

**BUY**

TP: Rs 1,550 | ▲ 15%

**NIIT TECHNOLOGIES**

| IT Services

| 24 July 2019

## Healthy Q1 despite pockets of weakness in BFS

**Adjusted for GIS divestment, NIIT Tech (NITEC) reported organic revenue growth of 4% QoQ CC and EBITDA margins of 16.9% in Q1FY20, marking a better-than-expected operating performance. Deal wins and executable order book were healthy. Management reported challenges at one large BFS client but no loss of wallet share. NITEC continues to focus on predictable and profitable growth for FY20. We remain positive on the stock and reiterate BUY, rolling forward to a revised Jun'20 TP of Rs 1,550 (Rs 1,500 earlier).**

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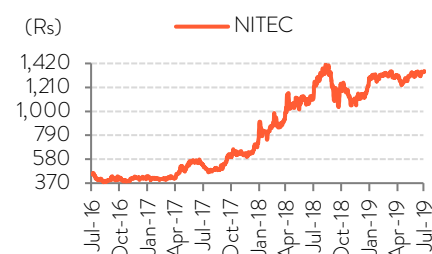
**Operating performance healthy ex-GIS divestment:** NITEC's reported Jun'19 quarter performance was adversely affected by divestment of the GIS business and select non-recurring expenses. Ex-GIS impact, organic revenue growth stood at 4% QoQ CC, bettering our estimate of 2.7%. Similarly, adj. EBITDA margins came in at 16.9% (-70bps QoQ) vs. 16% estimated. Consolidation of Wishworks contributed Rs 108mn in revenue for the quarter.

Ticker/Price	NITEC IN/Rs 1,353
Market cap	US\$ 1.2bn
Shares o/s	62mn
3M ADV	US\$ 8.8mn
52wk high/low	Rs 1,425/Rs 1,031
Promoter/FPI/DII	31%/42%/27%

Source: NSE

**Deal wins and executable orders continue to trend up:** Fresh order intake at US\$ 175mn rose for the eighth straight quarter. Also, combined order flows from North America and Europe grew 26% YoY. The 12-month executable order book at US\$ 395mn (+13.8% YoY) improved for the seventh quarter in a row.

### STOCK PERFORMANCE



Source: NSE

**Not immune to BFS challenges:** As with industry peers, NITEC reported pockets of weakness in the BFS segment, which constrained revenue growth from the top 5 clients (-6.5% QoQ in dollar terms). Management stated that these challenges were specific to one account with no loss of wallet share.

**Retain BUY:** We trim FY20 EPS estimate by 4.5% on exceptional charges reported in Q1FY20 but largely keep FY21 forecasts unchanged. Retain BUY with a revised Jun'20 TP of Rs 1,550, based on an unchanged target P/E of 17x.

### KEY FINANCIALS

Y/E 31 Mar	FY18A	FY19A	FY20E	FY21E	FY22E
Adj. net profit (Rs mn)	2,802	4,089	4,472	5,462	6,369
Adj. EPS (Rs)	45.4	66.2	72.4	88.4	103.1
Adj. EPS growth (%)	3.5	45.9	9.4	22.1	16.6
Adj. ROAE (%)	15.3	21.2	20.2	21.5	21.7
Adj. P/E (x)	29.8	20.4	18.7	15.3	13.1
EV/EBITDA (x)	16.0	12.4	10.5	8.5	7.1

Source: Company, BOBCAPS Research

**BOB Capital Markets Ltd is a wholly owned subsidiary of Bank of Baroda**

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### Earnings call highlights

- **FY20 outlook:** Management intends to drive robust and predictable growth while maintaining EBITDA margins around 18%. The company does not foresee any risks in Europe from Brexit uncertainty given its concentrated exposure in the travel and specialty insurance segments in the region.
- **Operating margins:** NITEC’s Q1FY20 reported EBITDA margins of 14.4% were adversely impacted by (1) compensation revision (-240bps QoQ), (2) annual visa costs (-90bps QoQ), and (3) one-time costs such as ex-gratia rewards, divestment and M&A costs (-250bps QoQ). Operating margin tailwinds of ~100bps from Ind-AS 116 adoption helped partially negate the headwinds.

