



Patni Computer Systems—in-line results

BUY

CMP: Rs.457

Target Price: 583

Industry: Information Technology

Stock Info	
Market Capital	Rs.5981 cr
Free float	Rs. 2395 cr
Equity Capital	Rs.26.2cr
Avg. Trading Vol.	248298 (Qty)
52 WK High/Low	624/412
Face Value	Rs. 2

BSE Group	B/BSE200
BSE Code	532517
NSE Symbol	PATNI
Bloomberg	PATNI IN
Reuters	PTNI.BO
BSE Sensex	19941
NSE Nifty	5987

Shareholding Pattern (30 th Sept.'10)	
Promoters	45.9%
Domestic Institutions	4.0%
Foreign Institutions	42.3%
Non Promoters Corp.	3.7%
Public & Others	4.2%
Govt. Holdings	0.0%

Q3CY10 results highlights

Results as per expectation: Patni Computer Systems posted their 3QCY10 results which though better than their guidance of \$176-177mn were in line with our expectations. Its' top-line grew by a whopping 7.8% QoQ in rupee terms to Rs.822.6cr and 6.7% in dollar terms to \$178.8mn. The company's net income was however down by 1.6% at Rs.144.5cr as compared to Rs.146.7cr in Q2; while in dollar term net income was at \$28.7mn vis-à-vis \$31.7mn in Q2.

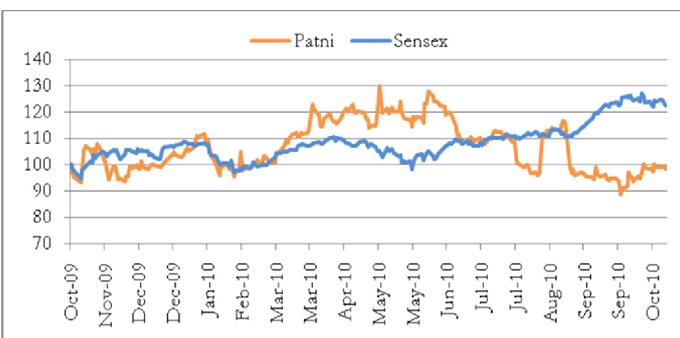
Lower margins: Patni continued to face pressure on its margins mainly due to high employee cost, lower utilisation as well as higher attrition. Gross margins were at 33.9% in Q3 compared to 35% in Q2. Going ahead, considering its strong hiring plans we expect margins to remain under pressure.

Robust employee addition: The company increased its employee base by ~1650people on a net basis. It also plans to add another 1000 in the last quarter. A major cause of worry for Patni has been the high attrition rate which refuses to go down. At 25.9% in Q3CY10, attrition is at its peak level for Patni and continues to remain a major worry for it. Though we expect attrition to moderate in the coming quarters, the company will continue to face supply side constraint which will prove detrimental for a major uptick in its growth rates.

Muted guidance: In spite of posting good result in Q3, Patni's guidance for the last quarter of CY10 is disappointing. It has guided for top-line revenue of \$180-181mn indicating a growth of only 0.7-1.2% ; while its' bottom-line guidance of \$22.5-23mn indicates negative growth. This is in contrast to the strong growth rates that are being expected by most of the top-tier IT companies as well as many mid-caps. We believe that despite some significant recruitments done at the mid-management and senior level, the company is yet to garner better share of its' clients' IT wallet share. This is a key parameter that has resulted in the company's growth rates becoming stagnant.

Valuation: Patni's weak guidance as well as its inability to get attrition under control will result in the company continuing to face supply-side constraint which will result in the company lacking behind industry growth rates in the coming quarters. Despite pocketing some good deals in the last couple of quarters, it is yet to show significant improvement in its growth capability. Besides, we believe margin pressure will continue even in CY11E.

