

UBS Investment Research

First Read: Patni Computer

Lowering attrition rates will be key to turn-around

■ Results in-line, below sector peers

Patni reported 4QCY06 revenues of US\$156mn (UBS:US\$158mn), up 1.1% q-o-q, net profits of US\$27.85mn (UBS:US\$26mn), up 8.2% q-o-q. EBIT margins declined 31bps q-o-q. Attrition rate moved up to 29.1%, up 200bps q-o-q. Excluding one-time gain of US\$1.1mn, net profits were in-line.

■ Key reason for sluggish performance

Revenue decline from top client (down 17% q-o-q) and impact of client transition to another vendor resulted in overall "flat" volumes q-o-q in March quarter for Patni. Also, increase in attrition rates resulted in salary increase, higher than industry average (offshore: 18-20%, onsite: 4-4.5%).

■ Lower attrition reflects business confidence

We note, while client transition could impact revenue growth, EBITDA margins will be impacted by salary increase and currency appreciation by 200-250 bps q-o-q in June quarter. Finally, with attrition rates at 25%+ levels, Patni will have to continue to take measures on HR front in coming quarters to combat attrition, thus impacting EBITDA margins.

■ Valuation: Re-iterate cautious view

We believe, lower attrition reflects business confidence and hence, will be key to gauge the turn-around. We will revisit our estimates shortly. Our price target is based on medium-term growth of 16%, terminal growth of 3% and WACC of 13%.

Highlights (Rs m)	12/03	12/04	12/05E	12/06E	12/07E
Revenues	11,648	14,765	19,747	25,767	33,788
EBIT (UBS)	2,172	2,947	3,200	3,537	4,271
Net income (UBS)	1,843	2,623	2,922	3,344	3,913
EPS (UBS, Rs)	14.74	20.99	21.22	24.26	28.39
Net DPS (UBS, Rs)	1.00	2.00	4.00	5.00	5.00

Profitability & Valuation	5-yr hist. av.	12/04	12/05E	12/06E	12/07E
EBIT margin %	-	20.0	16.2	13.7	12.6
ROIC (EBIT) %	-	74.9	58.6	49.7	50.4
EV/EBITDA x	-	7.9	12.8	10.6	8.2
PE (UBS) x	-	13.9	20.4	17.8	15.2
Net dividend yield %	-	0.7	0.9	1.2	1.2

Source: Company accounts, Thomson Financial, UBS estimates. (UBS) valuations are stated before goodwill, exceptionals and other special items. Valuations: based on an average share price that year, (E): based on a share price of Rs432.15 on 25 Apr 2007 23:39 HKT

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Global Equity Research

India

Software

Rating **Neutral 2**
Unchanged

Price target **Rs475.00/US\$11.70**
Unchanged

Price **Rs432.15/US\$10.65**

RIC: PTNI.BO BBG: PATNI IN

26 April 2007

Trading data (local/US\$)

52-wk. range	Rs468.55-261.10/US\$11.29-5.57
Market cap.	Rs59.6bn/US\$1.47bn
Shares o/s	138m (ORD)
Free float	49%
Avg. daily volume ('000)	66
Avg. daily value (Rsm)	28.6

Balance sheet data 12/05E

Shareholders' equity	Rs16.6bn
P/BV (UBS)	3.3x
Net cash (debt)	Rs3.84bn

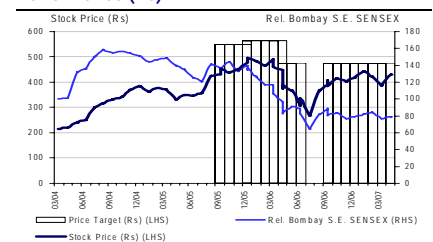
Forecast returns

Forecast price appreciation	+9.9%
Forecast dividend yield	0.9%
Forecast stock return	+10.8%
Market return assumption	12.8%
Forecast excess return	-2.0%

EPS (UBS, Rs)

	12/05E		12/04
	UBS	Cons.	Actual
Q1E	4.94	-	0.00
Q2E	4.58	-	0.00
Q3E	5.51	-	5.93
Q4E	6.19	-	5.26
12/05E	21.22	15.80	
12/06E	24.26	23.22	

Performance (Rs)



Source: UBS

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ANALYST CERTIFICATION AND REQUIRED DISCLOSURES BEGIN ON PAGE 2

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■ Patni Computer Systems

Patni Computer Systems Limited (Patni) was incorporated in 1978 and is headquartered in Mumbai, India. The company was an early participant in India's software industry. It has over 11,000 employees and 26 sales offices globally. It has clients in 15 countries and development facilities in eight cities in India. Patni is one of the leading providers of IT services from India (ranked sixth by Nasscom).

■ Statement of Risk

A sharp downturn in IT spending could result in downward revision of our earnings estimates. We assign the stock a predictability level of 2.

■ Analyst Certification

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UBS Investment Research: Global Equity Ratings Definitions and Allocations

UBS rating	Definition	UBS rating	Definition	Rating category	Coverage ¹	IB services ²
Buy 1	FSR is > 6% above the MRA, higher degree of predictability	Buy 2	FSR is > 6% above the MRA, lower degree of predictability	Buy	47%	37%
Neutral 1	FSR is between -6% and 6% of the MRA, higher degree of predictability	Neutral 2	FSR is between -6% and 6% of the MRA, lower degree of predictability	Hold/Neutral	42%	36%
Reduce 1	FSR is > 6% below the MRA, higher degree of predictability	Reduce 2	FSR is > 6% below the MRA, lower degree of predictability	Sell	12%	28%

1: Percentage of companies under coverage globally within this rating category.