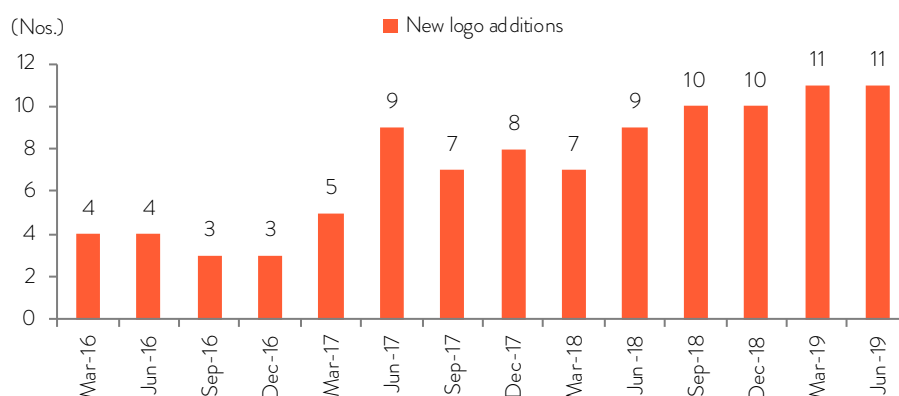
**FIG 1 – NITEC WON 3 DEALS WITH TCV OF US\$ 10MN+ IN JUN'19 QUARTER**

Date of deal win	No. of large deals	Remarks
Jun'19	3 (US\$ 10mn+ TCV)	▪ 2 in insurance vertical and 1 in Travel
Mar'19	2 (US\$ 20mn+ TCV)	▪ 1 each in travel & transportation and insurance verticals
Dec'18	2 (US\$ 20mn+ TCV)	▪ 1 each in BFS and insurance verticals
Sep'18	2 (US\$ 20mn+ TCV) + 3 (US\$ 10mn+ TCV)	<ul style="list-style-type: none"> <li>▪ US\$ 23mn deal with an existing BFS customer in the US</li> <li>▪ US\$ 24mn deal with an existing insurance customer in the US</li> <li>▪ 2 US\$ 10mn+ deals in the travel vertical</li> <li>▪ US\$ 10mn+ deal from a commercial leasing and lending client</li> </ul>
Jun'18	3 (US\$ 10mn+ TCV)	<ul style="list-style-type: none"> <li>▪ Onboarding and wealth management support expansion for a BFS client</li> <li>▪ Driving data and digital transformation initiatives for one of the largest European airlines</li> <li>▪ Product development support mandate from a key travel major</li> </ul>
Mar'18	2 (US\$ 20mn+ TCV)	<ul style="list-style-type: none"> <li>▪ US\$ 35mn managed services contract from a new London-based client</li> <li>▪ Deal win from an existing BFSI client</li> </ul>
Dec'17	3 (US\$ 20mn+ TCV)	▪ 3 large deals in the US against tier-I competition, including 2 from the insurance vertical
Sep'17	1 (US\$ 20mn+ TCV)	▪ Deal win from an existing US travel client
Jun'17	1 (US\$ 20mn+ TCV)	▪ Large multi-year engagement with an existing US travel client

