

L.E.K.

Special Report

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# Brazil's Burgeoning Private K-12 Market





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**About L.E.K. Consulting**

L.E.K. Consulting is a global management consulting firm that uses deep industry expertise and rigorous analysis to help business leaders achieve practical results with real impact. We are uncompromising in our approach to helping clients consistently make better decisions, deliver improved business performance and create greater shareholder returns. The firm advises and supports global companies that are leaders in their industries — including the largest private- and public-sector organizations, private equity firms, and emerging entrepreneurial businesses. Founded in 1983, L.E.K. employs more than 1,400 professionals across the Americas, Asia-Pacific and Europe.

For more information, go to [www.lek.com](http://www.lek.com).

# Brazil's private K-12 poised for growth

In early 2018, Brazil's largest for-profit education company, Kroton Educational SA, acquired Somos Educação S.A. for \$1.8 billion.<sup>1</sup> This is the latest in a string of high-profile investments in Brazil's private education sector. Consistent investment activity confirms a growing shift toward private sector provision, making Brazil among the most active education investment landscapes in emerging markets. In the K-12 segment, private sector growth is outpacing that of the public sector across Latin America (see Figure 1).

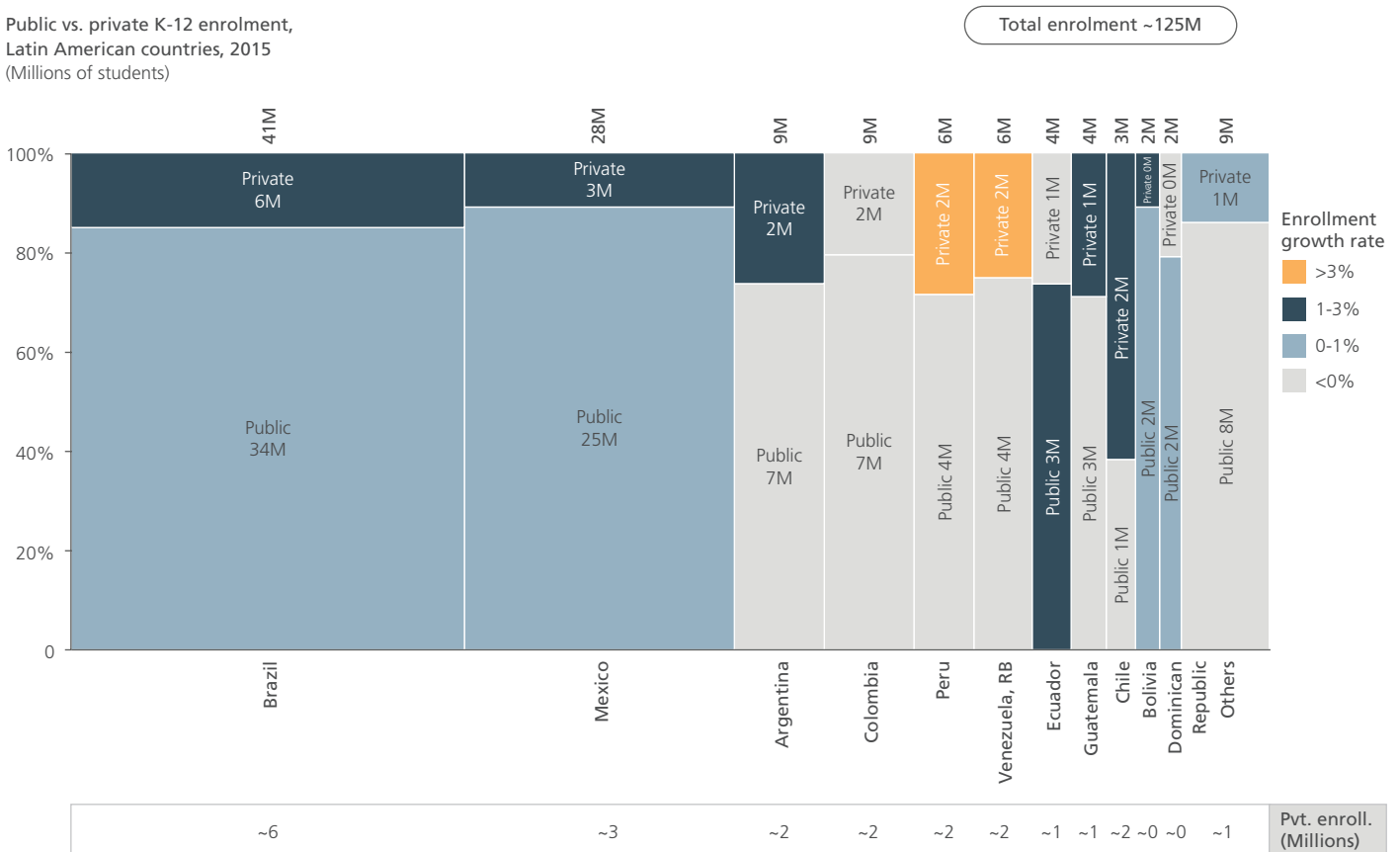
Brazil's private education sector has grown significantly in the past two decades. This growth has been fueled by the following key factors:

1. **Poor-quality public provision:** Brazil's public schools are overburdened and characterized by high student-teacher ratios and low learning outcomes. The state of public

education has driven demand for private provision, which delivers higher quality outcomes (see Figure 2).

2. **Rising affordability:** In the past two decades, Brazil's middle class has grown from 15% of the population to over 30% in 2018.<sup>3</sup> Increasing affordability, paired with a higher demand for features such as English language training and a more modern curriculum, has fueled demand for private schools.
3. **Favorable regulatory environment:** Brazil's government recognizes and supports the growing role of the private sector in serving the population's needs. This is evident in the favorable regulatory environment for private education institutions. In K-12, for-profit ventures are allowed and there are no explicit restrictions on fee growth.

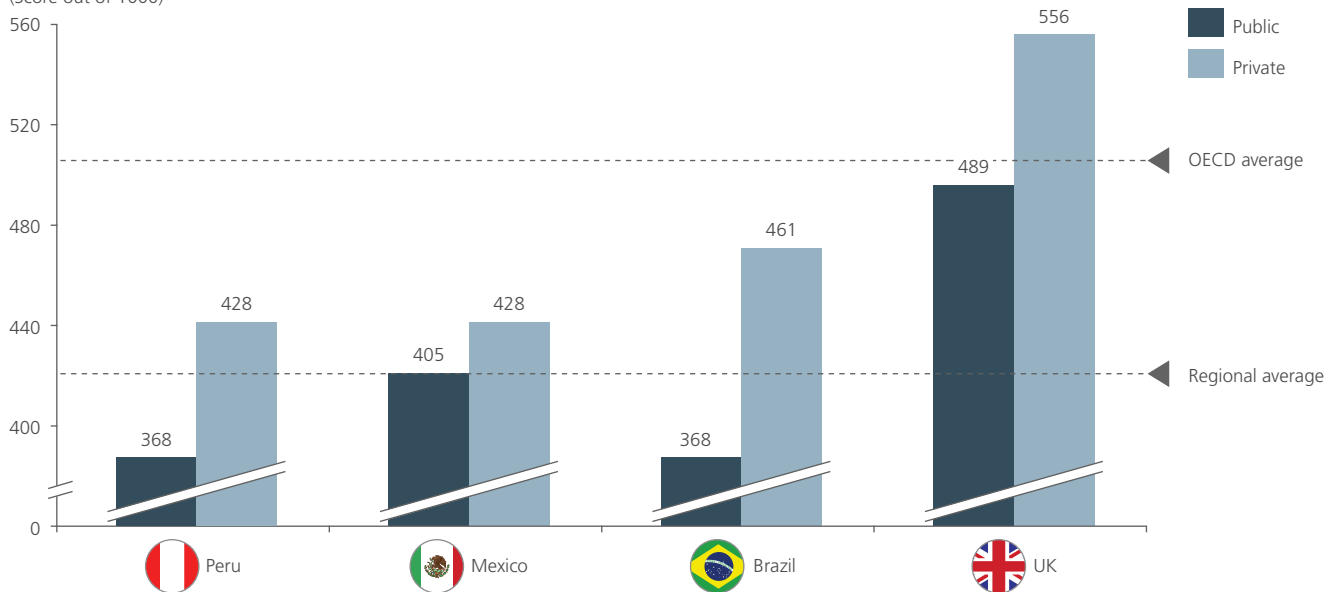
Figure 1  
Public vs. private K-12 enrollment, Latin American countries, 2015<sup>2</sup>



