

**ENTREPRENEURSHIP IN EDUCATION:
The Business of Un-recognized Schools**

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INTRODUCTION: A BUSINESS PLAN FOR AN UNRECOGNISED SCHOOL

The 1990s taught us that regulations had become a barrier to economic growth and progress. Unshackled, India responded by doubling the 'Hindu rate of growth'; heralding a new liberal era of policy-making. Yet today India remains a country where reforms are largely stillborn, especially in areas like education.

So far, the government's glacial pace has not stalled private initiative in education. Even as the Government sleeps, poor parents are waking up to a new sort of freedom: the freedom to choose a better education for their children. For in the space of a few years, private unrecognised schools have become a major alternative to the government system¹, especially for the children of the poor. These schools however, can cost a fortune for many poor parents, and students there cannot appear for All-India board exams. Still, such schools are popular and are apparently, growing in number.

Some studies have suggested that this is because these schools are superior to those that the children leave behind². Yet little is known in depth about these schools, the way they operate, their finances, the facilities they typically offer and environment they exist in. Currently we are in the dark, unable to fully understand what impact current government policies are having on these schools, or what impact they might have in the future.

This project aims to bridge that gap, by studying these schools as businesses, albeit ones which face a certain amount of official persecution. I focused my research on schools in Mumbai and the outer suburbs, with the aid of NGOs (Non-Government Organisations) like *Pratham*, and other individuals who took an interest in our project. For the research, I interviewed principals and school owners directly. The result is a complete business plan, a detailed and relatively comprehensive look at everything an entrepreneur would need to know to succeed in this business. Through this we hope to understand the private market in education better than we do today, and formulate policy prescriptions that are better suited to its needs.

¹ Tooley James, and Others (Kindon, G (1996), Aggarwal, Y (2006))

² Tooley, James. September 2005. Private Schools Serving the Poor: Working Paper: A Study from Delhi, India. Accessed on 26 February 2007 at <http://www.ccs.in/ccsindia/pdf/Delhi-Report-Tooley-new.pdf>

GOVERNMENT REGULATIONS AND STANDARDS

Indian regulations and bureaucracy can be a formidable challenge for any entrepreneur. Those who want to start schools however, probably have it worse than many others. To start with, the laws in place make running a profitable school illegal. Years of jurisprudence, right from the Unni Krishnan judgement³, have reinforced the notion that for-profit schools are inherently evil. Consequently, a web of regulations has emerged to cater to official sentiments, and micromanage schools along the way. However, as we will see in our study, most entrepreneurs have found a way around this.

To run a school, an entrepreneur must tackle, and learn to love, the Maharashtra Employees of Private Schools (M.E.P.S) (Conditions of Service) Regulation Act⁴, of 1977 and that of 1981. Both Acts together govern the treatment of every employee in a private school, from the level of pay to discharge, seniority and qualifications. Under Schedule 'B' of the M.E.P.S Act 1981, a school may hire only teachers with a Diploma in Education and those who have passed the Primary Teachers Certificate Exam to teach at the primary class level (1st to 4th standard). Teacher salaries at this level must be in line with Government standards, set by the Fifth Pay Commission at Rs 5,000/ month.

Additionally, under Appendix 38 of the M.E.P.S Act of 1981, a school may not have less than 70 children in a single division. However, if the school has 71 students or more it may create additional divisions. The school must however take permission from the authorities, which can delay the process indefinitely.

Failure to comply with these and other regulations affects recognition, a status that allows the children of a secondary school to sit for C.B.S.E board exams and get a government approved degree. At the primary level, a recognized school can issue a transfer certificate, which allows the child to make a smooth transition into secondary school. Since a government approved degree typically carries more weight than an ordinary diploma, recognition is a coveted status that is much sought after by parents.

In the city of Mumbai, recognition is conferred on schools by the Education Department of the Mumbai Municipal Corporation⁵. Schools typically apply for recognition after they already opened, to the Superintendent, Private Primary Schools, Education Department in a prescribed format. A form⁶ is available from that office that lists 26 documents and forms that must be submitted along with the application. School authorities must submit evidence that they are a registered society, details of the fees they wish to charge, and have their bank balance audited for at-least three years, amongst other things. The

³ Unni Krishnan Judgement. Judgement Information System, Supreme Court.

⁴ Dighe, S.D, N.G Patkar and A.K Gupta. 2005. The Maharashtra Employees of Private Schools (Conditions of Service) Regulation Act, 1977.

⁵ BMC Education website. Accessed in February 2007 at

<http://www.mcgm.gov.in/forms/Masterdisplay.aspx?dno=MTA%3D-Hk%2Buffz58TY%3D&slmno=MTA%3D-Hk%2Buffz58TY%3D&tlmno=MQ%3D%3D-Yh62L2fcsbg%3D>

⁶ Education Department. *Final Checklist for Recognition of Schools in Greater Mumbai*. Municipal Corporation of Greater Mumbai.

schools are examined by the Superintendent, after which the sanction of the Education Committee is sought. After this is received, the schools are deemed to be recognized.