We are therefore lowering our CY11E profit estimates though we have marginally upped our top-line estimate. We thereby roll forward our target price to Rs.583 per share as compared to Rs.607 earlier. We have arrived at the target price by assigning a PE multiple of 13x to our CY11E EPS estimates as compared to 14x earlier to factor in industry lacking growth prospects. At CMP, the stock is trading at 10.6xCY10E and 10.2xCY11E earnings of Rs.43.2 and Rs.44.9 per share respectively. We however reiterate our "Buy" call on the stock as we believe at its' current market price it is available at cheap valuations—more so because of its' cash balance of \$317.8mn (Rs.1416cr) which makes up ~24% of its market cap.



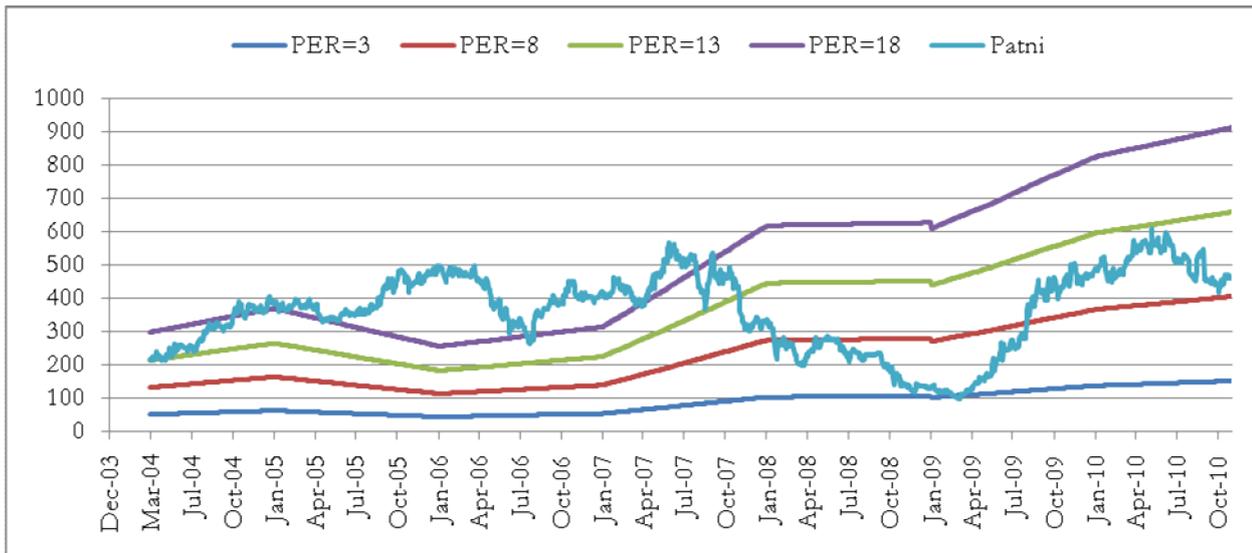
Particulars (Rs. in cr)	CY09	CY10E	CY11E
Net Revenue	3275.6	3365.3	3595.1
Growth %	0.9	2.7	6.8
Net Profit	586.6	561.0	585.1
Growth %	33.9	-4.4	4.3
EPS (Rs)	45.7	43.2	44.9
P/E	9.9	10.6	10.2
P/BV	1.7	1.9	1.7

Background

Headed by Mr.Narendra K.Patni, who is the chairman of the organization, Patni Computer Systems Ltd. is one of the oldest and among the most prominent Information Technology companies of India. Established in the year 1978, the company has been providing world-class IT consulting and software services to Global 2000 companies for almost three decades. The company has successfully serviced more than 400 Fortune 1000 companies all over the world. It has a total employee base of about 16,556, 22 Global delivery Centres mainly in India, US and UK and 27 Sales offices spread all over the world. The Company at present has 280 active clients across 28 countries.

The company derives its revenues from five types of services—with the majority of it coming from the traditional service line of Application Development and Maintenance (ADM). However, the company is trying to diversify itself to other lucrative segments too in the recent times both organically and inorganically.

