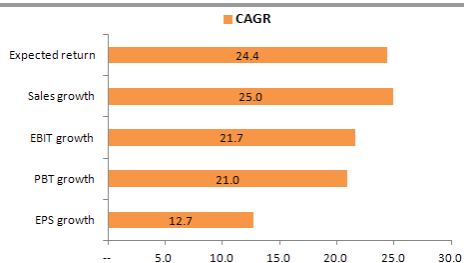




Initiating Coverage

Industry IT Services

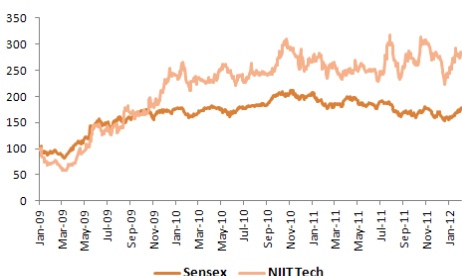


Price	233
Target Price	290
Initiating Coverage	Buy
Expected share price return	24.4%
Expected dividend yield	3.4%
Expected total return	27.8%

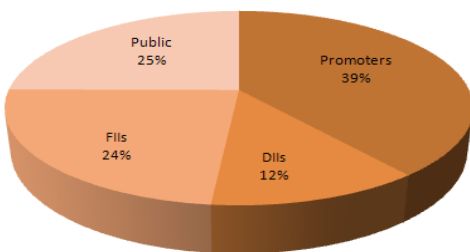
Market Data

Market Cap.	₹13,899mn/ US\$281mn
Share Cap. (mn)	59.6
52 Wk High/Low	245/ 164
Avg. Vol. (Weekly)	158,730

(Price Performance (RIC: NITT.NS, BB: NITEC IN))



Shareholding Pattern (As on Dec 31, 2011) (%)



Financials (₹ mn)	FY11	FY12E	FY13E
Revenues	12,323	15,831	19,245
EBIT	2,090	2,422	3,093
EBIT margin (%)	17.0	15.3	16.1
Net income (adjusted)	1,823	1,985	2,355
Adjusted EPS –			
diluted (₹)	30.5	32.8	38.8
RoE (%)	27.5	24.2	24.0
RoIC (%)	32.8	25.5	29.1
RoCE (%)	23.4	18.9	20.4
P/E (x)	7.6	7.1	6.0
P/BV (x)	1.8	1.6	1.3
EV/EBIT (x)	5.9	5.1	4.0

NIIT Technologies (NITEC IN)

February 13, 2012

Low valuations – high potential

Buy (CMP: ₹233/share)

Mkt Cap ₹13,899mn; USD 281mn

We initiate coverage on NIIT Technologies (NITEC) with a Buy rating and one-year Target Price of ₹290. In our opinion, the current stock prices do not factor in the growth potential and visibility provided by the increased order book. NITEC has been benefiting from its long-term focus on niche verticals of BFSI and transportation, an evidence of which is visible in its marquee client base and recent large-sized deals won by the company. We expect revenues (in US\$ terms) and earnings to grow at CAGR of 18% and 15%, respectively over FY12-14E, with stable profit margins. We believe the current valuations of 7.1x and 6.0x its FY12E and FY13E earnings, respectively are inexpensive with a 3.4% dividend yield offering further comfort.

Valuations not factoring growth opportunities

The CMP of ₹233 ascribes a meager 22% value to future growth opportunities for NITEC. This is materially lower when compared to large as well as mid-tier peers in the industry. In our opinion, the market expectations of low growth in NITEC's future earnings are unduly pessimistic, especially considering an order intake of US\$361mn in 9MFY12 compared to US\$266mn in entire FY11. More importantly, the order book executable over the next 12 months has risen from US\$169mn at the beginning of FY12 to US\$245mn at the end of Q3FY12. Historically, the ratio of revenues to the order book executable at the beginning of the year has been in the range of 1.8x to 2.6x.

Long-term client relationships with niche vertical focus

Since its inception, NITEC has had an exclusive focus on BFSI and transportation verticals. Revenue contribution from these verticals has been gradually increasing and was ~73% in FY11. The company has established long-term relationships with marquee clients in these verticals which include names like British Airways, Sabre, SEI, Cathay Pacific, Virgin Group, ING and AXA. NITEC has also been diversifying its client base as number of clients contributing >US\$1mn in revenues has increased from 32 in FY10 to 56.

Healthy revenue and earnings trajectory

Driven by strong order book, we expect revenues (in US\$ terms) for the company to grow at a CAGR of 18% over FY12-14E. Our FY13E revenue estimate of US\$397mn is 1.6x (vs the 1.8x-2.6x historical range) the executable order book of US\$245mn at the end of Q3FY12. EBIT margin is expected to remain stable in 15-16% range with multiple levers like increasing share of non-linear offerings, offshore leverage and broadening of employee pyramid. After a muted performance in FY12 because of higher tax rates, we expect earnings to grow at a CAGR of 15% over FY12-14E. We have assumed exchange rate of ₹48.5/US\$ and ₹47.5/US\$ for FY12E and FY13E, respectively. Our conservative revenue and margin estimates provide room for upward revision in estimates in future.

Asset heavy and working capital intensive deals pose a risk

NITEC participates in deals that involve takeover of existing technology infrastructure assets and workforce. The company also participates in government deals that require it to supply technology hardware for the project. The execution risk profile and working capital requirements in such deals are higher than normal IT services projects. The company saw its FY11 working capital rising because of such deals.

A preferred play in mid-tier space; initiate with Buy

We have valued the company at 7.5x its FY13E earnings yield at one-year Target Price of ₹290. We expect the company to announce a dividend per share of ₹8 for FY12 resulting in a lucrative dividend yield of 3.4%. In our view, strong growth visibility coupled with attractive valuations makes NITEC a good investment candidate amongst mid-tier technology companies. Hence, we initiate coverage on NITEC with a Buy rating and a Target Price of ₹290.

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INVESTMENT RATIONALE

Valuations not factoring growth opportunities

NITEC's current valuations at a CMP of ₹233 and estimated FY12 earnings of ₹32.8 indicate that market expectations on the company's future growth prospects are very low. At our cost of equity assumption of 18%, compared to 12-14% for tier-1 and 16% for larger mid-tier peers, the value of future growth opportunities built into current market price is just 22%. This represents a significant discount to large as well as mid-tier peers in the industry, where future growth potential accounts for an average of 57% and 42%, respectively of current valuations.

Table 1: Value of future growth

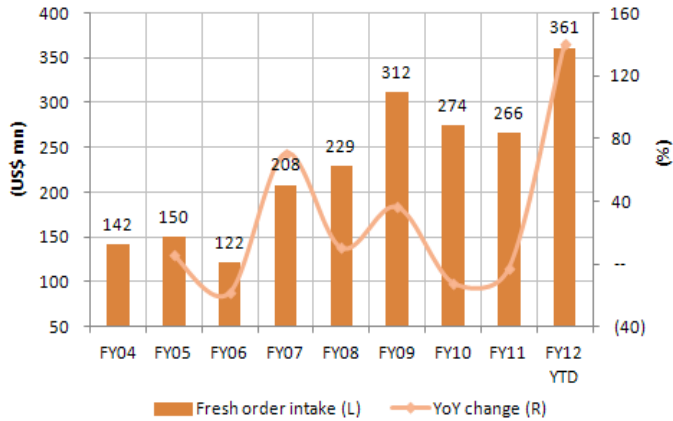
Company name	Y/E End	CMP (₹) (A)	FY12E EPS (₹) (B)	Cost of equity (%) (C)	Adj. zero growth price (₹) (D = B/C)	Implied value of future growth (₹) (E = A-D)	Value of future growth as % of CMP (%) (F = E/A)	2yr EPS CAGR forecast (%) (G)
TCS	Mar	1,233	54.5	12.0	454	779	63	18
Infosys	Mar	2,790	148.2	12.0	1,235	1,556	56	13
Wipro	Mar	449	23.6	13.0	181	268	60	11
HCL Tech	Jun	469	34.2	14.0	244	224	48	10
Average tier-1	--	--	--	--	--	--	57	13
Tech Mahindra*	Mar	650	65.4	15.0	436	214	33	9
Mphasis*#	Oct	373	38.4	16.0	240	133	36	(1)
Hexaware*#	Dec	110	8.3	16.0	52	58	53	15
Mindtree*	Mar	455	47.8	16.0	299	156	34	9
KPIT Cummins*	Mar	164	15.7	18.0	87	77	47	19
Infotech Enterprises*	Mar	143	13.1	18.0	73	70	49	20
Persistent Systems*	Mar	315	33.3	18.0	185	130	41	13
Average mid-tier	--	--	--	--	--	--	42	12
NIIT Technologies	Mar	233	32.8	18.0	182	51	22	15