Private schools can either be aided or un-aided. The aided schools have their salaries paid by the government, in line with government approved pay-scales. However, the free money comes with plenty of strings attached. Principals of such schools must get government approval to appoint a teacher⁷, allowing others to influence the staffing decisions of their schools. Fee levels are typically low and are set according to the standard. At the school this researcher visited, fees were Rs5 to Rs6 per month. Nevertheless, this status has been becoming increasingly difficult to get, based on the feedback from principals, and has been closed for English medium schools.

Unaided, recognized schools have more freedom in hiring, and other matters, but do not appear to have much freedom when it comes to setting fees. The government formula stipulates that the school must take total costs, including salaries, and divide them by the number of students. There is a provision to include a certain percentage for development costs, which may have become more liberal over time.

However, the independence of unaided schools is under attack. In recent years Parliament has sought to interfere in this area and dictate how such institutions may operate. In response to a bid to set a quota for backward castes in such schools, the Supreme Court declared in its judgement on August 12, 2005, in the case of *P.A. Inamdar & Ors. vs. State of Maharashtra & Ors*⁸ that such actions violated the private nature of the institution. The State could not intervene in admissions policy, by setting a quota or demanding reservations on any criteria except merit.

State interference however would still be legitimate in other areas. Schools were to remain debarred from profiteering or charging a capitation fee, but a 'reasonable surplus' varying from 6 to 15 percent would be allowable for development and expansion purposes.

In response, Parliament unanimously passed the *93rd Constitution Amendment Act*⁹ giving itself the right to make any law regarding admissions in any educational institution (aided or unaided) with for the benefit of socially and educationally backward groups. At this point it is unclear how much freedom such schools will continue to exert as a result of this far-reaching initiative.

Unrecognized schools by contrast, are almost totally unregulated. They are can set their own fees and standards, hire and fire teachers at will, admit whom they please and operate with minimal governmental interference. This is not because the government

⁷M.E.P.S Act (Pg 342 and 149) (Also see circulars)

⁸ P.A. Inamdar & Ors. vs. State of Maharashtra & Ors. Supreme Court of India Judgement Information System. Accessed on 30 March 2006 at <http://judis.nic.in/supremecourt/qrydisp.asp?tfnm=27111>
Summary: http://prayatna.typepad.com/education/2005/08/summary_of_the_.html

⁹ India Code Information System (INCODIS). *The Constitution (Ninety-Third) Amendment Act, 2005*. Accessed on 30 March at <http://indiacode.nic.in/coiweb/amend/amend93.htm>
Summary: http://prayatna.typepad.com/education/2006/04/implications_of.html

hasn't tried to rein them in. From time to time, the government announces and implements drives against such schools only to withdraw the campaign when it is out of the public spotlight. However, the possibility that the government may shut down more schools in the future represents a very real risk to entrepreneurs in this area.

Despite the threat, unrecognised schools seem to have become booming businesses that cater to all levels of society. At the elite level, according to education consultant Mr. Mohit Lalwani¹⁰, schools are aligning themselves with foreign certifications like the International Baccalaureate (IB) in place of the I.C.S.E and C.B.S.E boards. This allows them to skip the Indian education bureaucracy entirely, while still giving their students the option to rejoin it at any stage (A No-Objection Certificate is required.).

At the lower level, options are expanding for the poor as well. In the city of Mumbai, unrecognized schools are coming up increasingly in suburban areas typically close to or inside a slum area. Although free of government regulation, these schools do not exist in a vacuum of government oversight. As mentioned before, the survival of such schools is often jeopardized by the government's attempts to shut them down. Naturally, most entrepreneurs try to maintain a good relationship with the authorities, and bribes are a common practice.

Unlike their elite cousins, these schools seem to want recognition, but cannot fulfil the requirements. The solution is to take an undertaking, a formal commitment that the school will meet the conditions at some point in the future. This solves the problem temporarily, and allows the school to operate legally. However, it's doubtful if these schools will ever be able to comply with the rules as ordained. Most claim they cannot afford to pay salaries on the scale the government has set, because parents are too poor.

Some other conditions, including provisions for open spaces are also difficult to comply with or afford in the city or suburbs, especially in slum areas. A recent amendment to the BMC's development control rules is typical: all new schools have to keep 40% of their space aside for open spaces¹¹. At one of the schools I surveyed, complying with this law would mean an additional rent of Rs 8,800 every month. This works out to an additional Rs. 5 to Rs. 9 a month per child in rental costs- a 10% to 20% hike in fees. More problematic however, would be the issue of space itself. If they cannot find it inside the slum area, schools may have to move further away. This would mean losing students, a large number of whom come to the school for its proximity.

Not surprisingly, most regulations seem to be doing more harm than good. Any entrepreneur would struggle to learn the ropes, unless they had some sort of political backing. Hopefully this section has helped make that task a little easier, and shed some light on the problem areas. From now on, we will focus more on identifying the business case and model that these schools operate on.

¹⁰ See file "Mohit Lalwani" in Appendix

¹¹ Nair, Shalini. 2007. No Schools Without Playgrounds: BMC. *Times of India*, 23 February.

