

Q4FY07 result

NIIT Limited

Bloomberg: NIIT IN
Reuters: NIIT.NS
Mkt cap: INR 18.0bn/USD 0.4bn

BUY
Current price: INR 911*
Target price: INR 1,198**

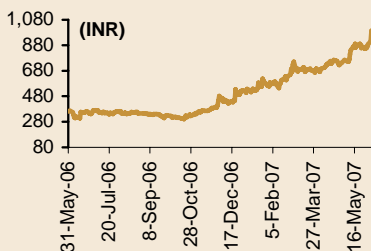
Individual training business leads the way

We revise our price target to INR 1,198

**Revised from INR 1,011. Horizon: March 2008

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Stock performance


(%)	Absolute	Relative to	
		Sensex	Sector
3 months	31.6	19.0	35.6
6 months	108.5	104.4	119.9
12 months	173.7	91.2	101.8

Key financials (consolidated)

Y/E 31 Mar	FY07	FY08E	FY09E
Net sales (INR m)	7,950	10,687	12,754
Net profit (INR m)	657	1,005	1,595
Adj EPS (INR)	29.7	45.5	72.2
PER (x)	30.7	20.0	12.6
PCE (x)	17.9	13.0	9.4
EV/EBITDA (x)	24.3	14.9	9.7
Price/Book (x)	7.0	5.4	4.0
ROE (%)	23.5	30.5	36.2
ROCE (%)	9.4	15.8	23.3
Consensus EPS (INR) *		35.6	40.7

*Bloomberg (Standalone)

Higher-than-expected revenues

NIIT Limited's (NIIT) Q4FY07 and full-year FY07 revenues were ahead of our expectation. Consolidated net revenues for Q4FY07 were up 123% YoY, to INR 2,566m from INR 1,149m in Q4FY06, while FY07 revenues were up 76% to INR 7,951m compared to INR 4,507m for FY06. Operating profits for the quarter and the full year were up 24% and 29% respectively. Net profits for the same periods were also up 107% and 46% respectively.

ElementK disappoints on margin front

Though the revenues were ahead of our expectation, operating margins for the quarter disappointed due to almost flat operating margins from ElementK. Individual business surprised with stronger-than-expected revenue and margin numbers. Operating margins in this business stood at 19.8% for Q4FY07, ahead of our estimate of 17.4%.

We revise our price target upwards to INR 1,198; maintain BUY

We expect NIIT to record a fully diluted EPS of INR 45 in FY08 and INR 72 for FY09. The stock trades at INR 911, which is 20x FY08E and 13x FY09E. On an EV/EBITDA basis for the core business, it trades at 10x FY09E. Our revised sum-of-the-parts (SOTP) valuation estimates a one-year forward price target of INR 1,198, which implies 31% upside potential from current levels. We maintain BUY.

Figure 1: Q4FY07 and FY07 results

	Q4FY07	Q4FY06	QoQ chg (%)	Q3FY07	QoQ chg (%)	FY07	FY06	YoY chg (%)
Net revenues	2,566	1,149	123	2,251	14	7,951	4,507	76
Operating expenses	2,363	9,84	1,40	2,073	14	7,176	3,906	84
EBITDA	204	165	24	178	15	774	601	29
Other income	-8	-21	-46			-55	39	
Depreciation	130	102	27	125	4	473	373	27
Profit before tax	66	42	57	7	843	247	267	-7
Tax	11	7		-9		4	30	
Net profit	55	35	57	16	244	242	237	2
Share of associate's net profit	117	46	154	92	27	331	164	102
PAT after associate's profit	172	81	107	108	59	573	401	46
No of shares (m)	19.76	19.32		19.45		19.76	19.32	
Basic EPS	8.7	4.2		5.6		29.0	20.8	
Fully diluted EPS	7.8	3.7		4.9		26.0	18.2	
EBITDA margins (%)	8.0	14.4		7.9			13.3	

