



Tree House Education

Preschool growth continues

Revenue and EBITDA below estimates

Tree House Education (THEAL IN) reported mixed numbers, with a 10% QoQ drop in top line while bottom line fell by 34%. Revenue at INR 358mn was 13% below our expectation, led by a change in the course period to March ending. EBITDA margin stabilized after the previous quarter's 61.7%, a high number, due to high centre operating cost as well as lower revenue base. PAT grew by 15.5%.

FCF to turn positive in FY15 on K-12 capex completion

During FY14, Tree House spent capex of about INR 1bn, out of which ~57% went towards K-12 investment. The company has completed 24 out of 26 schools and is left with about INR 150mn. Further, it plans to thrive on an asset-light model, with the sale of schools worth INR 900mn. In FY15, all K-12 schools will commence and it will also get back security deposits worth INR 1,200mn, thereby reducing ~40% of the asset size. We expect the company to turn FCF-positive in FY15.

Steady preschool addition with minimal capex should add value

Tree House added 111 schools in FY14, out of which 86% preschools are self-owned. It plans to add 250 self-owned preschools on current base of 386 preschools. **We have factored in an addition of 160 preschools about one-third of the company target.** With 8,000 preschools required in the next five years, the industry offers significant growth potential. Capex of INR 5mn per school also does not require heavy investment.

Value will accrue once FCF turns positive

We have marginally revised down our revenue and PAT estimates by 2% each. We reiterate our DCF-based TP of INR 370 per share, which assumes a WACC of 14% and a 5% terminal growth rate, offering 10% potential upside. At CMP of INR334 it offers 11% upside. The stock is valued 6x FY16E EV/EBITDA and 12x FY16E P/E. We feel the stock has the potential to re-rate once its K-12 asset light approach is executed, which should improve liquidity and return ratios significantly.

Rating: Accumulate

Target Price: INR 370

Upside: 10%

CMP: INR 335 (as on 28 May 2014)

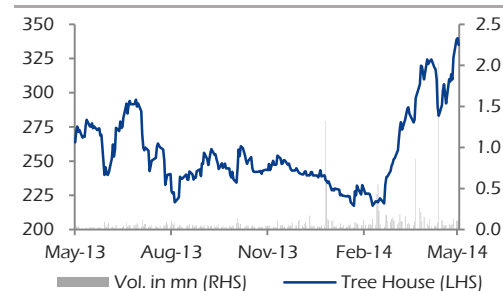
Key data

Bloomberg /Reuters Code	THEAL IN/THEA.BO
Current /Dil. Shares O/S (mn)	37/37
Mkt Cap (INR bn/USD mn)	12/211
Daily Volume (3M NSE Avg)	74,246
Face Value (INR)	10

1 USD = INR 58.9

Note: * as on 28 May 2014; Source: Bloomberg

Price & Volume



Source: Bloomberg

Shareholding (%)	Q1FY14	Q2FY14	Q3FY14	Q4FY14
Promoter	27.8	29.3	30.9	31.2
Institutional Investors	12.2	11.8	11.4	14.7
Other Investors	49.5	48.6	48.0	44.1
General Public	10.6	10.3	9.8	10.0

Source: BSE

Price performance (%)	3M	6M	12M
Sensex	16.3	19.6	21.8
Tree House	48.2	35.1	23.1
Navneet Education	40.7	43.0	23.5

Source: Bloomberg

Y/E March (INR mn)	Q4FY14	Q4FY13	YoY(%)	Q3FY14	QoQ (%)	Q4FY14E	Variance (%)
Net Sales	358	283	26.4	397	(10.0)	410	(12.8)
Operating Expenses	168	128	31.3	152	10.3	202	(17.0)
% of Sales	46.9	45.1	3.9	38.3	22.5	49.3	(4.8)
EBITDA	190	155	22.4	245	(22.6)	208	(8.7)
EBITDA Margins (%)	53.1	54.9	(1.8)	61.7	(8.6)	50.7	2.4
Depreciation	44	32	37.7	45	(0.7)	59	(24.6)
Interest	25	17	50.9	20	28.6	24	NA
Other Income	-	32		0		0	NA
PBT	121	138	(12.7)	181	(33.5)	125	(3.9)
Tax	40	39	3.4	60	NA	31	31.1
Effective Tax Rate (%)	33.2	28.0	18	33.3	(0.2)	24.3	36.5
Net Income	81	99	(18.9)	121	(33.5)	95	(15.2)
NPM (%)	22.5	35.1	(35.9)	30.5	(26.1)	23.1	(2.7)
EPS	2.2	2.9	(25.6)	3.3	(33.6)	2.5	(13.9)

