

MPS BUSINESS QUALITY INSIGHTS

Strategic Assets		Distinctive Architecture	
Strong Macmillan legacy brand that has been a pioneer in this space. Strong foundation - Intellectual Property, domain skills, and highly-skilled people.	Competitive Forces/ Bargaining Power	Customers	B2B - All major publishers in the journal & Education segment. Some of the key customers are- Wiley, Reed Elsevier, McGraw Hill, Cengage, Springer, MacMillan, Oxford with Billin \$ Sales. Some like Elsevier \$ 5 Bn Annual Sales. Publishing market is a USD 700 BN, while digital publishing market is ~ USD 33 BN but growing at a fast clip. Outsourced publishing technology services market is estimated to be ~ USD 1.5 BN market and growing at 15%. The outsourcing penetration for publishers is pretty low at the moment (< 2-3%) but expected to rise given a) realization of importance of technology platforms and b) cost pressures faced by them. These two drivers should increase outsourcing spends for publishers going forward
Strong customer base with potential to increase wallet share significantly			The publishing industry is undergoing dynamic fast-paced changes - technology, content formats, consumption devices. Publishers who are not able to adapt are falling behind. Thus technology spends are expected to increase manifold. This coupled with low growth and high cost pressure is leading to increase in outsourcing to vendors. Large Publishers are all consolidating Technology Vendor base. At the moment there are only 5-6 players who have become big and qualify to be 'core vendors' for author-to-reader pre-publishing services . The publishers have strong dependence on existing vendors. This in a way evens out the bargaining power. There are a huge number of relatively smaller players, who have some technology solution components and customers, but probably are not nimble enough to adapt to pace of tech change and/or are in financial struggle. Many of them qualify as Acquisition targets for the 5-6 bigger players.
Stickyness with clients - being fully integrated into customer processes & platforms. Becoming indispensable vendor for their clients		Segments	Strong stickyness with customers. Extremely difficult for even existing large vendors to access new customers. Acquisitions are proving to be a better route to faster new customer access. Outsourcing budgets of large publishers are huge but do not see much of growth year on year. Cost pressures being high, the accent is on getting more out of the same budgets each year. With most large publishers choosing to consolidate Vendor base, pace of customer penetration may accelerate for the top-rated players.
Low cost structure - presence in India- Dehradun			Journals -33% Books -26% Fullfillment -10% MPS Technology - 10%
Strong investments in technology and platforms - enables reusability for clients and manage pricing pressure from clients with higher productivity/efficiency gains			Unlikely to get a piece of the action as Customers are very reluctant to part with existing solutions/build from scratch. Customer process/platfrms married deeply to existing Vendor processes/solutions
Nimble management - 'Move your own Cheese'. Continual investments in imagining the future, re-skilling, to be future ready		Other IT/Players	Size of the addressable pie unattractive for the IT Majors
Disproportionate Future?			Acquisition of a pre-publishing technology vendor by regular IT players look remote at the moment
Core Vendors Trend - Ratioinalisation and consolidation of vendor base - Increasing share of outsourcing budget to key players like MPS		Industry/ Competition	It's a closed industry group mostly. Everyone knows everybody - who matters. Large Customers cannot discard/replace/move away from existing technology solution pieces. If they have an issue with a small vendor (technology, nimbleness, financial) normally they will nudge bigger stable players with a good track record like MPS - to look at acquiring. Customer-blessed Acquisitions!!
Investment in technology and products - DigiCore platform could be huge going forward			SPS, Aptara, Innodata, SPI Global, NewGen are players who have scaled up to a level. SPS is a player that has stellar margins
One of the strongest among the 5-6 key players on this front. MPS has been making continual investments in building blocks for end-to-end Technology Platforms			Company Revenue (FY14 Revenue) EBITDA, % SPI Global 1000 + 20% Aptara 626.4 20% Innodata 390 11% SPS Global 208.4 52% Newgen 120 41%
MPSTrak, MPSInsight, DigiCore - also to be available as SAAS (Software as a Service). Probably the only one to have already invested in building a Front End (FE) apart from the pre-publishing (Back-End) platforms			Addressable Opportunity Size is huge. Given the size of the larger individual players vis-à-vis annual publisher budgets there seems to be huge headroom for everyone to grow. Keeping pace with technology changes, focus on controlling costs, retaining/growing customer confidence and aligning closely with Client road-maps - key factors to sustainable growth
Complete FE+BE Pre-publishing to Publishing platform being built/deployed grounds-up by MPS for a Scientific publisher			

