

NIIT Tech reported a slightly higher than expected revenue at INR 5.14bn (SPAe: 5.09bn) on the back of higher govt. based business contribution. However its margins declined by 116bps to 15.8% due to cost overruns in GIS business and Morris transformation deal. PAT reported an increase by 30% QoQ on the back of higher other income on account of revaluation gains. We consider the lower volume growth as 1-2 quarter phenomenon due to natural catastrophes taking a toll on the NITL business and thus expect a rebound by H1FY14. Hence, we continue to recommend BUY with a 15-month Target Price of INR 329 based on 7.3x FY14E earnings.

Revenue Growth - Stable

NIIT Tech reported 2.9% sequential revenue growth to INR 5.14bn. The constant currency growth was 4.4% partially offset by currency movement. Government's CCTNS and commodity board projects in India laid the groundwork for the growth through System Implementation and Package Implementation services. Europe (largest revenue contributor) also performed well with 5.7% volume growth with US flat at 1%.

Margin - Decline

Operating margins at 15.8% are the lowest ever for the company barring Q2FY12 which was affected by Morris transformational costs. The margins declined by 116bps QoQ because of (i) Negative margins of -7% in GIS due to cost overruns in APDRP (ii) NITL's slower growth led by natural calamity (hurricane Sandy) and (iii) Morris transformation cost for new project. We expect margins to improve slightly in Q4, it being a traditionally strong quarter for GIS and also wearing off the effect of Sandy though partially offset by higher hardware spend for the new govt. project.

Deal Details

The company added 4 new clients two in APAC and 1 each in India and Europe. It saw deal intake worth \$83mn taking the 12-month executable order book to \$242mn (\$252mn in constant currency).

Growth Avenues

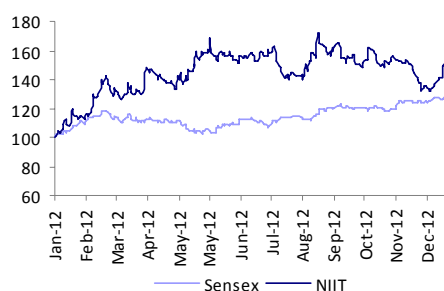
Q3FY13 delta growth was fueled mainly by India (up 23.4% QoQ) driven business through govt. (64.6%) projects of CCTNS (revenue contribution of INR 266mn) and Commodity (tobacco) board for providing managed services (12.2%) and SI & PI (14.3%). IP business declined by -7.4% due to softness in NITL affecting BFS vertical. Insurance business was also affected as one of NIIT's largest customers is undergoing massive restructuring in US.

Outlook and Recommendation

NIIT's high margin non-linear business continues to contribute 21% to the topline though at lower margins. We expect a sharp recovery in this business in H1FY14 on the back of (i) Morris transformation completion, thus moving the business to transaction pricing (ii) Commodity board transaction pricing business coming onboard (iii) Wearing off Sandy effect improving NITL's growth and margins which have been traditionally at 25%+ (iv) Cost over-runs in APDRP done; along with Q4 being a seasonally strong quarter for GIS and (v) Strong deal pipeline with 3-4 large deals on the table. Factoring this we not only expect revenue CAGR of 19% over FY12-14E but also expect the company to revisit its 18% operating margin levels by H1FY14 resulting in an EPS CAGR of 16% over FY12-14E. Thus, we continue to recommend BUY with a 15-month TP of INR 329 at 7.3x FY14E earnings.

Shareholding (%)	Dec-12
Promoters	31.33
FII's	26.83
DIIS	17.57
Others	24.27

Relative Price Performance



Key Data	
BSE Code	532,541
NSE Code	NIITTECH
Bloomberg Code	NITEC IN
Reuters Code	NITT.NS
Shares Outstanding (mn)	59.3
Face Value	10.0
Mcap (INR bn)	16.6
52 Week H/L	324.8/196.3
2W Avg. Qty, NSE	23,000
Free Float (%)	65.00%
Beta	0.66

