

20th November, 2006

Sanjeev Hota

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Stock details

NSE Code	PARADYNE
BSE Code	532672
Market Cap (Rs bn)	0.71
Free Float (%)	32
52-wk Hi/Lo (Rs)	93/42
Avg Daily Vol (BSE)	28666
Avg Daily Vol (NSE)	18372
Shares o/s (mn) FV Rs 10	10.88

Source: Company Emkay Private Client Research

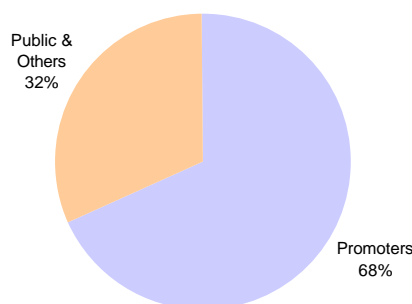
Summary table

Rs. mn	FY06A	FY07E	FY08E
Total Revenue	867.3	1352.9	1854.0
Growth %	26.6	56.0	37.0
EBITDA	97.9	189.4	278.1
EBITDA margin %	11.3	14.0	15.0
Net Profit	73.0	136.5	202.8
*EPS (Rs)	6.7	12.5	18.6
CEPS (Rs)	7.7	14.2	20.9
EV/EBITDA	6.9	3.3	1.8
EV/Sales	0.8	0.5	0.3
ROE %	35.8	37.8	38.3
ROCE %	37.3	44.5	46.6
P/E (x)	9.8	5.3	3.5
P/CEPS (x)	8.8	4.8	3.2

*EPS based on current equity of 108.8 mn of face value of Rs 10 per share

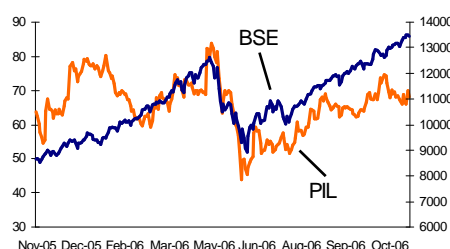
Source: Company Emkay Private Client Research

Shareholding pattern (30 Sept. 06)



Source: Company and Emkay Private Client Research

One Month Perfo. (Rel to sensx)



Source: Capitaline

Paradyne Infotech Ltd.

RECOMMENDATION: BUY

Price: Rs. 68

Target Price: Rs. 150

Paradyne Infotech (PIL) is one of the few domestic focussed IT players with core competency in Application software & services and Technology IMS (Infrastructure Management Services). Paradyne enjoys strategic alliances with various Global technology giants like Sun, IBM, Oracle, Acer and is one of the Level 1 Turnkey Solution providers empanelled by Department of Information Technology, Government of Maharashtra along with few selected major IT companies like IBM, TCS, Wipro, CMC, Tata Infotech, etc.

PIL's service and product offerings are varied and cater to different industry segments like banking and finance, government sector, education, retail, manufacturing, and ISV (Independent Software Vendor). Paradyne's business is spread along four Strategic Business Units (SBUs). These are software services and Products, managed service provider (MSP), system integration and BPO services.

Paradyne is a profit making company since inception, with its focus approach in building scale in domestic market and moving from a low end system integrator to more diversified services and product offerings which amply reflected in a 64% CAGR in net profit between FY04-06, with revenues in the same period revenue growing at a CAGR of 30%, with EBITDA margin expanding from 6% to 12% between FY04-06.

At the current valuation of 5x FY07E and 4x FY08E earning and 2x FY08E EV/EBITDA, we rate the PIL stock a BUY with a target price of Rs 150 based on the DCF approach.

Investment Highlights –

Domestic IT spend on a sharp upswing – Indian Information and Communications Technology (ICT) companies may be missing a significant opportunity by concentrating their efforts on India's much-hyped export market and failing to capitalize on the country's burgeoning domestic market. According to Gartner estimates, India continues to be the fastest growing ICT market globally with the market estimated to grow at a combined annual growth rate (CAGR) of 19% from 2004 through 2008. Though starting from a much smaller base, this is significantly faster growth than the second fastest growing ICT market in the world - China. Gartner estimates that ICT spending in India will surpass US\$54.8 billion by 2008E, a rise from US\$29.5 billion in 2004. Domestic demand for IT in India is witnessing a gradual transformation from being predominantly hardware driven towards a solutions oriented approach resulting in a growing emphasis on services.

PIL enjoys a strong business presence in the Managed Services Space, with marquee clients – According to Nasscom, the domestic MSP (Managed Services Space) market from \$140 million in 2005 is well inroad to touch \$190 million in 2006. These figures are testimonial to the fact that the Indian market is moving towards an era of outsourcing services in the domestic space. As Paradyne is having a strong presence in the managed services space within the domestic market, these developments augur well for PIL.

EBIDTA Margins on a northward move, from 6% in FY04 to 12% in FY06-

In the last three financials years preceding FY06, with the management's focussed approach in ramping up the high margin Managed Services business and Products business and to reduce the contribution of System integrations revenue, has been reflected in the 520bps-operating margin expansion to 11.3% for FY07 vis a vis 6.5% in the FY04. The margin expansion was on the back of reduction in the system integration revenue, which stood at around 65% as compared to 84% in the year 2004. On the other hand, for the H1FY07, the EBITDA margins further improved to 15.2%, as system integration now accounts for less than 40% of revenue.

Risks & Concerns-

Paradyne's business is largely focused in Indian market. This makes future success highly dependent on IT spending of banks, financial institutions and other Indian companies and continuance of demand for its products and services from these industries in India. Therefore, any structural changes in the spending may materially affect its business growth.

Aggressively pursuing the inorganic initiatives in US region to expand its geographical footprint and clients offering

Business Outlook and Valuation – High growth visible

The Paradyne stock trades at 4x FY08E a EV/EBITA of 2x on FY08E. We expect Paradyne to grow at a CAGR growth of 46% and 67% in revenue and net profits likely to touch Rs 1854 mn with net profits estimated at 203 mn respectively by FY08E.