Source: Company, BOBCAPS Research

**NITEC focuses on targeted client adds and accelerated growth from existing clients**

**FIG 2 – STEADY NEW LOGO ADDITION**



Source: Company, BOBCAPS Research

**FIG 3 – JUN'19 QUARTER PERFORMANCE**

(Rs mn)	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20	YoY (%)	QoQ (%)
<b>Revenue (US\$ mn)</b>	<b>124.3</b>	<b>130.9</b>	<b>134.8</b>	<b>138.0</b>	<b>138.5</b>	<b>11.4</b>	<b>0.4</b>
<b>Revenue (Rs mn)</b>	<b>8,249</b>	<b>9,074</b>	<b>9,717</b>	<b>9,722</b>	<b>9,627</b>	<b>16.7</b>	<b>(1.0)</b>
<b>Operating expenditure</b>	<b>6,942</b>	<b>7,440</b>	<b>7,912</b>	<b>8,015</b>	<b>8,238</b>	<b>18.7</b>	<b>2.8</b>
Cost of revenues	5,437	5,897	6,280	6,293	6,374	17.2	1.3
as % of sales	65.9	65.0	64.6	64.7	66.2	-	-
SG&A expenses	1,505	1,543	1,632	1,722	1,864	23.9	8.2
as % of sales	18.2	17.0	16.8	17.7	19.4	-	-
<b>EBITDA</b>	<b>1,307</b>	<b>1,634</b>	<b>1,805</b>	<b>1,707</b>	<b>1,389</b>	<b>6.3</b>	<b>(18.6)</b>
Depreciation	312	319	314	303	401	28.5	32.3
<b>EBIT</b>	<b>995</b>	<b>1,315</b>	<b>1,491</b>	<b>1,404</b>	<b>988</b>	<b>(0.7)</b>	<b>(29.6)</b>
Other Income	210	215	4	47	172	-	-
<b>PBT</b>	<b>1,205</b>	<b>1,530</b>	<b>1,495</b>	<b>1,451</b>	<b>1,160</b>	<b>(3.7)</b>	<b>(20.1)</b>
Total Tax	300	363	445	296	318	6.0	7.4
<b>Adjusted PAT</b>	<b>905</b>	<b>1,167</b>	<b>1,050</b>	<b>1,155</b>	<b>842</b>	<b>(7.0)</b>	<b>(27.1)</b>
(Profit)/loss from JVs/Assoc/MI	46.0	49.0	49.0	44.0	22.0	-	-
<b>APAT after MI</b>	<b>859</b>	<b>1,118</b>	<b>1,001</b>	<b>1,111</b>	<b>820</b>	<b>(4.5)</b>	<b>(26.2)</b>
<b>Extraordinary items</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>57</b>	<b>-</b>	<b>-</b>
<b>Reported PAT</b>	<b>859</b>	<b>1,118</b>	<b>1,001</b>	<b>1,111</b>	<b>877</b>	<b>2.1</b>	<b>(21.1)</b>
<b>Reported EPS</b>	<b>13.9</b>	<b>18.1</b>	<b>16.2</b>	<b>18.0</b>	<b>13.3</b>	<b>(4.5)</b>	<b>(26.2)</b>
<b>Margins (%)</b>						<b>(bps)</b>	<b>(bps)</b>
EBITDA	15.8	18.0	18.6	17.6	14.4	(142)	(313)
EBIT	12.1	14.5	15.3	14.4	10.3	(180)	(418)
EBT	14.6	16.9	15.4	14.9	12.0	(256)	(288)
PAT	10.4	12.3	10.3	11.4	9.1	(130)	(232)
Effective Tax rate	24.9	23.7	29.8	20.4	27.4	252	701

Source: Company, BOBCAPS Research

**FIG 4 – JUN'19 QUARTER OPERATING METRICS**

Particulars	Q1FY20 (% Contr. to Revenue)	QoQ (%)	YoY (%)
<b>Revenue by geography</b>			
North America	49	(1.0)	14.4
Europe	35	5.0	27.6
RoW	35	(12.0)	3.7
<b>Revenue by vertical</b>			
Banking and Financial Services	16	(1.0)	9.8
Insurance	29	2.6	16.7
Transportation	28	2.7	21.0
Manufacturing & Retail	27	(7.8)	12.5
<b>Revenue mix onsite/offshore</b>			
Offshore	34	(1.0)	10.2
Onsite	66	(1.0)	20.4
<b>Client concentration</b>			
Top 5	27	(7.8)	16.7
Non-Top 5 client	73	1.8	16.7

Particulars	Q1FY20 (% Contr. to Revenue)	QoQ (%)	YoY (%)
Top 10	39	(5.8)	26.4
Top 20	53	(2.8)	26.2
Non-Top 20 client	47	1.2	7.6
Digital revenues (% of revenues)	34	13.8	40.3
Number of employees	10,297	34	533
Attrition (%)	12.9	70bps	280bps
DSO	67	5days	(8days)

Particulars	Q4FY19	Q3FY19	Q1FY19
<b>Significant new customer additions</b>			
USA	5	6	5
Europe	3	0	3
ROW	3	5	1
Total	11	11	9
<b>Fresh order intake (US\$ mn)</b>			
USA	100	94	69
Europe	58	45	56
ROW	17	31	26
<b>Total</b>	<b>175</b>	<b>170</b>	<b>151</b>
Executable orders over next 12 months (US\$ mn)	395	390	347

Source: Company, BOBCAPS Research

## Valuation methodology

Revamped leadership, a deeper domain focus and sharpened sales & delivery are reshaping NITEC’s growth prospects. We stay positive as we believe the company is on course for predictable and profitable growth.