Source: Company, Brics Research

Figure 2: Business-wise performance

		(INR m)							
		Q4FY07	Q4FY06	YoY chg (%)	Q3FY07	QoQ chg (%)	FY07	FY06	YoY chg (%)
Individual	Net revenues	673	442	52	560	20	2,470	1,670	48
	OP	133	50	166	93	43	434	128	239
	OPM (%)	19.8	11.3		16.6		17.6	7.7	
Institutional	Revenue	228	277	-18	226	1	847	1,175	-28
	OP	25	46	-46	27	-7	99	213	-54
	OPM (%)	11.0	16.6		11.9		11.7	18.1	
Corporate	Revenue	486	431	13	479	1	1917	1,662	15
	OP	68	69	-1	65	5	283	262	8
	OPM (%)	14.0	16.0		13.6		14.8	15.8	
New* initiatives	Revenue	35			25	40	73		
	OP	-27			-48	-44	-91		
	OPM (%)	-77.1			-192		-125		
ElementK*	Revenue	1145			960	19	2643		
	OP	4			41	-90	72		
	OPM (%)	0.3			4.3		2.7		
Total	Revenue	2,567	1,150	123	2,250	14	7,950	4,507	76
	OP	203	165	23	178	14	797	603	32
	OPM (%)	7.91	14.3		7.9		10.0	13.4	

Source: Company, Brics Research

* These businesses started in FY07

Segment-wise business analysis

Individual Business

Individual business delivers strong growth in Q4FY07

Individual business continued to deliver strong growth in revenues coupled with margin expansion. Net revenues were up 52% YoY for Q4FY07 and about 48% for FY07. Operating margins were up at 19.8% from 16.6% in Q3FY07. During FY07, margins in the Individual business catapulted to 17.6% from 7.7% in FY06.

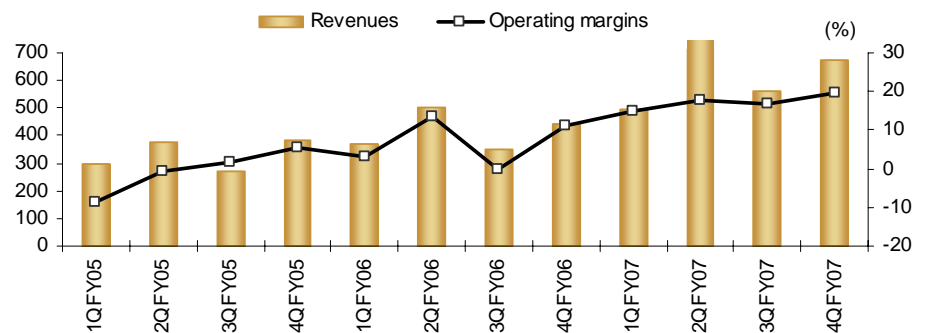
China drives growth

China led the growth in revenues in this quarter delivering a 100% YoY growth. It now contributes 20% of the full-year system-wide revenues for the Individual business.

Capacity utilisation improves further

Capacity utilisation improved by 100bp to 52% for Q4FY07. For FY07 capacity utilization were at 54% compared to 46% for FY06. This improvement comes on the back of an 18% seat capacity addition during the year. Total seat capacity increased from 140,000 for FY06 to 165,000 for FY07. The company plans to increase seat capacity steadily to around 236,000 seats by FY10.

Figure 3: Individual business – revenues and margins

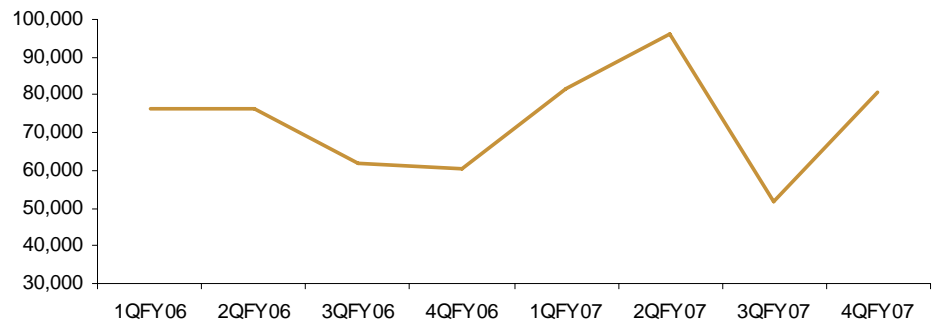


Source: Brics Research

Enrolments remain strong

Net enrolments registered a strong 33% growth for Q4FY07, and stood at 80,632 compared to 60,565 for Q4FY06. Career registrations were up 23% for FY07, while engineering and computer science students enrolments went up 32% YoY. Total enrollments for the flagship GNIIT program were up by around 37% in FY07 at 52000 compared to 38000 in the previous year. However according to the management the number of students enrolling for the complete 3-year program has more than doubled to around 20000 in FY07 compared to around 9000 in FY06.