Source: Systematix Institutional Research; *based on Bloomberg estimates; # for Mphasis and Hexaware FY12 refers to CY11 financials

Rising order book offers strong revenue growth visibility

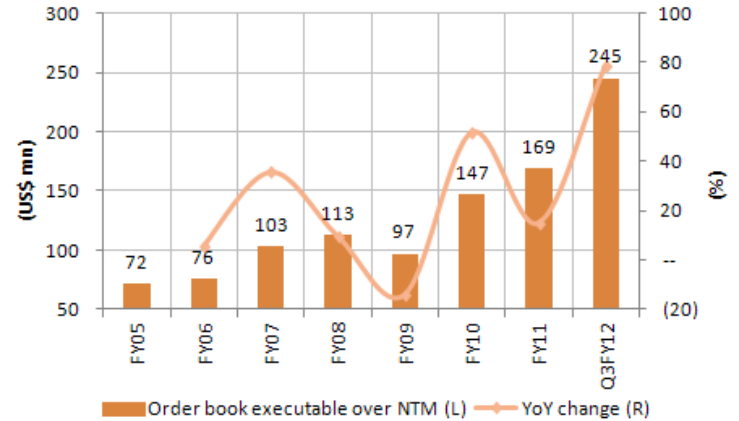
NITEC's consistent focus on targeting key verticals like BFSI, transportation and government has started yielding results. The company has seen sharp uptick in order inflows in the last few quarters. In 9MFY12, the company has received new orders of US\$361mn, which is 141% higher than the same period last year. The order backlog to be executed over the next 12 months has increased by 79% YoY to US\$245mn at the end of Q3FY12. More importantly, NITEC has seen an improvement in its ability to compete and win deals against the larger peers examples of which are Morris and Eurostar deals. The strong order books and backlog are also good indicators of revenue visibility ahead. As a thumb rule, the ratio of revenues to the order book executable at the beginning of the year for the company has been 1.8x-2.6x considering the past track record.

Chart 1: Fresh order intake



Source: Company, Systematix Institutional Research

Chart 2: Order book executable over next 12 months



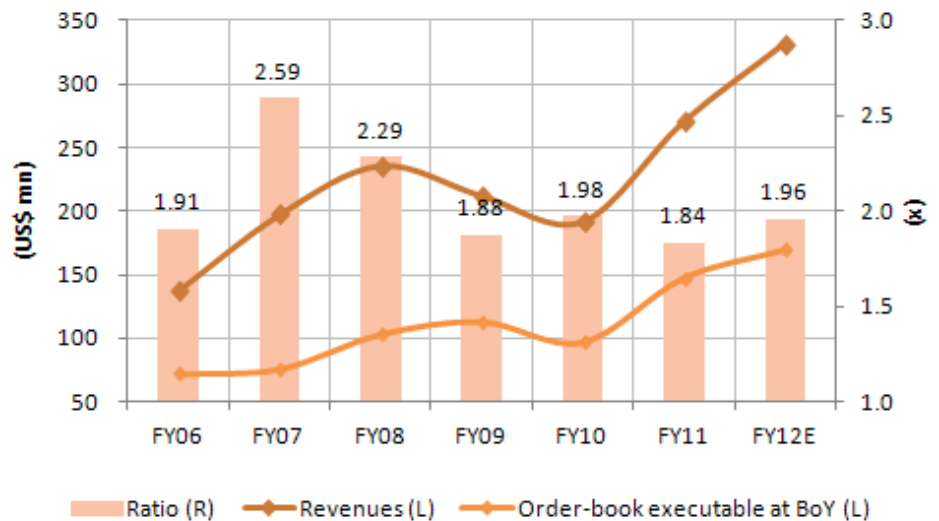
Source: Company, Systematix Institutional Research

Table 2: Large deal wins in FY12 table along with salient features of deal

Particular	Deal Size (US\$ mn)	Details
Eurostar	~US\$35mn	Multiple year transformation engagement for remote infrastructure services and hosting of critical applications. The deal involves execution of 17 transformation projects before London Olympics in 2012.
Morris JV	US\$85mn	It's a 60:40 JV in favour of NITEC and includes transfer of IT assets and employees. Revenue stream of US\$85mn over the next five years.
CCTNS	US\$40-45mn	NITEC has won the implementation of CCTNS (Crime and Criminal Tracking Network & Systems) from two states - Tamil Nadu and Jharkhand. The project will be executed in four phases over eight quarters. The company is pursuing two more states for similar orders.

Source: Company and Systematix Institutional Research

Chart 3: Strong correlation between order back-log and NTM revenues

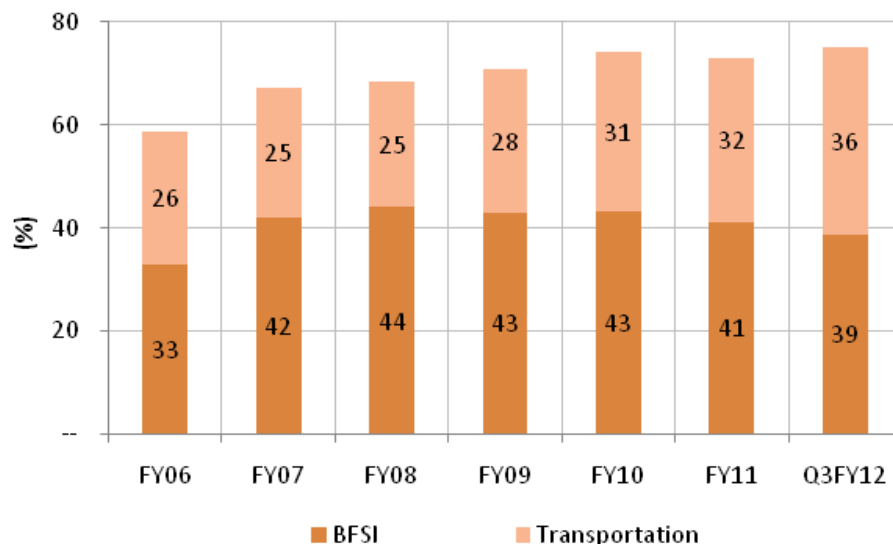


Source: Company, Systematix Institutional Research

Niche focus and non-linear offerings acting as key differentiators

Since inception NITEC has had specific focus on the BFSI and transportation verticals to drive growth. In BFSI, the company has had specific focus on the insurance vertical (~65% of BFSI revenues). The company's success in putting this strategy in action is evident from the fact that the contribution to revenues from these verticals has been steadily increasing. BFSI and transportation contributed 75% and 73% to revenues in 9MFY12 and FY11, respectively as compared to 59% in FY06.

