

Indian Education Services Sector

Minister gives top priority to education in the run-up to the budget – Educomp, Everonn to benefit most

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- The Indian finance minister recently commented that education would be given top priority in the coming union budget. This stance is in-line with earlier budgets where spend on education has been increasing sharply (50% CAGR over three years).
- We expect this growth in budget allocations to continue strongly when the minister announces the budget on 29 February. This would give sustained long-term growth for companies targeting this spend.
- The biggest beneficiaries would be companies aggressive in the government school ICT projects; allocations to these increased four times in FY08 over the previous year. Our discussions with vendors reveal that projects involving close to 30,000 schools would be up for bidding over the next few months.
- We thus maintain our positive stance on Educomp and Everonn, which are aggressive in the government school ICT project space and the K-12 space in general. We maintain our OUTPERFORM ratings on these two stocks.

Government school ICT projects could benefit most

The government introduced the "ICT in schools" scheme in FY3/06, to drive greater computer penetration in rural government schools in India. ICT (Information and Communication Technologies) projects involve outsourcing setting up of computer labs in government schools, with an aim to use them in the education process over the long term. Companies such as Educomp, Everonn, and NIIT directly target this spend in their ICT businesses.

This project was probably one of the biggest beneficiaries of recent increases in spends on education sector; budget allocations increased nearly four times in the FY08 budget. We expect strong growth in budget allocations to continue toward this project.

Figure 1: Valuation metrics

Company	Ticker	CS Rating	Price		P/E (x)		P/B (X)
			Local	Target	T+1	T+2	
Educomp Solutions Ltd	EDSL IN	O	3,870	5,235	104.3	46.7	40.6
Everonn Systems	ESIL IN	O	770	785	89.4	43.8	20.7
NIIT	NIIT IN	U	119	123	27.6	19.2	6.5

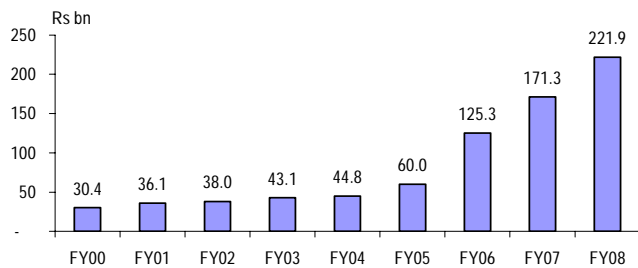
Note: O = OUTPERFORM, N = NEUTRAL, U = UNDERPERFORM
 Source: Company data, Credit Suisse estimates

Education to be accorded highest priority in coming budget

The finance minister recently reiterated strongly that education would get top priority in the coming union budget, probably even higher than agriculture (*Economic Times*). He stressed that the country's high growth rate necessitated improving literacy levels and education standards in the country.

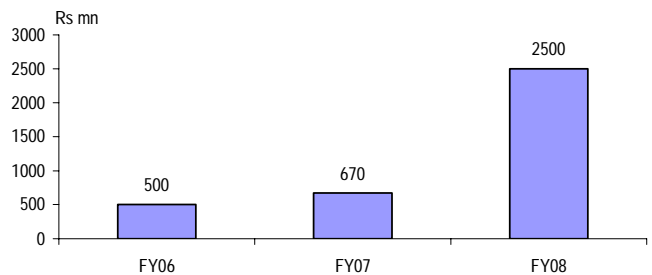
We note that successive budgets since 2005-06 have seen sharp increases in budget allocations to the education sector. The recent comments from the finance minister indicate that these allocations could continue to grow strongly.

Figure 2: Allocations to school education in successive budgets



Source: indiabudget.nic.in, Credit Suisse estimates.

Figure 3: Government budget allocations to "ICT in schools" project



Source: indiabudget.nic.in, Credit Suisse estimates.

This sharp increase in spends is showing in the large number of projects that are coming up for bid in coming months. Our discussions with vendors reveal that bids for ICT projects for close to 30,000 government schools are expected to come up over the next few months (compared to less than 15,000 schools that Educomp, Everonn, and NIIT are together working in currently). These projects would be across major states like Karnataka, Andhra Pradesh, Maharashtra, Punjab, Himachal Pradesh, etc.

