; THEAL has a 50% stake in the JV. Of these, the company has sold 1 school property for ~₹17cr; for another property, it has signed a MOU for sale of its land and building in Vadodara for a consideration of ₹52.5cr.

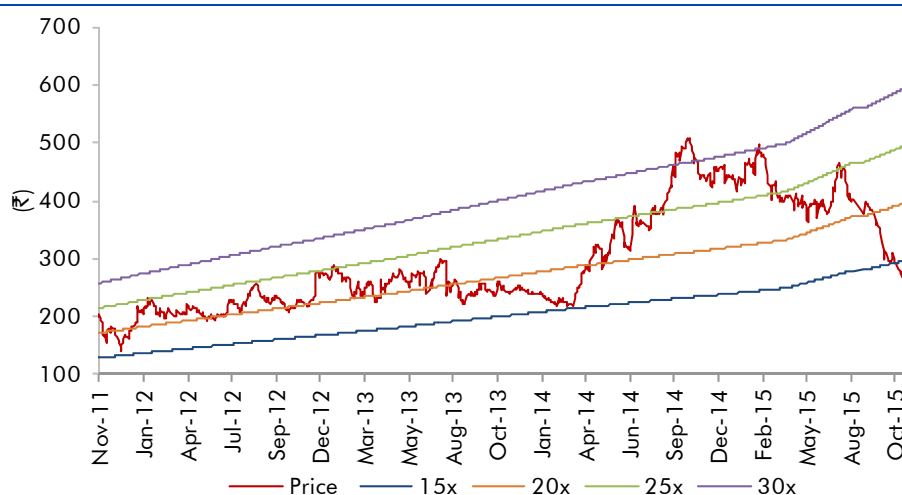
Payment of debt

Currently the company is more focused on expansion and debt reduction. The company has raised ₹200cr through a QIP to fund its expansion plans. Further, it would be selling its K-12 school property, and would utilize its free cash flows to offset debt. The company expects to be virtually debt free within two years.

Outlook and Valuations:

We continue to remain positive on the stock, as we believe THEAL will continue to register robust growth going ahead. The growth would come on the back of consistent expansion of pre-schools and repayment of debt which would boost earnings. We expect the company to report a CAGR of ~23% in the top-line and ~21% in the bottom-line over FY2015-17E. **We recommend a Buy rating on the stock, with a target price of ₹314.**

Exhibit 4: One Year Forward PE



Source: Company, Angel Research

Competition

The education sector in India is largely unorganized and the business of pre-schools is highly fragmented and competitive. In addition to competition from unorganized players in the pre-schools business, THEAL faces a lot of competition from organized players in the market where it competes with various pre-schools like Kidzee, Euro Kids, and Roots to Wings (operated by Educomp Solutions).

Key Risks

Geographical concentration risk: Around 42% of the company's pre-schools are located in and around Mumbai metropolitan. This suggests a geographical concentration risk to the company.

Regulatory risk: Government introduced regulations on pre-schools may impose restrictions on the company.

Company Background

Tree House Education and Accessories Limited (THEAL) runs quality pre-schools and also provides educational services to K-12 schools throughout the country. THEAL has revolutionized the concept of pre-school pedagogy in India through the use of innovative teaching methods and child-focused personal care. The company currently has 647 pre-schools, of which, 540 are self-operated. These are present across 88 cities in India (data as of June 30, 2015). The company also provides school management services to 24 K-12 schools in 3 states in India.

Profit and loss statement (Standalone)

Y/E March (₹ cr)	FY12	FY13	FY14	FY15	FY16E	FY17E
Total operating income	77	114	158	207	256	315
% chg	96.8	48.0	37.9	31.6	23.4	23.2
Total Expenditure	35	52	68	89	110	134
Personnel Expenses	10	13	17	24	30	38
Others Expenses	26	39	51	65	79	96
EBITDA	42	62	89	119	146	181
% chg	148.4	47.2	44.4	33.0	23.4	23.8
(% of Net Sales)	54.4	54.1	56.6	57.2	57.2	57.5
Depreciation & Amortisation	8	13	17	27	36	46
EBIT	34	48	72	92	110	135
% chg		41.6	49.2	27.2	19.9	22.4
(% of Net Sales)	44.3	42.4	45.8	44.3	43.0	42.8
Interest & other Charges	7	7	8	15	18	18
Other Income	4	7	1	7	8	10
(% of PBT)	12.3	14.4	2.0	8.5	8.0	7.9
Share in profit of Associates	-	-	-	-	-	-
Recurring PBT	32	49	66	84	100	127
% chg		54.7	35.1	26.8	19.1	27.0
Prior Period & Extraord. Exp./(Inc.)	-	-	-	-	-	-
PBT (reported)	32	49	66	84	100	127
Tax	10	16	22	23	30	38
(% of PBT)	31.4	31.8	33.5	27.3	30.0	30.0
PAT (reported)	22	33	44	61	70	89
ADJ. PAT	22	33	44	61	70	89
% chg		53.9	31.8	38.6	14.7	27.0
(% of Net Sales)	28.1	29.2	27.9	29.3	27.3	28.1
Basic EPS (₹)	5.1	7.9	10.4	14.4	16.5	21.0
Fully Diluted EPS (₹)	5.1	7.9	10.4	14.4	16.5	21.0
% chg	135.7	53.9	31.8	38.6	14.7	27.0