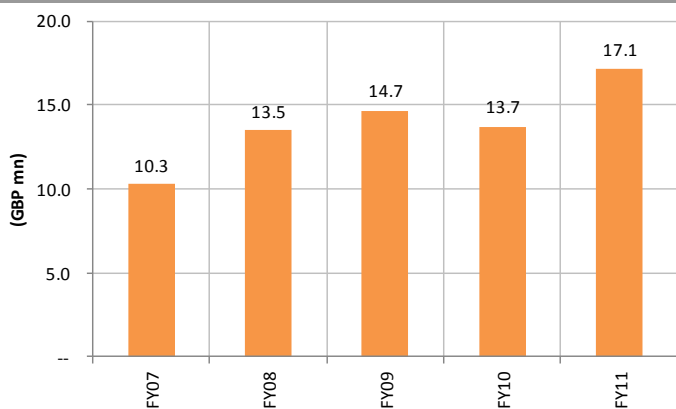
Chart 4: Contribution of BFSI and transportation to revenues increasing



Source: Company, Systematix Institutional Research

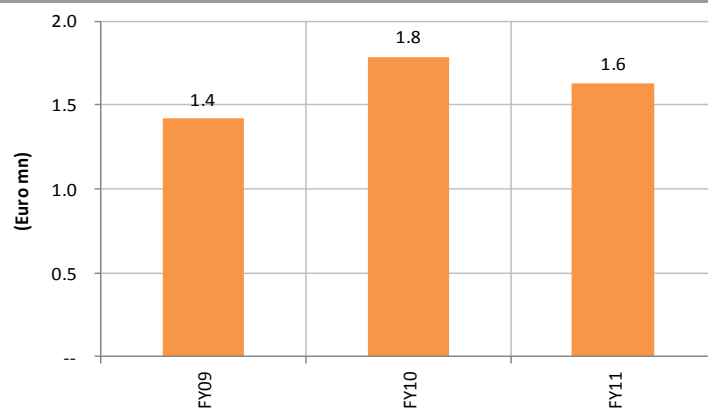
NITEC has also actively used the acquisition route in order to augment its services offerings. In 2006, the company acquired ROOM Solutions,UK (now NIIT Insurance Technologies, UK) which focuses on the commercial insurance market in UK and Europe. Post-acquisition, the company has been successful in ramping up Room Solutions' revenues. In the period FY07-11, revenues of Room Solutions grew at a CAGR of 13.6%, which higher than the overall company growth. More importantly, NITEC has been successful in improving margins for Room Solutions (27% operating margin in 9MFY12) through offshoring leverage. Further, leverage the market strength of Room Solutions NITEC has launched the IPF3 platform for commercial insurance, upgradation to which is expected to drive further revenue growth.

Chart 5: NIIT Insurance Tech (ROOM Solutions) revenues



Source: Company, Systematix Institutional Research

Chart 6: NIIT Airlines Technologies (Softec) revenues



Source: Company, Systematix Institutional Research

Recently, it acquired Proyecta Sistemas, a Spanish firm with focus on travel and financial services verticals. Proyecta has revenues of ~US\$10mn and EBITDA margin of ~10%. Its client list includes names like Iberia Airlines (merged with British Airways), Banco Santander and Merrill Lynch. NITEC intends to drive revenue growth in Proyecta through cross-selling opportunities and improve margins through offshoring.

Table 3: Details of past acquisitions

Year	Target	Details
2006	ROOM Solutions (UK)	ROOM Solutions was focused on commercial insurance market with strength in Lloyd's insurance market. When acquired the company had revenues of US\$25mn and ~120 employees.
2008	Softec GmbH (Germany)	Softec was specialist in providing IT solutions and services in the airline revenue accounting and operations space. The acquisition was to strengthen NITEC's transportation portfolio.
2011	Proyecta (Spain)	Focused on travel and BFS verticals with marquee customer names. Expertise in CRM, business intelligence, revenue/yield management, mobility.
2011	Morris Communicaiton (US)	NITEC invested US3.2mn in the joint venture and took over IT assets as well as ~100 people from Morris.

Source: Company and Systematix Institutional Research

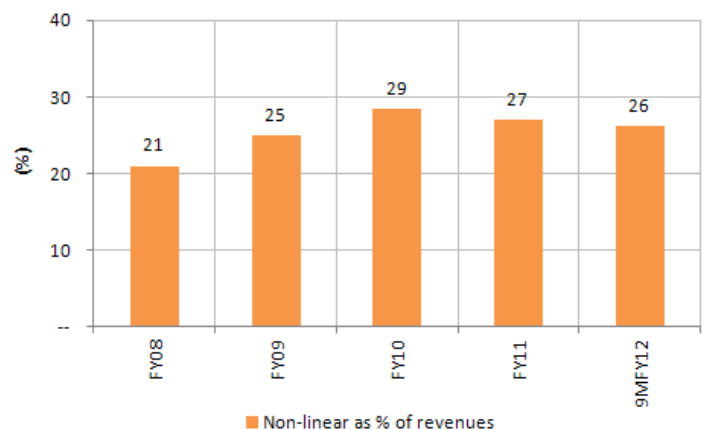
Another important differentiator for NITEC as compared to the other mid-tier IT services companies is its growing portfolio of non-linear revenues. In FY11, the company derived 27% of its revenues from non-linear initiatives which include 1) managed services, 2) platform-based services, and 3) recently launched cloud-based offerings. The recently signed Eurostar and Morris deals too have non-linearity built in the delivery. With ramp-ups from these deals, the management intends to increase the share of non-linear initiatives to ~30% of revenues in the near term.

Table 4: Non-linear initiatives

Service offering	Revenue contribution (FY11)	Details
Managed services	13%	Offers IT infrastructure and applications as completely administered services. This helps companies to focus on their core business as responsibility of IT infrastructure lies with NITEC.
Platform-based solutions	14%	NITEC has wide portfolio of platform-based solutions. Its insurance platform "Subscribe" has sizeable share in Lloyd's insurance market. Likewise, its "MonaLisa" platform is deployed in more than 30 international airlines.
Cloud computing	n.a.	The company has partnership with Hitachi (Asia) Thailand for infrastructure-as-a-Service over cloud. The company also offers Software-as-a-Service through is "Procure-Easy", "Bank Easy" and "Prefer" platforms.

Source: : Company and Systematix Institutional Research

Chart 7: Non-linear initiatives contribution to revenues



Source: Company and Systematix Institutional Research; contribution in FY11 and 9MFY12 impacted because of pass-through revenues

Table 5: Platform-based offerings

Owned - IP	Details
Subscribe	Provide solutions and services to the non-life commercial insurance markets (Insurers and Reinsurers) in London, US, Bermuda, and Continental Europe. Approximately 28% of the Lloyd's insurance business is transacted through this platform.
Monalisa	Offers a comprehensive revenue accounting system, route cost analyser and log book management. The product is compliant with IATA's SIS initiative and integrates seamlessly with the legacy technology environments in the organizations. The platform currently has more than 30 airlines as clients.
Acumen	Acumen has been developed to target management information requirements of the non-life commercial insurance market. The platform offers enterprise-wide data warehousing capabilities in a flexible, modular and scalable architecture.
Exact	The platform catering to insurance clients supports detailed risk assessment of onshore and offshore risks using a risk aggregation engine and a powerful GIS\ mapping interface.
IPF3	Based on Microsoft .NET architecture, IPF3 is designed to provide a processing platform for commercial insurance software. The platform can be accessed via the web, the desktop and mobile devices, thus allowing global deployment.
IP in partnerships	Details
Cosys	The platform is part of the strategic tie-up with Singapore Airport Terminal Services. The platform helps air cargo ground handling agents improve their cargo handling capabilities.
GeBiz	GeBiz is developed by Singapore 's Defence Science and Technology Agency (DSTA). As per contract with DSTA the development and maintenance support of GeBiz will be outsourced to NITEC. The platform has around 150 government agencies with ~15,000 users.

