

NIIT

Transcript of the Earnings Call for the Second Quarter results Jul - Sep 2004 27 October 2004

Operator: Good evening ladies and gentlemen. I am Swati the moderator for this conference. Welcome to the NIIT Ltd Earnings Call. Mr. Vijay Thadani NIIT Ltd Chief Executive Officer is your call leader today. For the duration of the presentation all participant lines will be in the listen-only-mode. After the presentation the question and answer session will be conducted for the international participants connected to Airtel International Center. After that a similar question and answer session will be conducted for the participants in India. Now I hand over to Mr. Vijay Thadani of NIIT Ltd. Thank you and over to you sir.

Vijay Thadani: Good evening, this is Vijay Thadani and the NIIT Technologies Ltd call just got over and we are just using the same telephone line to make the second call, which is NIIT Ltd. I would like to give you a quick overview of the activities in the last quarter. I think the first from housekeeping corporate governance issues relating to re-listing of NIIT, as well as listing of NIIT Technologies. In our last discussion they were at that point of time on record dates and since then on 16th August NIIT Ltd got re-listed and NIIT Technologies got listed, which is not news to you, on August 30th, but I just thought to mention that because that completes the de-merger process, which took, if all this period was to be added, a good 10 month period, but that is an exercise which is completed, so just to put a completion to it.

Now let's talk about NIIT Ltd result for the second quarter. As usual, I will first talk a little bit about the industry environment that we experienced, from then get on to some numbers and going to some operating metrics and then we can have a question answer session. So first the industry environment, I think the last quarter, which we had, which is traditionally a good quarter for the Learning Business was inline with our thinking and inline with what we had anticipated in terms the sentiment in the market and what was happening. I will first talk about India, where I think the predominant business that we were engaged in is the India individual business on one side and India Institutional on the other. So we noticed that the sentiment for IT career is making a cautious return. There has been a much better acceptance of IT careers and anticipation for IT career in the metros, which is obviously led by the increased job requirements and recruitment which the IT outsourcing firms, software outsourcing firms and BPO firms are doing and the second, the fact that in remote centers, which are far from metros, that effect is at a lag which is what we have experienced in the past as well.

I think one of the most interesting indicators of this additional interest was the fact that NIIT conducted an IT Aptitude Test, a national IT aptitude test, which is a test conducted for the first time in the country. There is an aptitude test for nearly every discipline, medicine, engineering, management, but there was none for IT and I think naturally NIIT had the responsibility to do that and NIIT did that. The response to that was extremely encouraging. We had 65,746 people appear for this exam, which was conducted at a very short notice about three week's notice in the month of September and this is also the time

when people have already taken their admissions in colleges and stuff like that, but 65,746 is nearly half of the number of people who take the IIT exam every year, so that tells you the interest, which is building up in IT career, but that interest to get converted into registration and the quality of registration that we are looking for is what I will talk about when we talk about the results.

The second thing was, there was a definitive pull from employers for quality people and the word quality people is underlined, because employers are looking for people whom they can get functionally operating very, very quickly and that was one of the definitive pull we saw from employers, 35% increase in hirings in the last 12 months is one of the statistics Dataquest came up with and primarily the increased hirings are at entry level, which is basically the kind of crowd that NIIT and other entry level institutions come up with.

Adding to that the rising salary levels and attrition rate talk about the impending demand, but I must say there is a stronger pull from the employer side than there is an acceptance of the same from the student side, but I think that always takes a while to build momentum and we saw the building of that momentum in the last quarter.

In China, the second geography that I would like to talk about, the interesting development is that IT education is becoming a part of the mainline university education and NIIT is playing a role in that and I will talk about that, so that was an important thing. IDC has also predicted a very healthy growth for China in years to come, which I will talk about when I talk about the future and the fact that China is very actively looking at higher end skills in software project management and software engineering, software architecture and that was another thing which we noticed.

On the global scale mostly in the developed world which is US and Europe, there was a slower growth in IT training, though slightly better than what it was last year, and IDC has predicted a slow growth now, but it will pickup momentum in 2-3 years time. There is a definite potential for outsourcing of learning and training. That is driven by two drivers - cost reduction and global rollouts, as organization spread their wings across the world. And the last thing was that the Corporate Spending on E-learning was increasing and technology base learning was on an increase and we saw the benefit of that in our international business.

In India very specifically there are two important statistics, which I would like to talk about. First as far as the IT training market is concerned, Dataquest in July end issue came up with the numbers for IT industry and in fact there has been a small de-growth in IT training, but I think it is more coming out of the restructuring of the industry and in terms of formal and non-formal getting mixed up and Dataquest only taking non-formal as the only number, but it has de-grown the private IT training industry.