Source: UNESCO Institute of Statistics, World Bank Data, Press Reports

Figure 2  
PISA mathematics scores, select countries, 2015<sup>4</sup>

Program for International Student Assessment (PISA) mathematics scores,  
Select countries, 2015  
(Score out of 1000)



Note: The Programme for International Student Assessment (PISA) is a worldwide study by the Organisation for Economic Co-operation and Development (OECD) in member and nonmember nations intended to evaluate educational systems by measuring 15-year-old school pupils' scholastic performance on mathematics, science, and reading

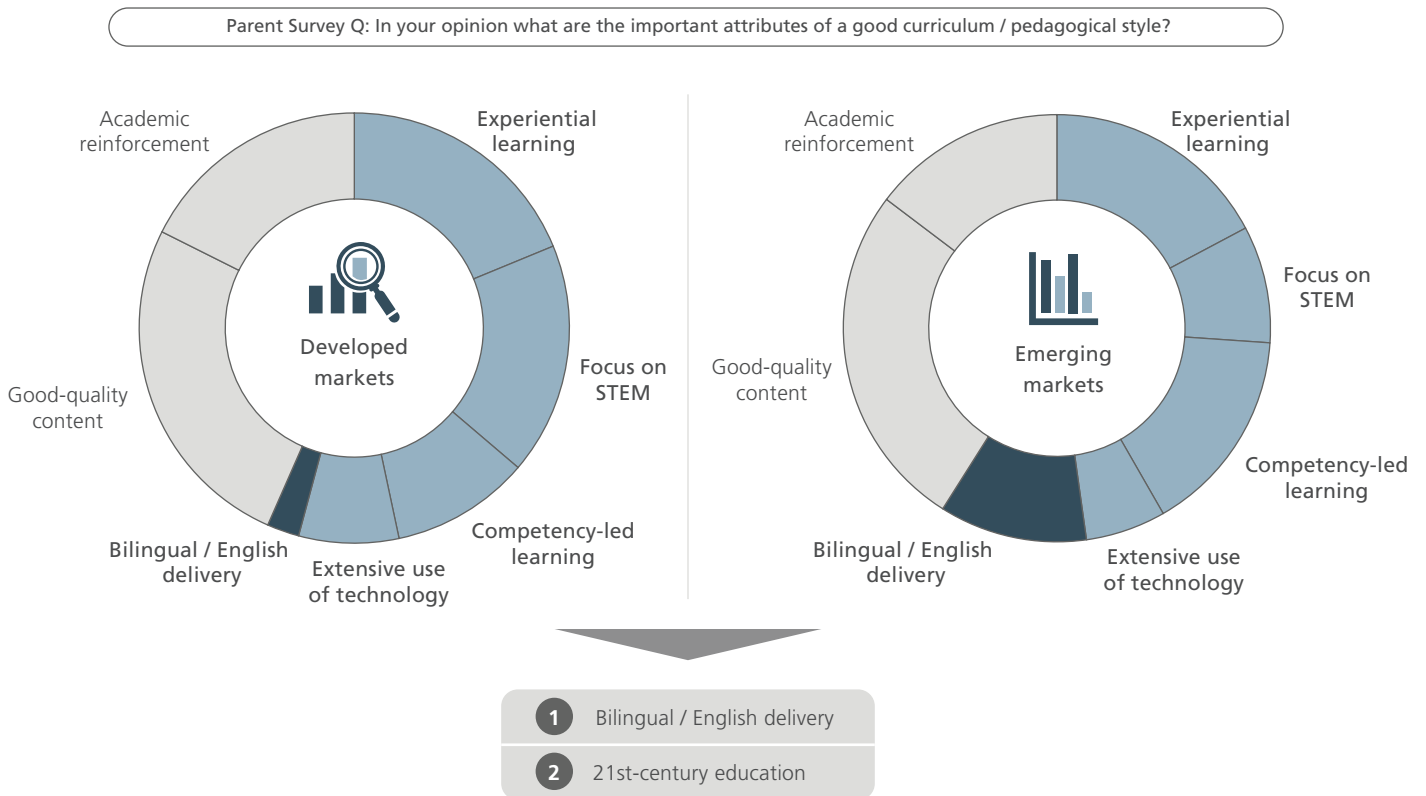
Source: OECD

Private provision in Brazil accounts for less than 20% of the overall K-12 market, while in other emerging markets like India, it is 30%. L.E.K. Consulting's global education practice believes that this shift to private provision will continue in Brazil, given the need for quality education and headroom for growth.

