



June 11, 2012

Dear clients and colleagues,

We spent the last two weeks attending various growth conferences in the US. We had the opportunity to meet over 50 different companies including a dozen existing holdings in the Global Small Cap Portfolio. All companies expressed confidence in the accelerating economic recovery and are back in growth mode. Many companies currently see their margins at peak levels, making further margin expansion unlikely in the near term. On the other hand, rising raw material prices add more pressure resulting in margin compression. In term of growth strategy, expansion to fast-growing regions was mentioned in almost every presentation. Commonly cited regions are China, India, Brazil, and Middle East.

One of the holdings we met at the conference is NIC Inc., which we have owned since 2009 (last reviewed in our comment of June 19, 2009). NIC is a well-managed company offering great growth opportunity in the years ahead.

NIC Inc. (EGOV US - U\$11.52)

www.egov.com

Founded in 1991, it is the premier provider of official government websites, online services, and secure payment processing solutions for more that 3,000 federal, state and local agencies across the United States. The customized online government solutions simplify complex processes allowing the private sector to interact quickly and easy with federal, state, and local governments. The company builds and manages official government websites and e-Government services for 27 states and 2 federal partners.

NIC operates a unique self funded business model, allowing governments to build eGovernment services without using taxpayer funds. NIC absorbs the costs to build the portal's technical infrastructure and develop the eGovernment services. The revenue stream comes from fees generated from the online transactions and subscriptions. To put that in perspective, more than \$18B in secure payments were processed in 2011. NIC's revenue can be described as annuity-like, as they do not have to win back customers year after year.

Market Data

Market cap \$741M, p/e (12/2013) 24.6x, ev/sales (12/2013) 2.9x, ev/ebitda (12/2013) 11.3x, gross margin 40%, profit margin 12.6%.

Target Market Size

Research firm Input's "State and Local IT Market Forecast 2011-2016" study predicts the demand for vendor-furnished information systems and services by U.S. state and local governments will increase from \$54.8B in 2011 to \$63.1B in 2016.

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Competitive advantages

NIC's unique model and strong track record help in winning contracts. There is no direct competitor, helping it have a dominant market position. The closest indirect competitors would be state governments that run their portal internally. Other large players such as IBM have limited presence in this niche.

Growth strategy

The company can expand its operations by winning the remainder 23 state government portals. Organic growth can be achieved by new services and adoption of these from existing states. NIC can also grow by winning federal contracts, by growing internationally or by developing new applications.

Risk

Risks include lower-than-expected RFP activity, renewals of contracts at less favorable conditions and negative publicity in the event of a security breach.

Investment Theme

The current economic condition has considerably reduced governments' ability to fund their IT needs. Thus, it makes perfect sense for them to outsource their web-based portal. As technologies continue to advance, citizens, and businesses' needs and willingness to use broader online services will increase. NIC has the expertise to fully exploit this market.

Valuation

Target price = \$18, using DCF model at growth rate of 15% for the next 7 years, 6% at maturity, risk premium of 9%, and payout at maturity of 45%.

Have a good week.

The Global Alpha Team

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