PATNI COMPUTER SYSTEMS RESEARCH

EQUITY RESEARCH November 18, 2009

RESULTS REVIEW

Share Data

Market Cap	Rs. 61.1 bn
Price	Rs. 476.65
BSE Sensex	16,998.78
Reuters	PTNI.BO
Bloomberg	PATNI IN
Avg. Volume (52 Week)	0.2 mn
52-Week High/Low	Rs. 522.70 / 94
Shares Outstanding	128.1 mn

Valuation Ratios

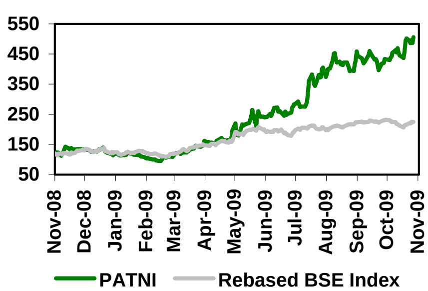
Year to 31 December	2009E	2010E
EPS (Rs.)	39.5	42.1
EPS Growth (%)	22.6%	6.4%
PER (x)	12.8x	12.0x
EV/ Sales (x)	1.8x	1.7x
EV/ EBITDA (x)	9.6x	8.4x

Shareholding Pattern (%)

Promoters	48
FIIs	10
Institutions	7
Public & Others	35

Holding >1% (Non-Promoter)	
FID Funds Mauritius Ltd	2.5
General Atlantic Mauritius Ltd	2.1
Life Insurance Corporation of India	1.1
HDFC Trustee Comp. Tax Saver Fun(	1.0

Relative Performance



Patni Computer Systems — Sell

Recent stock rally restricts upside potential

Patni Computer (Patni)'s net sales stood at USD 167.2 mn in Q3'09 was ahead of its guidance of USD 163-165 mn. Net sales grew 3.3% qoq primarily due to volume growth of 3% and favourable currency movement of 0.3%. EBITDA margin declined 73 bps qoq but improved 35 bps yoy to 20%, owing to improved utilization and operational efficiencies. We have upgraded our revenue growth for CY09 and CY10, on expectation of improvement in demand from IT and ITES sectors. Consequently we have raised our target price from Rs. 370 to Rs. 400. However, the stock has rocketed more than 175% in the last two quarters, hence, we maintain our Sell rating.

Upgrade revenue growth estimate for CY09 and CY10: As the Company garners more than 90% of its revenue from the US and UK markets, we have upwardly revised our revenue growth for CY09 and CY10 by 190 bps and 560 bps to 1.1% and 9.4%, respectively, given the improvement in demand outlook in these regions in the last few months. Besides, the Company's focus on micro-verticals, strengthening of management team and expansion of geographical footprint is showing early signs of success in its order pipeline. Additionally, the Company is also targeting acquisition in South-Asian market to reduce its dependence on the US market. Patni has cash reserve of nearly USD 306 mn to fund such acquisitions.

Expensive valuation: During the last six months the stock has rallied more than 175% whereas during the same period the BSE IT index has rose nearly 65%. Moreover, the stock at the CMP is trading at P/E of 15x, which is 30% discount to the IT sector's P/E of 22x. However, historically Patni trades at more than 50% discount to the sector's P/E, hence we believe that the stock is expensive at the CMP.

Key Figures (Consolidated)

Quarterly Data	Q3'08	Q2'09	Q3'09	YoY%	QoQ%	9M'08	9M'09	YoY%
(Figures in Rs mn, except per share data)								
Net Sales	8,015	7,796	8,017	0.0%	2.8%	22,621	23,578	4.2%
EBITDA	1,572	1,614	1,601	1.8%	(0.8%)	3,962	4,294	8.4%
Net Profit	1,802	1,360	1,686	(6.5%)	24.0%	3,795	3,811	0.4%
Margins(%)								
EBITDA	19.6%	20.7%	20.0%			17.5%	18.2%	
NPM	22.5%	17.4%	21.0%			95.8%	88.7%	
Per Share Data (Rs.)								
EPS	13.2	10.5	12.8	(3.1%)	22.3%	27.5	29.3	6.3%

Result Highlights

Patni's revenue grew 3.3% sequentially to USD 167.2 mn, from USD 161.9 mn in the preceding quarter. Revenue growth was primarily driven by volume growth of 3% and currency impacts of 0.3%. In rupee terms revenue advanced 2.8% qoq to Rs. 8 bn.

EBITDA margin declined 73 bps qoq, but increased 35 bps yoy to 20%. The jump in EBITDA margin was on account of higher utilization and impact of cost rationalization measures.

Other Key highlights of the quarter:

- On operating expenses, sales and marketing expenses were higher at 8.5% sequentially, due to higher investments made during the quarter in regional expansion.
- G&A expenses were higher at 10.8% sequentially, marginally because of stock-based compensation increase during the quarter as the Company has added management team and aligned management incentives overall.
- The Company has successfully improved its utilization to 77% in Q3'09 from 74.4% in Q2'09 due to the overall rationalization of people supply chain.
- During the quarter, the Forex loss was USD 2.3 mn on account of mark to market forex contracts, revaluation of debtors and tax liabilities as against a loss of USD 4.1 mn in the previous quarter.
- The average realization for the quarter was Rs. 46.49 against average rupee cost rate of Rs. 48.4.

Company Guidance

For Q4'10, the Company has guided revenues in the range of USD 168 to USD 169 mn reflecting a marginal sequential increase of 1% on lower capacity due to lower number of working days during the last quarter.

Key Figures

Year to December	CY06	CY07	CY08	CY09E	CY10E	CAGR (%)
(Figures in Rs. mn, except per share data)						(CY08-10E)
Net Sales	26,080	26,911	31,173	31,739	34,586	5.3%
EBITDA	5,193	5,286	4,701	6,068	6,963	21.7%
Net Profit	2,150	4,836	4,380	5,102	5,431	11.3%
Margins(%)						
EBITDA	19.9%	19.6%	15.1%	19.1%	20.1%	
NPM	8.2%	18.0%	14.1%	16.1%	15.7%	
Per Share Data (Rs.)						
EPS	15.5	34.5	32.3	39.5	42.1	14.2%
PER (x)	27.0x	9.6x	15.7x	12.8x	12.0x	

Valuation

At the CMP the stock trades at a forward P/E of 12.8x and 12x for CY09 and CY10. Our DCF valuation (assuming a WACC of 15.7%, Rf of 7.76%, and terminal growth of 5%) gives a fair value of Rs. 400, which provides a downside of 16.2% over the CMP. Therefore we maintain our Sell rating on the stock.

Sensitivity of Our Fair Value Estimates:

Terminal Rate (%)	Cost of Capital (%)				
	14.7	15.2	15.7	13.8	14.2
4.0	424	404	386	467	447
4.5	432	412	393	478	457
5.0	442	420	400	491	469
5.5	452	429	408	505	481
6.0	464	439	416	521	495

Key Risks

The following factors can pose a risk to our rating:

- Inflow of large deals
- Favourable movement in currencies

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