As the Brazil K-12 market continues to develop, what are some key themes that investors should be aware of?

# Key themes for investors: what do parents really want?

Figure 3  
Parent survey findings, developed and emerging markets, 2018<sup>6</sup>



L.E.K.'s has in-depth insight on education market needs across geographies. We conduct frequent surveys of parents and teachers, with over 20,000 global surveys in 2018 alone. Based on our investigations, there is a growing worldwide focus on 21st-century education. This is characterized by experiential learning, competency-led education, a focus on STEM<sup>5</sup>, and the use of technology and personalized learning (see Figure 3). In emerging markets like Brazil, there is also significant demand for high-quality English language training. Parents globally and in Brazil report that these needs are not being met adequately. In this *Executive Insights*, we discuss Brazil's growing appetite for English in schools, and technology-enabled 21st-century education.

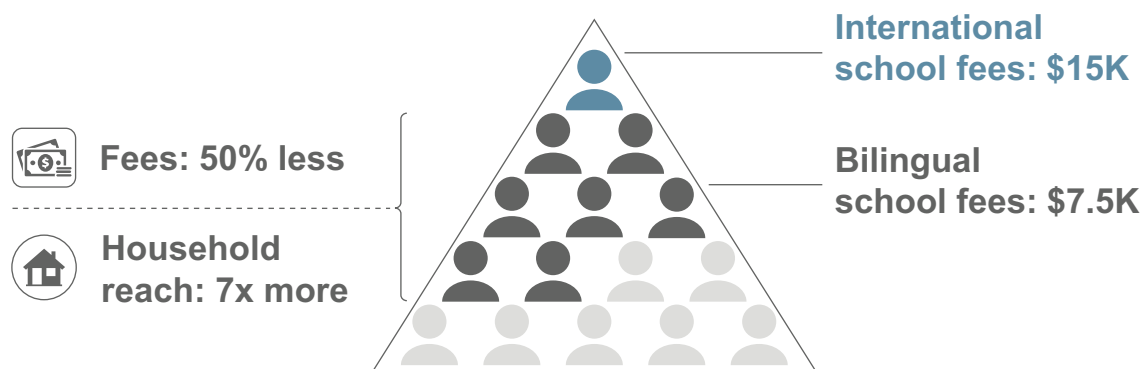
## 1. Increasing desire for English in schools

There has been a steep rise in demand for high-quality English instruction in schools. Historically, only premium international

schools offered high-quality English. However, with high fees (>. \$15,000), these schools catered to a small segment of the population (~1% of households) that often choose to send their children abroad for undergraduate studies.

A growing number of middle-income parents want to prepare their children for the global workforce while aspiring to send them to top local universities. These parents are looking for a more modern educational environment than that which is found in traditional national schools, including high-quality English instruction and a rigorous curriculum aligned to national standards. In order to cater to these needs, new models known as "bilingual schools" have emerged as the fastest-growing segment in the market. They offer a holistic international pedagogical approach while providing bilingual education that qualifies students for both local and international higher

Figure 4  
K-12 affordability, international vs. bilingual schools, Brazil<sup>7</sup>