Y/E (INR mn)	FY11	FY12	FY13E	FY14E
Net Sales	12,323	15,764	20,195	22,417
Growth (%)	34.87%	27.92%	28.11%	11.00%
EBIDTAM (%)	19.18%	17.02%	16.05%	18.33%
Adj. PAT	1,822	1,971	2,166	2,652
Growth (%)	44.19%	8.16%	9.87%	22.46%
Adj. EPS (INR)	30.52	33.27	36.55	44.76
P/E (x)	6.05	8.14	7.66	6.25
EV/EBIDTA	4.14	5.13	4.04	2.80
Net Debt/Equity	(0.14)	(0.24)	(0.27)	(0.35)
RoCE (%)	22.86%	19.35%	19.24%	20.95%
RoE (%)	27.93%	23.97%	22.15%	23.14%

Quarterly Performance Parameters
Fig.1: Quarterly Performance - Revenue growth of 2.86% on the back of cross-currency growth of 4.4%

Quarterly Performance	Quarterly Numbers					QoQ Growth Trend (%)					YoY Growth (%)
	3QFY12	4QFY12	1QFY13	2QFY13	3QFY13	3QFY13	2QFY13	1QFY13	4QFY12	3QFY12	
Revenues (INR Mn)	4,330	4,435	4,696	5,001	5,144	2.86%	6.49%	5.89%	2.42%	16.68%	18.80%
Less: Cost of Revenue	2,736	2,824	3,047	3,203	3,383	5.62%	5.12%	7.90%	3.22%	18.90%	23.65%
Gross Profit	1,594	1,611	1,649	1,798	1,761	-2.06%	9.04%	2.36%	1.07%	13.05%	10.48%
Gross Margins	36.81%	36.32%	35.11%	35.95%	34.23%						
Less: SG&A	814	867	898	950	948	-0.21%	5.79%	3.58%	6.51%	-5.35%	16.46%
EBIDTA	780	744	751	848	813	-4.13%	12.92%	0.94%	-4.62%	41.82%	4.23%
EBIDTA Margins	18.01%	16.78%	15.99%	16.96%	15.80%						
Less: Depreciation	92	111	126	138	142	2.90%	9.52%	13.51%	20.65%	10.84%	54.35%
EBIT	688	633	625	710	671	-5.49%	13.60%	-1.26%	-7.99%	47.32%	-2.47%
EBIT Margins	15.89%	14.27%	13.31%	14.20%	13.04%						
Add: Other Income (Net)	174	(46)	210	(115)	126						
PBT	862	587	835	595	797						
Less: Taxes	224	111	246	146	230						
Tax Rate	25.99%	18.91%	29.46%	24.54%	28.86%						
PAT	638	476	589	449	567	26.28%	-23.77%	23.74%	-25.39%	48.03%	-11.13%
PAT Margins	14.73%	10.73%	12.54%	8.98%	11.02%						
Less: Minority Interest	(2)	15	13	18	7						
Add: Extraordinary Items	-	-	-	-	-						
Net Income	640	461	576	431	560	29.93%	-25.17%	24.95%	-27.97%	39.74%	-12.50%
EPS (Diluted)	10.80	7.78	9.60	7.27	9.45	29.93%	-24.27%	23.45%	-27.97%	39.74%	-12.50%

Fig.2: Vertical Segmentation Performance

Vertical Breakdown	Share Proportion (%)					QoQ Growth Trend (%)					YoY Growth (%)
	3QFY12	4QFY12	1QFY13	2QFY13	3QFY13	3QFY13	2QFY13	1QFY13	4QFY12	3QFY12	
BFSI	36.00	34.00	34.00	33.00	31.00	(3.37)	3.36	5.89	(3.27)	7.70	2.30
Govt	5.00	7.00	8.00	5.00	8.00	64.58	(33.44)	21.01	43.39	45.85	90.08
Manufacturing	7.00	6.00	7.00	6.00	6.00	2.86	(8.72)	23.53	(12.21)	2.10	1.83
Transport	38.00	39.00	40.00	42.00	42.00	2.86	11.82	8.60	5.12	23.16	31.30
Others	14.00	14.00	11.00	14.00	13.00	(4.49)	35.54	(16.80)	2.42	25.66	10.31