Source: Company and Systematix Institutional Research

Long-term relationships with marquee clients

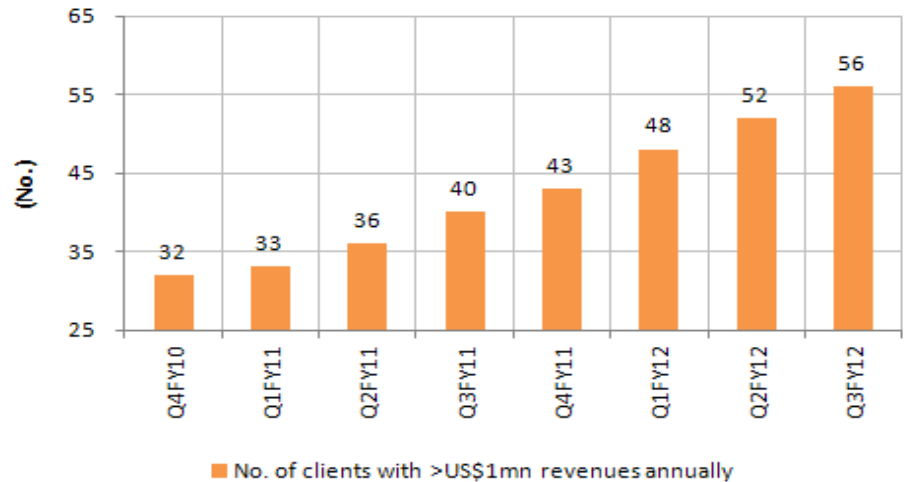
Leveraging its focus on travel and BFSI, NITEC has been successful in establishing a strong base of more than 50 customers each in both these verticals. Some of the marquee clients in these verticals include British Airways (now part of International Airlines Group), Sabre, Virgin Group, ING and AXA. The company has enjoyed long-term relationships with most of its top clients and has been successful in mining the accounts. NITEC has also been successful in diversifying its revenues sources by expanding its client base. At the end of Q3FY12, the company had 56 clients contributing more than US\$1mn in annual revenues as compared to 32 in FY10. Further, the contribution of top-20 clients to revenues has decreased from 67% in FY06 to 58% in Q3FY12.

Table 6: Marquee list of clients

BFSI	Transportation	Others
ING	British Airways	Holcim
SEI	Sabre	Morris
Trivent	Virgin Group	
AXA	Cathay Pacific	
Amlin	Emirates	
DBS	SITA	
	Toyota	
	Eurostar	

Source: Systematix Institutional Research

Chart 8: Number of clients contributing more than US\$1mn in revenues

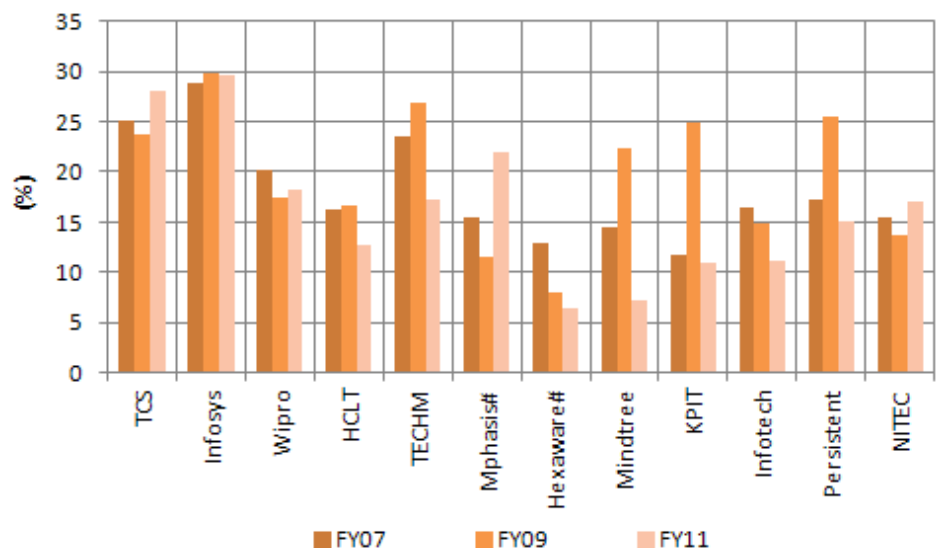


Source: Company

Sufficient levers to protect margin profile

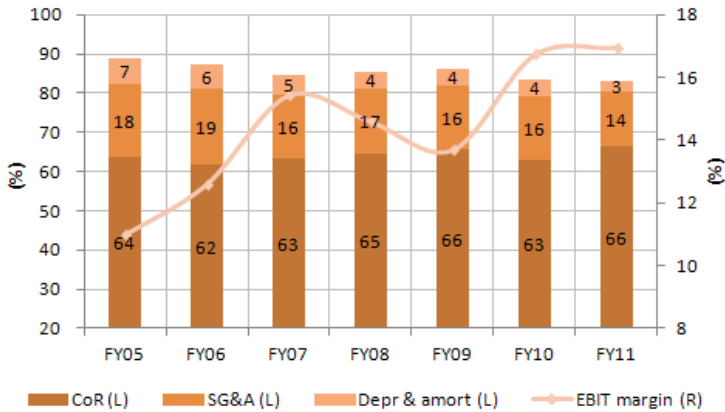
In an environment where most of the mid-tier IT companies are facing significant headwinds on margin front, NITEC has done a commendable job in maintaining its margin profile. Rather over the period FY08-11, a phase of recessionary and wage-related pressures for the mid-tier companies, NITEC has expanded its EBIT margin by 235bps (17% in FY11 vs 14.6% in FY08). EBIT margin in FY11 would have been higher at ~20% if we had excluded the impact of hedging losses in revenues and pass-through hardware business. The comfort to margins is attributed to the increasing share of non-linear revenues where profitability is higher as compared to traditional application development and maintenance services. The management also undertook sharp rationalisation of administrative expenses to protect margins. SG&A expenses as % of total revenues decreased by 245bps from 16.6% in FY08 to 14.2% in FY11.

Chart 9: EBIT margin – peer comparison



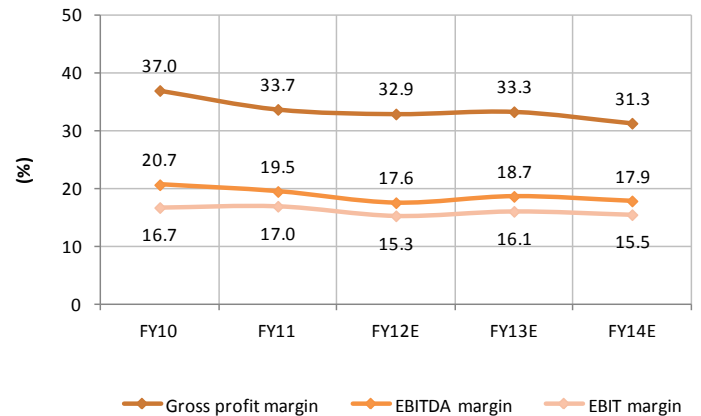
Source: Company, Systematix Institutional Research

Chart 10: NITEC margin performance



Source: Company and Systematix Institutional Research

Chart 11: Profit margin trend



Source: Company, Systematix Institutional Research

Going forward, we expect the margins of NITEC to remain stable in the range of 17-18% and 15-16% at EBITDA and EBIT levels, respectively. Our margin expectations include impact of pass-through revenues in FY12-14E. Though we expect the wage inflation to continue to put pressure on the company's profitability, we believe there are sufficient levers to protect margins. These levers include:

- 1) Increasing share of non-linear revenues: As mentioned earlier, the management intends to increase the contribution of non-linear offerings from current levels of 27%.
- 2) High utilisation rates: The company intends to keep operating at high utilisation rates. In Q3FY12, the company operated at an utilisation rate of 80.2% as compared to 84.4% in Q3FY11 and peak quarterly rate of 84.5%.
- 3) Expanding employee pyramid: The employee mix is highly skewed with employees with less than three years of experience comprising only ~30% of workforce. As the scale of operation increases, the management intends to increase this ratio. The shift towards broader employee pyramid will be rather gradual in our opinion.
- 4) The revenue share of onsite for NITEC stood at 63% in Q3FY12 and has increased by 600bps YoY. This is also higher when compared to the peers in the industry. We believe the increase in onsite effort is attributed to the recent acquisitions of Proyecta and Morris JV. As these acquisitions get absorbed into the company in FY13, we expect offshore contribution to increase and thus comfort margins.