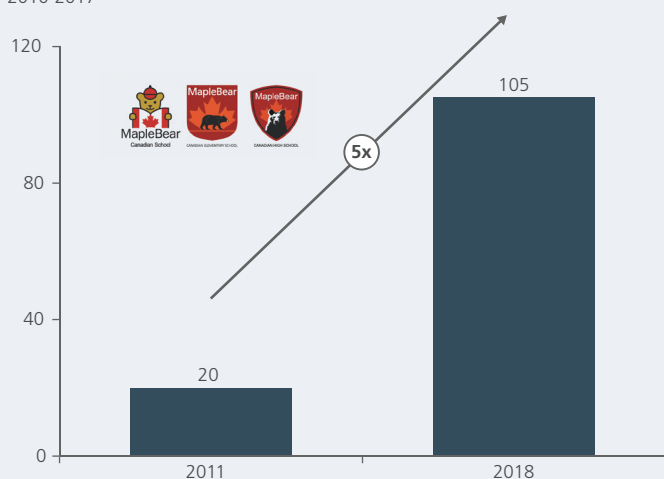
education. With fees that are around 50% lower than those of international schools, these schools reach over seven times the number of households in Brazil (see Figure 4).

The key challenge for this model is finding quality teachers who can deliver the bilingual curriculum, given the limited availability

of local bilingual teachers and the high cost of expat teachers. Providers must overcome this through better local teacher training and recruitment practices. Maple Bear, a bilingual school, has met this challenge by instituting internationally competitive training for local teachers. Training is led by Canadian teachers and is aligned to Maple Bear's customized bilingual curriculum (see Figure 5).

Figure 5  
Maple Bear case study<sup>8</sup>

Number of Maple Bear schools in Brazil, 2010-2017



### Key features

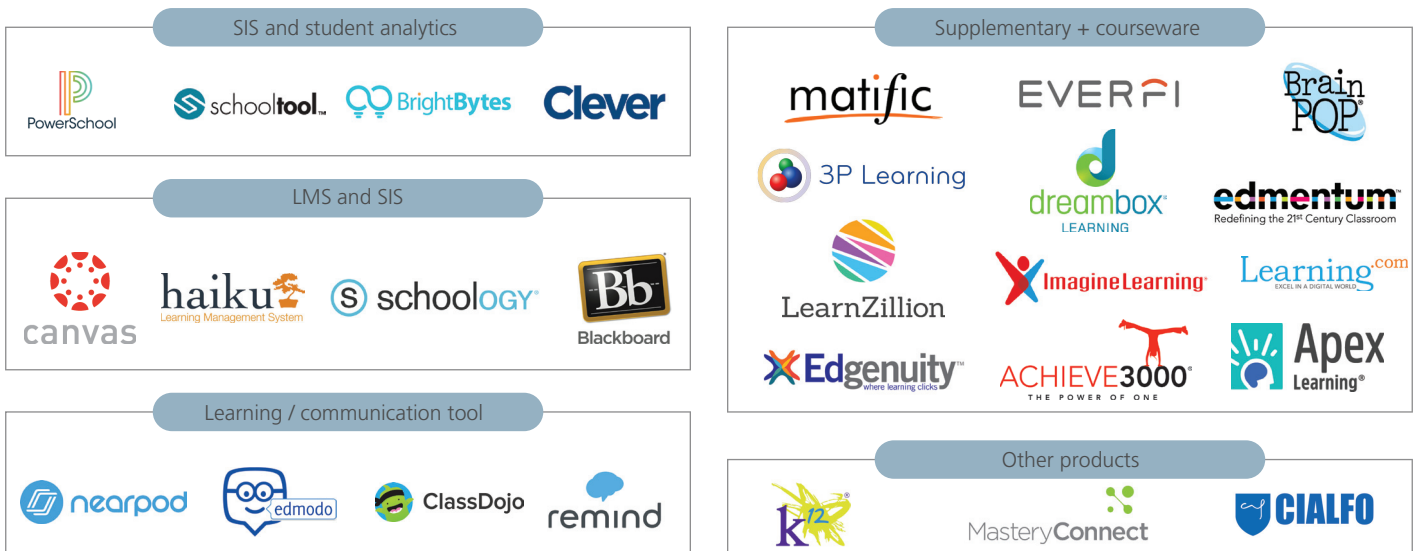
- International brand with a track record in bilingual education
- Local teachers with high-quality bilingual international training
- Canadian curriculum that integrates national standards
- Graduates receive a national diploma and Canadian certification



*Maple Bear offers an affordable alternative to international schools*



Figure 6  
Third-party technology-enabled providers



## 2. Technology as an enabler for quality 21st-century education

In line with global trends, Brazil is experiencing greater demand for more modern curriculum that delivers personalized learning. However, schools have limited resources to invest in the kind of teacher training and infrastructure that is required to deliver this type of education.