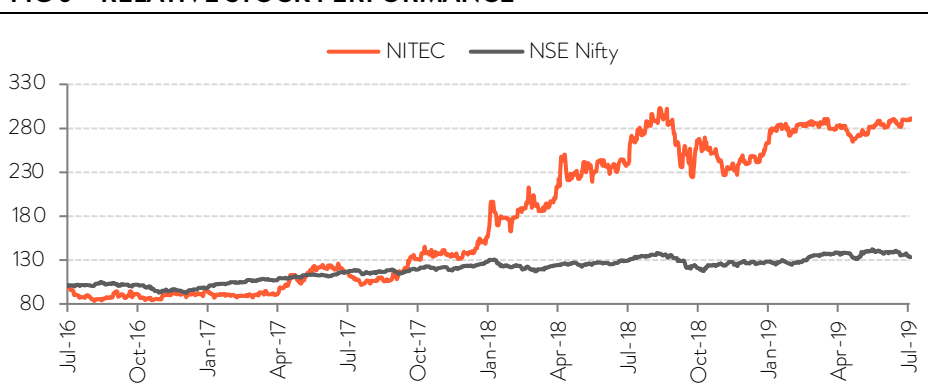
Post the Jun’19 quarter results, we trim FY20 EPS estimates by 4.5% and largely retain FY21 estimates. We introduce FY22 EPS of Rs 103, baking in 12.4% dollar revenue growth and 18.3% EBITDA margins. Rolling valuations forward, we have a revised Jun’20 target price of Rs 1,550 (vs. Rs 1,500 earlier), based on an unchanged one-year forward P/E multiple of 17x. Retain BUY.

**FIG 5 – REVISED ESTIMATES**

(Rs mn)	FY20E			FY21E			FY22E
	Old	New	Change (%)	Old	New	Change (%)	New
Revenues (US\$ mn)	595	597	0.4	666	669	0.5	753
YoY growth (%)	12.7	13.1	-	12.0	12.1	-	12.4
Revenues	41,640	41,275	(0.9)	46,649	46,864	0.5	52,679
EBITDA	7,492	7,311	(2.4)	8,394	8,574	2.1	9,639
EBITDA margins (%)	18.0	17.7	-	18.0	18.3	-	18.3
Net Profits	4,684	4,472	(4.5)	5,440	5,462	0.4	6,369
EPS (Rs)	75.8	72.4	(4.5)	88.1	88.4	0.4	103.1

Source: BOBCAPS Research

**FIG 6 – RELATIVE STOCK PERFORMANCE**



Source: NSE

## Key risks

Downside risks to our earnings estimates include:

- challenges at the company’s top clients,
- unfavourable US visa and immigration regulation changes,
- a sharp decline in demand, and
- adverse currency movement.

