

Equities

2 November 2011 | 8 pages

Patni Computer Systems (PTNI.BO)

Model Update

- We raise our CY10E/11E/12E earnings estimates by ~1-9% as we use revised currency forecasts of Rs. 48.5/47/46 for the rest of FY12/FY13/FY14 respectively. We also incorporate Q3CY11 results and make small changes to our pricing/volume/cost assumptions. We raise our target price to Rs305 (maintaining our earlier target multiple). Margin recovery is the key to watch for. We remain Sellers.

- Company Update
- Target Price Change
- Estimate Change

Sell	3
Price (02 Nov 11)	Rs333.20
Target price	Rs305.00
	<i>from Rs280.00</i>
Expected share price return	-8.5%
Expected dividend yield	1.5%
Expected total return	-7.0%
Market Cap	Rs44,707M
	US\$907M

Price Performance (RIC: PTNI.BO, BB: PATNI IN)



Statistical Abstract

FYE	Net Profit	EPS	P/E	D. Yld
31 Dec	(RsM)	(Rs)	(x)	(%)
2008A	4,433	34.49	9.7	0.9
2009A	5,720	43.10	7.7	0.9
2010A	6,017	44.73	7.4	18.9
2011E	3,023	22.32	14.9	1.5
2012E	3,692	27.25	12.2	1.8
2013E	4,541	33.52	9.9	2.1

Source: Powered by dataCentral

Earnings Revision

FYE	Net Profit	EPS	%	DPS
31 Dec	(RsM)	(Rs)	chg	(Rs)
2011E	3,023	22.32	9.4	5.00
Prev	2,766	20.39		5.00
2012E	3,692	27.25	6.7	6.00
Prev	3,465	25.54		6.00
2013E	4,541	33.52	0.7	7.00
Prev	4,515	33.28		7.00

Source: Powered by dataCentral

Surendra Goyal, CFA

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Fiscal year end 31-Dec	2009	2010	2011E	2012E	2013E
Valuation Ratios					
P/E adjusted (x)	7.7	7.4	14.9	12.2	9.9
EV/EBITDA adjusted (x)	4.2	4.3	5.7	4.4	3.5
P/BV (x)	1.2	1.4	0.7	0.6	0.6
Dividend yield (%)	0.9	18.9	1.5	1.8	2.1
Per Share Data (Rs)					
EPS adjusted	43.10	44.73	22.32	27.25	33.52
EPS reported	43.10	44.73	22.32	27.25	33.52
BVPS	269.45	239.07	499.78	520.30	545.99
DPS	3.00	63.00	5.00	6.00	7.00
Profit & Loss (RsM)					
Net sales	31,620	31,688	35,551	38,521	43,023
Operating expenses	-26,317	-26,672	-32,495	-34,675	-38,335
EBIT	5,303	5,016	3,057	3,846	4,688
Net interest expense	0	0	0	0	0
Non-operating/exceptionals	657	1,877	962	1,246	1,367
Pre-tax profit	5,960	6,894	4,018	5,092	6,055
Tax	-240	-877	-996	-1,400	-1,514
Extraord./Min.Int./Pref.div.	0	0	0	0	0
Reported net income	5,720	6,017	3,023	3,692	4,541
Adjusted earnings	5,720	6,017	3,023	3,692	4,541
Adjusted EBITDA	6,474	6,165	4,896	6,094	7,041
Growth Rates (%)					
Sales	-0.6	0.2	12.2	8.4	11.7
EBIT adjusted	27.5	-5.4	-39.1	25.8	21.9
EBITDA adjusted	23.1	-4.8	-20.6	24.5	15.5
EPS adjusted	25.0	3.8	-50.1	22.1	23.0
Cash Flow (RsM)					
Operating cash flow	4,263	4,337	3,565	4,093	5,913
Depreciation/amortization	1,171	1,149	1,839	2,249	2,354
Net working capital	-1,484	-1,945	-554	-801	185
Investing cash flow	169	840	-35,290	-1,490	-2,770
Capital expenditure	-689	-402	-3,464	-2,381	-3,273
Acquisitions/disposals	371	-447	-30,754	0	0
Financing cash flow	1,200	-9,325	32,605	-941	-1,098
Borrowings	-5	2	0	0	0
Dividends paid	-452	-9,614	-784	-941	-1,098
Change in cash	5,633	-4,148	879	1,663	2,046
Balance Sheet (RsM)					
Total assets	41,815	39,101	78,008	81,294	85,657
Cash & cash equivalent	20,384	16,236	17,115	18,777	20,823
Accounts receivable	0	0	0	0	0
Net fixed assets	6,850	6,103	7,729	7,861	8,780
Total liabilities	7,152	7,748	11,027	11,562	12,483
Accounts payable	0	0	0	0	0
Total Debt	4	6	6	6	6
Shareholders' funds	34,662	31,353	66,981	69,731	73,175
Profitability/Solvency Ratios (%)					
EBITDA margin adjusted	20.5	19.5	13.8	15.8	16.4
ROE adjusted	18.3	18.2	6.1	5.4	6.4
ROIC adjusted	32.5	24.6	5.7	4.4	5.6
Net debt to equity	-58.8	-51.8	-25.5	-26.9	-28.4
Total debt to capital	0.0	0.0	0.0	0.0	0.0

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Patni Computer Systems

Company description

Patni is a mid-tier Indian IT solutions provider and a pioneer of offshore IT services delivery. Founded in 1978, it operated both software and hardware businesses until 1999, when the hardware business was de-merged. It continues to operate as a global consulting and IT services provider. Recently, iGate acquired a majority stake in the company. Patni employs more than 18,000 professionals, who service about 300 global corporations. It has a sizeable presence in insurance, financial services, manufacturing and telecoms verticals. GE is Patni's largest customer, contributing to ~11% of revenues.