Educomp, Everonn in strong position to tap this spend

Outsourcing of school ICT projects is the easiest part of overall government spend on education that can be tapped by the private sector, in our view. (For more details, please read our report "India Education Service: Be part of the revolution," published 11 Dec-07)

Companies like Educomp and Everonn, which are aggressively pursuing such projects, are in the best position to tap the increasing government allocations to education sector, in our view. We maintain our OUTPERFORM rating on both these stocks.

On the other hand, NIIT could be selective in its bidding and may thus see lower number of project wins. Further, NIIT is more geared to (1) mature US corporate training market and (2) the domestic IT training market over which we have concerns on near-term demand. We maintain our UNDERPERFORM.

Companies Mentioned (Price as of 12 Feb 08)

Educomp Solutions Ltd (EDSO.BO, Rs3575.00, OUTPERFORM [V], TP Rs5235.00, MARKET WEIGHT)
Everonn Systems India Ltd (EVSI.BO, Rs731.10, OUTPERFORM [V], TP Rs785.00, MARKET WEIGHT)
NIIT (NIIT.BO, Rs114.55, UNDERPERFORM [V], TP Rs123.00, MARKET WEIGHT)

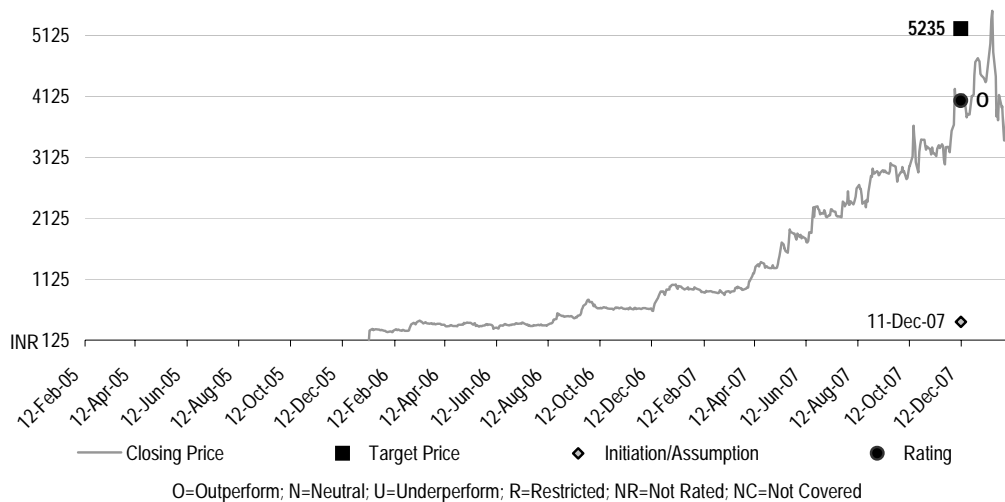
Disclosure Appendix

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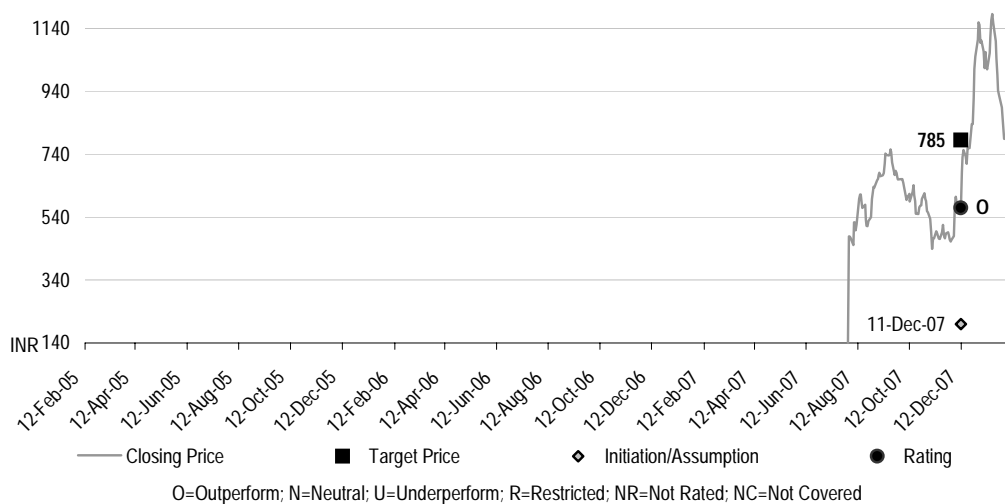
See the Companies Mentioned section for full company names.