Paradyne is also aggressively pursuing the inorganic growth initiatives in US region to expand its geographical footprint and clients offering, which we expect to materialize before FY07, which will further propel the growth visibility of the company for the coming years, our estimates do not factor any inorganic growth initiatives.

We initiate a BUY on the stock with a price target of Rs 150 based on the DCF approach, at our target price the stock will be valued at 8x for FY08E.

Background:

Encouraging past, Promising future

Incorporated in the year 1997 **Paradyne Infotech**, commenced business by providing System Integration and Networking Solutions and developing software solutions in Oracle technologies. Gradually the company achieved an ISO 9001:2000 certification and became an end-to-end IT services provider with core competencies in Application Software Services & Infrastructure Managed Services and System Integration Services. Paradyne soon grew as a reputed organization in the IT services sector.

Emphasizing process and Quality discipline

Paradyne core competency lies in Application software services, Technology IMS with highly experienced management team backed by a global advisory board consisting of academic and business luminaries across the globe. Paradyne Infotech has strategic alliances with various Global technology giants like Sun, IBM, Oracle, and Acer etc. Paradyne is also having subsidiary in USA, Dyne Techservices. Paradyne have partnered with global businesses; escalating towards innovation, better performance and rapid development in IT Services.

Paradyne is one of the Level 1 Turnkey Solution Provider empanelled by Department of Information Technology, Government of Maharashtra along with few selected major IT companies like IBM, TCS, Wipro, CMC, Tata Infotech, etc.

Company service offerings are varied, and straddle in many different industry segments, such as banking and finance, government sector, education, retail, manufacturing, and ISV, its clients include medium and large companies, and service engagements vary from few months to enormous years in effort.

The company entered the Indian capital markets in March 2005 with an initial public offer of 33 lakh shares at a fixed issue price of Rs.42, aggregating to 13.86 crores. The issue was oversubscribed by 45 times and the shares listed at a premium of 60%.

Key Milestones:

1997	- Incorporated as a IT Services and Solutions company - Started System Integration and Software Development services
1998	- Major business ties up with reputed business houses like, Raheja Group, Gujarat Pipavav Port Limited and Ajmera Group.
1999	- Paradyne was awarded with nation wide contract for automation of Indian Express locations across the country.
2000	- Setup a Development Center in India at Millennium Business Park, Mahape, and Navi Mumbai. - Started 100% subsidiary operations in US by the name of Sundune Corporation. - Awarded as "Excellence in Sales" by Sun Microsystems. - Awarded as an "Outstanding Business Partner" by IBM Corporation
2001	- Became ISO 9002 Certified Company, certified by QA International - Rated as 174th Company in India by Dataquest.
2002	- Acquired a Core Banking Software & started enriching the product with huge manyear investment - Made a foray in BFSI segment as a Turnkey IT Solution Provider.
2003	- Accredited as one of the top 10 ITSP (Information Technology Service Provider) Certified by Department of Information Technology Government of Maharashtra.
2004	- Became ISO 9001:2000 Certified Company, certified by QA International UKAS. - Awarded as an "Outstanding Business Partner" by Sun Microsystems.
2005	- Successfully entered the Indian Capital market with an IPO oversubscribed 45.1 times - Awarded by Deloitte for being the fastest 50 growing technology companies in India. - Winner in the Deloitte Technology fast 500 Asia Pacific 2005 program, which acknowledge and honors fast-growing technology companies across Asia Pacific. - Started full-fledged US operations with its 100% owned subsidiary Dyne Techservices Inc.

Operational Highlights

Particulars	Q2FY07	H1FY07	H1FY06	Grth (%)	FY06	FY05	Grth (%)
Sales	301	569	425.4	34	867	685	27
OPM%	15	14.8	12.2		11	10	
OP	46	84	52.1	61	98	66	48
Other Income	1	2	-2.2	LP	7	0	-
PBIDT	47	86	49.9	72	105	66	59
Interest	3	5	4.6	13	10	4	128
PBDT	44	81	45.3	78	96	62	54
Depreciation	4	8	5.0	54	11	4	184
PBT	40	73	40.3	81	85	58	46
Tax	6	11	5.9	86	12	8	57
PAT	34	62	34.4	81	73	50	44
Equity Capital	108.8	108.8	108.8		108.8	75.8	
EPS	3.1	5.7	3.2		6.7	6.6	

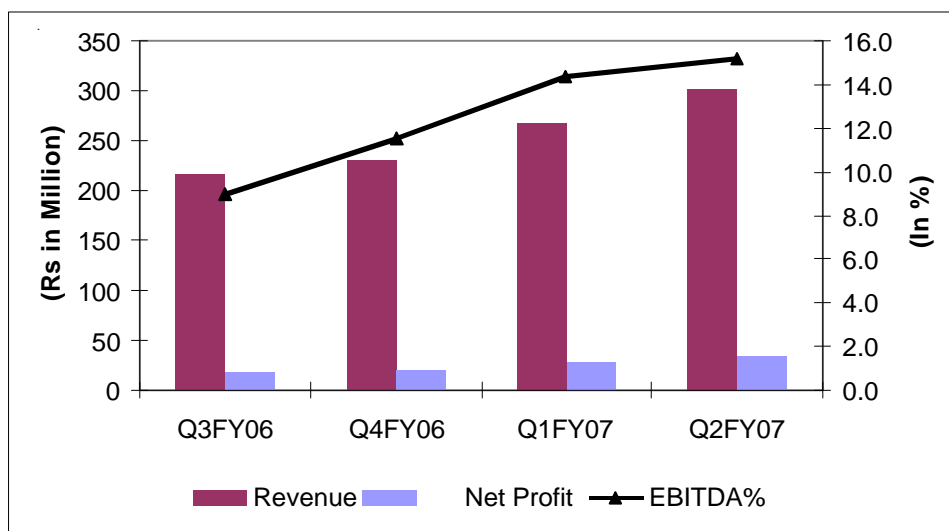
Source: Company & Emkay Private Client Research # LP.: Loss to profit
(Figures in Rs million)

Strong ramp up in the MSP and Product business, reflected in impressive margin expansion

The PIL's management's continual endeavor in ramping up the Managed Services business coupled with strong traction in the company's banking and HR products business reflected in strong H1FY07 numbers, with revenue growing by 34% to Rs 569 mn as compared to corresponding period previous year, whereas with 250bps expansion in the EBITDA margin to 14.8%, took net profit higher by 81% to Rs 62.1 mn. On the other hand, for Q2FY07, Paradyne clocked revenue of Rs 301 mn, EBITDA margin further improved to 15%, and net profit stood at 33.6mn.