Investment strategy

Our Sell (3) rating is based on a challenging outlook for tier-II IT companies, Patni's poor performance over many quarters and that the turnaround in margins may take time to play out. We are positive on the management change and focus but it will take time before things improve. Valuations are in line with other mid-tier companies and with the historical average (~12x 1-year forward compared to 5-year average of ~11x). In a tough environment, investors will wait for margin improvement to be visible. We expect ~10% revenue CAGR over CY10-13E.

Valuation

Our target price of Rs305 is based on 11x Jun'12E EPS based on slower revenue growth and macro uncertainty. This is close to the midpoint of the ~2-23x band that the stock has traded in over the past three-years. We believe that this is justified given that high cash on books balances the business risks due to the environment. We believe PE is the most appropriate valuation measure to value the stock given Patni's track record in profitability.

Risks

The key upside risks to our investment thesis on Patni are: (1) uptick in growth rates; (2) Improving trends on margins; (3) any significant depreciation of the rupee against the USD/EUR/GBP; and (4) sharp recovery in the US economy. If the impact of any of these upside risks is greater than we anticipate, the stock could exceed our target price.

Appendix A-1

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Patni Computer Systems (PTNI.BO)

Ratings and Target Price History

Fundamental Research

Analyst: Surendra Goyal, CFA

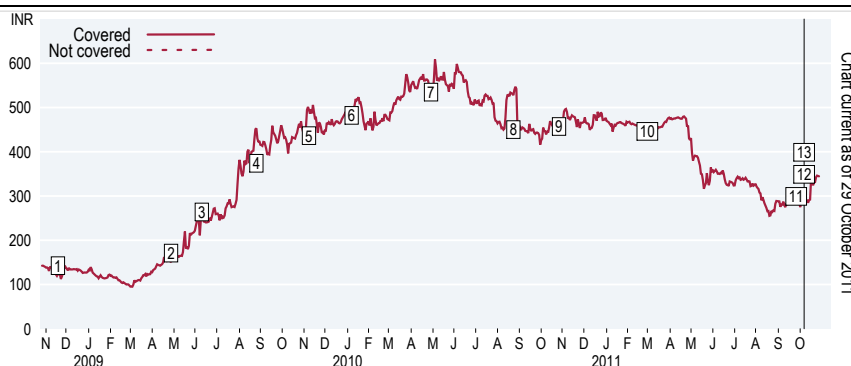


Chart current as of 29 October 2011

	Date	Rating	Target Price	Closing Price
1	19-Nov-08	3H	*125.00	123.45
2	28-Apr-09	3H	*150.00	150.40
3	10-Jun-09	3H	*240.00	259.90
4	26-Aug-09	*3M	*440.00	452.95
5	9-Nov-09	3M	*470.00	494.55

* Indicates change

	Date	Rating	Target Price	Closing Price
6	7-Jan-10	3M	*525.00	498.20
7	29-Apr-10	3M	*545.00	534.80
8	24-Aug-10	3M	*520.00	527.90
9	27-Oct-10	3M	*465.00	465.30
10	1-Mar-11	3M	*445.00	450.85

	Date	Rating	Target Price	Closing Price
11	27-Sep-11	3M	*280.00	295.50
12	7-Oct-11	Stock rating system changed		
13	7-Oct-11	*3	280.00	287.80

Rating/target price changes above reflect Eastern Standard Time

Patni Computer Systems (PTNI.BO)

Ratings and Target Price History

Best Ideas Research

Relative Call (3 Month)

Analyst: Surendra Goyal, CFA

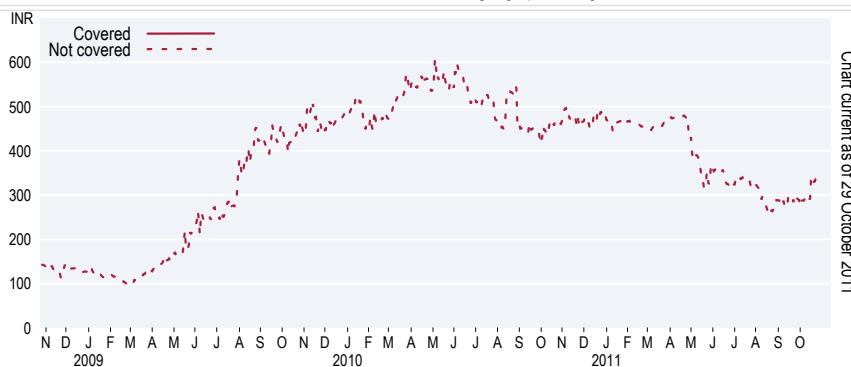


Chart current as of 29 October 2011

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	45%	42%	37%	50%	43%	46%

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