Figure 4: Enrolments



Source: Brics Research

Individual business to continue growing

We expect the Individual business to continue delivering strong growth on the back of improved capacity utilisation, new course offerings and timely fee hikes. Margins expansion of around 150bp is expected for FY08, with a 34% growth in revenues.

Figure 5: Individual business

	<i>(INR m)</i>			
	FY06	FY07	FY08E	FY09E
Net revenues	1670	2473	3,324	4,321
Growth (%)		48	34	30
Operating profits	128	434	632	907
Growth (%)		239	46	44
Operating margins (%)	7.7	17.5	19.0	21.0

Source: Brics Research

Institutional Business

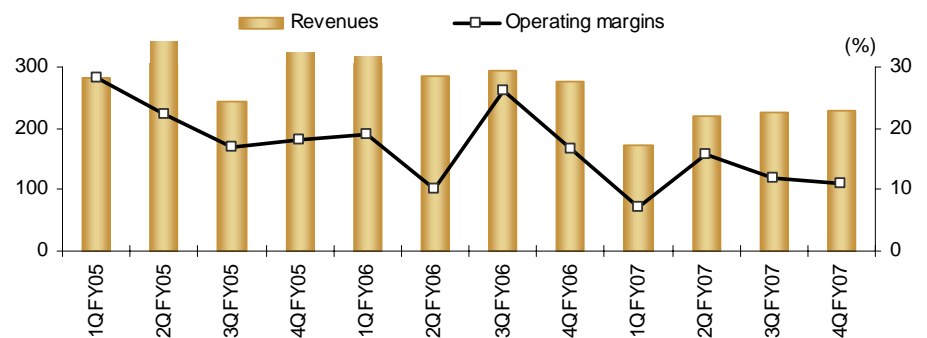
Institutional business gradually degrows

The Institutional business continued to degrow due to the company's decision to be selective in government business. Revenues for Q4FY07 were down 18% with a 600bp erosion in operating margins. Full-year revenues were down 28% and operating margins were 650bp lower at 12%.

Improved working capital situation

The defocus from governmental business has had a significantly positive impact on the working capital requirement of the company. Debtor days, which were at 150 days for FY06, have improved to 101 days for FY07.

Figure 6: Institutional business – revenues and margins



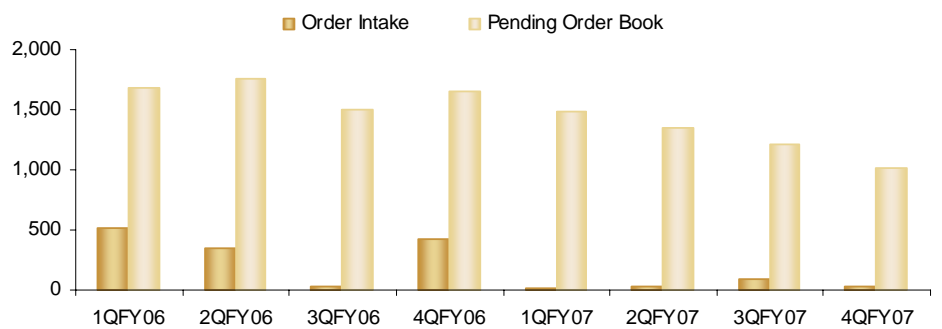
Source: Brics Research

Fresh order intakes slow down

Fresh order intakes have slowed down drastically for the Institutional business, resulting in significant shrinkage in the pending order book position. Closing order book for FY07 stood at INR 1,016m with 56% executable in the next 12 months.

Figure 7: Institutional business order book

(INR m)



Source: Brics Research

Institutional business to stabilise

We expect the institutional business to stabilise and show modest improvement in revenues and margins. The non-government business grew by 20% for FY07 and now contributes around 29% in revenues to the core business compared to 17% for FY06.

Figure 8: Institutional business

	FY06	FY07	FY08E	FY09E
Net revenues	1,175	847	889	978
Growth (%)		-28	5	10
Operating profits	213	99	106.68	117.36
Growth (%)		-54	8	10
Operating margins (%)	18.1	11.7	12.0	12.0

Source: Brics Research

Corporate Business

Stronger rupee affects revenues and margins

Corporate business delivered revenue growth of 13% for the quarter with operating margins of 14%. A stronger rupee had an impact of around 2.5 % on revenues. The Corporate business witnessed a 15% growth for FY07 with operating margins of around 15%.