PE Band



Source: Arianth Research

Q3 CY10 financial data

Y/E Dec. (Rs.in cr)	Q3CY10	Q3CY09	YoY%chng.	Q2CY10	QoQ%chng.
Sales and service income	822.7	801.7	2.6%	762.9	7.8%
Other income	48.9	32.0	52.6%	52.6	-7.0%
TOTAL	871.6	833.8	4.5%	815.5	6.9%
EXPENDITURE					
Personnel costs	487.6	473.4	3.0%	453.9	7.4%
Sales, general & administrative cost	179.5	168.2	6.7%	164.9	8.9%
Depreciation	31.4	31.2	0.9%	29.1	8.0%
Less: Transfer from re-valuation reserve	0.0	0.0	0.0%	0.0	0.0%
Interest cost	1.3	1.6	-17.4%	0.3	357.1%
Total	699.7	674.3	3.8%	648.1	8.0%
Profit for the year before taxation	171.8	159.5	7.8%	167.4	2.7%
Provision for taxation	46.0	14.5	216.5%	35.0	31.1%
MAT credit entitlement	-18.6	-22.69	-18.2%	-14.4	28.6%
Provision for taxation-fringe benefits	0.0	-0.94	-100.0%	0.0	0.0%
Profit for the year after taxation	144.4	168.58	-14.3%	146.7	-1.6%
<i>Effective Tax Rate%</i>	<i>15.9%</i>	<i>-5.7%</i>		<i>12.3%</i>	
<i>EBIDTA%</i>	<i>23.5%</i>	<i>23.1%</i>		<i>24.1%</i>	
<i>PAT%</i>	<i>16.6%</i>	<i>20.2%</i>		<i>17.9%</i>	
<i>EPS</i>	<i>11.1</i>	<i>13.2</i>	<i>15.9%</i>	<i>11.3</i>	<i>1.8%</i>

Profit and Loss Statement

(consolidated)

Cash Flow Statement Extract

Y/E Dec. (Rs. in cr)	CY08	CY09	CY10E	CY11E
Net Sales	3117.3	3146.2	3173.6	3403.4
<i>YoY%</i>	<i>15.9%</i>	<i>0.9%</i>	<i>0.9%</i>	<i>7.2%</i>
Other Inc.	130.4	129.4	191.7	191.7
Total Inc.	3247.6	3275.6	3365.3	3595.1
<i>YoY%</i>	<i>17.0%</i>	<i>0.9%</i>	<i>2.7%</i>	<i>6.8%</i>
Personnel costs	1832.9	1835.7	1900.6	2040.0
SGA	814.3	691.3	671.5	688.0
Depreciation	114.2	142.1	119.1	130.5
Interest	7.9	7.7	5.0	6.5
PBT	478.4	598.7	669.0	730.1
Tax	40.4	12.1	107.9	145.0
<i>Tax rate%</i>	<i>8.5%</i>	<i>2.0%</i>	<i>16.1%</i>	<i>19.9%</i>
PAT	438.0	586.6	561.0	585.1
<i>YoY%</i>	<i>-9.4%</i>	<i>33.9%</i>	<i>-4.4%</i>	<i>4.3%</i>
EPS	32.3	45.7	43.2	44.9