MPS BUSINESS QUALITY INSIGHTS (2)

What can go wrong?	Mitigation?
Poor acquisition(s). Unlike earlier acquisition, ticket sizes will be 5x to 10x bigger this time round. Could be much more complex	Customer blessed acquisitions; Management Track Record;
Organic scale-up may take time and this could impact growth rates in the interim	3 Acquisitions showing good traction; Core Vendor progress
Technology Disruption	Probably remote for a player like MPS who is ahead of the curve
Wage Costs Spiral	Probably still a few years away as Dehradun can accommodate 2x shifts; Productivity/Efficiency gains
Very High Customer Concentration	Deep Client Relationships; Client Confidence; Management rather views this as a Strategic Asset

MPS BUSINESS QUALITY INSIGHTS (3)

Business Value Drivers		Growth Rates	EBITDA Margin	Capital Turnover	ROIC	Invested Capital (Crs)	EPA/Sales	EPA/Sales - future value creation lead indicator Relevant to look at the last 3 year numbers as the company has turned around. If the company executes on its vision, the numbers could get better from here with improved scale	
		3 Year Average	68.00%	32.00%	2.20	54.00%	63.00	13.00%	
		5 Year Average	Loss to Profit	19.40%	2.20	28.00%	59.00	4.00%	
BQ Bottomline	Earnings Quality:	<i>Capital Efficiency; High Dividend Payout; Free Cash Flows</i>		<p>Strong cash flow relationship with profits. Average CFO/PAT last 4 years - 1</p> <p>Very strong dividend payout - average of > 60% as dividend payout</p> <p>Strong cash flow generation - Generated ~ 120 Crores of cash flow over FY12-FY15</p> <p>Strong Future Value creation - EPA/Sales @13% is exemplary among similar size businesses across sectors</p>					
	Nature of Industry:	<i>Competitive Intensity? Industry Growth rates?</i>		<p>Fragmented Industry. Overall industry is growing at ~ 15%. Core Vendor consolidation trend among large Publishers</p> <p>Annual Outsourcing budgets are stable, if not growing. Accent is getting more volume of work done at lower costs. Margin pressures are there. Players with sharp focus on controlling/reducing costs through controlled wage bill and continuous productivity/efficiency improvements, likely to sustain.</p>					
	Opportunity Size:	<i>How big is the runway? How many years out?</i>		<p>Publishing industry revenue pool is USD 700 + BN. Outsourcing spends of the publishing industry are abysmally low (penetration of ~2-3%) but growing. Current outsourcing opportunity is expected to be USD 1.2 BN growing at 15%.</p> <p>Compared to current size of leading players, the runway is huge and increasing. There is enough leeway for many players.</p>					
	Capital Allocation:	<i>Able to invest large Capital at high ROIC?</i>		<p>The capital allocation record so far has been spectacular. 3 successful acquisitions EPS, TSI, which are now fully integrated, and contributing significantly. The industry is fragmented with many struggling players with technology base but unable to maintain profitability and/or scale up. Opportunities to invest larger capital exists - to acquire technology/customer relationships base.</p>					
	Predictability:	<i>How many variables in the Business?</i>		<p>75% of business comes from top 10 clients. The business from large customers is steady, long term in nature. Predictability of the business therefore hinges on 2 key aspects.</p> <ol style="list-style-type: none"> 1) Revenue from top 5/10 clients; growth rate of the same 2) Employee cost as % of revenue - Management is focused to keep this within 40-45% range 					
	Sustainability:	<i>How hard is it to dislodge from its perch?</i>		<p>Customer stickiness is extremely high. Existing players have high entry barriers as they are deeply entrenched into the client's system which prohibits them from changing vendors frequently. This makes entry of new players extremely tough. MPS engagement with existing customers is deepening with increasing volumes each year.</p>					