Source: Company, Elara Securities Estimate

Key Financials												
YE March	Revenue (INR mn)	YoY (%)	EBITDA (INR mn)	EBITDA margin (%)	Adj PAT (INR mn)	YoY (%)	Fully DEPS (INR)	ROE (%)	ROCE (%)	P/E (x)	EV/EBITDA (x)	
FY13	1,143	48.0	618	54.1	333.3	53.9	9.6	11.1	13.5	35.0	21.5	
FY14	1,576	37.9	892	56.6	438.9	31.7	11.8	11.7	16.0	28.4	14.9	
FY15E	2,187	38.8	1,259	57.6	578.7	31.9	15.3	13.4	18.3	21.8	10.5	
FY16E	2,788	27.4	1,618	58.0	763.9	32.0	20.2	15.8	21.5	16.5	8.2	

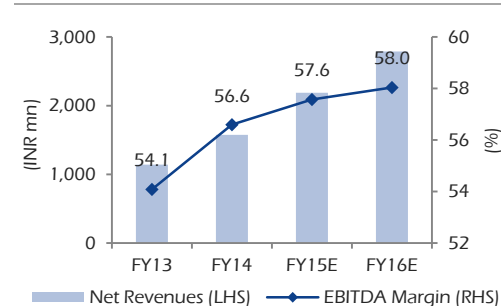
Note: pricing as on 28 May 2014; Source: Company, Elara Securities Estimate

Financials (YE March)

Income Statement (INR mn)	FY13	FY14	FY15E	FY16E
Net Revenues	1,143	1,576	2,187	2,788
EBITDA	618	892	1,259	1,618
Less :- Depreciation & Amortization	134	170	319	399
EBIT	484	722	941	1,219
Less:- Interest Expenses	66	76	84	84
Add:- Non operating Income	71	13	13	13
PBT	489	660	870	1,149
Less :- Taxes	155	221	291	385
PAT	333	439	579	764
Balance Sheet (INR mn)	FY13	FY14	FY15E	FY16E
Share Capital	360	372	372	372
Reserves	3,074	3,702	4,167	4,780
Borrowings	667	826	826	826
Long Term Liabilities and Provision	3	4	3	3
Deferred Tax Liability	44	51	51	51
Total Liabilities	4,148	4,956	5,419	6,032
Gross Block	1,850	2,937	3,911	4,585
Less:- Accumulated Depreciation	300	469	788	1,187
Net Block	1,550	2,468	3,124	3,399
Add:- Capital work in progress	398	285	285	285
Long Term Loans and Advances	1,693	1,871	1,854	1,764
Investments	100	115	115	115
Net Working Capital	407	217	42	469
Total Assets	4,148	4,956	5,419	6,032
Cash Flow Statement (INR mn)	FY13	FY14	FY15E	FY16E
Cash profit adjusted for non cash items	445	679	968	1,233
Add/Less : Working Capital Changes	(41)	(188)	269	54
Operating Cash Flow	403	491	1,237	1,288
Less:- Capex	(786)	(1,015)	(974)	(674)
Free Cash Flow	(383)	(524)	263	614
Financing Cash Flow	643	285	(198)	(235)
Investing Cash Flow	(1,036)	(1,154)	(943)	(571)
Net change in Cash	10	(379)	95	481
Ratio Analysis	FY13	FY14	FY15E	FY16E
Income Statement Ratios (%)				
Revenue Growth	48.0	37.9	38.8	27.4
EBITDA Growth	47.2	44.3	41.2	28.5
PAT Growth	53.9	31.7	31.9	32.0
EBITDA Margin	54.1	56.6	57.6	58.0
Net Margin	29.2	27.8	26.5	27.4
Return & Liquidity Ratios				
Net Debt/Equity (x)	0.1	0.2	0.1	0.0
ROE (%)	11.1	11.7	13.4	15.8
ROCE (%)	13.5	16.0	18.3	21.5
Per Share data & Valuation Ratios				
Diluted EPS (INR/Share)	9.6	11.8	15.3	20.2
EPS Growth (%)	33.5	23.5	29.9	32.0
DPS (INR/Share)	1.3	1.5	2.7	3.6
P/E Ratio (x)	35.0	28.4	21.8	16.5
EV/EBITDA (x)	21.5	14.9	10.5	8.2
EV/Sales (x)	11.6	8.4	6.1	4.8
Price/Book (x)	3.6	3.1	2.7	2.4
Dividend Yield (%)	0.4	0.4	0.8	1.1