Fig.3: Geographical Segmentation Performance

Geographical Breakdown	Share Proportion (%)					QoQ Growth Trend (%)					YoY Growth (%)
	3QFY12	4QFY12	1QFY13	2QFY13	3QFY13	3QFY13	2QFY13	1QFY13	4QFY12	3QFY12	
Americas	37.00	37.00	36.00	38.00	37.00	0.15	12.41	3.02	2.42	16.68	18.80
Europe	39.00	37.00	39.00	39.00	40.00	5.50	6.49	11.61	(2.83)	19.75	21.85
India	13.00	13.00	12.00	10.00	12.00	23.43	(11.25)	(2.26)	2.42	26.40	9.66
APAC	11.00	13.00	13.00	13.00	11.00	(12.97)	6.49	5.89	21.05	(1.27)	18.80

Fig.4: Services Segment Performance

Horizontal Breakdown	Share Proportion (%)				QoQ Growth Trend (%)						YoY Growth (%)
	3QFY12	4QFY12	1QFY13	2QFY13	3QFY13	3QFY13	2QFY13	1QFY13	4QFY12	3QFY12	
ADM	62.0	61.0	61.0	64.0	63.0	1.3	11.7	5.9	0.8	11.3	20.7
IP Assets	13.0	11.0	12.0	10.0	9.0	(7.4)	(11.3)	15.5	(13.3)	8.3	(17.8)
Managed Services	12.0	13.0	12.0	11.0	12.0	12.2	(2.4)	(2.3)	11.0	7.7	18.8
SI & PI	7.0	9.0	9.0	9.0	10.0	14.3	6.5	5.9	31.7	63.4	69.7
BPO / Others	6.0	6.0	6.0	6.0	6.0	2.9	6.5	5.9	2.4	133.4	18.8

Fig.5: Client Segment Performance

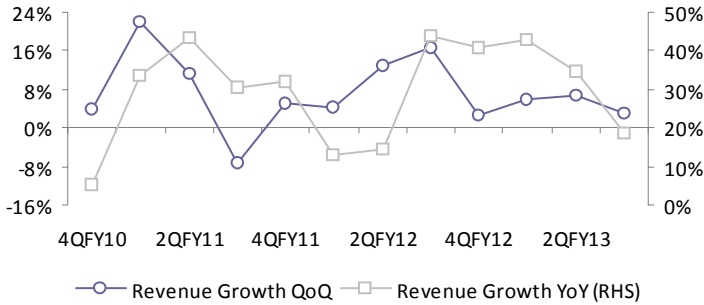
Client Conc. Breakdown	Share Proportion (%)				QoQ Growth Trend (%)						YoY Growth (%)
	3QFY12	4QFY12	1QFY13	2QFY13	3QFY13	3QFY13	2QFY13	1QFY13	4QFY12	3QFY12	
Top 5 Clients	29.00	30.00	30.00	32.00	34.00	9.29	13.59	5.89	5.96	12.79	39.28
Top 10 Clients	44.00	43.00	43.00	47.00	48.00	5.05	16.40	5.89	0.10	16.68	29.60
Top 20 Clients	58.00	59.00	60.00	64.00	65.00	4.47	13.59	7.68	4.19	12.79	33.14
Top 11-20 Clients	14.00	16.00	17.00	17.00	17.00	2.86	6.49	12.50	17.06	2.10	44.26
Non Top 20 Clients	42.00	41.00	40.00	36.00	35.00	0.00	(4.15)	3.30	(0.01)	22.51	(1.00)

(Source: SPA Research, Company Data)

Other Key Highlights:

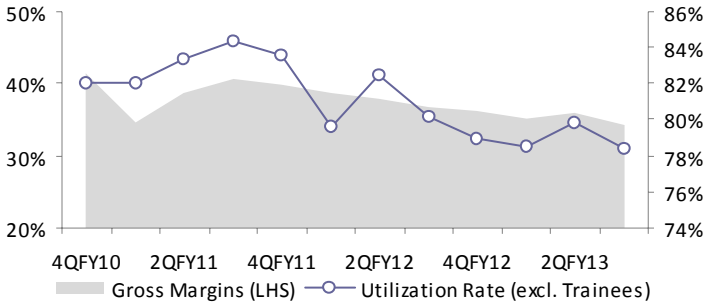
- 1) Company added 265 net hires (3.5% growth). Attrition was lower at 12.5% against 12.7% in Q2. Utilization dropped by 140bps to 78.4% in absence of significant volume growth.
- 2) Management indicated towards facing no pricing pressure from clients.
- 3) Debt stood at INR 92mn after payment of INR 215mn GBP denominated debt taken in UK. Cash increased by INR 536mn to INR 2,856mn and Free Cash Flow of INR 550mn
- 4) Top 5 Client continue to drive growth with a healthy rate of 9.3% sequentially while the non-top-20 client contribution was flat.
- 5) Revenue contribution from businesses and their margins: (i) GIS (INR 197mn down 14% QoQ with margins at -7%), (ii) NITL (INR 337mn @ 18%-19% margins), (iii) Proyecta (INR 144mn, with flat revenue growth), (iv) Morris (INR 303mn @ 9% margins) and (v) Sabre-Manila (INR 52mn @ 8%-9% margins).
- 6) Company to focus on more Tier-2 insurance companies for delta growth.
- 7) NIIT has outstanding hedges of \$49.7mn spread over the next four quarters at an average rate of INR 56.71/USD.

Fig.6: Seasonally weak Q3 leading to decline in Revenue growth



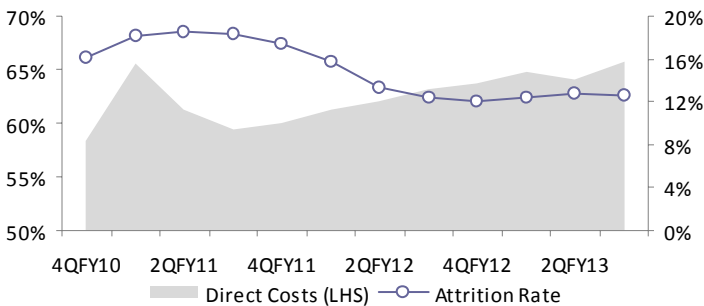
(Source: Company, SPA Research)

Fig.7: Seasonally weak Q3 leading to decline in Revenue growth



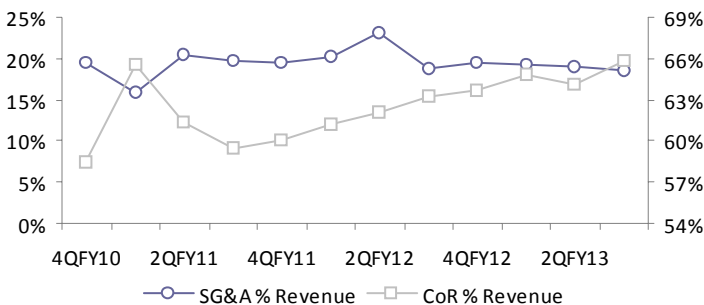
(Source: Company, SPA Research)

Fig.8: Cost overruns in GIS causing higher direct costs



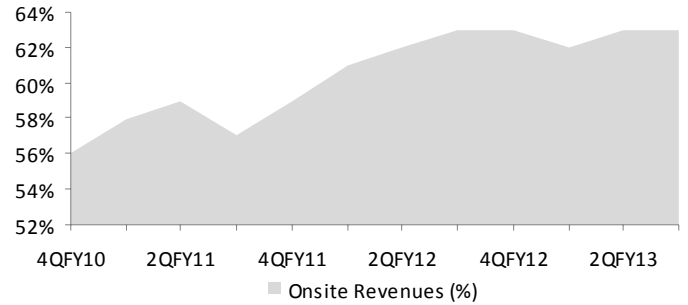
(Source: Company, SPA Research)

Fig.9: leading to higher CoR as a % of revenue, however lower SG&A spend partially compensating for some of that cost increases.



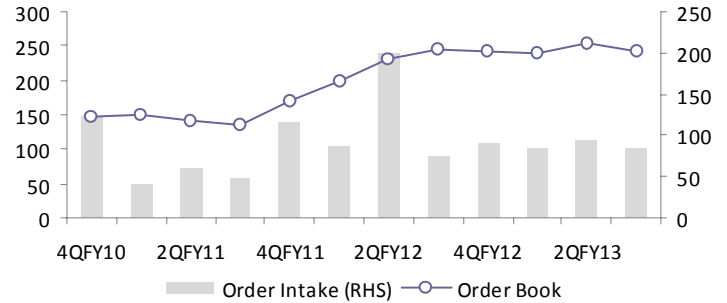
(Source: Company, SPA Research)

Fig.10: Onsite revenues stable but will dip due to increased offshoring from Morris acting as a significant margin lever going forward.