2: Percentage of companies within this rating category for which investment banking (IB) services were provided within the past 12 months.

Source: UBS. Ratings allocations are as of 31 March 2007.

KEY DEFINITIONS

Forecast Stock Return (FSR) is defined as expected percentage price appreciation plus gross dividend yield over the next 12 months.

Market Return Assumption (MRA) is defined as the one-year local market interest rate plus 5% (a proxy for, and not a forecast of, the equity risk premium).

Predictability Level The predictability level indicates an analyst's conviction in the FSR. A predictability level of '1' means that the analyst's estimate of FSR is in the middle of a narrower, or smaller, range of possibilities. A predictability level of '2' means that the analyst's estimate of FSR is in the middle of a broader, or larger, range of possibilities.

Under Review (UR) Stocks may be flagged as UR by the analyst, indicating that the stock's price target and/or rating are subject to possible change in the near term, usually in response to an event that may affect the investment case or valuation.

EXCEPTIONS AND SPECIAL CASES

US Closed-End Fund ratings and definitions are: Buy: Higher stability of principal and higher stability of dividends; Neutral: Potential loss of principal, stability of dividend; Reduce: High potential for loss of principal and dividend risk.

UK and European Investment Fund ratings and definitions are: Buy: Positive on factors such as structure, management, performance record, discount; Neutral: Neutral on factors such as structure, management, performance record, discount; Reduce: Negative on factors such as structure, management, performance record, discount.

Core Banding Exceptions (CBE): Exceptions to the standard +/-6% bands may be granted by the Investment Review Committee (IRC). Factors considered by the IRC include the stock's volatility and the credit spread of the respective company's debt. As a result, stocks deemed to be very high or low risk may be subject to higher or lower bands as they relate to the rating. When such exceptions apply, they will be identified in the Companies Mentioned or Company Disclosure table in the relevant research piece.

Companies mentioned

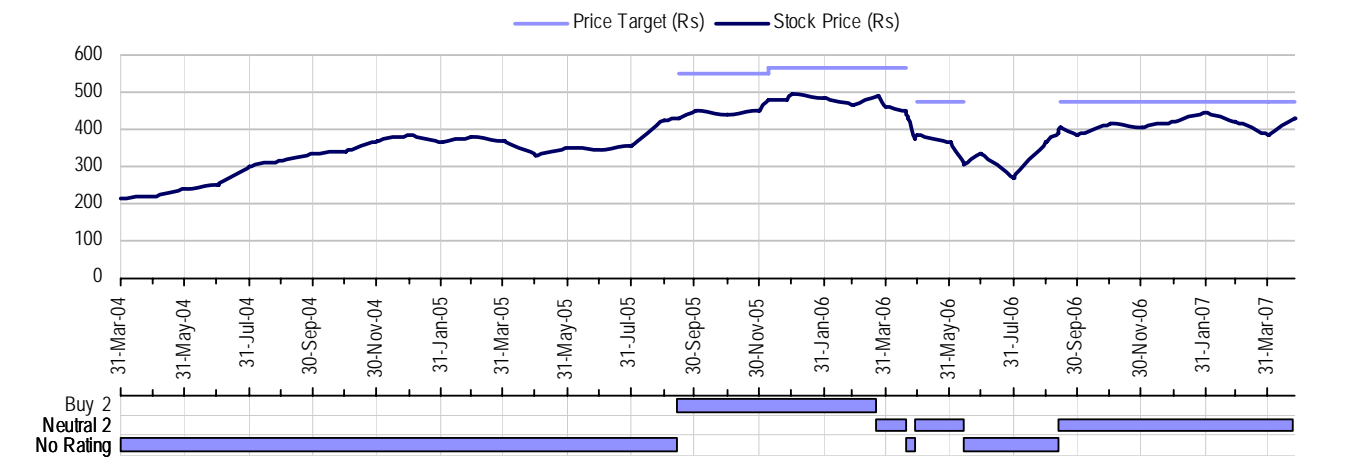
Company Name	Reuters	Rating	Price	Price date/time
Patni Computer ¹³	PTNI.BO	Neutral 2	Rs432.15	25 Apr 2007 23:39 HKT

Source: UBS. HKT: Hong Kong time.

13. UBS AG, its affiliates or subsidiaries beneficially owned 1% or more of a class of this company's common equity securities as of last month's end (or the prior month's end if this report is dated less than 10 days after the most recent month's end).

Unless otherwise indicated, please refer to the Valuation and Risk sections within the body of this report.

Patni Computer Systems (Rs)



Source: UBS; as of 25 April 2007.

Note: On September 9, 2006, UBS adopted new percentage band criteria for its rating system. (See 'UBS Investment Research: Global Equity Ratings Definitions and Allocations' table for details). Between October 13, 2003 and September 9, 2006 the percentage band criteria used in the rating system was 10%. Prior to October 13, 2003, the UBS ratings and their definitions were: Buy 1: Excess return potential >15%, smaller range around price target; Buy 2: Excess return potential >15%, larger range around price target; Neutral 1: Excess return potential between -15% and 15%, smaller range around price target; Neutral 2: Excess return potential between -15% and 15%, larger range around price target; Reduce 1: Excess return potential < -15%, smaller range around price target; Reduce 2: Excess return potential < -15%, larger range around price target. Excess return is defined as the difference between the FSR and the one-year local market interest rate.

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