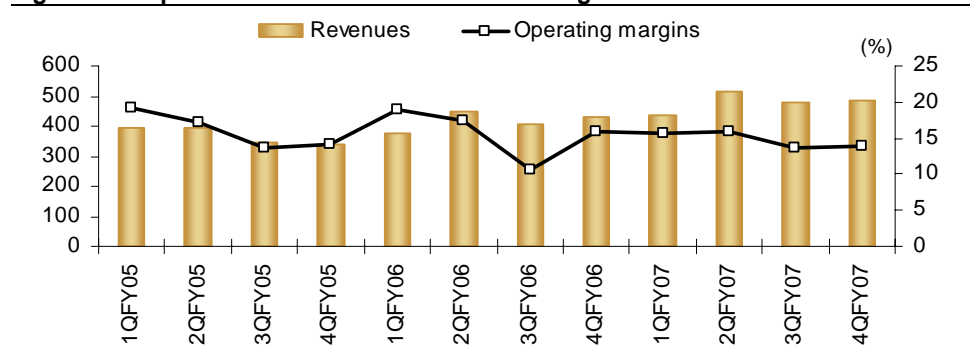
Improving product mix

The revenue product mix for the year improved with Content now contributing 48% to revenues, while Learning Delivery and Learning Technology contributed 33% and 18% respectively. Litmus is still small with just 1% contribution.

Takes on nine new customers

The technology vertical added nine new customers for the quarter. About 47,000 people took tests for the Income Tax TRP scheme under the aegis of Litmus.

Figure 9: Corporate business – revenues and margins



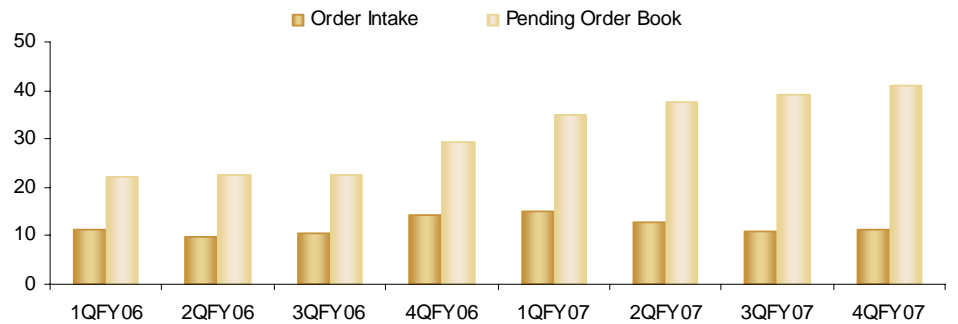
Source: Brics Research

Robust order book

Order book for the Corporate business continues to be strong. Fresh orders intakes were USD 11.4m for Q4FY07, while the pending order book stood at USD 40.9m at the end of the quarter.

Figure 10: Corporate business - order book

(INR m)



Source: Brics Research

We expect the Corporate business to sustain 15% YoY growth and its margins to improve gradually over the next two years. However, a stronger-than-expected rupee could impact revenues and margins for this business, in our view.

Figure 11: Corporate business

(INR m)

	FY06	FY07	FY08E	FY09E
Net revenues	1,662	1,917	2,205	2,535
Growth (%)		15	15	15
Operating profits	262	283	330.75	405.6
Growth (%)		8	17	23
Operating margins (%)	15.8	14.8	15.0	16.0

Source: Brics Research

ElementK

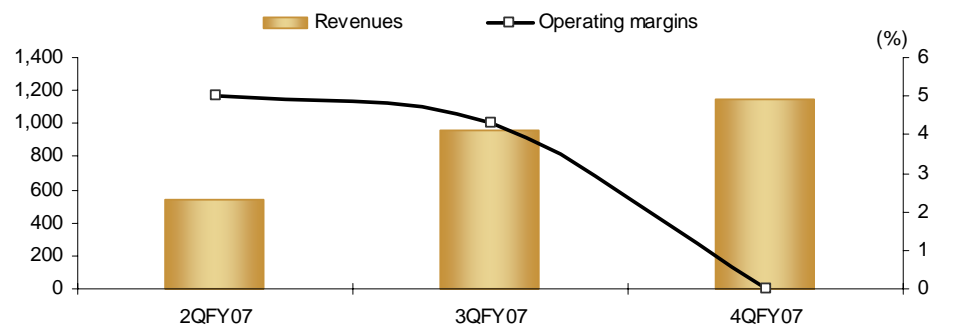
Margins disappoint

ElementK registered an EBITDA of just INR 4m for Q4-FY7, below our estimate of 5% operating margins. Since the company is a relatively recent acquisition, we expect this to be a one-off event. ElementK has reported operating margins of 2.7% for the full year.