BUSINESS STRUCTURE

Business structure typically deals with the kind of business organization: whether the company is a sole proprietorship, a partnership, a corporation or otherwise. Each has different strengths, and analyzing the form that prevails often gives clues to the complexity and organization of the market.

As expected, most operations seemed to be rather small, and not linked to any wider chain, or operating on efficiencies of scale. Often the owner was sitting in the school itself, operating in a position that is typically occupied by a principal. This seems consistent with the behaviour of owners of sole proprietorships or partnerships.

Recognition however, demands that the schools be run by a society or a trust. It is not known whether school owners go through the trouble of registering as such, or ignore the law completely.

Since slum areas are typically illegal, property has no official value as collateral. It is hard to believe that anybody would offer financing against property that could be demolished at any time. Still, at least one school in the survey said they had financing for their self-owned property; a reflection perhaps of other people's confidence in their school.

Still, formal financial support is likely to be hard to find. Since these schools are illegal, and because education is not an industry, banks do not typically lend money. Furthermore, since these schools must operate as non-profits, the public is not likely to take any interest in its shares. Hence, a preponderance of small scale enterprises seems rational. These are the easiest and cheapest to set up, and cost less to set up and operate than other, more complicated structures.

MARKET RESEARCH

For this study, I wanted to understand the potential of private unrecognised schools from the perspective of an entrepreneur. Our first task, is to determine whether there is enough demand or a sufficient need for these schools that could sustain them in the long run. We look at these and other questions in the following subsections

ECONOMICS

Private schools do not make any sense if people are not willing to pay for an education. To find out whether a market exists, we must try to calculate the number of children attending schools across the city, and the number who will do so in the future. We must also account for those students who are unable to pay, and the amount of demand for private unrecognised schools at present.

To assess the size of the education sector, we can begin by counting those children in recognised schools. According to the Brihanmumbai Municipal Corporation (B.M.C) the governing municipal authority for Mumbai, there are 1,056 recognised private primary schools in Mumbai, serving over 495,369 students, and 49 private secondary schools, serving 48,038 students (Data as on 1st March 2006¹²). Additionally, there were 1,177 municipal primary schools, serving 424,918 students¹³, and 51 municipal secondary schools serving around 80,000 students¹⁴. The latter data however could be suspect as previous studies have documented evidence that government schools inflate enrolment.

Assuming the numbers are correct, we still have to account for the number of children enrolled in unrecognised private schools. There is little official data for this, but the size can sometimes be inferred from reports in the press. According to a story in the Times of India, dated 20th of June 2003, the BMC has identified nearly 231 unrecognised schools¹⁵ in Mumbai, 48 of which are in the Western suburbs. However these are not separated by school type, clubbing big ICSE and (possibly) IB schools, with smaller and poorer cousins. The result is that total enrolment could vary from a conservative estimate, of just over 45,000, to a high of 115,000 or more.

However that data is for 2003. Recent reports suggest that the number of schools may have increased since then. According to a Times of India story, between the years 2000 and 2005, municipal schools lost about a 134,554 students to unrecognised private primary schools¹⁶. If the report is true, then the **size of the unrecognised sector in Mumbai could approach 250,000 students a year**¹⁷.

¹² Brihanmumbai Municipal Corporation. *Private Schools*. See Sheet "BMC STAT" in File "Data" in the Appendix.

¹³ Brihanmumbai Municipal Corporation. *Municipal Schools*. See Sheet "BMC STAT" in File "DATA" in the Appendix. This data is from the BMC's main education office at Dadar. It may include data about BMC run secondary schools as well.

¹⁴ The data on secondary schools was taken from the website for the Municipal Corporation of Greater Mumbai (M.C.G.M) also known as the Brihanmumbai Municipal Corporation or B.M.C.

¹⁵ 2003. Future of 100,000 students in limbo. *Times of India*, 20 June.

¹⁶ Shrinivasan, Rukmini. 2006. Mumbai civic schools have few takers. *Times of India*, 28 September.

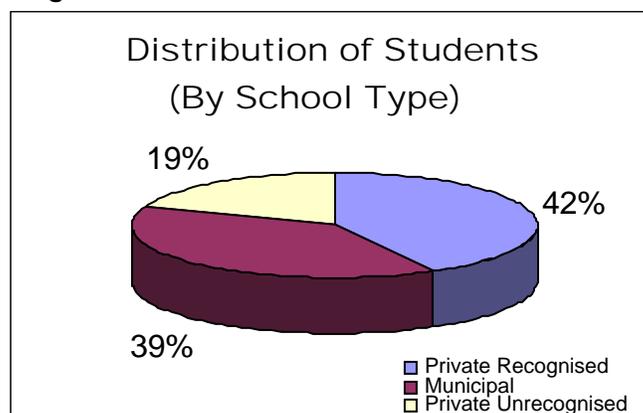
Adding the numbers we calculate that the **size of the education sector in Mumbai**, between 2005 and 2006, was **1,298,379 students a year**¹⁸. However, this number is fraught with many errors. It may undercount the number of students by ignoring those who never enrolled in government schools, or be inflated by government estimates. The number also does not count enrolment at unrecognised schools unknown to the BMC, and assumes that those who left municipal schools have joined private unrecognised schools in large numbers. The estimate also fails to count the number of children added to the school system every year as a result of the increasing population, and does not distinguish between elite unrecognised schools, and those for the poor.