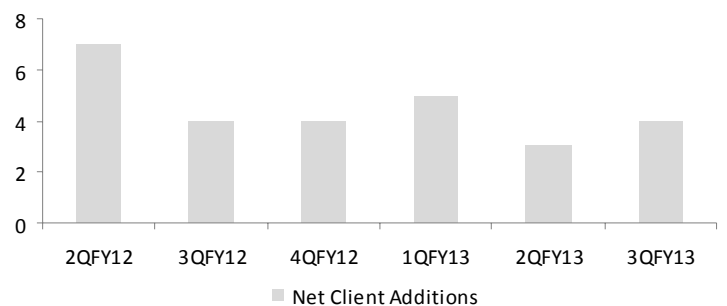
(Source: Company, SPA Research)

Fig.11: Order intake stable with order book in the range of \$240mn



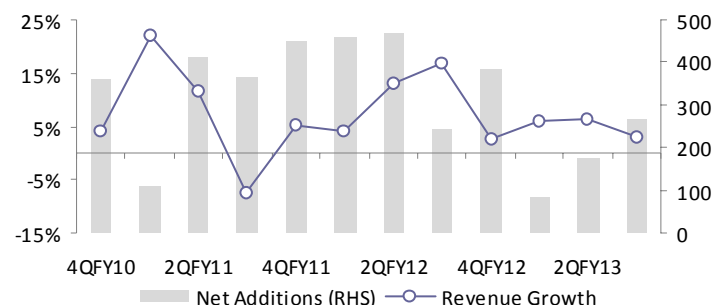
(Source: Company, SPA Research)

Fig.12: Four new clients added with total Mn \$ client count stable at 68.



(Source: Company, SPA Research)

Fig.13: Company on track by hiring 200-250 employees per quarter.



(Source: Company, SPA Research)

Financials

Income statement

Y/E Mar (INR Mn)	FY11	FY12	FY13E	FY14E
Net Sales	12,323	15,764	20,195	22,417
<i>Growth (%)</i>	<i>34.87%</i>	<i>27.92%</i>	<i>28.11%</i>	<i>11.00%</i>
Employee Cost	6,014	7,843	10,234	11,353
Development and Bought Out	2,155	2,533	3,199	3,212
S&M	138	132	303	269
G&A	1,654	2,573	3,219	3,475
Total Optg. Exps.	9,960	13,081	16,954	18,309
EBIDTA (excl OI)	2,363	2,683	3,241	4,108
EBIDTA Margin (%)	19.18%	17.02%	16.05%	18.33%
<i>EBIDTA Growth (%)</i>	<i>38.80%</i>	<i>13.53%</i>	<i>20.79%</i>	<i>26.78%</i>
Dep./Amortization	(315)	(364)	(458)	(523)
EBIT	2,049	2,319	2,782	3,585
<i>EBIT Margins (%)</i>	<i>16.62%</i>	<i>14.71%</i>	<i>13.78%</i>	<i>15.99%</i>
Interest Expense	7	-	7	7
Other Income	136	282	181	41
PBT	2,177	2,601	2,956	3,620
Tax Expenses	323	637	828	1,003
PAT	1,854	1,964	2,129	2,617
<i>PAT Margins (%)</i>	<i>15.05%</i>	<i>12.46%</i>	<i>10.54%</i>	<i>11.67%</i>
<i>PAT Growth (%)</i>	<i>45.24%</i>	<i>5.92%</i>	<i>8.38%</i>	<i>22.95%</i>
Minority Interest	32	(7)	(37)	(35)
APAT	1,822	1,971	2,166	2,652
<i>APAT Margins (%)</i>	<i>14.79%</i>	<i>12.50%</i>	<i>10.72%</i>	<i>11.83%</i>
<i>APAT Growth (%)</i>	<i>44.19%</i>	<i>8.16%</i>	<i>9.87%</i>	<i>22.46%</i>