Improving operating profile

An important concern that market has had for NITEC is the rising working capital intensity of the company. For instance, the cash realisation ratio (cash-flow from operations to net income) in FY11 was very low at 39% despite strong earnings growth of 44% in the year. Debtor days increased from 84 days in FY10 to 93 days in FY11 and stood at 91 days at the end of Q3FY12. The sharp rise in government business because of the BSF project and acquisition of Proyecta and Morris JV are largely responsible for the deterioration in working capital. Though we believe that working capital levels will remain higher as compared to historical trend (because of government business), we expect normalisation in FY12E and FY13E, especially considering that the ₹360mn debtors that were due from the BSF project have been realized in Q4FY12. We expect the company to generate strong operating and free cash flow of ₹2.5bn and ₹1.9bn, respectively in FY13E.

Table 7: Working capital scenario

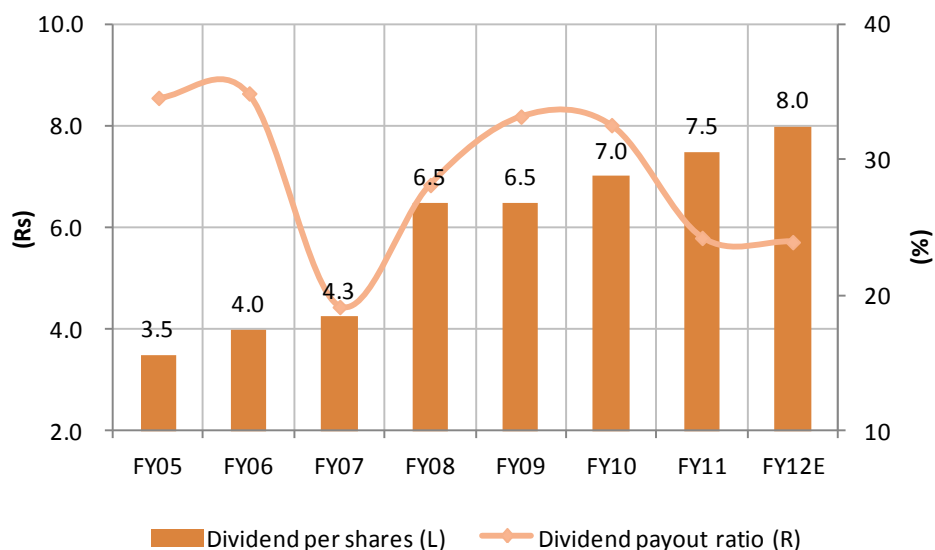
(Days)	FY06	FY07	FY08	FY09	FY10	FY11	FY12E	FY13E	FY14E
Days sales outstanding	80	69	83	81	81	84	93	90	88
Days Inventories outstanding	1	0	0	0	1	0	0	0	0
Days payable outstanding	53	43	46	46	51	39	38	40	40
Cash conversion cycle	27	27	37	35	31	45	55	50	49
Working capital / capital employed (%)	26	23	28	35	28	40	38	36	34

Source: Systematix Institutional Research

Healthy dividend payout and lucrative dividend yield

In the period FY06-11 NITEC maintained a healthy track record of dividend payout, even in the period of slowdown. Its dividend payout ratio varied from 19% to 35% in this period and the annual dividend increased at a CAGR of 13%. With improved financial profile, we expect the company to continue with a dividend payout ratio of ~25%. This essentially means that at CMP of ₹233, the stock is trading at a FY12 dividend yield of 3.4%, which we believe the highest in the sector.

Chart 12: Dividend per share and payout ratio



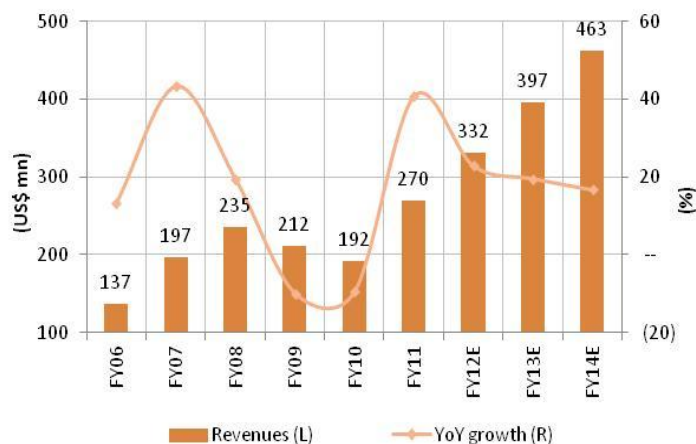
Source: Company and Systematix Institutional Research

FINANCIAL OVERVIEW

Expecting a revenue and earnings CAGR of 18% and 15% over FY12-14E

Revenues for NITEC, in US\$ terms, have grown at a CAGR of 12% over the last five years, excluding the impact of pass-through hardware revenues. The muted revenue growth is attributed to revenue challenges faced by the company during the FY08-10 recession. Post recession, revenue growth bounced back sharply and grew 27.5% YoY in US\$ terms in FY11. Earnings CAGR in FY06-11 has been healthy at 22% as the company improved in profit margins through increasing non-linear revenue and cost rationalisation.

Chart 13: Revenue growth trend



Source: Company, Systematix Institutional Research

Chart 14: Earnings growth trend



Source: Company, Systematix Institutional Research

Going ahead we expect the revenue performance to be strong with a CAGR of 18% over FY12-14E. The sharp rise in order book provides strong visibility in achieving these revenue targets. We expect margins to remain in the narrow range over the forecast period. Earnings growth in FY12 is expected to be muted at 7.5% because of the impact of higher income tax rates as the STPI tax benefits expired at the beginning of the year. However, over FY12-14E, we expect the company to have healthy earnings CAGR at 15%. Our estimates are based on average exchange rate of ₹48.5/US\$ and ₹47.5/US\$ for FY13E and FY14E, respectively.

We will like to highlight that our FY13 revenue estimates of US\$397 are 1.6x the executable order book over next 12 months of US\$245mn at the Q3FY12. Historically this ratio has varied between 1.8-2.6x. Also our stable margin expectation has upside risk because of multiple margin levers of non-linearity, offshore leverage and broadening of employee pyramid. These factors could lead to upward revision in our FY13 and FY14 EPS estimates of ₹38.8 and ₹43.1

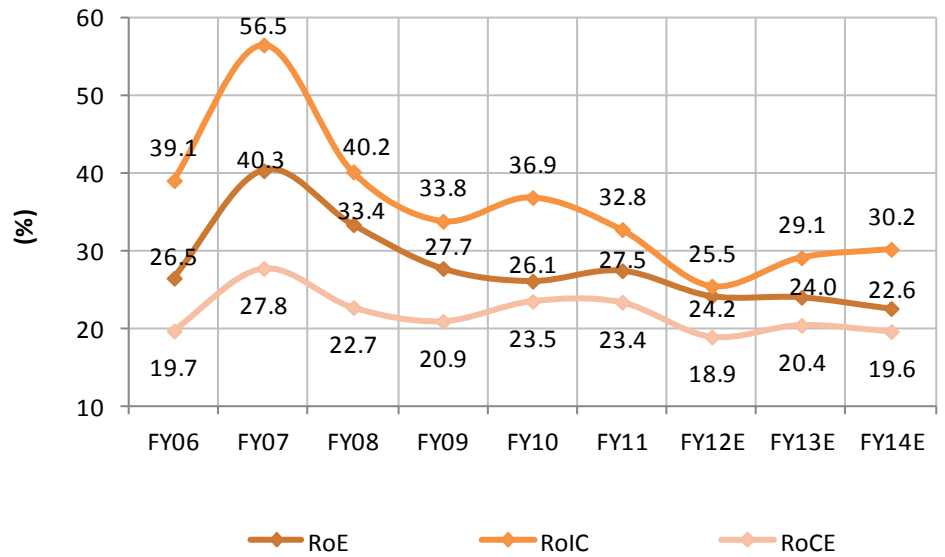
Cash flow generation volatile but expected to improve in FY13

As mentioned earlier, NITEC's cash flow from operations (CFO) took a hit in FY11 and FY12 because of higher working capital requirements due to acquisitions and sharp rise in Indian government's business. Though we expect the working capital scenario of normalise in Q4FY12 and FY13E, volatility in CFO generation cannot be ruled out. The execution of CCTNS deal has started from Q3FY12 and the hardware component of the deal is expected to be executed over H2FY12 and FY13. Though the company has learned from its experience in BSF order, rise in government business will impact working capital and CFO generation.