On the back of strong management approach and buoyant industry environment, Paradyne Infotech has shown considerably growth in the last four sequential quarters, with its revenue grew at a CQGR of 12% to Rs 301 mn and for the same time net profit grew at a stunning CQGR of 22% to Rs 34 mn for Q2FY07.

Quarterly Performance: Gaining strength to strength

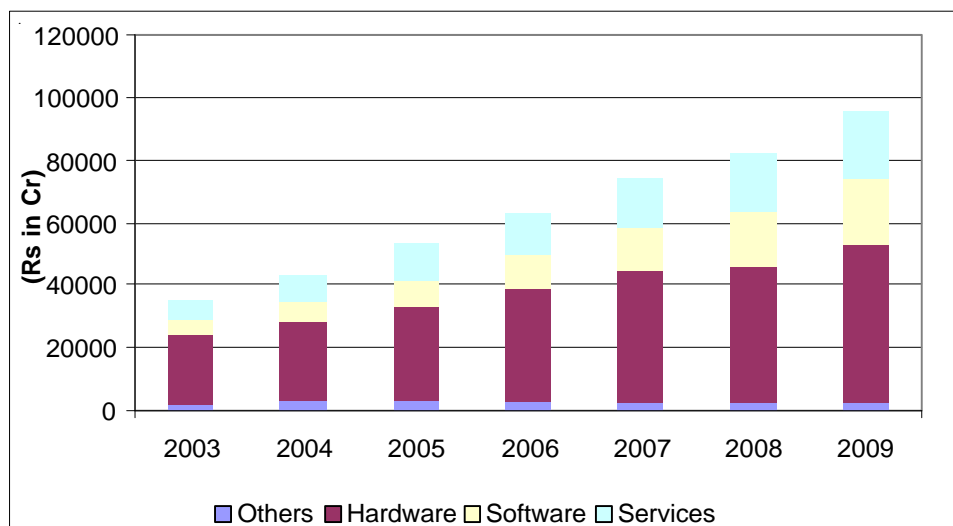


Industry Environment

Domestic demand for IT in India is witnessing a gradual transformation from being predominantly hardware driven towards a solutions oriented approach – resulting in a growing emphasis on services. In fact, revenue growth in the services segment alone has reported faster growth than that for the overall domestic IT market (including hardware, software and services) over the past few years. As depicted in the following chart, this trend is expected to continue over the forecast period.

Growth of IT Spending in India

Domestic IT spending, Moving from Hardware to Software



Source: Nasscom & :Emkay Private Client Research

The liberalization of Indian economic policy, de-regulation of key sectors and progressive moves towards further integrating India with the global economy has been a key driver of increased IT adoption in the country. This is best reflected in the fact that most indigenous players in telecom and banking, two key sectors with significant multinational corporation (MNC) participation, have significantly upgraded their levels of IT adoption to offer best-in-class services comparable to those offered by the global competition and these two sectors together account for approximately 35-40 percent of the domestic spend on IT services.

Increasing competitions driving the domestic IT spend

Similar competitive pressures in other more recently deregulated service sectors such as airlines and insurance, and the uptake in the manufacturing and industrial sectors; and the several large e-governance initiatives launched by the government under the National E-Governance Plan (NEGP) are expected to provide sustained growth in domestic demand for IT services over the next few years. Over the next five years, domestic spending on outsourced IT services is projected to more than double, from INR 103 billion in 2004 to over INR 238 billion in 2009.

Systems integration and network integration make up a high growth-large size category within the IT services engagements. These services will continue to be prime drivers of the domestic IT services market in the enterprise segment due to the increasing growth in the enterprise application implementation and increased demand for network integration from telecom & banking verticals.

Domestic IT Services spending in key verticals:

A significant portion of the domestic corporate IT spends still lies in-house, predominantly driven by a perceived lack of focus by service providers on the domestic market and a perceived absence of value generated by outsourcing. It is estimated that in-house spending on IT services (including training costs, salaries of in-house IT staff and associated overheads) still accounts for more than half of the corporate IT spend in India, while the outsourced / vendor addressed spends account for just 45 percent of the total.

Large portion of the domestic IT budget is still lying inhouse, singal higher outsourcing

Breakups	2004	2005	2006	2007	2008	2009	CAGR
IT Consulting	4,784	5,669	6,775	7,774	9,109	10,674	17.4%
System Integration	34,011	42,979	51,900	62,065	72,960	85,399	20.2%
Application Development	13,997	17,115	19,852	22,586	25,113	27,924	14.8%
End-to-end Outsourcing	6,328	8,221	10,247	12,343	14,344	16,850	21.6%
Discrete Outsourcing	16,731	21,055	25,819	31,401	36,262	41,509	19.9%
Deploy and Support	23,631	28,321	32,907	37,651	42,510	48,,186	15.3%
IT Education and Training	4,126	4,879	5,609	6,534	7,260	8,067	14.3%
Grand Total	103,606	128,239	153,109	180,354	207,559	238,607	18.2%

Source: IDC, 2005

A large proportion of the current IT services market is predicated on the banking, financial services and telecom verticals. While IT services for these verticals will continue to show strong growth, new verticals will need to be developed to increase the rate of growth of the IT services market in India.