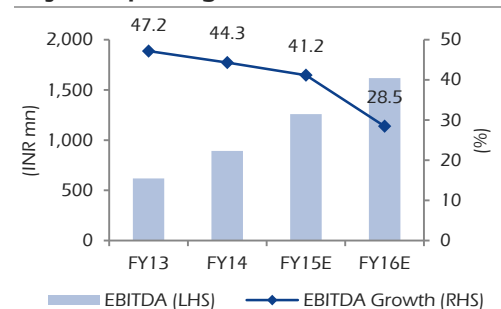
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Revenue & margin growth trend



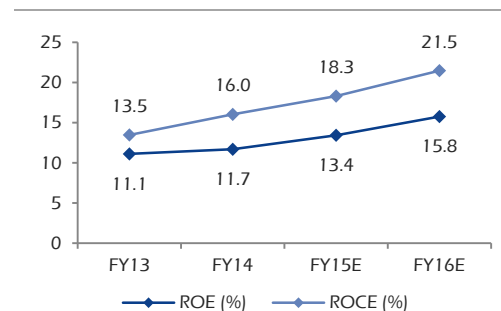
Source: Company, Elara Securities Estimate

Adjusted profit growth trend



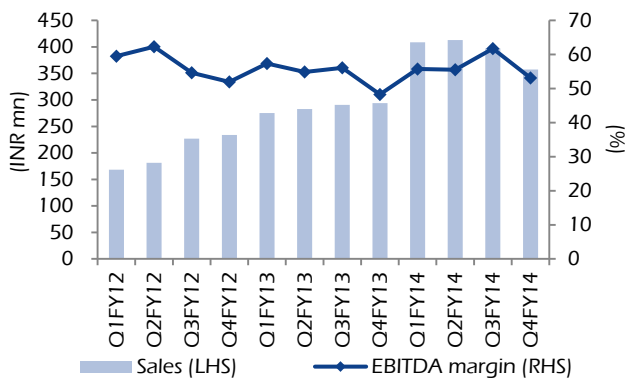
Source: Company, Elara Securities Estimate

Return ratios



Source: Company, Elara Securities Estimate

Exhibit 1: Quarterly run-rate stable



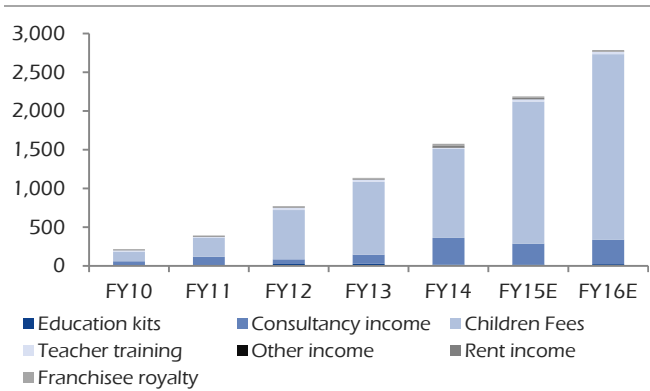
Source: Company, Elara Securities Research