Revenues better than expected

ElementK reported revenues of INR 1,145m for Q4FY07, which were ahead of our estimate of INR 900m. According to the management, net revenues of INR 2,643m for the first eight months of FY07 were 7% higher than last year on a like-to-like basis.

Figure 12: ElementK – revenues and margins



Source: Brics Research

Margins to improve going forward

We expect operating margins of ElementK to improve significantly in the next two years and reach the 9% mark by FY09. The management claims to have achieved its annualised cost saving target.

Figure 13: Element K

	(INR m)		
	FY07	FY08E	FY09E
Net revenues	2,643	3,965	4,163
Growth (%)		50	5
Operating profits	72	237.9	374.67
Operating margins (%)	2.7	6.0	9.0

Source: Brics Research

New Initiatives

NIIT's new businesses (Imperia & IFBI) registered net revenues of INR 35m for the quarter, with an operating loss of INR 27m. For the full year, revenues stood at INR 73m with an operating loss of INR 91m. About 2,500 students have been trained at IFBI and 700 people are enrolled with Imperia to date. The company plans to venture into other sectors that face talent development issues. It also expects to enter the Insurance training space by end-2008.

Currently there are 10 IFBI-Imperia centers in 8 cities. The company is planning to rapidly expand the center network to around 19 in FY08 and 30 in FY09. The cost of setting up a center is around INR 6 – INR 7 mn, in addition to this there is also some centralized costs associated with the new businesses. At full capacity a center can garner annual revenues of around INR 70 – INR 80 mn on an average.

The management expects to break even during FY08 with revenues of INR 350m for the period. For FY09, the company expects revenues of INR 950–1,000m and operating margins of about 25%.

Given some better visibility on the new businesses we have revised our revenue estimates to INR 300 mn in FY08 and INR 750 mn in FY09. We now expect these businesses to break even in FY08 and deliver a 15% operating margin in FY09.

Figure 14: New initiatives

	<i>(INR m)</i>		
	FY07	FY08E	FY09E
Net revenues	73	300	750
Growth (%)		311	150
Operating profits	-91	0	112.5
Operating margins (%)	-124.7	0.0	15.0

Source: Brics Research

Valuation

We revise our price target upwards to INR 1,198

We upgrade our one-year forward price target to INR 1,198. The revision is largely due to improved visibility of revenues and margins in the new businesses.

Figure 15: NIIT – SOTP valuation

	Revised	Previous	Methodology
NIIT's organic business	945	795	DCF based
NIIT Tech stake value	209	166	At 20% discount to current market price
Element K	44	50	EV/EBITDA multiple of 7x for FY09E
Total	1198	1011	

Source: Brics Research

Organic NIIT

We continue to use the DCF methodology to value NIIT's organic business. Based on this, our one-year forward price target for the organic business is INR 945. The increase in our price target comes from better visibility in the new businesses and lower working capital requirement due to a defocus from the Government business.

NIIT Technologies stake

NIIT holds 25% stake in NIIT Technologies, which has reported strong quarterly and annual financial performance during the last quarter, resulting in 30% appreciation in the stock price. At the current market price (CMP), the value of this investment translates into INR 262 per share for NIIT. Using a similar 20% discount to market price as used earlier, we now value this investment at INR 209 per share for NIIT.

ElementK

We have downgraded our value estimates for ElementK marginally due to the management's muted margins outlook. We continue to value this business at 7x FY09E EBITDA, which would result in a value of INR 44 per share for NIIT.

We maintain BUY

We expect NIIT to record a fully diluted EPS of INR 45 for FY08 and INR 72 for FY09. The stock trades at INR 914, which is 20x FY08E and 13x FY09E. On an EV/EBITDA basis for the core business, it trades at 10x FY09E. Our SOTP valuation estimates one-year forward target price of INR 1,198 which implies an upside potential of 31% from current levels. We maintain BUY.