As the Indian economy opens further opens up, other verticals including manufacturing, travel and tourism, healthcare, entertainment will increasingly look towards IT to increase competitiveness. For both new and existing verticals, the small and medium business (SMB) segment will represent an important source of growth for the domestic IT services market.

Business Divisions

Paradyne Infotech offers an array of services to meet the specific needs of industries like Banking & Finance, Education & Research, e-Governance, Manufacturing & Retail, Health Care and Telecom.

The company provides tailor made solutions to address the information needs of these industries and within that to focused areas. Paradyne's key core areas are e-Commerce, Business Intelligence, Business Process Management (BPM) and Customer Relationship Management (CRM).

Application Software Services:

Paradyne's offering addressed to varied industries and clients's need

Paradyne's software services give a complete road map to the business process that helps customers to meet their current and future business requirements, which eventually increases efficiency & productivity. Paradyne provides end-to-end solutions for business processes and effectively optimizes the productivity of its clients. Paradyne has a world-class software development centre at MBP IT Park, New Bombay. In today's fast-paced, result oriented world, with its experience and expertise, Paradyne understands business requirements of clients. Multiple skills and competencies combine to realize technology-driven business transformation to provide company-wide solutions that accelerate business growth.

Paradyne's Application Software Services are focused on the following core areas Product Development & Application Development Business Process Management (BPM) Customer Relationship Management (CRM)

Paradyne follows a Software Quality Assurance (SQA) plan that adheres to quality assurance needs at every phase of the software development life cycle. The SQA Plan establishes a uniform software development process, which is applicable throughout the software development life cycle. The quality of the software development work has superlative degree of standards ensured by stringent quality checks.

Technology Infrastructure Management Services (TIMS):

This SBU aims to deliver the most appropriate technology solutions as per the business requirement. The services provided shorten the timeline and offer significant cost advantage in terms of technology management. Paradyne optimizes the IT Infrastructure by improving operation efficiencies. The customer care ensures that systems are running optimally through out the life cycle of the services availed of by the clients. The purpose of TIMS provided by Paradyne is to augment the growth prospects of the client. The company has time and again proved its capabilities in this segment, which is perceptible in its experience record. The core competency of this division is in consulting and integration services and it caters to industry segments such as Banking & Financial, Educational & Research, e-Governance, Manufacturing & Retail, ISV's and Telecom.

Paradyne's Technology Infrastructure Management Services include:

- IT Consultancy Services
- Facilities Management Services
- Networks Management Services
- Remote Management Service
- Disaster Recovery Management Service
- Maintenance Services
- Application Management Services
- Database Management Services
- Server Management Services
- Security Services
- Storage Services

The company possesses the skills to come up with designs, which are complex in nature to satisfy unique challenges posed, by different industries and organizations.

Product Business: Poised to Attain Critical Mass

The company's product basket comprises FinWorQs and HrWorQ, which cater to the Banking Industry and the Human Resource function of an organization, respectively.

HrWorQ, is successfully running at many corporate on different technology platform

In the Banking & Financial services segment, the company has a niche market,. It caters to the small and mid size private sector banks and the Co-operative Sector banks. Although this segment is highly competitive, Paradyne is well positioned to take advantage of the growing 'IT consciousness' in this segment by capitalizing on its industry experience and quality of products and services.

HrWorQ, a complete suite of HR management system, is successfully running at many corporate on different technology platforms. With the outsourcing of Human Resource activities flourishing, HrWorQs will provide a major impetus to company's revenue, going forward.

The company's products have desired features of flexibility in terms of applications and technology, are based on advanced platforms, all this and more packaged into an attractive cost proposition.



HrWorQ provides a solution for a broad host of issues within the realms of Human Resource Management function, enabling the organization to expedite the business processes involved. HrWorQ enables users to put the right people in the right jobs, develop and reward top performers, retain key talent for the long term, and increase efficiency and operating performance throughout your organization HrWorQ provides an extensive workflow for transforming HR operations. With HrWorQ, users can: Streamline your HR systems Deploy employee and manager self-service to facilitate increased efficiencies, reduced costs, and a paperless work environment. HrWorQ self-service applications deliver secure, role-based information and transactions across the enterprise.

HrWorQ aligns the user's workforce with corporate goals and objectives. It drives organizational performance through workforce analytics and organizational development applications that cultivate and earning and manage performance.

Paradyne's HrWorQ Offering:



Source: Company

Financials Services: Banking Products



FinWorQs empowers banks to transform their business leveraging agile, new generation technologies.

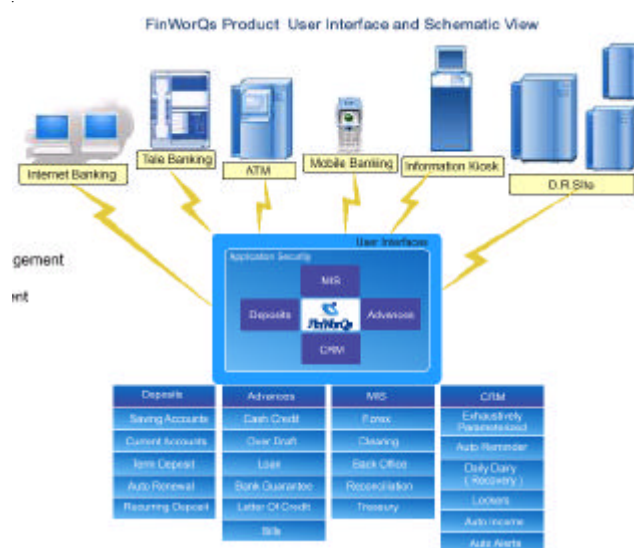
Paradyne's domain expertise and quality conscious approach enables it to cater to the myriad requirements of the Banking industry with its cutting edge technology. FinWorQs is an integrated, enterprise banking system designed to provide a state of the art Centralized Banking Solution for the global banking industry. This complete solution is centralized and provides a new generation IT architecture for the e-age. FinWorQs, the cutting edge technology with an advantage of functional domain expertise and highest quality standards is a most suitable mix, offered by Paradyne to Banking Industry. FinWorQs is developed with the philosophy of parameterized flexibility to have independency of authority / access for users, to cater the every changing requirements of banking customers.