As a result technology-enabled third-party products have emerged across the world to meet the rising demand for personalized education. A range of edtech models caters to teachers and students by providing customized services (e.g., classroom management or individually paced online exercises) (see Figure 6). These are primarily found in developed countries that are equipped with the right infrastructure and modern pedagogical approach.

Among emerging markets, Brazil presents a unique case, as the majority of private schools (40-50%) already use learning systems that provide content and services such as teacher training and classroom management tools. Learning systems such as UNO and Ari de Sá have pioneered technology-enabled tools to help deliver personalized learning and other forms of 21st-century skills. Traditional learning systems such as Anglo are also rapidly innovating in a bid to meet this need. Investors recognize the potential; Arco Educação, a Brazilian learning system and education service provider, was valued at ~15 times its revenue

(as a multiple afforded to high-growth SAAS<sup>9</sup> providers) when it was recently listed on the NYSE (see Figure 7).

There is significant headroom for growth in Brazil's technology-enabled education services market. Investors considering acquisitions must consider whether to provide these services through schools (B2B) or to provide them directly to students (B2C). The former approach may face longer growth cycles due to inadequate infrastructure in schools (Brazil has four times as many students per computer compared to the OECD<sup>11</sup> average). The latter approach may be easier but may face higher customer acquisition costs. The answer to this question will vary depending on the specific context and type of product being considered.

Undoubtedly, parents continue to judge schools primarily by student outcomes. Based on L.E.K. research, school chains that were able to provide high quality outcomes were also able to sustain growth rates despite an economic slowdown. However, if schools are able to provide bilingual education and 21st-century learning, parents will be willing to pay more. We anticipate that this will lead to "premiumization" in the market, with the emergence of higher-end schools that can command a higher market price by delivering differentiated, superior educational services.

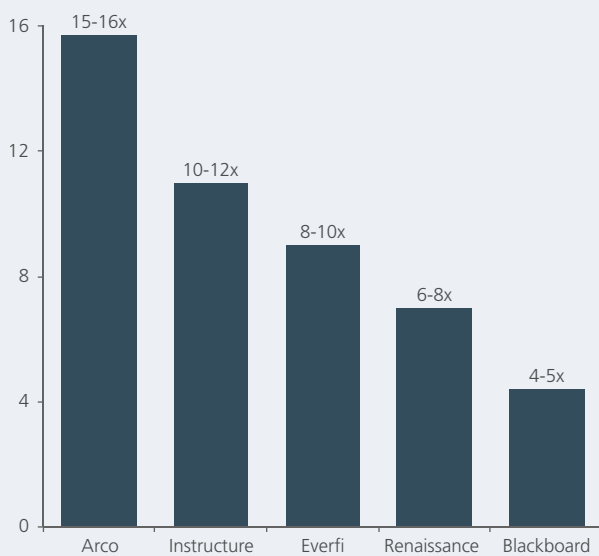
Investors who wish to capitalize on this opportunity should be aware of the key challenges that the market presents, and the potential solutions.



Figure 7  
Arco Educação case study<sup>10</sup>



Valuation (Revenue multiplier)