Y/E December (Rs.in cr)	CY08	CY09	CY10E	CY11E
Profit before taxation	478.4	598.7	669.0	730.1
Add: Depreciation	101.9	106.7	119.1	130.5
Other items	107.8	-6.6	-122.5	-60.9
Cash generated from operations	688.1	698.8	665.7	799.7
Income taxes paid	-106.7	-86.4	-107.9	-145.0
Net cash provided by operating activities	581.4	612.5	557.7	654.7
(Inc)/ Dec in FA	-189.5	-92.0	-170.7	-133.5
Dividend Received	50.6	50.3	50.3	50.3
Interest Received	5.0	1.8	1.8	1.8
Other items	33.7	-549.7	740.2	-
Cash Inflow/ (outflow) from Investments	-100.3	-589.6	-621.7	-81.3
Interest Paid	-0.2	-0.2	-5.0	-6.5
Dividend Paid	-48.8	-44.9	-1004.8	-45.3
Issue of equity shares	0.6	25.9	-	-
Other items	-237.6	-0.8	-	-
Cash Inflow/ (outflow) from Financing	-286.0	-19.9	-1009.8	-51.8
Effect of change in exchange rate	-30.6	-0.8	-	-
Net Cash Inflow/ (outflow)	164.6	2.1	169.6	521.5
Cash at beginning	128.5	293.1	295.2	464.8
Net Cash carried forward	293.1	295.2	464.8	986.3

Balance Sheet

Y/E Dec. (Rs. in cr)	CY08	CY09	CY10E	CY11E
Sources of Funds:				
Equity Capital(FV-Rs.2)	25.6	25.8	26.2	26.2
Share application money	0.0	0.0	2.4	0.0
Stock options outstanding	0.17	19.1	23.8	0
Reserves	2814.3	3506.0	3032.6	3622.0
Shareholder's Equity	2839.9	3550.9	3084.9	3648.2
Total Debt	1.8	0.9	0.9	0.9
Deferred Tax Liability	-13.4	-6.7	-10.3	-10.3
Total Liabilities	2855.1	3558.6	3096.2	3659.4
Application of Funds:				
Goodwill	490.7	476.5	495.7	495.7
Gross Block	1165.2	1312.7	1483.4	1616.9
Less: Acc. depreciation	516.8	619.5	738.1	864.2
<i>Net Block</i>	<i>648.4</i>	<i>693.3</i>	<i>745.3</i>	<i>752.7</i>
CWIP	250.2	133.7	133.7	133.7
Investments	1177.1	1775.2	1035.0	1035.0
Deferred Tax Asset	94.5	89.4	78.9	78.9
Current Assets:				
Debtors	545.1	508.9	480.4	491.4
Cash and equivalent	293.2	295.2	464.8	986.3
Unbilled revenue	149.5	91.8	84.8	86.7
Loans and Advances	200.6	256.2	300.0	330.0
Current Liabilities:				
Creditors & other liab	632.8	456.0	429.9	440.9
Provisions	302.7	296.6	292.5	290.0
Net current asset	194.3	390.5	722.4	730.9
Total Assets	2855.1	3558.6	3096.2	3659.4

Important Ratios

Y/E December	CY08	CY09	CY10E	CY11E
Performance Ratios				
EBIDTA %	18.5	22.9	23.6	24.1
Net Profit %	13.5	17.9	16.7	16.3
Sales per share (SPS)	229.9	245.3	243.3	260.9
Price/SPS	2.0	1.9	1.9	1.8
Dividend %	150	150	3300	150
Cash per share	21.6	23.0	35.6	75.6
Assets Turnover	1.1	0.9	1.1	0.9
Du Pont Analysis				
PAT / Net Sales	0.14	0.19	0.18	0.17
Net Sales / Assets	1.09	0.88	1.02	0.93
Assets / Equity	1.01	1.00	1.00	1.00
ROE %	15.4	16.5	18.2	16.0
Valuation Ratios				
Diluted EPS	32.3	44.9	41.8	43.6
Cash EPS	40.7	56.8	52.2	54.9
P/E	14.2	9.9	10.6	10.2
P/BV	2.2	1.7	1.9	1.7
EV/ EBIDTA	2.4	8.0	7.5	6.3
EV/ Sales	0.5	1.9	1.9	1.6
ROCE%	21.0	21.0	25.6	23.7

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Stock Rating Scale

		Absolute Return
BUY	:	>20%
ACCUMULATE	:	10-20%
HOLD	:	5-10%
REDUCE	:	<5%

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