Exhibit 2: Aggressive growth guidance

Particulars	2014-15	2015-16
Number of centers		
Self-Operated Tier I Opening	105	130
Self-Operated Tier II & III Opening	280	355
Additions in Tier II, III cities	45	45
Additions in Tier I	15	15
Global Champs	25	50
Under Fitouts (Tier II & III Cities)	30	30
Under Fitouts (Tier I)	10	10
Total self operated	510	635
Franchisees	147	197
New Franchise Centers Opened	50	60
Total Franchisees	197	257
Total Number of Centers	707	892

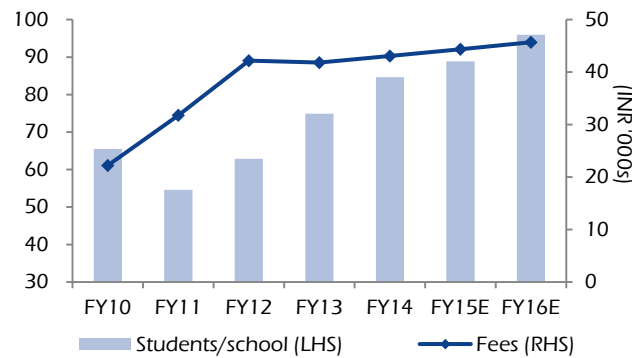
Source: Company, Elara Securities Research

Exhibit 3: Revenue growth led by preschool fee income (INR mn)



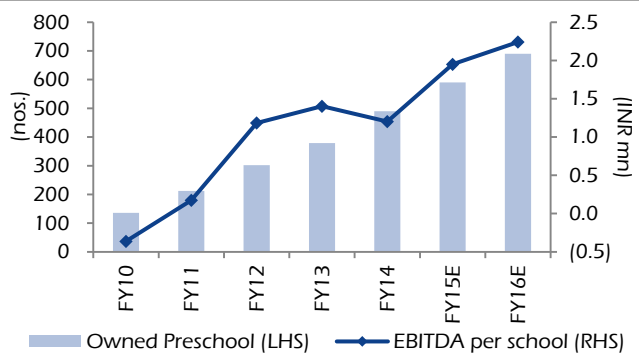
Source: Company, Elara Securities Estimate

Exhibit 4: Student/center to grow 7% over FY12-16E



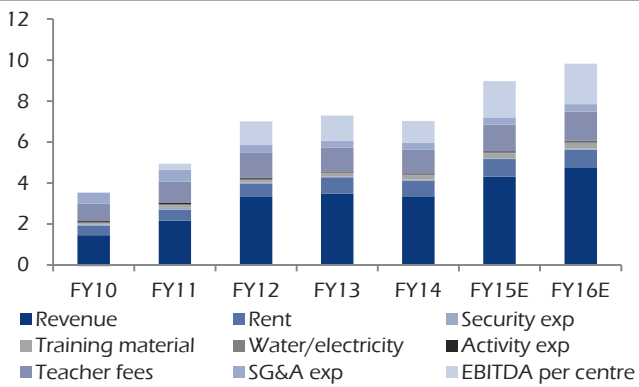
Source: Company, Elara Securities Estimate

Exhibit 5: Operating leverage kicks in with an increased school base



Source: Company, Elara Securities Estimate

Exhibit 6: Fixed cost structure leads operating leverage (INR mn)



Source: Company, Elara Securities Estimate

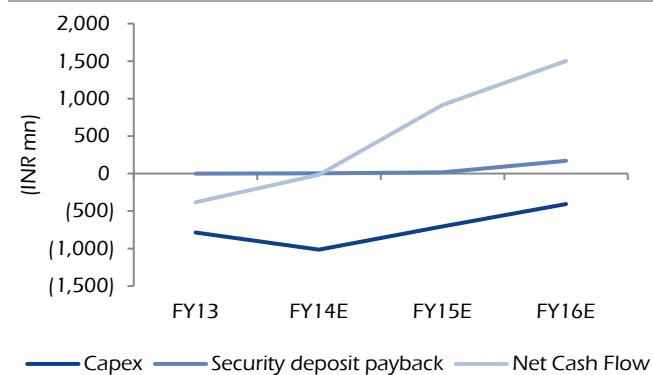
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Exhibit 7: Reengineering ROC

