

September 29, 2006

Stock Rating
Overweight

Industry View
Attractive

Patni Computer Systems

Revenue Momentum & Cost Containment on Track

Quick Comment: The three key questions for us while evaluating this stock, given the value that we see, are: (1) is the revenue momentum continuing? (2) are the margin improvement initiatives on track now, given past disappointments? (3) is there improvement on the employee attrition front? We recently had a discussion with the company management to address these questions. We think the answers to the first two questions are a definite "yes". On the employee attrition front, we did not get the sense that there is rapid progress yet, but at least there appears to be no deterioration either.

What's New: Revenue momentum appears to be good – GE revenue is expected to be stable and there is slightly better momentum in the insurance vertical. Initiatives to improve margins appear to be on track and the company seems well placed to meet its guidance for 100 bps expansion in the Sep-06 quarter.

Implications: We believe that Patni is an attractive stock with a lot of value. We estimate the stock is trading at 1.3x 12-month forward EV/sales, implying a discount of about 75% to the top-tier stocks. This is not an insignificant-sized company – it currently has a revenue run-rate of about US\$600 mn – and we forecast a revenue CAGR of 26% over this year and next. Low margins have been an issue – management seems fully focused on improving them and their initiatives appear to be on track.

Key Ratios and Statistics

Reuters: PTNI.BO Bloomberg: PATNI IN

India Software

Shr price, close (Sep 28, 2006)	Rs386.15
Mkt cap, curr (mn)	US\$1,163
52-Week Range	Rs508.00-251.00

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Some of the key highlights from our discussions are:

On the Revenue Front:

- The management continues to expect revenue from GE to be stable (notwithstanding GE signing a new vendor recently) and the contract has been renewed.
- The growth in insurance vertical has been relatively slow for Patni (2% CAGR over the four quarters ending Jun-06). While there appears to be no major new wins, the momentum seems slightly better with existing customers ramping up a bit.
- The management does not appear worried about a potential US slowdown.
- 4Q has more holidays and tends to be slower but we do not see Patni suffering a significant slowdown in growth.

On Margins:

- The management is confident of meeting its guidance for 3Q06 (100 bps improvement) and is focusing on improving utilization and G&A leverage.

- It does not, however, see any material upward movement in pricing on an “apple-apple” basis.

On the Employee Front:

- The progress on the high attrition front is not significant, though we do not think it is deteriorating either. The management appears to be focusing on flattening the pyramid.

On Acquisitions:

- The management continues to look at opportunities.

On Taxes:

- The management does not think any further provisions will need to be made to resolve the issues with the US tax authorities.

Company Description

Patni Computer Systems Ltd. provides IT consulting and software services to global organizations in the financial services, insurance and manufacturing industries. The company's services range from application development, re-engineering and maintenance, to business processes outsourcing and engineering services. General Atlantic Partners holds significant equity capital of the company and has representation on the Board of Directors.

Industry View: Attractive

MSCI Country: India

Asia Strategist's Recommended Weight: 2.2%
MSCI Asia/Pac All Country Ex Jp Weight: 6.8%



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(as of August 31, 2006)

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	Count	% of Total	Count	% of Total	% of Rating Category
Overweight/Buy	784	39%	294	44%	38%
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Total	2,004		665		

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Industry Coverage:India Software

Company (Ticker)	Rating (as of)	Price (09/29/2006)
Anantha Narayan		
HCL Technologies (HCLT.BO)	E (01/30/2004)	Rs550.00
Hexaware Technologies Limited (HEXT.BO)	O (06/22/2006)	Rs161.95
Infosys Technologies (INFY.BO)	O (04/17/2006)	Rs1847.90
Mphasis BFL Group (MBFL.BO)	E (03/15/2004)	Rs186.00
Patni Computer Systems (PTNI.BO)	O (08/08/2005)	Rs385.00
Polaris Software Lab Ltd. (POLS.BO)	U (08/08/2005)	Rs117.15
Satyam Computer Services (SATY.BO)	O (03/18/2002)	Rs818.55
Tata Consultancy Services (TCS.BO)	O (09/29/2004)	Rs1022.95
Wipro Ltd. (WIPR.BO)	E (03/22/2002)	Rs525.10
i-flex Solutions Ltd. (IFLX.BO)	E (10/31/2005)	Rs1434.00

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