Return ratios to inch down on account higher taxes and working capital

NITEC has a consistent track record to delivering RoEs and RoICs in excess of 20% and 30%, respectively. We expect the trend to continue over FY12E to FY14E as well. However, the return ratios are expected to inch down as effective tax rates and working capital intensity have increased. Despite the decline, return ratios are still healthy compared to other mid-tier peers.

Chart 15: Return ratios trend



Source: Company, Systematix Institutional Research

KEY CONCERNS

Exposed to slowdown in key economies and verticals

NITEC derives ~75% of its revenues from North America and Europe. A macro-economic slowdown in these economies will have an adverse impact on the technology spending of the company's clients. The impact on NITEC's revenues and profitability would be higher because of its mid-tier size. In the recent slowdown of FY08-10, the company's revenues in US\$ terms declined by 10% CAGR.

Supply-side led cost pressures

The cost of recruiting and retaining experienced talent is higher for a mid-tier company. Such supply-side pressures lead to the company choosing the trade-off between wage inflation and higher attrition. From margin perspective both these outcomes have negative effect. In our forecast we have factored gross margin decline because of wage inflation. Better operating efficiencies at SG&A level are expected to comfort margins over FY12-14E.

Asset heavy deals could impact profitability

NITEC participates in deals that involve takeover of existing technology infrastructure assets and workforce. The company also participates in deals that require it to supply technology hardware for the project. The execution risk profile and working capital requirements in such deals are higher than normal IT services projects.

Rupee appreciation to have adverse impact on margins

NITEC derives ~90% of its revenues in currency, which is not its reporting currency i.e. rupee. However, most its operating expenditure is denominated in the rupee because of employee costs in offshore development centres. A sharp rupee appreciation thus will have a negative impact on NITEC's profitability.

ATTRACTIVE VALUATIONS; INITIATE WITH BUY

Valuation attractive despite stock appreciation

NITEC's stock price has appreciated by ~27% YTD and ~14% in the last one month. In comparison the Sensex and BSE IT index have appreciated by ~10% each in last one month. Despite the stock's sharp appreciation, we believe valuations are attractive compared to the peers in the industry, based on historical valuation trend, future growth prospects, and lucrative dividend yield.

Table 8: Stock price performance

(%)	1m	3m	6m	1yr
NITEC	14.3	6.1	19.6	27.1
BSE IT	10.4	5.3	20.9	(1.5)
Sensex	9.9	3.2	5.4	0.1

Source: Bloomberg, Systematix Institutional Research

Consistent delivery will lead to valuation re-rating

In the past five years, NITEC has traded in a wide valuation range of 18x to 2.5x on a one-year forward P/E basis. At CMP of ₹233, the stock is trading at 7.1x and 6.0x on FY12E and FY13E earnings, respectively. Despite the stock outperforming the sector in terms of price performance over the one year, the current valuations are still lower than both large as well as mid-tier peers. In our opinion, a re-rating of the stock is possible considering 1) improved visibility for revenues because of strong order book, 2) reduced margin volatility with possibility of improvement over FY13E and FY14E, 3) improvement in cash flow generation as working capital scenario stabilises and 4) consistent RoE in excess of 20%, dividend CAGR of 10% and dividend yield of 3.4%.

Table 9: Valuation – peer comparison

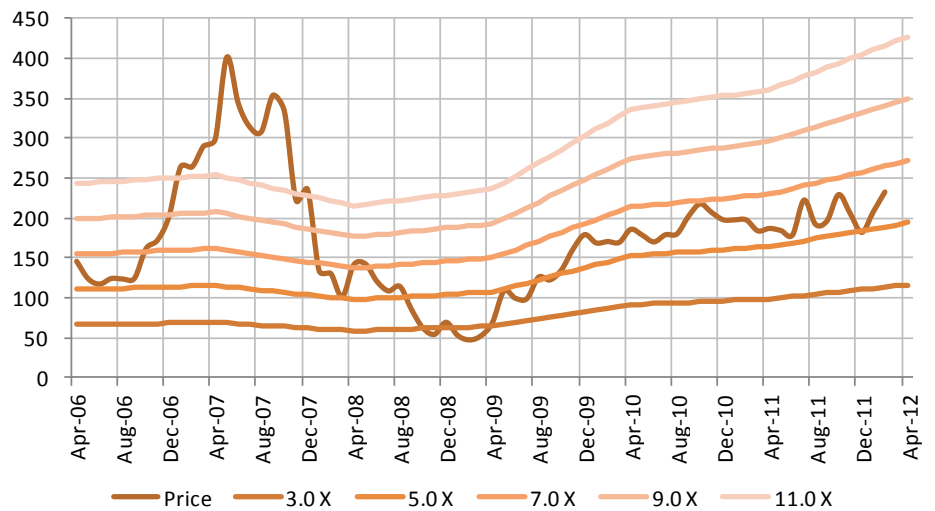
Company Name	Y/E End	CMP (₹)	MCap (₹ mn)	EV (₹ mn)	P/E(x)			EV/EBIT(x)			P/BV(x)		
					FY11	FY12E	FY13E	FY11	FY12E	FY13E	FY11	FY12E	FY13E
TCS	Mar	1,233	2,404,642	2,246,534	27.7	22.6	17.8	21.4	15.7	13.3	9.5	7.8	6.1
Infosys	Mar	2,790	1,613,498	1,710,047	23.4	18.8	16.1	21.1	16.9	14.6	5.8	4.9	4.1
Wipro	Mar	449	1,095,460	1,121,081	20.7	19.1	15.7	19.4	16.8	14.0	4.6	3.9	3.3
HCL Tech	Jun	469	320,696	338,941	20.0	13.7	11.7	15.7	10.4	9.6	3.8	3.1	2.6
Tech Mahindra*	Mar	650	83,984	94,506	12.6	9.9	9.4	10.6	11.7	10.7	2.4	2.0	1.7
Mphasis*#	Oct	373	78,389	54,592	7.2	9.7	9.7	5.0	6.5	6.1	2.4	2.0	1.7
Hexaware*#	Dec	110	31,096	17,654	29.5	13.2	10.9	26.4	7.8	5.2	3.3	3.0	2.5
Mindtree*	Mar	455	18,497	14,812	17.8	9.5	8.9	13.8	7.0	6.0	2.3	2.0	1.7
KPIT Cummins*	Mar	164	14,781	13,324	13.9	10.4	8.7	12.0	8.2	6.4	2.4	2.1	1.7
Infotech Enterprises*	Mar	143	15,707	14,170	11.3	10.9	8.3	10.8	6.8	5.8	1.5	1.4	1.2
Persistent Systems*	Mar	315	12,752	11,190	8.5	9.5	8.3	9.6	6.8	5.8	1.7	1.5	1.3
Sector median	--	--	--	--	17.8	10.9	9.7	13.8	8.2	6.4	2.4	2.1	1.7
Tier-1 median	--	--	--	--	22.1	18.9	15.9	20.3	16.2	13.6	5.2	4.4	3.7
Mid-tier median	--	--	--	--	12.6	9.9	8.9	10.8	7.0	6.0	2.4	2.0	1.7
NIIT Technologies	Mar	233	13,899	12,415	7.6	7.1	6.0	5.9	5.1	4.0	1.8	1.6	1.3

Source: Company, Systematix Institutional Research; *based on Bloomberg estimates; # for Mphasis and Hexaware FY11 refers to CY10 financials

Initiate coverage with one-year Target Price of ₹290; Buy

For our target price, we have relied on P/E-based approach. Our target P/E multiple is 7.5x FY13 EPS, giving us a one-year target price of ₹290. This translates to an EV/EBIT multiple of 5x on FY13 financials. We will like to highlight that even at our target valuation multiples the stock will be trading at discount to the mid-tier peerset by 15-25%. A consistent quarter-on-quarter delivery in financial performance along with change in business mix, in favour of non-linear and annuity revenues, will lead to further re-rating of the stock. In our view, strong growth visibility coupled with attractive valuations makes NITEC a good investment candidate amongst mid-tier technology companies. Hence, we initiate coverage on NITEC with a Buy rating and a Target Price of ₹290.