FinWorQs is a completely centralized, customer centric, fully integrated solution addressing the needs of Foreign Banks, Nationalized Banks and Co-operative Banks. Based on open systems, this extensively parameterized user-friendly banking solution is brought to banking industry by Paradyne.

FinWorQs, core-banking solution from Paradyne, empowers banks to transform their business leveraging agile, new generation technologies. FinWorQs addresses the core banking, treasury, wealth management, consumer and corporate e banking, mobile banking, alerts and cash management requirements of retail, corporate and global banks worldwide. It is a highly scalable new generation IT architecture solution that addresses both the back office and front office requirements of banks in a seamlessly integrated manner.

FinWorQs- Key Features

- Centralized Banking
- Retail Management
- Treasury Management
- Forex Management
- Customer Relationship Management
- Human Resource Management
- Mobile Banking
- Tele-banking
- ATM Management
- MIS Reporting



Source: Company

Paradyne Alliances: Building Collaborative Partnerships Model



Paradyne has strategic relationship with Oracle for Customized Package development based on Oracle RDBMS. Paradyne is an Oracle Technology Partner (OTN), the highest level in Oracle's Technology. That level provides extensive developer support and certification to ensure that Paradyne's products that manage Oracle's family of products are always built upon the latest Oracle technologies and tested to ensure interoperability.

To strengthen the domain expertise, Industry and Services practices, Paradyne has partnered with several entities prominent in their respective industries, Geographies and technologies



Paradyne has strategic alliances with Global server computing giant Sun Microsystems as Platinum Partners and iForce Partners for their entire range of RISC, Java-based Solutions Enterprise solutions, I-planet and Storage Solutions as a privileged Sun ONE family member. Sun has awarded Paradyne the prestigious award of 'Outstanding Business Partner for Sun Microsystems'.



Paradyne Infotech is IBM's Premium Business Partner for their Intel Servers, Laptops, Desktops and Services. Paradyne has specialized in providing IBM solutions and have been successfully providing support on the entire range of IBM products.



Paradyne Infotech is the Partner of Cisco Systems for the entire range of its Networking products. Paradyne specializes in providing enterprise-net working solution to its customers and has a past history of successful implementation of Cisco solutions. Cisco end-to-end enterprise network solutions form the most comprehensive line of networking products available in the industry. From the branch office to the WAN and campus backbone, Cisco products are the leading choice of the enterprise.



Paradyne is a Premium Business Partner of Acer for their Intel based systems and Services offerings. Paradyne believes the strategic alliance with Acer will help it acquire the necessary technical support to prosper in the explosive global Internet and multimedia markets.



Paradyne is a Microsoft Certified Business Partner focused on providing technology solutions built on Microsoft Technologies to clients. Paradyne has experience in designing and deploying Microsoft Technology solutions and in Microsoft operating systems, collaborative solutions, security and operations and systems management platforms.

Key Clients: Diversified base, across industries

Paradyne offers comprehensive solutions focused on specific areas across various business verticals. The company's approach provides the clients with significant cost advantages by incorporating highest standards of efficiencies in their processes.

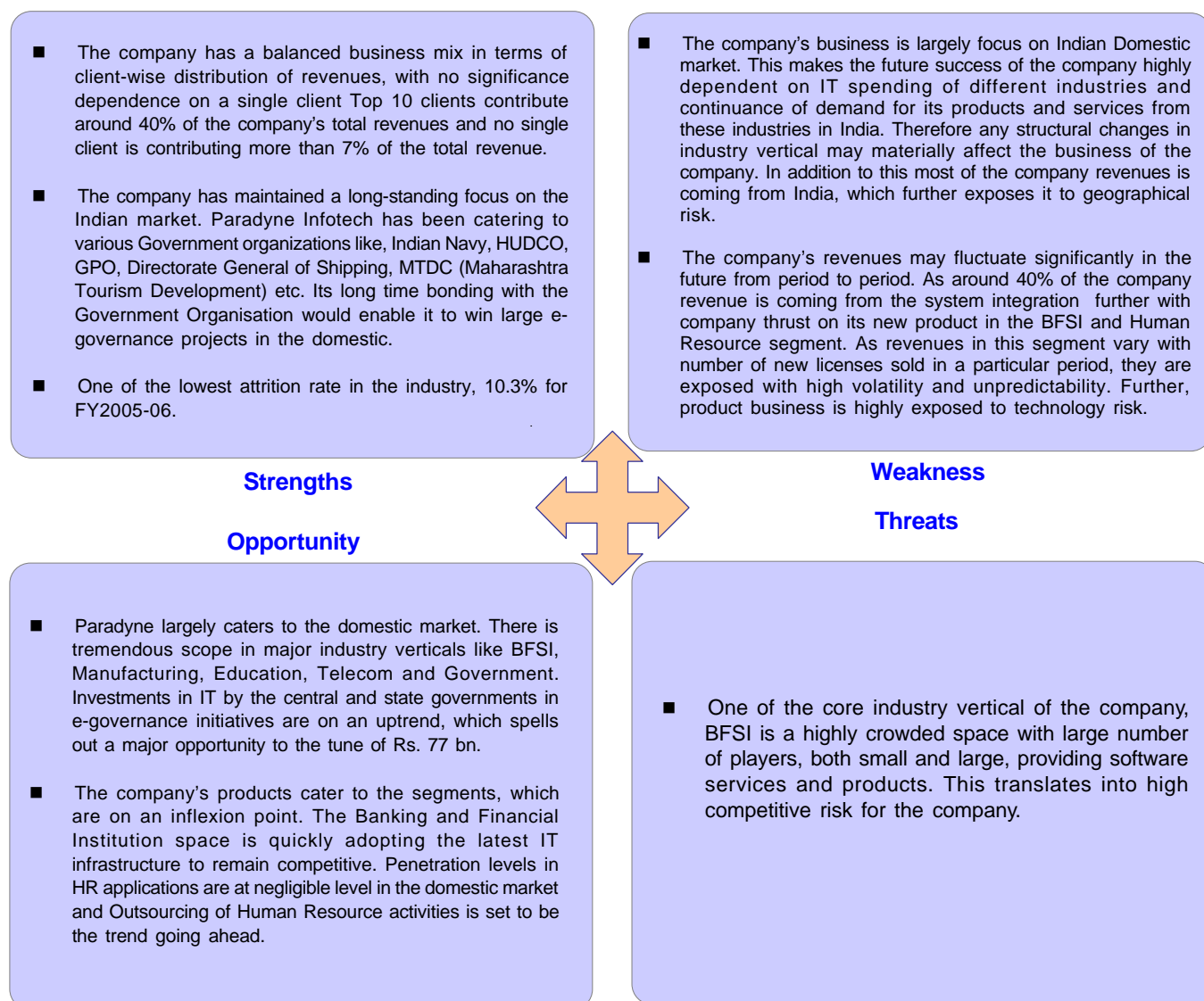
The following are the segment-wise list:

Paradyne's diversified clients base across verticals, no single clients contribute more than 7% of the revenue

Banking & Financial	Education & Research
JM Morgan Stanley IDBI Bank SIDBI Bank of India Corporation Bank Mandvi Bank The Ratnakar Bank Punjab National Bank NABARD Bank of Baroda	VNIT Nagpur Symbiosis Institute of Management Donbosco Institute of Technology Indira Gandhi Institute of Development & Research Lala Lajpat Rai Management Jai Hind College Shah & Anchor Kutchi Engg. College Maharashtra Institute of Technology Pune Engineering College Indian Institute of Tropical Meteorology
E-Governance	Telecom & Internet Ser. Providers
Income Tax Indian Navy HUDCO IRMRA TIFR MTDC MAHADA Mumbai Police EPF Organization Western Railways Food & Drugs Administration Maharashtra State	Reliance Infocomm Idea Cellular IOL Broadband MTNL ECI Telecom India Pvt. Ltd. Hathway Cable & Datacomm Hughes Telecom Broadllyne Infoservices
Independent Software Vendors	Manufacturing & Retail
Geometric Software Solutions KPIT Cummins BMC Software Zycus Infotech Eftia OSS Solutions 3D PLM Software Solutions Comsoft Infotech GCP Inc. Avenues Syntel Limited Sungard Offshore Services	Rochem Separations Systems Globus Stores ONGC Nimbus Communications UTV motion Pictures Samsara Shipping Mercator Lines Saigal Sea Trade National Insurance Co. Ltd. Outlook Publishing India Pvt. Ltd.

Source: Company

SWOT profile for PIL



Source: Emkay Private Client Research

Investment Positives:

Domestic IT spends on a sharp upswing: an unstoppable mega trend

Building end-to-end solutions capability, leveraging the Indian focus

Indian Information and Communications Technology (ICT) companies may be missing a significant opportunity by concentrating their efforts on India's much-hyped export market and failing to capitalize on the country's burgeoning domestic market. According to Gartner estimates, India continues to be the fastest growing ICT market globally with the market estimated to grow at a combined annual growth rate (CAGR) of 19% from 2004 through 2008. Though starting from a much smaller base, this is significantly faster growth than the second fastest growing ICT market in the world - China. Gartner estimates that ICT spending in India will surpass US\$54.8 billion by 2008E, a rise from US\$29.5 billion in 2004. Domestic demand for IT in India is witnessing a gradual transformation from being predominantly hardware driven towards a solutions oriented approach resulting in a growing emphasis on services.

The liberalization of Indian economic policy, de-regulation of key sectors and progressive moves towards further integrating India with the global economy has been a key driver of increased IT adoption in India. This is best reflected in the fact that most indigenous players in telecom and banking, two key sectors with significant multinational corporation (MNC) participation, have significantly upgraded their levels of IT adoption to offer best-in-class services comparable to those offered by the global competition, two sectors together account for approximately 35% to 40 % of the domestic spend on IT services. Competitive pressures in more recently deregulated service sectors such as airlines and insurance; the uptake in the manufacturing and industrial sectors; and the several large e-governance initiatives launched by the government under the National E-Governance Plan could provide further sustained growth in domestic demand for IT services over the next few years.

PIL enjoys a strong business presence in the Managed Services Space-

According to Nasscom, the domestic MSP (Managed Services Space) market from \$140 million in 2005 is well inroad to touch \$190 million in 2006. These figures are testimonial to the fact that the Indian market is moving towards an era of outsourcing services in the domestic space. As Paradyne is having a strong presence in the managed services space within the domestic market, these developments augur well for PIL.

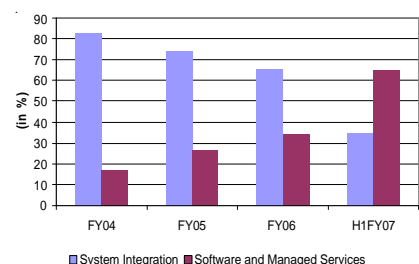
Well positioned in MSP, augur well to reap the higher spending coming from across the industries

On the other hand, with recent government initiatives to open Kiosks for the development of IT awareness in the semi rural and rural areas is another pleasant signal for the company's growth prospects since its services and solutions are well received in the areas of e-governance where it has already delivered some high quality projects under the domestic e-governance programme. As government is increasing its thrust to increase the IT spending in India coupled with industries are also increasing their IT investments, the growth prospects seems to be encouraging.

Paradyne has enjoyed a proven experience in the domestic IT arena in Managed Services space, with several illustrious client relationships in the Banking and Financials, Educations and Research, Telecom and ISP, e-governance, Manufacturing, Retails and Independent Software Vendors.