The other interesting statistic in the same issue was the improvement in the market share of NIIT. NIIT in that issue is now stated as 2.2 times its nearest competitor and we must realize that our nearest competitor were number two and number three of couple of years earlier and all together much larger than NIIT, but in this particular April 2003 to March 2004, NIIT has indeed stolen a lead in terms of market share and fairly strong lead. So

those were some things, which we noticed in the industry environment, I will get down to the highlights of the results. The details have been available on the website, as well as press release so that we will handle in the questions.

The most important thing is the 6 month Net Profit of the Rs 227 million is surpasses last 12 months fiscal profit of Rs189 million, so in 6 month we had nearly 30% more than what we were in the full 12months. The quarterly net profit is at Rs 118 million, which is versus a Rs 67 million loss in the same period last year and it is also increased beyond Rs 109 million, which we experienced last quarter. This resulted in higher earning per share at 6.11 rupees this quarter. This is backed by System wide Revenue increase of the 10% year on year and 22% quarter on quarter.

This was to be expected as July, August, September is typically our peak period and I think 10% year on year basically talks about the strength of the IT training market, as it is coming back and NIITs strong position which is emerging day by day. The operating efficiencies were visible in the operating margin and operating profit. Operating profit has grown 233% year on year at Rs140 million with Operating Margin at about 13%, which is an improvement of more than 800 basis points over the same period last year. In terms of Earning Per Share I already mentioned it is at 6.1 rupees per share this quarter compared to 5.6 rupee and cumulatively therefore in the six months, we have had an earning per share of Rs 11.7.

Talking a little bit about Balance Sheet, we have had significant improvement in the debtors position. It has reduced from 122 days of sales to, at a highest sales value at 97 days of sales. We had an asset addition of just 28 million this quarter and a return on average capital employed has improved to 17.8% annualized compared to 17.4% that we had last quarter. Getting to some operational metrics, geography wise revenue mix was nearly 51% actually towards international and 49%, which is a small improvement over last quarter, last quarter it was 53%-47%. This was to be expected because this is normally the best quarter for the Indian business and we had 23% year on year revenue growth as far as India is concerned. In China, in International, I think China was the major growth area this quarter and the reason was a very important exercise which we commenced about 6 months ago a business model, which we called the NIIT Inside where NIIT becomes embedded inside the university curriculum and we launched this very aggressively in one of the provinces in China which resulted in fairly large size revenue in this quarter given China's size of revenue, so that contributed to a kicker as far as the China revenues were concerned. The overall segmental analysis, International revenues were 51% and I think they showed 18% growth quarter on quarter, Addition of 4 new clients, including one from higher education segment and in end of quarter Order Book of nearly 19 million, \$18.96 million to be precise. In India Individual the second largest, it posted 31% quarter on quarter and 14% year on year growth and I will go into a little bit more detail about that.

India Institutional had a 24% quarter on quarter and 30% year on year growth with a fresh order intake, which was also very healthy of about 428 million rupees. In other schools order from another state, which contributed to a very healthy order book as we go forward. In terms of segmental profitability, as you can see India individual is coming back, but it is not yet profitable in this quarter. India institutional and International have

been contributing to most of the operating profits, but the situation is improving in each one of the areas. I had mentioned in the last call that India Institutional operating profit in the last quarter was high because of a bullet revenue recording and it would stabilize at a lower level, which it is in the current quarter.

In terms of our reach, the numbers of centers are at 3783, we added 35 net centers in the Institutional area and in the Individual area, in fact we did some consolidation. We combined some centers and we have increased the size of some other centers. So in terms of number of centers is 773, International centers remain at the same in China the push in on NIIT Inside model, which is inside the university campuses and therefore that would not be visible in the number of center. In India Individual FUTURZ, our flagship product grew 44% quarter on quarter in revenue terms and registrations improved 24% quarter on quarter. In CATS as well, we had an 8% improvement sequentially in registrations and 26% in revenues, which also talks about the fact that we got a better realization than we used to get in the past and better realization is a multiple of the fee per hour of instruction multiplied by the duration for which the student attends the course, so that average realization improved very significantly, both quarter on quarter, as well as year on year.

SWIFT the portal, that portal is becoming less and less relevant in the overall scheme of things because of the fact that much of that is now being done within a school and college as part of normal curriculum. Well at the same time there is an overall literacy segment, which is a big net, which we spread to increase the size of market that we can address going forward. In terms of Order Book, we have an order book of Rs 218.6 crores in the India Institutional and in International, we have a closing order book of \$18.96 million as I mentioned. In terms of over all head count, we added 66 people net during the quarter, most of them in the India Individual segment, given the fact that we launched some new education centers, which are company owned. The total strength at quarter end was 1729. That would complete the coverage. The shareholding pattern, there has been a small change. The FIIs and promoter holdings have increased a little bit during the quarter.