Income statement						<i>INR m</i>
Year ending 31 Mar	FY05	FY06	FY07E	FY08E	FY09E	
Net sales	3,984	4,507	7,950	10,687	12,754	
<i>Growth (%)</i>	<i>(43.7)</i>	<i>13.1</i>	<i>76.4</i>	<i>34.4</i>	<i>19.3</i>	
Operating expenses	(3,495)	(3,906)	(7,153)	(9,379)	(10,834)	
Core EBITDA	489	601	797	1,308	1,919	
Other income	96	85	90	100	100	
EBITDA	585	685	887	1,408	2,019	
Depreciation	(345)	(373)	(469)	(541)	(543)	
EBIT	240	312	419	868	1,477	
Interest paid	(23)	(46)	(84)	(172)	(137)	
Pre-tax profit	217	266	335	696	1,340	
Tax (current + deferred)	(10)	(29)	(9)	(104)	(241)	
Profit after tax	207	237	326	592	1,098	
Minority interests	149	164	331	414	497	
Net profit	356	401	657	1,005	1,595	
Adjusted net profit	356	401	657	1,005	1,595	
<i>Growth (%)</i>	<i>393.7</i>	<i>12.5</i>	<i>63.8</i>	<i>53.1</i>	<i>58.6</i>	

Balance sheet						<i>INR m</i>
Year ending 31 Mar	FY05	FY06	FY07E	FY08E	FY09E	
Current assets	2,154	3,298	4,098	4,607	5,350	
Investments	424	400	420	441	463	
Fixed assets	1,238	1,387	2,000	2,290	2,553	
Total assets	3,816	5,084	6,518	7,337	8,366	
Current liabilities	999	1,289	1,375	1,476	1,559	
Total Debt	412	1,090	2,255	2,145	1,716	
Total liabilities	1,411	2,379	3,630	3,621	3,275	
Paid-up capital	193	193	221	221	221	
Reserves & surplus	2,156	2,456	2,667	3,495	4,869	
Shareholders' funds	2,405	2,705	2,888	3,716	5,090	
Minorities	56	56	0	0	0	
Total equity & liabilities	3,817	5,084	6,518	7,337	8,366	

Cashflow						<i>INR m</i>
Year ending 31 Mar	FY05	FY06	FY07E	FY08E	FY09E	
Pre-tax profit	217	266	335	696	1,340	
Depreciation	345	373	469	541	543	
Tax paid	(10)	(29)	(9)	(104)	(241)	
Chg in working capital	(873)	(562)	(438)	(665)	(287)	
Cashflow from operations (a)	(321)	48	357	468	1,354	
Capital expenditure	(101)	(419)	(1,082)	(830)	(806)	
Chg in investments	315	25	(20)	(21)	(22)	
CF from investing (b)	215	(395)	(1,102)	(851)	(828)	
Free cashflow (a+b)	(107)	(347)	(745)	(383)	526	
Equity raised/(repaid)	0	0	28	0	0	
Chg in minorities	171	164	275	414	497	
Debt raised/(repaid)	153	678	1,165	(110)	(429)	
Dividend (incl. tax)	(109)	(122)	(144)	(177)	(221)	
Other financing activities	(143)	(81)	(302)	0	0	
CF from financing (c)	72	640	1,022	127	(154)	
Net chg in cash (a+b+c)	(34)	293	276	(257)	373	

Key ratios					
Year ending 31 Mar	FY05	FY06	FY07E	FY08E	FY09E
Adjusted EPS (INR)	18.4	20.8	29.7	45.5	72.2
Adjusted EPS growth (%)	393.7	12.5	43.2	53.1	58.6
Core EBITDA growth (%)	1.3	22.8	32.7	64.1	46.7
Core EBITDA margin (%)	12.3	13.3	10.0	12.2	15.0
Pre-tax margin (%)	5.4	5.9	4.2	6.5	10.5
ROE (%)	15.5	15.7	23.5	30.5	36.2
ROCE (%)	9.1	9.5	9.4	15.8	23.3
Net debt/Equity (%)	2.2	16.3	46.0	39.7	13.2

Valuation parameters					
Year ending 31 Mar	FY05	FY06	FY07E	FY08E	FY09E
PER (x)	49.4	43.9	30.7	20.0	12.6
PCE (x)	25.1	22.7	17.9	13.0	9.4
Price/Book (x)	7.3	6.5	7.0	5.4	4.0
Yield (%)	0.6	0.7	0.7	0.9	1.1
EV/Net sales (x)	4.5	4.1	2.4	1.8	1.5
EV/Core EBITDA (x)	36.9	30.7	24.3	14.9	9.7

NIIT: Recommendation history

Date	Stock price (INR)	Recommendation	Price target (INR)	Report
4-May-07	764	BUY	1011	Time for some training
9-May-07	770	BUY	1011	Visit note
7-Jun-07	911	BUY	1198	Q4FY07 result - Individual training business leads the way - We revise our price target to INR 1,198

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