Some of these marquee clients in their respective fields are JM Morgan Stanley, SBI, IDBI Bank, Corporation Bank, Punjab & Maharashtra Bank, Reliance Infocomm, Idea Cellular, IOL Broadband, MTNL, Hathway Cable & Datacomm, Hughes Telecom, and Broadlyne Infoservices, Indian Navy, HUDCO, IRMRA, TIFR, GPO, MTDC, MAHADA, Mumbai Police, EPF Organization and Directorate General of Shipping, Globus, ONGC Etc. Developing these existing client relationships and taking good referrals from them for further business development can keep volumes ticking for the company in the coming years

Business Model Transformation



Source: Company and Emkay Private Client Research

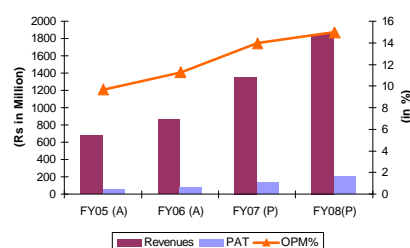
EBITDA Margins on a northward move, from 6% in FY04 to 12% in FY06-In the last three financials years preceding FY06, with management focussed approach in ramping up the high margin Managed Services business and Products business and to reduce the contribution of System integrations revenue, has been reflected in the 520bps-operating margin expansion to 11.3% for FY07 vis a vis 6.5% in the FY04. The margin expansion was on the back of reduction in the system integration revenue, which stood at around 65% as compared to 84% in the year 2004. On the other hand, for the H1FY07, the EBITDA margins further improved to 15.2%, as system integration now accounts for less than 40% of revenue.

Going forward, as Paradyne is now more focusing on high margin Managed Services business and steadily ramping up its products in BFSI and HR space coupled with strong order build-up seen in e-governance, manufacturing, energy, education and telecom space, augurs well for the company growth visibility and higher profitability in the coming years.

On the other hand, with company's strategy to capture mid-cap and co-operative banks that can't match the budgets of large players like I-flex and Infosys, is expected to allow Paradyne create a niche market for itself. In addition to this, most banks either have age-old legacy or DOS-based systems. The kind of connectivity and the parameters that RBI has been pushing for mandate a move to core banking will provide a big opportunity for growth. The management of the company is optimistic, to increase the revenue contribution from this segment exponentially in the coming years, which further aid the company to improve its profit margin.

Financial Outlook

Financials: On an upward move



Source: Company and Emkay Private Client Research

Topline and Bottomline to grow at a CAGR of 46% and 67% between FY06A-08E-Paradyne Infotech has built a strong platform for growth with its strong execution skills and long standing relationships with clients. Hereon, Paradyne is well poised to reap the benefits of these initiatives, going forward with strong all-round momentum in domestic IT industry, with incremental spending coming from across the industries coupled with Paradyne suitable positioning in the domestic IT industry, we expect Paradyne to record a CAGR of 46% and 64% in revenue and net profit over FY06A-08E.

Exciting H1FY07 numbers: The PIL's management's continual endeavor in ramping up the Managed Services business coupled with strong traction in the company's banking and HR products business reflected in strong HFY07 numbers, with revenue growing by 34% to Rs 569 mn as compared to corresponding period previous year, whereas with 250bps expansion in the EBITDA margin to 14.8%, took net profit higher by 81% to Rs 62.1 mn. On the other hand, for Q2FY07, Paradyne clocked revenue of Rs 301 mn, EBITDA margin further improved to 15.2%, and net profit stood at 33.6mn.

High margin business ramp up to aid margin improvement- In the last three financials years preceding FY06, with management focussed approach in ramping up the high margin Managed Services business and Products business and to reduce the contribution of System integrations revenue, has been reflected in the 520bps-operating margin expansion to 11.3% for FY07 vis a vis 6.5% in the FY04. The margin expansion was on the back of reduction in the system integration revenue, which stood at around 65% as compared to 84% in the year 2004. On the other hand, for the H1FY07, the EBITDA margins further improved to 15.2%, as system integration now accounts for less than 40% of revenue.

Going forward, as Paradyne is now more focusing on high margin Managed Services business and steadily ramping up its products in BFSI and HR space coupled with strong order build-up seen in e-governance, manufacturing, energy, education and telecom space, augurs well for the company growth visibility and higher profitability in the coming years.

On the other hand, with company's strategy to capture mid-cap and co-operative banks that can't match the budgets of large players like I-flex and Infosys, is expected to allow Paradyne create a niche market for itself. In addition to this, most banks either have age-old legacy or DOS-based systems. The kind of connectivity and the parameters that RBI has been pushing for mandate a move to core banking will provide a big opportunity for growth. The management of the company is optimistic, to increase the revenue contribution from this segment exponentially in the coming years, which further aid the company to improve its profit margin.

Company's strategy to capture mid-cap and co-operative banks that can't match the budgets of large players, allow Paradyne create a niche market for itself

Inorganic initiatives on card, to fasten the growth pace- The Indian IT industry presents a mix of numerous challenges and immense opportunities, Paradyne with its diversified industry and offering is well poised to capitalise this opportunity. On the other hand, in order to spread its wings beyond Indian boundaries and Paradyne has already has a subsidiary in US, going forward Paradyne is likely to capitalize on this tremendous business opportunity in Indian as well as in the US market by pursuing a mix of organic and inorganic growth initiatives that will ensure greater penetration of the market and higher share of IT spending. Company is in the process of short listing companies for its inorganic growth initiatives in the US region and most probably it is going to finalize before end of FY07, which will give a fillip to the company to fasten its growth acceleration in the coming years. However, our current estimates do not factor any upside from the company's inorganic growth.

VALUATION

Business Outlook and Valuation – High growth visible

Over the years, Paradyne focussed growth strategy has reflected in substantial pick up in the revenue and profitability, in the last three financials years preceding FY06, revenue recorded a CAGR of 30% to Rs 867 mn for FY06, whereas substantial expansion in the EBITDA margin from 6.5% to 11.3%, has reflected in 64% CAGR in the net profit to Rs 73 mn.