Nevertheless, if we use this number, then the division of students between the private unrecognised, recognised, and municipal school system appears to be as in Table 1.1 below.

Table 1.1: Distribution of Students by School Type.

Type of School	Number of Students	Percentage
Private Recognised	543407	42%
Municipal	504918	39%
Private Unrecognised	250054	19%

Figure 1.1



From the study results, education appears to have a lot of potential. Most schools in the sample reported that they had no problems filling seats. A number of schools were rejecting applications; one school turned away almost two-thirds of all aspirants¹⁹. However, school principals do have an incentive to exaggerate the number of applicants they receive and likewise reject; therefore this data is probably not highly accurate. It also is not clear whether rejections were on the grounds of merit (a problem of poor demand), or supply related constraints, such as poor infrastructure or insufficient teachers.

Accessed online on February 25, 2007 at the Times of India Online.

¹⁷ See Sheet "DistriofStudbySchooltype" in file "DATA" in the Appendix.

¹⁸ Same as Above.

¹⁹ See Appendix. "School Report"

Nevertheless, responses from schools to this question are summarised below (Table 1.2).

Table 1.2: Percentage of Students Admitted

Type of School	Area	Percent Admitted*
School A, Recognised, Aided	Mazagaon	25%
School B, Unrecognised	Antop Hill	73%
School C, Unrecognised	JJ Hospital	33%
School D, Unrecognised	Baiganwadi	NA

Note: * As a percentage of forms sold.

CUSTOMER PROFILES

The 'customers' at unrecognised schools aren't really the students themselves. Sure the kids matter, but it's the parents who must be sold on the quality of education itself. To understand how school owners did this, let's look more closely at the profile and psychology of the typical parent in this study²⁰.

Almost all the schools in this study had a large Muslim clientele. This was not by design, but a reflection of the areas in which I was allowed to conduct this study. Many parents, especially those whose children attended unrecognised schools, were poor or otherwise lower-income. Family incomes, as reported by principals, ranged from Rs. 3,000 to Rs. 8,000 a month (except at the aided school).

Parents from different socio-economic backgrounds seemed to want different things for their children. At the private aided school, authorities said that parents were looking for a holistic education, and asking about computer courses, sports and other extracurricular activities. At unrecognised schools, parents were happy if their kids were learning English, and performing better than children elsewhere. To keep and attract students, some schools offered computer training as well or scholarships and reduced fees. Parents, school authorities said, also wanted schools to be recognised. Unfortunately, most schools were operating only in a semi-recognised status.

Schools from low income areas were also more likely to cite proximity to students as a chief attraction for parents. Granted this study cannot be considered authoritative, but this seemed to be a general trend. According to principals, poorer parents could not afford to walk too far accompanying children, since they would be missing work. In the daily struggle for survival, parents needed that extra time to ensure that they had enough money to bring home in the evening. Location was crucial for girls as well, since parents were not willing to let them walk alone to schools that were too far away. This means that neighbourhood schools could often compete for students, even if the education was better elsewhere.

²⁰ See "School Report" in the Appendix. All data used can be found in this file unless cited otherwise.

Nevertheless, principals did not appear to be taking their customers lightly. Parents, they said, were very vociferous, and it was difficult to keep their trust. Even at reputed schools, principals said that parents were willing to fight anything they felt was unfair to their children. For any new school owner, principals had some salient advice: don't count on getting any free publicity; the first word-of-mouth referrals come only after three to four years of operations.

That is important, since word-of-mouth is the primary way in which parents find out about good schools in their neighbourhood. Children at any school, who are ahead of their peers elsewhere, quickly find themselves joined by others from the neighbourhood. This is because most parents make a decision about a school after observing or hearing about the performance of its students.

Parents also respond to conventional marketing, including posters, pamphlets and door to door outreach. Some schools also resort to making presentations at neighbouring primary schools, or to groups of influential parents.

To teach effectively, schools need to maintain discipline in the classrooms. Too much discipline however, can drive children away. Parents are not averse, even in poor areas, to pulling out their kids if they have been hit by teachers. School owners must run a difficult balancing act to keep the status quo. The solution is to hire teachers with the training and experience to handle a classroom.

LOOKING AT THE COMPETITION

Unrecognised Schools face competition from other private schools, both recognised and unrecognised, and from schools established by the municipality.

The latter have several advantages over unrecognised schools including, proper buildings, open spaces, and large classrooms. As a result of the mid-day meal scheme, municipal schools can also offer free food, a perk only private aided schools can match.

Yet government schools aren't for everybody. One reason appears to be the distance between them and the students they cater to. At one site, the government primary school was 1.5 kilometres away. At another site in Mankhurd, *Pratham* volunteers told me that the municipal school was on the other side of the city, away from the slum areas. Students had to cross railway tracks to get there.