Chart 16: One-year forward P/E

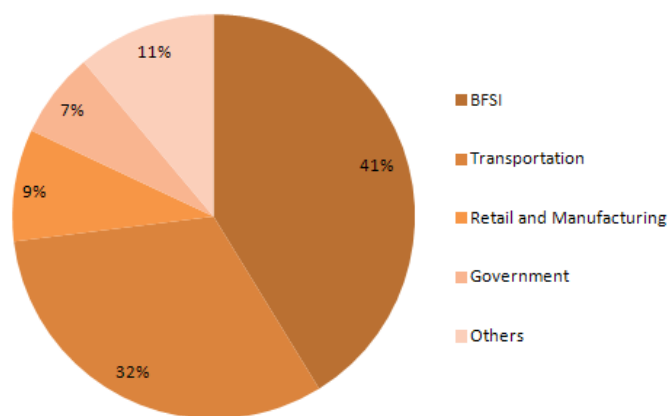


Source: Capitaline, Systematix Institutional Research

COMPANY OVERVIEW

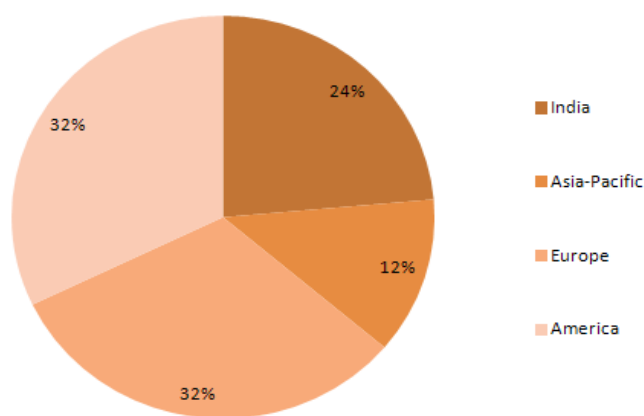
NITEC is a mid-tier technology services company with niche focus on organisations operating in insurance, financial services, and travel & transportation verticals. The company was spun-off into an independent company in 2004 from the parent NIIT. NIIT continues to hold ~25% equity in NITEC. The company offers services in application development & maintenance, managed services, BPO and cloud computing. Its client list includes marquee names like British Airways (now part of International Airlines Group), Sabre, ING Group, SEI investments, Holcim, Virgin Group, Cathay Pacific, Eurostar, etc. The company's key geographies of operations are North America, Europe, the Middle-East, Asia-Pacific and India. NITEC's FY11 revenues stood at US\$244mn (excluding pass-through component of hardware) and have grown at a CAGR of 12% over the last five years.

Chart 17: Industry-wise revenue contribution



Source: Company, Systematix Institutional Research

Chart 18: Geography-wise revenue contribution



Source: Company, Systematix Institutional Research

A key differentiator for NITEC is its non-linear initiatives. The company offers managed services, platform-based solutions and cloud computing services. It owns several IP-led platforms like Subscribe, Monalisa, Acumen, RFS, Exact, etc. and offers platform solutions in partnerships like Cosys and Gebiz. The contribution of non-linear offerings has been gradually increasing for the company and stood at 27% of revenues in FY11.

Table 10: Shareholding pattern

Shareholder	% holding
Promoters	39.2
Public - more than 1% holding	
LIC	1.2
UTI - Dividend Yield Fund	1.9
AKM Systems	2.1
Morgan Stanley (Mauritius)	2.2
HDFC Mid-cap Opportunities Fund	2.5
Blackrock India (Mauritius)	4.2
Fidelity Advisor Small- Cap Fund	6.3
Total	59.4

Source: BSE, Systematix Institutional Research

KEY MANAGEMENT PERSONNEL

Rajendra Pawar, Chairman and Managing Director: Mr. Pawar is the Chairman and Co-founder of the NIIT Group that encompasses two businesses - NIIT Limited and NIIT Technologies Limited. He pioneered the computer education market in India by establishing the group in 1981. Mr. Pawar is the current Chairman of India's IT industry body NASSCOM. Mr. Pawar is also member on the Prime Minister's National Council on Skill Development. Acknowledging his contribution to the IT industry in India, Mr. Pawar has been awarded the country's prestigious civilian honour, Padma Bhushan by the President of India.

Arvind Thakur, Chief Executive Officer: Mr. Thakur joined the NIIT Group in 1985 and also serves as the Joint Managing Director on NITEC's board. He graduated in engineering from the premier Indian Institute of Technology in India. Thereafter he pursued post graduation in Industrial Engineering from NITIE in Mumbai. He is also a Director in an innovative venture, Hole-in-the Wall Education Ltd. that enables technology to be deployed to educate the masses

Pratibha Advani, Chief Financial Officer: Ms. Advani joined NITEC in September 2010 Barclays Shared Services Pvt. Ltd. (a subsidiary of Barclays Bank Plc.) where she was Chief Financial Officer. Her previous experience includes firms like GE-SBI Cards, GE Money (India) and ITC. During her stint at GE she was the recipient of the GE Chairman's Award & Management Award for the best Finance function. She is a qualified Chartered Accountant with Six Sigma certification and LEAN training

Deepak Khosla, Global Head of Sales and Marketing: Mr. Khosla joined NITEC in June 2011 from Patni Computers (iGate Patni) where he was President – SAARC. An alumnus of Jamnalal Bajaj Institute of Management Studies in Mumbai, he started his sales career with HCL Ltd. His other experience include successful spells with organizations like SAS Inc., Digital Equipment Corporation (DEC) and Dun and Bradstreet.

Lalit Dhingra, Head – North America: Mr. Dhingra joined the NIIT Group in 1991 and is responsible for building the North American operations of NITEC. He is an alumnus of Indian Institute of Technology (Delhi). Before joining NITEC he had worked with C-DOT and HCL Group. He is also on the board of NIIT Healthcare Technologies and NIIT Media Technologies.

Sunil Surya, Head – Europe: Mr. Surya joined NITEC in September 2010 from Hexaware where he was responsible its operations in European region. He has more than decade of experience in structuring and managing large outsourcing deals for Fortune 500 companies. Mr. Surya has done MBA from Jamnalal Bajaj Institute of Management Studies, Mumbai.

Arvind Mehrotra, Head – Asiac-Pacific: Mr. Mehrotra has over twenty-five years of corporate experience during which he has held various middle and senior management positions across the IT services and the publications sectors. He has been with NIIT Technologies for over a decade and has played a key role in the growth of the organization over the years.