Balance Sheet (Standalone)

Y/E March (₹ cr)	FY12	FY13	FY14	FY15	FY16E	FY17E
SOURCES OF FUNDS						
Equity Share Capital	34	36	37	42	42	42
Equity Share Warrants	-	10	3	-	-	-
Reserves & Surplus	223	297	360	615	682	768
Shareholders Funds	256	343	401	657	725	810
Total Loans	51	67	83	106	140	120
Deferred Tax Liability	3	5	5	5	5	5
Total Liabilities	311	415	489	768	870	935
APPLICATION OF FUNDS						
Gross Block	154	185	293	393	533	663
Less: Acc. Depreciation	17	30	46	73	109	156
Net Block	137	155	247	320	424	507
Capital Work-in-Progress	20	40	28	28	28	28
Investments	31	10	11	11	11	11
Current Assets	149	240	240	462	471	469
Inventories	4	5	6	7	8	10
Sundry Debtors	6	7	29	39	48	60
Cash	48	49	11	161	100	35
Loans & Advances	7	10	7	10	13	16
Other Assets	85	169	187	244	302	347
Current liabilities	25	30	38	54	65	81
Net Current Assets	123	210	202	408	406	388
Deferred Tax Asset	0	0	0	0	0	0
Mis. Exp. not written off	-	-	-	-	-	-
Total Assets	311	415	489	768	870	935

Cash Flow statement

Y/E March (₹ cr)	FY12	FY13	FY14	FY15	FY16E	FY17E
Profit Before Tax	32	49	66	84	100	127
Depreciation	8	13	17	27	36	46
Other Income	(29)	(58)	(35)	(56)	(60)	(46)
Change in Working Capital	3	3	6	15	18	18
Direct taxes paid	(7)	(18)	(19)	(23)	(30)	(38)
Cash Flow from Operations	(0)	(3)	0	-	-	-
(Incr)/ Decr in Fixed Assets	6	(14)	35	47	65	107
(Incr)/Decr In Investments	(73)	(71)	(96)	(100)	(140)	(130)
Other Income	(29)	21	(2)	-	-	-
Cash Flow from Investing	(101)	(49)	(97)	(100)	(140)	(130)
Issue of Equity/Preference	135	50	20	201	-	-
Incr/(Decr) in Debt	-	-	-	20	34	(20)
Dividend Paid (Incl. Tax)	-	(3)	(4)	(2)	(2)	(3)
Others	(21)	17	9	(15)	(18)	(18)
Cash Flow from Financing	114	64	24	203	13	(41)
Incr/(Decr) In Cash	19	1	(38)	151	(62)	(64)
Opening cash balance	29	48	49	11	161	100
Closing cash balance	48	49	11	161	100	35

Key Ratios

Y/E March	FY12	FY13	FY14	FY15	FY16E	FY17E
Valuation Ratio (x)						
P/E (on FDEPS)	48.6	31.6	24.0	17.3	15.1	11.9
P/CEPS	35.8	22.6	17.3	12.0	9.9	7.8
P/BV	4.1	3.1	2.6	1.6	1.5	1.3
Dividend yield (%)	0.3	0.4	0.5	0.8	0.9	1.3
EV/Sales	13.3	9.3	7.1	4.8	4.2	3.6
EV/EBITDA	24.4	17.2	12.5	8.3	7.4	6.2
EV / Total Assets	3.0	2.4	2.1	1.2	1.2	1.1
Per Share Data (₹)						
EPS (Basic)	5.1	7.9	10.4	14.4	16.5	21.0
EPS (fully diluted)	5.1	7.9	10.4	14.4	16.5	21.0
Cash EPS	7.0	11.0	14.4	20.7	25.1	31.9
DPS	0.8	1.1	1.3	2.0	2.3	3.1
Book Value	60.6	81.2	94.7	155.3	171.3	191.5
Returns (%)						
ROCE	11.1	11.8	14.9	12.0	12.7	14.5
Angel ROIC (Pre-tax)	14.9	13.8	15.7	15.6	14.6	15.3
ROE	8.4	9.7	11.0	9.3	9.6	10.9
Turnover ratios (x)						
Asset Turnover (Gross Block)	0.6	0.7	0.6	0.6	0.6	0.6
Inventory / Sales (days)	17	15	13	13	12	12
Receivables (days)	27	22	67	68	69	70
Payables (days)	23	12	13	13	14	14
WC cycle (ex-cash) (days)	22	25	67	68	67	68

Research Team Tel: 022 - 39357800

 E-mail: research@angelbroking.com

 Website: www.angelbroking.com

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Disclosure of Interest Statement	Tree House
1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

Note: We have not considered any Exposure below ₹1 lakh for Angel, its Group companies and Directors

Ratings (Based on expected returns over 12 months investment period):	Buy (> 15%)	Accumulate (5% to 15%) Reduce (-5% to -15%)	Neutral (-5 to 5%) Sell (< -15)
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