Even when municipal schools were nearby, the quality was typically so poor, that parents often opted for private schools instead. That is not to say that private schools were much better as a whole, only that they were a little less mediocre. Private school principals however, said that the lack of teacher attendance, inadequate inspection, high student to teacher ratios and poor maintenance at municipal schools, gave them a big advantage.

Aided schools also represent a threat to schools in the slum areas. Since fees at such schools are low, they could in theory, attract students away. However there are only a few aided schools in Mumbai close to slum areas, and admissions there are highly competitive. As a result, the majority of slum children have to look elsewhere.

The main competition to unrecognised schools comes from within their own. Any area with an unrecognised school typically has two or more such schools nearby. Here, depending on the area, the location, academic strength, and quality of the school make all the difference.

OPERATING A SCHOOL: DATA AND ANALYSIS

To construct an accurate model of an unrecognised school, we must know more about how these schools operate. The data below helps shed some light on this question, and provides some perspective on what it's like to be a school entrepreneur.

Let us begin by taking a look at the heart of every school: the quality of its teachers. Quality is not the same as credentialed, but the government believes otherwise. According to the law, recognised schools can hire only teachers with advanced degrees. Of the three unrecognised schools visited, only one had a full complement of BA/ BEd teachers as per the government standards. The other two however, did have a number of BA and BEd on staff.

Apparently, this sort of talent comes fairly cheap. At the entry level, the highest salary paid in an unrecognised school, was only Rs 3,000 a month. A teacher with experience, could hope to get only Rs. 4,500. Teachers at municipal schools however, can get upwards of Rs. 12,000 a month.²¹

Getting the right set of teachers is useless, if they don't have a place to teach. You need a building, close to where your students live. Location, as we have seen earlier, does make a big difference to the success of a school. A possible drawback is that since locations in these areas are typically illegal, they may offer no formal protection in the case of a dispute or a demolition.

Quality is also a problem. Most schools visited did not appear to be more than a simple structure, sometimes with an additional level for classrooms. None were open air, but that may be a quirk of this study. Owners maximised the use of space; classrooms had less than 7 square feet per child. The size of the typical classroom ranged from less than 150 square feet to 350 square feet. They typically had desks and benches for students, and a pulpit for teachers, along with a blackboard and chalk. Some classes had additional storage cabinets, hanging off the wall.

All schools had an office, with a desk and chair, and a cupboard for storage. Some schools had a computer in for administrative work, but it is not clear how they obtained the power to run it.

Rents, even in slum areas, can be fairly steep. A 3000 square foot school in the Central Suburbs for instance, can cost Rs 22,000 a month or more. Unfortunately, there is not enough data to properly compare rental costs across different schools. To construct a financial model, we shall have to make assumptions about the rental cost of our school.

²¹ Shrinivasan, Rukmini. 2004. Salaries eat up 86 pc of BMC school budget. *Times of India*, 18 September. Accessed online on February 27, 2007 at the Times of India Online.

On paper, schools have to comply with several regulations to be recognised. Apart from development control (DC) rules, schools have to be a registered society, supply information on the fees they wish to charge, offer teachers municipal pay scales, and carry fixed deposits for 6 months of salary payments²². You also have to comply with all notices issued by the Education Department prior to and following the date you establish the school.

Unrecognised schools however, barely comply with any of this. To get around the rules most schools adopt elaborate techniques, and pay officers in private to allow the school to continue. However, none of the schools surveyed wanted to discuss it, and therefore no hard numbers are available. Another way to deal with the problem is to take an undertaking with authorities to comply with the rules at some specified point in the future. This has already been discussed before.

To convince parents to come to your school, you need a good marketing strategy. Parents need to know where the school is and how it compares to others in the area. Popular ways of marketing include: hiring children to hold posters, passing out pamphlets, a simple notice on a school board, and a door-to-door outreach program. A school of a thousand students or more may spend Rs. 10,000 a year on such efforts, for two to three years before it gets any students coming in on a referral basis.

In any venture, there are bound to be those who default on the fees due. Since new children cannot be admitted after the academic year has already begun, most defaulters are probably given some leeway to pay fees. This reflected in the data collected; schools reported that some students had not paid fees for six months or more. Since exact numbers or percentages were not shared, we will have to make our own estimate (8% of revenues) for outstanding accounts and bad debt in our model.

Apart from credit, most schools offered scholarships to at least some children. At one school, the principal claimed that a quarter of the students were studying on reduced fees or for free²³. However precise numbers are again, not available, and like before we must make our own assessment. To be on the safe side, we should assume that schools gave at least 3% of revenues in scholarships and fee concessions.

²² See Appendix. Education Department. *Final Checklist for Recognition of Schools in Greater Mumbai*. Municipal Corporation of Greater Mumbai.

²³ See Appendix. "School Report"

MOVING TO THE MODEL

As we move into the final section of this paper, we should begin to assemble the data into an accessible format and look at all the assumptions that underlie them. Given below is a short catalogue of these, followed by a list of start-up expenses an entrepreneur is likely to incur.