Financial summary

INCOME STATEMENT ₹ mn	FY11	FY12E	FY13E	FY14E
Revenues	12,323	15,831	19,245	22,016
Growth yoy (%)	34.9	28.5	21.6	14.4
Cost of revenues	8,169	10,619	12,835	15,120
Other operating expenses	1,750	2,430	2,819	2,961
EBITDA	2,404	2,782	3,591	3,935
EBITDA margin (%)	19.5	17.6	18.7	17.9
Depreciation & amortisation	315	360	499	524
EBIT	2,090	2,422	3,093	3,411
EBIT margin (%)	17.0	15.3	16.1	15.5
Interest expenses	7	22	27	18
Other income	95	274	120	130
Profit before taxes	2,178	2,675	3,187	3,524
Income taxes	323	697	807	869
Earnings from associates	--	--	--	--
Minority interests	32	(8)	25	30
Exceptional items (post-tax)	--	--	--	--
Net income (reported)	1,823	1,985	2,355	2,625
Growth yoy (%)	44.4	8.9	18.6	11.4
Adjustment for one-off items	--	--	--	--
Net income (adjusted)	1,823	1,985	2,355	2,625
Growth yoy (%)	44.4	8.9	18.6	11.4
Diluted EPS (adjusted)	30.5	32.8	38.8	43.1
Growth yoy (%)	42.5	7.5	18.1	11.1

CASH FLOW STATEMENT ₹ mn	FY11	FY12E	FY13E	FY14E
Net income (reported)	1,823	1,985	2,355	2,625
Depreciation & amortisation	315	360	499	524
Δ in working capital	(1,338)	(546)	(350)	(235)
Other operating cash items	(85)	(5)	15	18
Cash flow from operations	715	1,794	2,519	2,931
Capital expenditure (net)	(493)	(500)	(600)	(750)
Δ in investments	60	(400)	(650)	(750)
Other investing cash items	--	(541)	--	--
Cash flow from investing	(433)	(1,441)	(1,250)	(1,500)
Share issue/repurchase	65	19	28	22
Dividends paid	(487)	(554)	(646)	(738)
Δ in debt	(120)	500	(150)	(200)
Other sources/uses of cash	--	--	--	--
Cash flow from financing	(542)	(35)	(769)	(916)
Effect of exchange rate	24	--	--	--
Δ in Cash & cash equiv.	(236)	318	500	515

VALUATION RATIOS	FY11	FY12E	FY13E	FY14E
P/E (x)	7.6	7.1	6.0	5.4
P/BV (x)	1.8	1.6	1.3	1.1
EV/EBIT (x)	5.9	5.1	4.0	3.6
EV/Sales (x)	1.0	0.8	0.6	0.6
EV/FCFF (x)	84.6	21.9	6.7	5.9
Dividend yield (%)	3.2	3.4	4.0	4.5
FCFF yield (%)	1.1	4.1	13.3	15.1

Source: Company, Systematix Institutional Research

BALANCE SHEET ₹ mn	FY11	FY12E	FY13E	FY14E
↳ Cash and cashe equiv.	1,194	1,512	2,013	2,527
↳ Trade receivables	2,871	3,578	4,097	4,469
↳ Unbilled revenues	799	813	953	1,090
↳ Inventories	6	16	19	22
↳ Other current assets	1,354	1,677	1,942	2,156
Current assets	6,223	7,596	9,024	10,265
Net fixed assets	2,399	2,592	2,747	2,989
Goodwill	122	69	16	--
Intangible assets	809	1,350	1,350	1,350
Investments	443	843	1,493	2,243
Other non-current assets	143	143	143	143
Total Assets	10,139	12,593	14,772	16,989
↳ Trade payables	973	1,267	1,540	1,761
↳ Other current liabilities	1,536	1,750	2,055	2,324
Total current liabilities	2,508	3,016	3,594	4,086
Debt funds	110	610	460	260
Other non-current liabilities	--	--	--	--
Minority interests	43.0	38.2	53.2	71.2
↳ Contributed capital	653	672	700	722
↳ Cumm. retained earnings	5,232	6,663	8,372	10,258
↳ Other reserves	1,594	1,594	1,594	1,594
Shareholder equity	7,478	8,928	10,665	12,573
Total liabilities and equity	10,139	12,593	14,772	16,989

RATIOS	FY11	FY12E	FY13E	FY14E
Return ratios (%)				
RoE	27.5	24.2	24.0	22.6
RoIC	32.8	25.5	29.1	30.2
RoCE	23.4	18.9	20.4	19.6
Working capital ratios (days)				
Receivable days	84	93	90	88
Inventory days	0	0	0	0
Payable days	39	38	40	40
Asset turnover ratios (x)				
Total assets turnover	1.3	1.4	1.4	1.4
Fixed assets turnover	5.3	6.3	7.2	7.7
Liquidity ratios (x)				
Current ratio	3.7	3.6	3.5	3.5
Quick ratio	3.4	3.4	3.5	3.6
Net debt / equity	(0.3)	(0.2)	(0.3)	(0.4)
Interest coverage ratio	299.3	117.7	115.7	189.7
Per share ratio (₹)				
Diluted EPS (adjusted)	30.5	32.8	38.8	43.1
BVPS	126.2	149.8	177.4	207.8
Tangible BVPS	110.5	126.0	154.7	185.5
Dividends per share	7.5	8.0	9.3	10.5
Growth ratios (%)				
Revenues	34.9	28.5	21.6	14.4
EBTIDA	27.3	15.7	29.1	9.6
EBIT	36.7	15.9	27.7	10.3
Net income (adjusted)	44.4	8.9	18.6	11.4
Diluted EPS (adjusted)	42.5	7.5	18.1	11.1

Source: Company, Systematix Institutional Research

APPENDIX I: DuPONT ANALYSIS

Chart 19: Lower profit margins and reducing leverage impacting return on equity

RETURN ON EQUITY					
FY09	FY10	FY11	FY12E	FY13E	
27.7%	26.1%	27.5%	24.2%	24.0%	

NET PROFIT MARGIN					
FY09	FY10	FY11	FY12E	FY13E	
11.7%	13.8%	14.8%	12.5%	12.2%	

EBIT MARGIN					
FY09	FY10	FY11	FY12E	FY13E	
13.7%	16.7%	17.0%	15.3%	16.1%	

INTEREST BURDEN					
FY09	FY10	FY11	FY12E	FY13E	
103.4%	92.9%	104.2%	110.4%	103.0%	

TAX BURDEN					
FY09	FY10	FY11	FY12E	FY13E	
82.7%	88.9%	83.7%	74.2%	73.9%	

ASSET TURNOVER RATIO					
FY09	FY10	FY11	FY12E	FY13E	
1.41x	1.23x	1.47x	1.54x	1.56x	

LONG TERM ASSETS / SALES					
FY09	FY10	FY11	FY12E	FY13E	
0.29x	0.31x	0.25x	0.21x	0.21x	

CURRENT ASSETS / SALES					
FY09	FY10	FY11	FY12E	FY13E	
0.42x	0.50x	0.44x	0.44x	0.43x	

INVENTORIES / SALES					
FY09	FY10	FY11	FY12E	FY13E	
0.00x	0.00x	0.00x	0.00x	0.00x	

TRADE RECEIVABLES + UNBILLED REVENUES) / SALES					
FY09	FY10	FY11	FY12E	FY13E	
0.22x	0.22x	0.23x	0.25x	0.25x	

CASH EQUIVALENTS / SALES					
FY09	FY10	FY11	FY12E	FY13E	
0.11x	0.16x	0.11x	0.09x	0.09x	

OTHER CURRENT ASSETS / SALES					
FY09	FY10	FY11	FY12E	FY13E	
0.08x	0.11x	0.10x	0.10x	0.09x	

LEVERAGE RATIO					
FY09	FY10	FY11	FY12E	FY13E	
1.68x	1.53x	1.26x	1.25x	1.26x	

LONG TERM ASSETS / EQUITY					
FY09	FY10	FY11	FY12E	FY13E	
0.68x	0.59x	0.45x	0.41x	0.41x	

CURRENT ASSETS / EQUITY					
FY09	FY10	FY11	FY12E	FY13E	
1.00x	0.94x	0.81x	0.84x	0.85x	

Source: Company, Systematix Institutional Research

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Stock Ratings

BUY (B)	The stock's total return is expected to exceed 20% over the next 12 months.
ACCUMULATE (A)	The stock's total return is expected to be within 10-20% over the next 12 months.
HOLD (H)	The stock's total return is expected to be within 0-10% over the next 12 months.
SELL (S)	The stock's total return is expected to give negative returns over the next 12 months.
NOT RATED (NR)	The analyst has no recommendation on the stock under review.

Industry Views

ATTRACTIVE (AT)	Fundamentals/Valuations of the sector are expected to be attractive over the next 12-18 months.
NEUTRAL (NL)	Fundamentals/Valuations of the sector are expected to neither improve nor deteriorate over the next 12-18 months.
CAUTIOUS (CS)	Fundamentals/Valuations of the sector are expected to deteriorate over the next 12-18 months.

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