Particulars (INR mn)	FY13	FY14	FY15E	FY16E
EBIT	484	722	941	1,219
Net Assets (after K-12 assets sale)	4,444	5,104	5,330	5,681
ROC (%)	10.9%	15.1%	18.0%	22.1%

Source: Company, Elara Securities Estimate

Exhibit 8: Turning cash flow positive (INR mn)



Source: Company, Elara Securities Estimate

Exhibit 9: Valuation overview

Particulars (INR mn)	Amount
Gross Asset Value	14,090
Add: Cash & Equivalents	685
Less: Debt	826
Market Cap	13,948
Diluted Shares (mn)	37.7
Fair Value per Share (INR)	370
Current Market Price (INR)	335
Upside (%)	10%

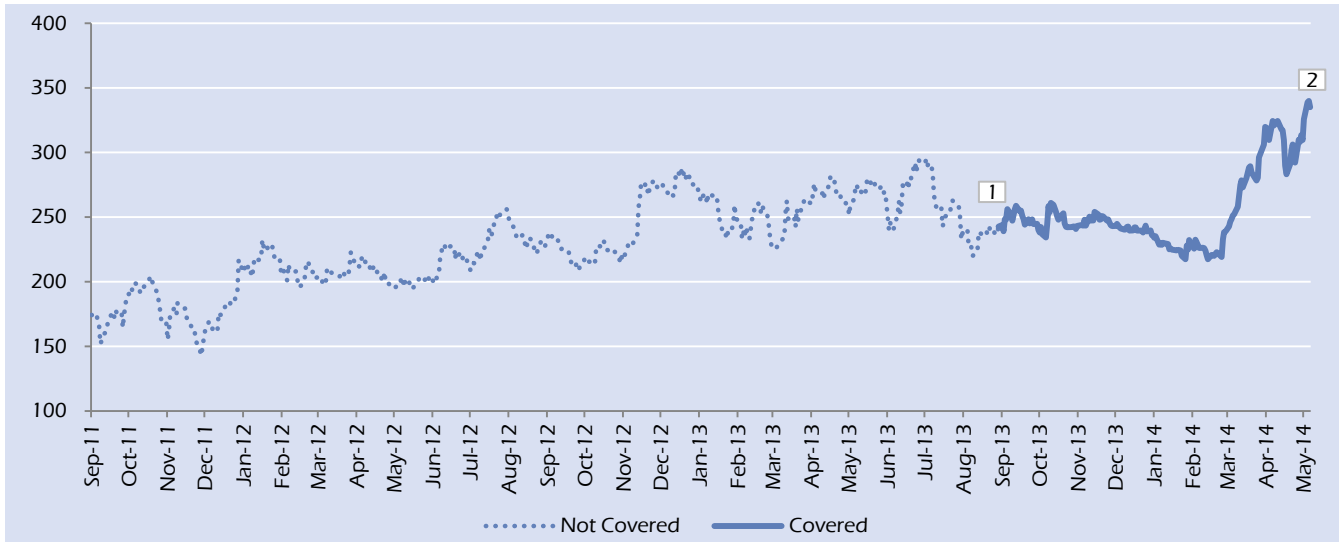
Note: as on 28 May 2014; Source: Bloomberg, Elara Securities Estimate

Exhibit 10: Change in estimates

Particulars (INR mn)	Previous		Current		Change (%)	
	FY15E	FY16E	FY14E	FY15E	FY14E	FY15E
Revenue	2,121	2,675	2,187	2,788	3	4
EBITDA	1,193	1,505	1,259	1,618	6	8
PAT	592	777	579	764	(2)	(2)

Source: Elara Securities Estimate

Coverage History



Date	Rating	Target Price	Closing Price
23-Sep-2013	Buy	INR 370	INR246
28-May-2014	Accumulate	INR 370	INR335

Guide to Research Rating

BUY	Absolute Return >+20%
ACCUMULATE	Absolute Return +5% to +20%
REDUCE	Absolute Return -5% to +5%
SELL	Absolute Return < -5%

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