ASSUMPTIONS

Financial Viability:

The goal of the model school in question is to be financially independent.

Bank Credit is not available:

Truly unrecognised schools are not likely to have much access to a loan, since the school itself is not regularised, and is often illegal. Personal credit is possible, but would result in attachment of the individuals own property.

Schools have to assume the risk of defaults and/or irregular payment:

For convenience, this number along with the value of scholarships offered is assumed to be 11% of yearly revenues. (Outstanding accounts are 5%, bad debt is an additional 3%, and scholarships and concessions are around 3% of revenues)

School is about to start its first year:

The school has to build up a reputation, and must therefore spend money on advertising. It also has to build up the number of students over the years (it does not open with full occupancy) and will therefore probably make a loss the first year.

Small School in the Central Suburbs:

The school is built for 160 children, in a slum somewhere between Sion and Chembur. The carpet area of the school is the same as that built up, around 960 square feet.

Rental rates are the same as the school surveyed in the area above

The school surveyed in our sample near Chembur and Sion, was paying Rs. 7.33 a square foot in rent monthly. At this rate, our model school would be paying Rs 7,040 a month in rent alone.

Advertising costs were sustained over three years.

All schools in the survey did some sort of advertising, ranging from a simple board outside and a notice of admission dates, to mass market campaigns with posters, pamphlets and a door to door outreach program. Although costs varied, the duration of these programs did not. All schools had to maintain advertising for at least three years. For the purpose of this model, the cost of such programs is estimated at Rs. 5 per child annually. Thus for our model school, advertising would run at least Rs. 800 a year.

Teachers in unrecognised low-income schools are paid quite little

The survey of schools found that salaries for primary teachers were typically lower than teachers at municipal or recognised schools. In primary schools, teacher salaries ranged from Rs 1,500 to Rs 3,500 a month for starters, and up to Rs 4,500 for someone with experience. Most schools pay a travelling allowance. Pay at recognised schools typically starts at Rs 5,000 a month. However, most schools do have to pay a travel allowance.

The model school is entirely primary. (From the 1st to the 4th Standard)

This eliminates much of the pressure to get recognised. It also simplifies our model further since now we only have to concentrate on the salaries for a single type of teacher.

Teachers are paid at the prevailing wage.

To be on the safe side we shall assume that the model school is on the same pay scale as other schools in the area. Thus all primary teachers at the model school get an average of Rs. 1,800 a month.

The school is able to fill about a third of the seats in the first year.

Since the school lacks a reputation, it's likely that only a few parents would make the move in the very first year. Still, we assume that management was able to bring around 53 new children to the school in the very first year.

After the first year, admissions grow by half every year.

To demonstrate the usefulness of the model in a short time frame, I have assumed that admissions grow very quickly. This may be unrealistic, but it could also reflect a process of learning, effective advertising, positive feedback and a renewed interest in the school's offerings.

The school is able to charge moderate fees.

New schools could face pressure to cut fees in the face of an established player. In this area there are three private schools, one of which charges only Rs 50 a month. However, the principal said he was still losing students to pricier schools, because parents prioritised a stronger English language curriculum. We will therefore assume that our school is one such school and is able to charge Rs. 120 a month for its superior English language training.

Word of mouth is minimal until the school is at least three years old.

No free publicity, the school must invest time and money on its own for at least three years. Students once in however, do not leave.

Compliance costs limited to 5% of Yearly Revenues.

Schools in the survey did not share data on off the table payments to bureaucrats and other authorities. To account for this expense, I have made my own estimate, keeping in mind previous studies of the subject of corruption in developing countries²⁴. (*Batra,*

²⁴ Kauffman and Stone (2003)

The School purchased just the right amount of furniture in the first year.

We assume for our study, that the principal knew exactly how many children were going to enroll in his school and bought furniture accordingly. This would mean furniture for around 53 children distributed amongst the classrooms.

School has the same inputs as schools in the study.

This includes benches with backrests, a desk for the teacher, fans in the office, cabinet for files etc.

Depreciation is 20% annually on all assets.

To make the study more realistic, depreciation was included in the cash flow statement.

STARTUP EXPENSES

The major expenses incurred in establishing a school, are summarised in the categories below. Market pricing was substituted for data that was missing from the survey.

Building:

Size: 960 square feet.

Area: Central Suburbs

Lease ²⁵ :	Rs 7,040 (for the first month)
Renovations ²⁶ :	Rs 4,000
	<u>Rs. 11,040</u>

Capital Expenditure List:

Furniture:	Benches and Tables:	Rs 3,100 (for 17) (laminated tables) ²⁷
	Teacher's Desk:	Rs 3000 (for 2) ²⁸
	Office Desk:	Rs 4000 (ordinary)
	Filing cabinet/Safe:	Rs 5,625 ²⁹ (50x30x17 cabinet) (with VAT)
	Office chairs:	Rs 900 ³⁰ (for 3 simple wooden chairs)
Equipment	Blackboards ³¹ :	Rs 1,200 (Rs 600 each, 24"x36")*
	Notice board ³² :	Rs 300 (Rs 300 each, 18" x 24")*

²⁵ From "School Report." See Appendix.