Key Assumptions

Ajusted Beta	1.06
Risk Free Rate	7.50%
Market Risk Premium	7.00%
Cost of Equity	14.92%
Cost of Debt	10.00%
Debt	43.59
Equity	761.46
WACC	14.47%

Source:Emkay Private Client Research

NPV	1,358
Net debt	(80)
Value	1,438
Value/share	132
One year forward	150

Source:Emkay Private Client Research

The Paradyne stock trades at 4x FY08E an EV/EBITA of 2x on FY08E. We expect Paradyne to grow at a CAGR growth of 46% and 67% in revenue and net profits likely to touch Rs 1854 mn with net profits estimated at 203 mn respectively by FY08E.

We initiate a BUY on the stock with a price target of Rs 150 based on the DCF approach, at our target price the stock will be valued at 8x for FY08E.

DCF	FY07	FY08	FY09	FY10	FY11	FY12	FY13	FY14
PAT	136.47	202.77	270.80	283.94	288.60	274.53	269.28	263.32
Depreciation	18.31	25.09	36.15	41.58	43.65	45.84	47.21	48.63
Interest (1-tax rate)	10.70	14.67	19.09	18.59	17.57	15.57	14.43	13.38
Change in NWC	(90.52)	(78.98)	(90.03)	(58.52)	(22.43)	(23.55)	(14.84)	(15.28)
Capex	(40.00)	(40.00)	(60.25)	(69.29)	(87.31)	(76.40)	(62.95)	(48.63)
FCFF	13.56	94.21	137.58	179.11	204.95	204.85	224.27	234.66
Discounted Value	13.56	71.89	91.71	104.30	104.25	91.03	87.06	793.79

* Terminal value

Source: Emkay Private Client Research

The following grid gives a sensivity analysis based on diffrent scenarios

	WACC		
Terminal Growth	14.5%	16.5%	17.5%
3%	150	135	128
4%	159	140	133
5%	169	147	138

Source:Emkay Private Client Research

Profit & loss statement (Rs mn)

Year to Mar	FY05A	FY06A	FY07E	FY08E
Net Sales	685.1	867.3	1,352.9	1,854.0
% Growth	34.0	26.6	56.0	37.0
EBIDTA	66.1	97.9	189.4	278.1
% Growth	98.0	48.0	93.6	46.8
Other Income	0.2	7.3	2.2	3.0
Interest	4.2	9.7	12.6	17.3
Depreciation	3.7	10.6	18.3	25.1
PBT	58.3	84.9	173.3	256.0
% Growth	114.4	45.6	104.1	47.7
Tax	4.0	6.3	24.2	36.0
Adj PAT	50.4	73.0	136.5	202.8
% Growth	85.3	44.8	87.0	48.6
Dividend (%)	15.0	10.0	10.0	10.0
EPS (Rs)	6.7	6.7	12.5	18.6
BVPS (Rs)	7.1	7.7	14.2	20.9

Balance sheet (Rs mn)

Year to Mar	FY05A	FY06A	FY07E	FY08E
Eqty Cap	75.8	108.8	108.8	108.8
Reserves	39.2	184.1	320.8	521.9
Networth	115.0	292.9	429.5	630.7
Secured loans	34.6	43.1	43.1	43.1
Unsecured loans	0.5	0.5	0.5	0.5
Total loans	35.1	43.6	43.6	43.6
Total Liability	157.6	349.6	486.2	687.4
Net Block	61.5	81.0	102.7	117.6
Investments	20.5	20.5	20.5	20.5
Deffered Tax Assets	7.5	13.1	13.1	13.1
Inventory	20.5	20.5	20.5	20.5
Debtors	85.0	161.7	251.8	334.7
Cash balance	3.1	91.9	129.0	255.1
Other CA	10.2	19.7	32.3	39.8
Current Liabilities	28.7	33.9	51.7	70.0
Provisions	13.9	16.9	25.9	37.9
NCA	67.5	233.2	348.6	534.8
Total Assets	157.6	349.1	486.2	687.4

Ratio Analysis

Year to Mar	FY05A	FY06E	FY07E	FY08E
OPM %	9.7	11.3	14.0	15.0
NPM %	7.4	8.4	10.1	10.9
ROE %	52.2	35.8	37.8	38.3
ROCE %	50.0	37.3	44.5	46.6
Asset Turnover (x)	11.1	10.7	13.2	15.8
Avg. Collec. Period (Days)	44.7	67.1	67.0	65.0
Valuation ratios				
P/CF per share (x)	9.5	8.8	4.8	3.2
EV/Cash Profit (x)	13.9	25.5	14.8	11.9
EV/EBIDTA (x)	11.4	6.9	3.3	1.8
EV/Sales (x)	1.1	0.8	0.5	0.3
Mkt Cap/Sales(x)	7.6	5.8	3.2	2.8
CEPS (Rs)	7.1	7.7	14.2	20.9
P/ BV (x)	9.5	8.8	4.8	3.2

Cash Flow Statement (Rs mn)

Year to Mar	FY05A	FY06A	FY07E	FY08E
PAT	50.4	73.0	136.1	202.8
Depreciation	3.7	10.6	18.3	25.1
Change in WC	(9.6)	(78.0)	(75.9)	(60.1)
Operating CF	44.6	5.7	78.5	167.8
Capex	(57.5)	(29.3)	(40.0)	(40.0)
Misc Exp	(27.0)	(1.2)	-	-
Investing CF	(84.5)	(30.5)	(40.0)	(40.0)
Dividends	(10.7)	(12.4)	(1.6)	(1.6)
Debt	20.9	8.5	-	-
Investments	(0.0)	-	-	-
Financing CF	35.4	113.7	(1.6)	(1.6)
Net Change	(4.6)	88.9	36.9	126.1
Opening Cash	7.8	3.2	92.1	129.0
Closing Cash	3.2	92.1	129.0	255.1

Source:Emkay Private Client Research

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