Talking about Future outlook, we see that the increase hiring, which I think in every single result of IT services industry has talked about an increased hiring in the times to come and the quality of that hiring also points to one more aspect, which is for more and more focused skilled man power with focus skills so that people can use them on projects straight away. In fact in the last quarter, in the last six months, we have added nearly double the number of engineers that we have trained in our GNIIT curriculum, which is an indicator of the fact as to the need for finishing schools skills even after engineering and we see that as a big market going forward, which we are focusing on.

The second thing which we are focusing on is very specific skills that, which we would train our people for in the final semester based on the large requirements of the large IT majors and we finished three such assignments in last quarter and the employers are very happy with the end results, so we see that as a very interesting opportunity going forward. In the International area, I think E-learning in the corporate space in US, the growth of IT manpower in China and development of IT manpower in China and the embedding of IT education in university education are opportunities that we see forward. Next quarter is low in terms of seasonality traditionally, a quarter, which is lowest in the 12 month period and therefore our revenues will go down in comparison to this quarter. However,

maintaining the growth rate on an year on year basis at the current levels of the 10% and which is inline with our projections is what we intend to do and therefore over the 12 month period, we also see that the operating margin will be at 10% as we had talked about in the last call as well after the correction that we made, so 10% overall revenue growth and 10% operating margin for the 12 month period is what we had projected for this fiscal which is what we will be on track for.

Currently our operating margin is better than 10%, but we must remember that the next two quarters are typically lower in revenue size and therefore, to that extent there will be an impact on the operating margin. With that I would like to open this for question and answers and joining me for the Q&A is P. Rajendran the Chief Operating Officer, as well as R.S. Pawar the Chairman.

Operator: Thank you very much sir. I now handover the proceedings to Fareeda, at Airtel International Center, to conduct the question and answer session for the international participants. After this we will have a question and answer session for the participants in India. Over to you Fareeda.

Operator: Thank you Swati. At this time international participant may press 01, if they would like to ask a question on pressing 01, participant will get a chance to present their question on a first inline basis. International participant who wish to ask a question may please press 01. Please press 01 now. At this moment there are no further question from participant outside India. I would like to handover the proceeding back to Swati.

Thank you very much Fareeda. We will now begin the question and answer interactive session for the Indian participants connected to audio conference service from Airtel. Participants who wish to ask questions may please press *1 on their touchtone enabled telephone keypad. On pressing *1, participants will get a chance to present their questions on a first inline basis to ask a question please press *1 now. The first question comes from Mr. Bhattacharya from UBS Mumbai. Mr. Bhattacharya you may ask your question now.

Bhattacharya: Thanks. Good evening. The first question is, if you look at from the training side of the business, if you look at the output where it is headed in terms of the bias of or rather people where they joined post NIIT training, how would you put the percentage mix as how much of this goes now to the software companies and between end user corporate etc, could you give us a split?

Vijay : Yes, I would not have the exact split, but I can give you qualitatively.

Bhattacharya: Sure.

Vijay: Nearly two-third of the end output of NIIT goes to the IT services industry, IT and BPO services industry and about one third goes to user organizations. IT services, I would include captives as well as those who are doing outsourcing.

Bhattacharya: Sure, and it is possible to say how much of it goes to IT services companies, everything including captive etc excluding the BPO that is?

Vijay: Well, a large percentage would be to IT.

Bhattacharya: I see, the second question is, I mean as you rightly point out...

Vijay: BPO has their own and they do a lot of corporate training as well.

Bhattacharya: Right, as you have rightly pointed out the volume growth for the industry seems to be pretty high, how do you see the supply demand scenario or what kind of salaries are at the output which goes into the IT services companies getting right now as opposed to let's say a year back?

Vijay: Okay, I would say that about on an average there is a 15% to 20% increase in salary level, more like 20% and less like 15% but it varies because averaging can give you any number depending on what number you average, but we are seeing an average increase, I think what these organizations are willing to pay a premium for, is specific skills that they want. I had mentioned this last quarter also, one of the exercises which we did in the previous six months was a survey with the industry of what specific skills that they require and what kind of people would they like to employ and the feedback we got was, it is not a particular skill set, but in a particular quarter based on a particular project that they have or what they are gearing up for.

There are very clear requirements of the skill mix which is required. Now the formal sector cannot adapt to that requirement, I mean if they say I want this guy to have so much depth in SQL Server, but so much more in DB2 then you may either DB2 or you may have SQL Server, you may not have both in any course, so what they want is the specific skill set, what we call, people like to choose their own topping of the pizza. So what we do is make sure that in the fourth semester we customized the fourth semester to meet that particular employer's need and we did three pilots, we designed our whole curriculum around that and the first output of that, which was their people who were doing the earlier curriculum we customized their last semester and fulfilled the requirements of one of the largest IT services companies amongst the, you know, the tier one companies and we met that requirement in 30 days time and it is a number which they were not expecting to be fulfilled in that time in by their own recruitment mechanisms, that is getting specific skills, and once they get specific skills they are willing to pay a premium in salaries for that.