## FINANCIALS

### Income Statement

Y/E 31 Mar (Rs mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Total revenue</b>	<b>29,914</b>	<b>36,762</b>	<b>41,275</b>	<b>46,864</b>	<b>52,679</b>
EBITDA	5,012	6,453	7,311	8,574	9,639
EBIT	3,739	5,205	5,654	6,776	7,695
Net interest income/(expenses)	0	0	0	0	0
Other income/(expenses)	298	476	700	935	1,218
Exceptional items	0	0	0	0	0
EBT	4,037	5,681	6,354	7,711	8,913
Income taxes	950	1,404	1,591	1,889	2,184
Extraordinary items	0	0	0	0	0
Min. int./Inc. from associates	285	188	292	360	360
<b>Reported net profit</b>	<b>2,802</b>	<b>4,089</b>	<b>4,472</b>	<b>5,462</b>	<b>6,369</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>2,802</b>	<b>4,089</b>	<b>4,472</b>	<b>5,462</b>	<b>6,369</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY18A	FY19P	FY20E	FY21E	FY22E
Accounts payables	0	0	0	0	0
Other current liabilities	5,115	6,345	7,124	8,089	9,093
Provisions	2,943	3,626	4,071	4,622	5,196
Debt funds	224	224	224	224	224
Other liabilities	455	455	455	455	455
Equity capital	615	615	615	615	615
Reserves & surplus	17,348	20,001	22,989	26,642	30,841
Shareholders' fund	17,963	20,616	23,604	27,257	31,456
<b>Total liabilities and equities</b>	<b>26,700</b>	<b>31,266</b>	<b>35,478</b>	<b>40,647</b>	<b>46,424</b>
Cash and cash eq.	4,102	7,102	10,660	15,004	20,036
Accounts receivables	5,911	7,352	8,255	9,373	10,536
Inventories	0	0	0	0	0
Other current assets	2,701	3,324	3,732	4,237	4,763
Investments	3,955	3,955	3,955	3,955	3,955
Net fixed assets	8,800	8,302	7,645	6,847	5,903
CWIP	7	7	7	7	7
Intangible assets	0	0	0	0	0
Deferred tax assets, net	1,231	1,231	1,231	1,231	1,231
Other assets	0	0	0	0	0
<b>Total assets</b>	<b>26,700</b>	<b>31,266</b>	<b>35,478</b>	<b>40,646</b>	<b>46,423</b>

Source: Company, BOBCAPS Research

**Cash Flows**

Y/E 31 Mar (Rs mn)	FY18A	FY19P	FY20E	FY21E	FY22E
Net income + Depreciation	4,199	5,525	6,421	7,620	8,673
Interest expenses	(34)	(476)	(700)	(935)	(1,218)
Non-cash adjustments	0	0	0	0	0
Changes in working capital	(128)	(151)	(87)	(107)	(112)
Other operating cash flows	(213)	0	0	0	0
<b>Cash flow from operations</b>	<b>3,824</b>	<b>4,898</b>	<b>5,634</b>	<b>6,577</b>	<b>7,344</b>
Capital expenditures	(879)	(750)	(1,000)	(1,000)	(1,000)
Change in investments	(290)	0	0	0	0
Other investing cash flows	(1,311)	476	700	935	1,218
<b>Cash flow from investing</b>	<b>(2,480)</b>	<b>(274)</b>	<b>(300)</b>	<b>(65)</b>	<b>218</b>
Equities issued/Others	66	0	0	0	0
Debt raised/repaid	0	0	0	0	0
Interest expenses	0	0	0	0	0
Dividends paid	(810)	(1,624)	(1,776)	(2,169)	(2,530)
Other financing cash flows	0	0	0	0	0
<b>Cash flow from financing</b>	<b>(744)</b>	<b>(1,624)</b>	<b>(1,776)</b>	<b>(2,169)</b>	<b>(2,530)</b>
<b>Changes in cash and cash eq.</b>	<b>600</b>	<b>3,000</b>	<b>3,558</b>	<b>4,344</b>	<b>5,032</b>
<b>Closing cash and cash eq.</b>	<b>4,102</b>	<b>7,102</b>	<b>10,660</b>	<b>15,004</b>	<b>20,036</b>

**Per Share**

Y/E 31 Mar (Rs)	FY18A	FY19P	FY20E	FY21E	FY22E
Reported EPS	45.4	66.2	72.4	88.4	103.1
Adjusted EPS	45.4	66.2	72.4	88.4	103.1
Dividend per share	15.0	21.8	23.9	29.2	34.0
Book value per share	290.8	333.7	382.1	441.2	509.1

**Valuations Ratios**

Y/E 31 Mar (x)	FY18A	FY19P	FY20E	FY21E	FY22E
EV/Sales	2.7	2.2	1.9	1.6	1.3
EV/EBITDA	16.0	12.4	10.5	8.5	7.1
Adjusted P/E	29.8	20.4	18.7	15.3	13.1
P/BV	4.7	4.1	3.5	3.1	2.7