²⁶ An estimate of costs to make repairs to a small roof.

²⁷ To get a proper estimate, I had a carpenter quote me a price for 17 benches and tables. This is in my estimation might still be quite low, and entirely dependent on where the school is located (transport is extra)

²⁸ Same as above. Quote is for two desks.

²⁹ Venus Steel Products (India). 301, Kalbadevi Road, Mumbai -2.

³⁰ A ballpark figure.

³¹ Abdul Rehman Street- Near Crawford Market

³² Same as above

Fixtures:	Fans ³³ :	Rs 2,818.75 (3 oscillating table fans with VAT)
	Other ³⁴ :	<u>Rs 3,000</u>
		Rs. 23,943.75

Supplies:

	Chalk (2 boxes):	Rs 24 (1 box has a 144 pieces)
	Other:	Rs 300 (Staplers, Pens, and other stationary)
	Record Books:	<u>Rs.128 (For 2 books of 300 pages each)</u>
		Rs. 452

Advertising:

Every Year for three years:

	Posters/Leaflets:	<u>Rs 800³⁵</u>
		Rs 800

Contingencies and Working Capital:

	Contingencies ³⁶ :	Rs 20,000
	Working Capital ³⁷ :	<u>Rs 65,299</u>
		Rs 85,299

SUMMARY STATEMENT

Startup Expenses

Building and Location:	Rs 11,040
Capital Expenditure:	Rs 24,395.75
Advertising:	Rs 800
Contingencies	Rs 10,000
Working Capital	<u>Rs 65,299</u>
Total Startup Expenses:	Rs 1,11,535

³³ GMC Fans, General Electric Stores, Sardar Griha Building, Lohar Chawl, Mumbai -2

³⁴ Other fixtures, include lights, air conditioners, etc

³⁵ See "Assumptions"

³⁶ "Contingencies" are funds set aside for unpredictable expenses, or cost overruns. In this case, it is an arbitrary figure.

³⁷ "Working Capital" is defined as the difference between current assets and current liabilities. In this model however, it is assumed that suppliers do not extend credit, and banks do extend loans, because of the lack of formal protection. Hence working capital was assumed to be equal to the amount needed to meet the operating costs of the school for a year.

FINANCIAL PLAN

12 MONTH PROFIT AND LOSS STATEMENT

To illustrate the economic incentives at work in a private school, I have used data from the estimate of start-up costs along with other numbers in the study to draw a 12 month cash flow statement for the firm

In this model, the school burns through cash in the first year, losing up to 90% of its initial cash balance. This is largely due to high rental costs, high salaries and expenditures on equipment and furniture. Compliance (corruption) costs also drain profits, as do a large amount of receivables.

To get these results, I assumed some costs that were not supplied by any of the school owners in the survey. Apart from the corruption or compliance costs, I guessed at a number for travel allowances, based on what might be offered to a single teacher travelling in from another area. The number given for repairs and 'outside services' (the cost of assembling furniture and other capital goods, and transporting it to the site.) also fall under this category.

Some other numbers were omitted, due to a lack of data. I ignored the cost of electricity, water connections, and other utilities, primarily because school owners did not share this information with me. Nevertheless, it is an expense that should not be ignored in our model.

Finally, some assumptions may not match with how entrepreneurs behave in real world situations. For example, the model assumes that the school owner rents a building that is too large for the initial class, but continues the lease as is in the hope that enrolments in the next year catch up with the excess space. In the real world, entrepreneurs may try to renegotiate the lease, sublet the excess space, or shut down the school and terminate the contract.

The incentive to do so is clear in the model. Losing the extra space, could save the school close to Rs 40,000 over the year. This arrangement would still leave room for a 200 sq foot office, and 2 classrooms of 159 square feet each.

By playing around with the numbers in the statement we can tease out some interesting findings. In the model I have assumed that the school has two teachers with 26-27 children per class. This is not true of the majority of the schools we surveyed, a more typical number would be close to 50 students per class. In that case, the school would have only one teacher. Putting that into the model would mean cutting salaries in half, and that along with the savings on rent, could help the school eke out a thin operating profit. However, that disappears all together, if we subtract depreciation and outstanding dues.

Cutting salaries could help the school become more profitable. Savings of just Rs. 300 a month would boost monthly operating margins to about 7%. Collecting on outstanding dues would also boost profits. Bringing in a quarter of the outstanding accounts for the year would boost the operating margin to 21% for the month, assuming all the other changes above stick. Keeping the amount of receivables (outstanding accounts) down would boost operating margins by 5% over the year, and eliminating scholarships would add another 3%. That would be enough to more than double operating margins (from 7% to 15%), assuming everything else remained constant. In practice however, this seems to be more difficult than it appears.