	Disproportionate Future:	<i>Building blocks in place for disproportionate future? Do multiple Optionalities exist?</i>		<p>Continuous investments in technology and platforms over the last 2-3 years. With the acquisitions fully integrated, a more complete technology services portfolio allows MPS to offer richer breadth of services and tap more customers. MPS now has a complete back end suite of pre-publishing products, along with investments in Front-End publishing product suite - currently being deployed for a Scientific Publisher group. In 3-5 years, these building blocks may play a big role in driving profitability and establishing newer more profitable</p>					
	Business Strategy & Planned Initiatives:	<i>Is the company likely to grow efficiently & emerge stronger in next 2-3 years?</i>		<p>Publishing outsourcing market is expanding. MPS has deep client relationships and is now slowly getting positioned among top 2-3 in the industry - pre-qualifying as Core Vendor - a stable credible technology partner to large publishers. MPS's investments in platforms & technology will help it in driving productivity gains and improve efficiency. MPS's management has a sharp focus on controlling costs with a strong track record - previously ran a commodity BPO business at stellar margins.</p>					
	Key Monitorables:	<i>Next 2-3 years - what are the key monitorables, key health indicators?</i>		<ol style="list-style-type: none"> 1) Revenue from top 5/10 clients; growth rate of the same 2) Employee cost as % of revenue - Should be less than 45% 3) Acquisition- What/Why/Price 					
	Near Term Visibility:	<i>Next 2-3 years - how strong is the visibility?</i>		<p>10-15% organic growth visibility looks easily achievable. Even higher organic growth may be achievable on the back of a) Large publishers focusing on vendor rationalisation b) Acquisitions starting to bring in strong results c) Management hunger for growth.</p> <p>Management is on record about doubling revenues in next 3 years, by bridging the gap through acquisitions - for which they have CASH raised. Management's confidence is also evidenced by the solid dividend payout over the last 2-3 years.</p>					
	Long Term Visibility:	<i>5-10 years on - how likely to survive & prosper?</i>		<p>Over next 5-10 years business should become stronger- scale up. Technology and outsourcing spends should increase for publishers given the way content consumption is happening. Successfully integrating next bigger ticket acquisition and reaching to double current size is a critical milestone. If Management keeps executing, MPS could become a very strong player in its domain.</p>					
Valuation Spotlight?	BQ Category:	<i>Laborious? Or Disproportionate Smarts?</i>		<p>Large Publishers are becoming increasingly more dependent on a few core vendors to survive & prosper. MPS is in a sweet spot today - it enjoys high client confidence and is positioned strongly to build on its technology and IP strengths, front-end and back-end publishing platforms. MPS business is displaying signs of building-in disproportionate SMARTS in its business model over medium to longer term. A category. Might migrate to A+ over 3-5 years, if it successfully executes on its vision & strategy.</p>					
	Business Transition Track Record:	<i>Managed significant business transition to its advantage? What impresses most?</i>		<p>The new management did justice to the strong capabilities and brand of Macmillan. Quickly turned around the business within 1-2 years. Management has strong focus and is nimble. Their capital allocation record so far has been terrific.</p>					
	Performance vs Perception GAP:	<i>Current P/E or Perception captures business quality/performance? How big is the GAP?</i>		Current P/E- 21X PE ex Cash- 18X EV/EBITDA- 12X	<p>Such a business should ideally get 20-25X P/E given the consistency, predictability, and sustainable nature of business and Management pedigree. Freedom to execute (low competition intensity), and Optionalities in medium to long term give high confidence</p>				