Source: Company website, Newspaper articles, L.E.K. research and analysis

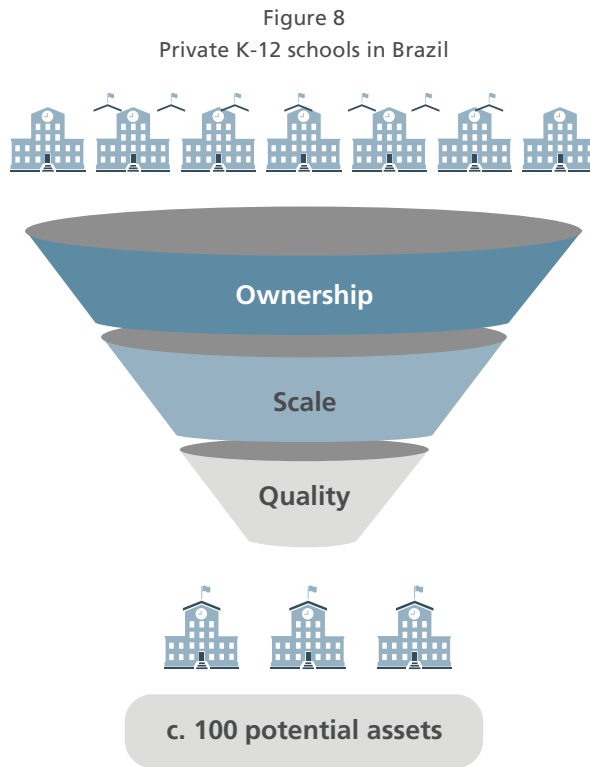
### Key features

- Reaches 1,140 schools and 400K+ students, with a net revenue of ~\$75M (2018)
- Mission-critical platform replacing traditional K-12 content with modern and integrated content
- Proprietary technology and content that combines growth and profitability across a resilient and growing sector
- Unique "B2B2C" business model using schools as distributors to its students



Arco differentiates itself by providing modern, technology-enabled content for K-12 schools

# Challenges



## 1. Limited scaled assets for acquisition

There are few scaled assets that are suitable for acquisition. The market is currently dominated by “mom and pop” operations; less than 5% of enrollments fall under the organized sector. Small stand-alone providers account for the remaining provision, so the process of consolidation will be slower and more challenging. L.E.K. advises that investors follow structured criteria to select suitable assets, analyzing factors such as ownership, location, quality, scale and opportunity for fee growth (see Figure 8). In a recent study of the top 20 cities in Brazil, L.E.K. found some 100 potentially acquirable targets after adjusting for ownership, scale and quality.

## 2. EBIDTA margins and valuation considerations

EBIDTA margins in private K-12 are limited by relatively low scale and tuition fees. In fact, the average enrollment of a private school

in Brazil (c. 250) is lower than that of other countries such as China (c. 425) and the U.K. (c. 325) (see Figure 9). Investors need to carefully align their EBIDTA value expectations as they consider strategies for consolidating the market.

