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Higher Education: tough road for private equity

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RAJA
PARTHASARATHY
Managing director, IDFC Private Equity

HIGHER EDUCATION: TOUGH ROAD FOR PRIVATE EQUITY

As far back as early 2004, **IDFC Private Equity Co. Ltd**

first explored a potential investment in Manipal Universal Learning as part of our social infrastructure investing mandate, but did not pursue it further for various reasons. As we continued to explore other investments in the education sector, we began to appreciate that this company was the only one that had the right combination of brand, scale and promoter ethos. Over time, as our team became more comfortable with the inherent scalability of the education services model and the strength of the Manipal brand, we re-engaged with the Pai family on a possible investment. As promoters of the Manipal Educational and Medical Group (MEMG), Dr Ramdas Pai and his son Ranjan had nurtured MEMG's 50-year reputation for integrity and quality in education and healthcare. We initiated talks with the company for an investment in the entire "for-profit" education services businesses, instead of only one part.

Early on, we also identified vocational training as an investment opportunity, given the unorganized nature of the skills-training sector and the widening skills gap in India. It was our view that the single largest obstacle to high gross domestic product growth was not so much the bottleneck in infrastructure but the availability of trained and skilled manpower. Our team impressed the promoters with our passion for education and with our enthusiasm to introduce them to potential business partners such as City and Guilds even before making the investment.

The company's distance education programmes that were offered in partnership with Sikkim Manipal University (SMU), the first government-private initiative in the region, and supported through a network of around 500 distributed learning centres nationwide, were subject of a court directive challenging educational institutions offering distance education beyond state borders. We tapped into our network of advisers to understand how this was likely to unfold. This ability to take informed regulatory calls has been a strength of IDFC PE; a year into our investment, events played out as we had anticipated, and the Distance Education Council approved SMU's distance education programmes.

Higher education in India has always been a difficult field for private equity (PE) due to the requirement that providers of degree-granting institutions are not permitted to earn distributable profits; rules surrounding K-12 education are similarly difficult. Between 2005 and 2009, private equity investment in education totalled less than \$300 million, a mere drop in the ocean as compared with the overall growth capital requirements of the sector.

Hence, the company's strategy of expanding its footprint globally in order to mitigate single-country risk, balancing unregulated and lightly regulated sectors across its business portfolio, and associating with best-in-class partners to support

the rapid scale-up of new businesses was both coherent and compelling.

For a few years before we invested, the company had been registering steady growth, but the wider education opportunity had barely been scratched. In September 2006, IDFC PE and Capital International invested approximately \$70 million for a 30% stake in the company. At the time, the company's principal business, providing support services to distance education, had less than 50,000 students.

Among the reasons why we first turned down the investment opportunity in 2004 was because we believed the company need-ed new professional leadership. And so even before we made our investment, we identified a new chief executive who had a prov-en track record in scaling businesses and was passionate about education. Anand Sudarshan, who was known to our team, was hired from the information technology (IT) sector. Our team also introduced one of our advisers to the Pai family and he became a trusted sounding board for the family and the management.

Over the next four years, we initiated and supported a wide range of strategic acquisitions: India's largest testing service (MeriTrac), a leading Caribbean medical college (American Uni-versity of Antigua), a Singapore-based online MBA provider (U21Global) and a joint venture with the world's largest skills certification agency (City and Guilds, UK), among other things.

What has allowed the company to raise more private capital than any other company in India's education sector has been the reputational integrity of the Manipal brand, the company's clean financial structure (no complex web of trusts and management companies), the lightly/non-regulated and profit-focused nature of the constituent businesses in their respective geographies, the expanded professional management team, and the progressive approach of the Pai family towards the role of external stake-holders in the company.

In the four years since our investment, the core business of providing support services to distance education has seen a rise from 50,000 students to 180,000 students; revenue and operating profit have risen around four times. Today, it is a global educa-tion services firm with a portfolio of exciting businesses, ranging from semi-skilled training to medical education. It is a pioneer in infusing technology into learning and teaching, and has won sev-eral accolades. The road ahead is filled with opportunity, which further strengthens the firm's positioning for an eventual listing.

The views expressed by the author are personal.

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