Key Ratio

YE Mar	FY11	FY12	FY13E	FY14E
Per Share Data (INR)				
Reported EPS	30.52	33.27	36.55	44.76
Adj. EPS	30.52	33.27	36.55	44.76
<i>Growth (%)</i>	<i>43.47%</i>	<i>8.99%</i>	<i>9.87%</i>	<i>22.46%</i>
CEPS	34.09	38.70	46.75	59.26
DPS	7.51	7.50	8.00	8.50
BVPS	112.03	138.31	162.22	190.91
FCFPS	2.87	16.74	16.76	43.57
EVAPS	14.07	11.29	12.79	18.79
Return Ratios (%)				
RoCE	22.86	19.35	19.24	20.95
RoIC	25.65	21.10	20.63	22.72
CRoIC	20.37	17.77	17.94	19.22
Du Pont Analysis				
Tax Burden	0.85	0.76	0.72	0.72
Interest Burden	1.06	1.12	1.06	1.01
Sales Turnover	0.17	0.15	0.14	0.16
Asset Turnover	1.61	1.74	1.94	1.81
Debt Liabilities	1.15	1.10	1.08	1.09
RoE	27.93%	23.97%	22.15%	23.14%
Valuation Ratios				
P/E (x)	6.05	8.14	7.66	6.25
P/BV (x)	1.65	1.96	1.72	1.47
PEG (x)	0.14	0.91	0.78	0.28
MCap/ Sales (x)	0.89	1.02	0.79	0.72
EV/EBIDTA (x)	4.14	5.13	4.04	2.80
Payout Ratio (%)	24.42%	22.55%	21.89%	18.99%

Balance Sheet

Y/E Mar (INR Mn)	FY11	FY12	FY13E	FY14E
Share Capital	593	593	593	593
Reserves and Surplus	6,886	8,319	9,719	11,718
Total Networkth	7,478	8,912	10,312	12,311
Minority Interest	43	36	(1)	(36)
Secured	110	100	100	100
Unsecured	1	0	-	-
Total Debt	110	100	100	100
Source of Funds	7,631	9,048	10,411	12,375
Net Block				
Net Block	1,894	2,099	2,181	2,148
CWIP	1,437	688	689	595
Investments	443	452	406	1,092
Current Assets	6,223	7,967	9,623	11,236
Current Liabilities	2,508	2,360	2,669	2,869
Net Current Assets	3,715	5,607	6,954	8,368
Deferred Tax Assets	143	203	181	172
Application of Funds	7,631	9,048	10,411	12,375

Cash Flow

Y/E Mar (INR Mn)	FY11	FY12	FY13E	FY14E
EBT	2,177.2	2,601.0	2,956.4	3,619.7
Less: Other Income/Excp.	(55.7)	(40.0)	(41.3)	(41.0)
Add: Depreciation	314.6	364.0	458.3	523.3
Add: Interest Paid	7.0	-	7.0	6.5
Less: Taxes Paid	(500.2)	(637.0)	(827.8)	(1,002.7)
Change in Working Capital	(1,337.6)	(712.3)	(1,015.7)	(31.5)
Others	58.1	0.2	0.2	0.2
CFs from Operations (a)	663	1,576	1,537	3,075
Change in Fixed Assets	(493.3)	(584.0)	(544.0)	(493.0)
Change in CWIP	1.0	2.0	3.0	4.0
Change in Investments	60.4	536.5	167.3	(445.0)
Others	58.8	40.0	41.3	41.0
CFs from Investments (b)	(374)	(7)	(335)	(897)
Change in Equity	65.4	-	-	-
Change in Debt	(120.4)	(9.0)	-	-
Dividend Paid	(486.6)	(519.9)	(554.6)	(589.3)
Interest Paid	(7.0)	(8.3)	(7.0)	(6.5)
CFs from Financing (c)	(549)	(537)	(562)	(596)
Change in Cash (a+b+c)	(259)	1,031	640	1,582
Opening Cash	1,430	1,194	2,225	2,866
Exchange Difference	24	-	-	-
Closing Cash	1,194	2,225	2,866	4,447
FCF	170	992	993	2,582

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