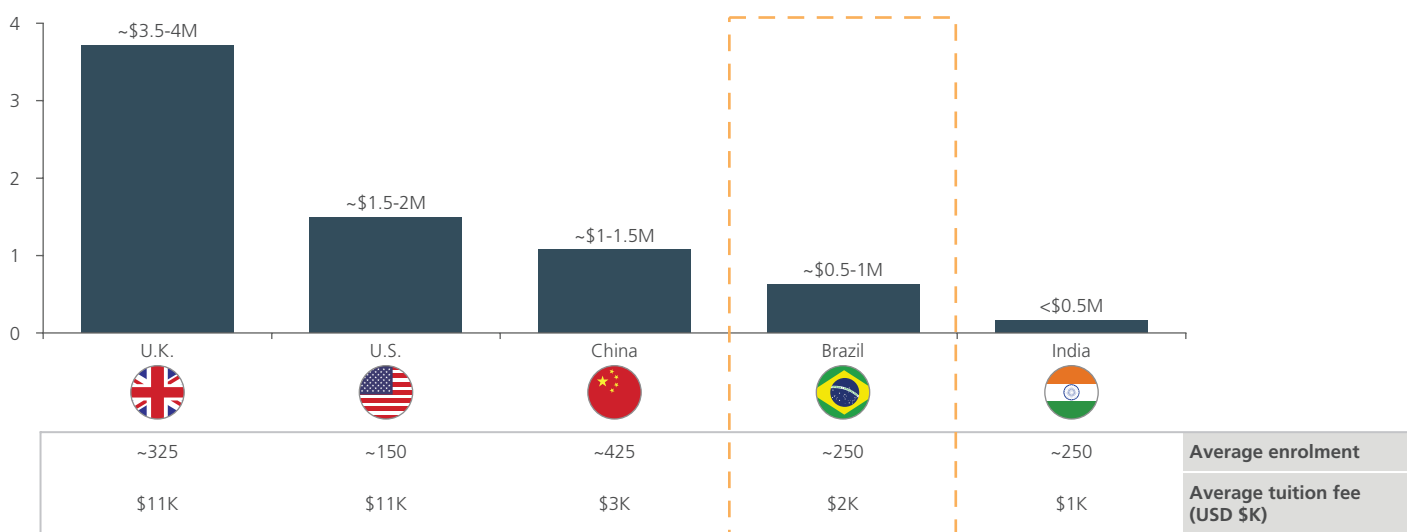
## 3. Diverse regional needs

Brazil has a diverse range of regional education needs. This is partially a relic of the differing entrance exams that large regional universities used in the past, which schools used to shape their curriculum. Over time, this led to a diverse educational landscape across the country. Although universities increasingly use a standardized national entrance exam, there is still a legacy of differentiation that means new operators may find it challenging to serve this range of needs with standardized offerings.

Investors and operators can overcome these challenges with sound strategic planning and a rigorous analysis of Brazil's K-12 landscape.

Figure 9  
Average private school scale, select countries, 2016<sup>12</sup>

Average private school scale,\* select countries  
2016  
Millions of dollars



\*Note: Calculated using average scale and fees



# Conclusion

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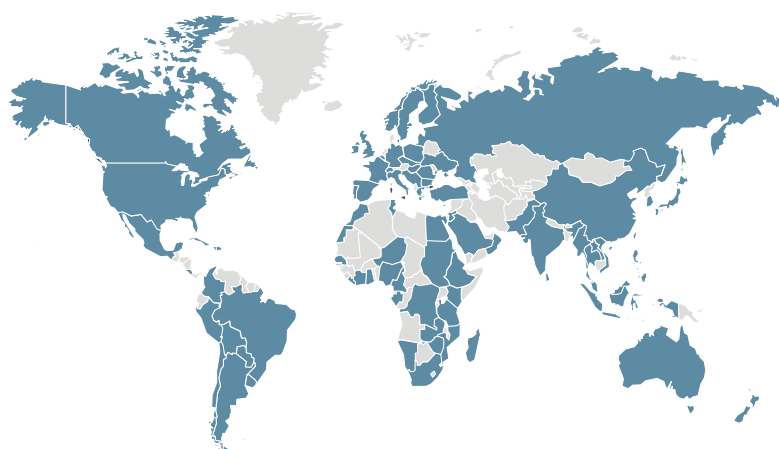
Brazil's private K-12 market is a hotbed of opportunities for investors and operators. Mounting demand for higher-quality education, combined with a wealthier population and supportive government regulations, has created optimal conditions for market entry. A greater focus on bilingual education and technology-enabled 21st-century learning are among the emerging themes

that investors should keep in mind. However, success will be determined by how well investors can identify the gaps in the market in order to meet local needs. Those that are able to gain in-depth insight into Brazil's K-12 education landscape will be well-placed to seize one of Latin America's largest education opportunities.

# About the Global Education Practice

The L.E.K. Global Education Practice (GEP) is a specialist international team whose members bring experience in more than 600 education sector engagements across more than 90 countries. This dedicated group of 60-plus consultants and five partners and principals is based in Singapore and serves a global client base from China to Chile. Our experts bring

insights on education businesses, investment opportunities, market dynamics and impact across education subsectors from K-12 to edtech. GEP leaders have served CXOs and boards of some of the world's largest education sector businesses and advised on most major deals over USD\$200 million since 2010.



■ Education cases led on-ground by members of L.E.K. Global Education Practice

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# Endnotes

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<sup>1</sup> <https://exame.abril.com.br/negocios/cade-aprova-compra-da-somos-pela-kroton/>

<sup>2</sup> L.E.K. Consulting research

<sup>3</sup> <http://www.worldbank.org/en/news/feature/2012/11/13/middle-class-in-Brazil-Latin-America-report>

<sup>4</sup> <https://nces.ed.gov/surveys/pisa/idepisa/dataset.aspx>

<sup>5</sup> Science, technology, engineering, and mathematics

<sup>6</sup> L.E.K. Consulting research

<sup>7</sup> L.E.K. Consulting research

<sup>8</sup> L.E.K. Consulting research

<sup>9</sup> Software as a service

<sup>10</sup> L.E.K. Consulting research

<sup>11</sup> Organisation for Economic Co-operation and Development

<sup>12</sup> L.E.K. Consulting research