**DuPont Analysis**

Y/E 31 Mar (%)	FY18A	FY19P	FY20E	FY21E	FY22E
Tax burden (Net profit/PBT)	69.4	72.0	70.4	70.8	71.5
Interest burden (PBT/EBIT)	108.0	109.1	112.4	113.8	115.8
EBIT margin (EBIT/Revenue)	12.5	14.2	13.7	14.5	14.6
Asset turnover (Revenue/Avg TA)	116.5	126.8	123.7	123.1	121.0
Leverage (Avg TA/Avg Equity)	1.4	1.5	1.5	1.5	1.5
Adjusted ROAE	15.3	21.2	20.2	21.5	21.7

Source: Company, BOBCAPS Research | Note: TA = Total Assets

**Ratio Analysis**

Y/E 31 Mar	FY18A	FY19P	FY20E	FY21E	FY22E
<b>YoY growth (%)</b>					
Revenue	7.4	22.9	12.3	13.5	12.4
EBITDA	6.9	28.8	13.3	17.3	12.4
Adjusted EPS	3.5	45.9	9.4	22.1	16.6
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	16.8	17.6	17.7	18.3	18.3
EBIT margin	12.5	14.2	13.7	14.5	14.6
Adjusted profit margin	9.4	11.1	10.8	11.7	12.1
Adjusted ROAE	15.3	21.2	20.2	21.5	21.7
ROCE	12.6	18.1	20.3	25.5	30.7
<b>Working capital days (days)</b>					
Receivables	66	66	69	69	69
Inventory	0	0	0	0	0
Payables	107	132	127	128	129
<b>Ratios (x)</b>					
Gross asset turnover	3.5	4.3	5.2	6.5	8.3
Current ratio	1.6	1.8	2.0	2.3	2.5
Net interest coverage ratio	NA	NA	NA	NA	NA
Adjusted debt/equity	(0.2)	(0.3)	(0.4)	(0.5)	(0.6)

Source: Company, BOBCAPS Research



## Disclaimer

### Recommendations and Absolute returns (%) over 12 months

**BUY** – Expected return >+15%

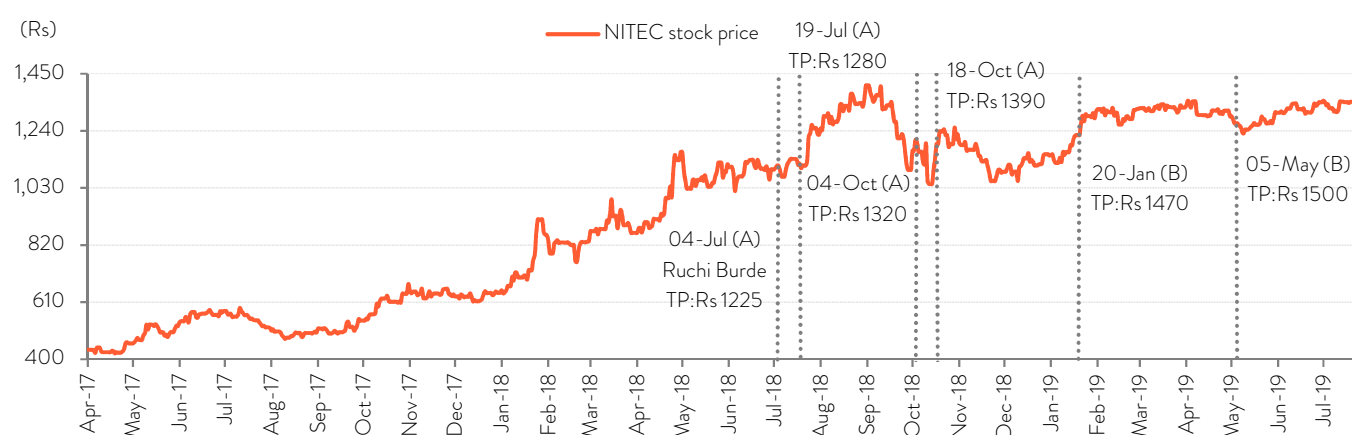
**ADD** – Expected return from >+5% to +15%

**REDUCE** – Expected return from -5% to +5%

**SELL** – Expected return <-5%

**Note:** Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

### HISTORICAL RATINGS AND TARGET PRICE: NIIT TECHNOLOGIES (NITEC IN)



B – Buy, A – Add, R – Reduce, S – Sell

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