Bhattacharya: Sure, but looking at the volume growth approximately about 50% per annum and I am sure they will need people at the entry level, why should not the growth rate for the full year be higher, closure to about 20% at least for the training side of the business rather than being 10%?

Vijay: Yes, I think there are three components to that. There is an Institutional component, there is an International component and there is the Individual component. If you notice this year in the Individual component, our growth has been higher. The second thing I must tell you is that the market does not, market in this case the customer is not so well connected to the organizations requirement and therefore it takes a while for us to move the consumer momentum, to get the momentum of the consumer going and that is

the reason for activity like the National IT Aptitude Test, which rekindles the people's interest in IT career. The problem is not to get volumes, the problem is to get the right quality volume and I think that is the focus we have had in our last two quarter enrolments, we do see that there is an acceleration and we feel that momentum will improve.

Bhattacharya: Thank you, best of luck.

Vijay: Thank you.

Operator: Thank you very much sir. The next question comes from Mr. Dipen from Kotak, Mumbai. Mr. Dipen you may ask your question now.

Dipen: Okay, as you have well explained the revenue side obviously just wanted to get some feel on the margin side. You said the margin for the full year could stabilize at around 10% level obviously that is mainly because that revenues will go down over the next couple of quarters, but just wanted to know on a most strategic basis like, are there anymore avenues left for the company to cut down on the fixed cost or are there any other avenues to cut down more cost or will the margins move inline with the revenue growth and whenever the revenue growth dips we can see further dips in margins?

Vijay: Okay, there is an operating leverage available, as you know we have a fixed cost structure and variable cost structure

Dipen: Correct.

Vijay: So therefore margins will typically be out of line with the revenue growth, which means if the revenues slows down, the impact on margin will be higher, if the revenues picks up the benefit to the margin will also be higher. We do see there are areas in which our fixed cost structure can be further reduced, but I think there are the numbers of basic customer, consumer education and marketing activities, which need to be undertaken to increase the interest. Actually the industry is clamoring right now to get more 70% - 90% to apply for IT career for places other than those who got through the star engineering colleges. See the interesting thing which is happening is people who get 85% and above, who get admissions in let's say in tier one engineering colleges, those people anyway get lapped up by the industry and we do finishing school for them. Then there is the in between crowd, which would like to take other career opportunities, which are, now many more career opportunities are available whether banking, insurance and so many others right. And therefore they do not take up IT career and then the next slot which takes up IT career is people who did not make it to those engineering colleges, tier one, and two, they go to the tier three and four where a large number of people are taking on engineering education, but are not coming out with skills, which the industry requires. That is where we see our major role right now, because people also want engineering degrees, but they also want the right skills and I think one of the successes we have had this quarter, last two quarters, is offering that GNIIT to an engineer and creating a combination which is truly a same or better combination as computer science guy who had done B-tech computer science, so those are indicators of the future.

Dipen: Okay, the other housekeeping question like that tax rate for this year has been about, this quarter has been about 4% or 5% for the first half, I believe that this tax rate should remain at around these levels because of the accumulated losses?

Vijay: Yes, tax, yeah, we have tax assets available, but as a rule we do not take the benefit of that as we mentioned about two to three quarters ago. Since last October, we have not been taking the benefit of deferred tax asset, so we do have tax losses available in the balance sheet.

Dipen: Okay, and the other income component, do you expect any significant variation in that or it should remain at around this particular levels of Rs 2.8 or 3 crores?

Vijay: It will reduce going forward.

Dipen: What could be the reason for that?

Vijay: Well exchange rate is one issue, which contributes to other income. The second thing is interest on deposits and mutual funds and you know what we do with the spare cash. So, as we go forward, as our investment increases, we do see that the other income component will come down.

Dipen Okay. Thanks very much.

Operator: Thank you very much sir. Participants who wish to ask questions may please press *1. I repeat participants who wish to ask questions may please press *1. At this moment there are no further questions from participants. I would now handover the floor back to Mr. Vijay Thadani for the final remarks.

Vijay Thadani: Well thank you very much all of you, I know it has been a long call given you have to attend two companies calls, so thank you very much for being here with us and as usual we always get lot of insights from the questions you asked. I am sure there will be more questions you will have, but please do not hesitate to address them to Nidhi Aggarwal, Sanjay Mal or myself and we will be very happy to answer them for you. Thanks once again for your cooperation, as well as your patience in being on this call. Good night.

Operator : Ladies and Gentlemen this concludes the earnings call, you may now disconnect your lines. Thank you for connecting to Audio Conference Services from Airtel, and have a nice evening.