Another option is to adjust timings so as to cycle more classes through the same classrooms. Thus a school that has teachers with strong English language skills could teach primary children in the day and offer more expensive, adult-oriented English classes in the evenings, when people get off work. This has the advantage of playing to the school's strengths; teachers who are skilled at English language instruction for beginners, and plenty of empty space, while adding to the economies of scale by dividing relatively fixed costs like rent among a greater number of customers.

In fact this is likely to be the way schools are actually operating. When not taking a morning class, schools are probably sublet for other things, or perhaps used to teach seniors, or impart adult education. Otherwise, running a school would be a fairly poor investment. Running a school that could be shut down at any time by the authorities would require a return that far exceeds other forms of equity (stocks or convertible bonds) **By keeping the student teacher ratio at about 50:1, and halving the rented space, the school owner could break even in the first year itself, and realize a 40-50% profit in the next.**

The statement of the school's 12 month cash flow appears below as shown. For the excel sheet with calculations, please look at the Appendix.

Cash Flow (12 months)

ABC School

Fiscal Year Begins: Jan-07

	Pre-Startup EST	Jan-07	Feb-07	Mar-07	Apr-07	May-07	Jun-07	Jul-07	Aug-07	Sep-07	Oct-07	Nov-07	Dec-07	Total Item EST
Cash on Hand (beginning of month)	111,535	93,076	64,198	58,508	53,119	47,729	42,339	36,949	31,559	26,170	20,780	15,390	10,000	10,000

CASH RECEIPTS

Cash Sales			5,851	5,851	5,851	5,851	5,851	5,851	5,851	5,851	5,851	5,851	5,851	5,851
Collections fm CR accounts														
Loan/ other cash inj.														
TOTAL CASH RECEIPTS	0	0	5,851	5,851	5,851	5,851	5,851	5,851	5,851	5,851	5,851	5,851	5,851	0
Total Cash Available (before cash out)	111,535	93,076	70,049	64,359	58,970	53,580	48,190	42,800	37,410	32,021	26,631	21,241	15,851	10,000

CASH PAID OUT

Purchases (supplies)		452												
Gross wages (exact withdrawal)			3,600	3,600	3,600	3,600	3,600	3,600	3,600	3,600	3,600	3,600	3,600	3,600
Travelling Allowance			410	410	410	410	410	410	410	410	410	410	410	410
Outside services		545												
Repairs & maintenance	4,000													
Advertising	100	400	300											
Compliance costs		3,816												
Accounting & legal														

Rent	7,040	7,040	7,040	7,040	7,040	7,040	7,040	7,040	7,040	7,040	7,040	7,040	7,040	7,040
Telephone														
Utilities														
Scholarships and Concessions			191	191	191	191	191	191	191	191	191	191	191	191
Interest														
Other expenses (specify)														
Other (specify)														
Miscellaneous														
SUBTOTAL	16,959	12,253	11,541	11,241	11,241	11,241	11,241	11,241	11,241	11,241	11,241	11,241	11,241	0
Loan principal payment														
Capital purchase (furniture)		16,625												
Capital purchase (equipment)	1,500													
Capital purchase (fixtures)	5,819													
Reserve and/or Escrow														
Owners' Withdrawal														
TOTAL CASH PAID OUT	18,459	28,878	11,541	11,241	11,241	11,241	11,241	11,241	11,241	11,241	11,241	11,241	11,241	0
Cash Position (end of month)	93,076	64,198	58,508	53,119	47,729	42,339	36,949	31,559	26,170	20,780	15,390	10,000	4,610	10,000

ESSENTIAL OPERATING DATA (non cash flow information)														
Sales Volume (rupees)			6,360	6,360	6,360	6,360	6,360	6,360	6,360	6,360	6,360	6,360	6,360	69,960
Accounts Receivable			318	318	318	318	318	318	318	318	318	318	318	3,498
Bad Debt (end of month)			191	191	191	191	191	191	191	191	191	191	191	2,099
Depreciation	122	407	407	407	407	407	407	407	407	407	407	407	407	5,001

BREAK-EVEN ANALYSIS

Breakeven Analysis

ABC School

Cost Description	Fixed Costs (Rs)	Variable Expenses (%)
Inventory or Materials		0.6
Direct labor (includes payroll taxes)	545	0.0
Other expenses (fixtures)	5,819	0.0
Other expenses (furniture)	16,625	0.0
Salaries (includes payroll taxes)	-	28.0
Supplies	-	0.6
Repairs & maintenance	4,000	0.0
Advertising	800	0.0
Travel Allowances	-	6.0
Accounting and legal	-	0.0
Rent	45,564	0.0
Compliance (Corruption costs)	-	5.0
Depreciation	5001	
Other (Equipment)	1,500	0.0
Owner's draw	-	0.0
Total Fixed Expenses	Rs 79,854	
Total Variable Expenses		40.2

Breakeven Sales level = Rs. 1,33,513

The school would need to make sales of at least Rs 11,126 a month (Rs 1,33,513 a year) to break even (not including scholarships, and outstanding payments) in the first year of operations. Above this level, marginal costs begin to decline, and any revenues over and above the variable cost constitute profit.

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