3-Year Price, Target Price and Rating Change History Chart for EDSO.BO



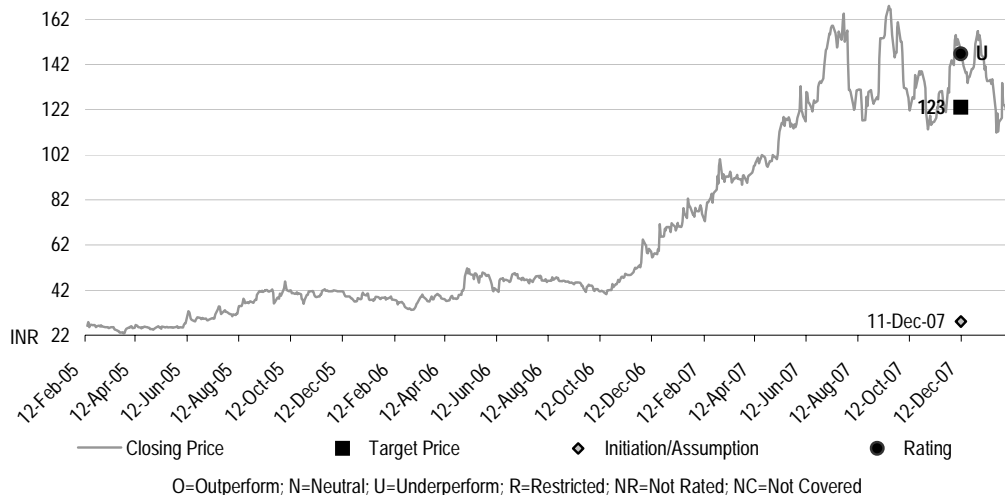
EDSO.BO Date	Closing Price Price (INR)	Target Price Price (INR)	Rating	Initiation/ Assumption
11-Dec-07	4,054.1	5235	OUTPERFORM	X

3-Year Price, Target Price and Rating Change History Chart for EVSI.BO



EVSI.BO Date	Closing Price Price (INR)	Target Price Price (INR)	Rating	Initiation/ Assumption
11-Dec-07	568.85	785	OUTPERFORM	X

3-Year Price, Target Price and Rating Change History Chart for NIIT.BO



NIIT.BO Date	Closing Price Price (INR)	Target Price Price (INR)	Rating	Initiation/ Assumption
11-Dec-07	146.7	123	UNDERPERFORM	X

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Neutral: The stock's total return is expected to be in line with the industry average* (range of $\pm 10\%$) over the next 12 months.

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Price Target: (12 months) for (EDSO.BO)

Method: We value Educomp on a DCF model. We assume strong near term growth rates, 12.9% medium term growth and 3% terminal growth, 10.6% WACC. This gives a target price of Rs5235.

Risks: The key risks to our target price of Rs5235 for Educomp are: 1) execution risks as the company is in early growth stage in its business lines, and is also launching new businesses like K-12 schools 2) change in regulation thereby impacting the business model

Price Target: (12 months) for (EVSI.BO)

Method: We value Everonn on a DCF model. We assume strong near term growth rates, 11.7% medium term growth and 3% terminal growth, 10.6% WACC. This gives a target price of Rs785.

Risks: The key risks to our target price of Rs785 on Everonn include: 1) execution risks as the company is in early growth stage in its business lines, and is also launching new businesses 2) change in regulation thereby impacting the business model

Price Target: (12 months) for (NIIT.BO)

Method: Our Rs123.00 target price for NIIT Ltd is derived on a sum-of-the-parts basis. The core business is valued on a DCF model. We assume strong near term growth rates, 6.7% medium term growth and 3% terminal growth, 10.6% WACC. This gives a target price of Rs100 for core business. We value the stake in NIIT technologies using 3-month average price at Rs23 per share of NIIT Ltd. This gives a target price of Rs123 per share of NIIT Ltd.

Risks: The key risks to our Rs123.00 target price for NIIT Ltd include: 1) strong growth in IT training enrolments in India, where we expect a slowdown 2) strong growth and higher than expected margin improvement in the company's US corporate business

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