



Patni Computer Systems-the iGate deal

BUY

CMP: Rs.457

Target Price: 583

Industry: Information Technology

Stock Info		BSE Group		Shareholding Pattern (30 th Sept.'10)	
Market Capital	Rs.5928 cr	BSE Code	B/BSE200	Promoters	45.9%
Free float	Rs. 2371 cr	NSE Symbol	532517	Domestic Institutions	4.0%
Equity Capital	Rs.26.2cr	Bloomberg	PATNI IN	Foreign Institutions	42.3%
Avg. Trading Vol.	248298 (Qty)	Reuters	PTNI.BO	Non Promoters Corp.	3.7%
52 WK High/Low	550/385	BSE Sensex	19224	Public & Others	4.2%
Face Value	Rs. 2	NSE Nifty	5762	Govt. Holdings	0.0%

Highlights of the Patni-iGate deal

What's the deal?: Patni Computer Systems' search for a buyer ended with the Promoter's group and General Atlantic Mauritius agreeing to sell off their combined 63% stake to iGate for a consideration of Rs.503.5 per share (total~\$921mn). A further \$299mn will be used to buy shares in the mandatory open offer of 20% thus bringing the total transaction size to \$1.22bn. The deal brings together two highly recognised IT companies with complementary service offerings. An important point to be noted is that there is no 'Non-compete agreement' as speculated by the media.

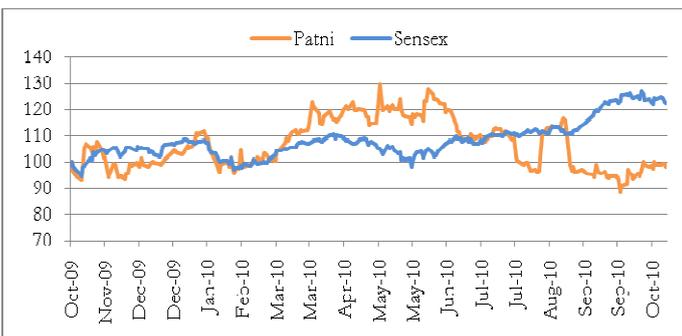
How it is being funded?: iGate will be funding the deal through a mix of debt and equity. It will be issuing equity to PE firm Apax Partners in the range of \$270-480mn (depending on the success of the open offer). Secondly, iGate will also be taking debt of \$700mn along with \$50mn revolving line of credit.

What has iGate to offer?: With ex-Infoscion Phaneesh Murthy at the helm of affairs, iGate has 7 global delivery centres, and offices in 16 countries. It has employee strength of 8,278 and revenues of \$252mn for the 12 month ended 30th September, 2010. It is a classic case of a small fish gobbling down a bigger fish, making it an unique transaction in the Indian IT sector. Also, going by Murthy's track record, one can expect more strength coming in the sales and marketing front, which in turn may help Patni to overcome its' client mining problems as well as become more aggressive. This is positive for Patni as it is likely to push it in catching up with the industry growth rates.

What has Patni to offer?: One of the oldest software company in India, Patni has 22 global delivery centres, offices in 30 locations worldwide, 282 customers and an employee strength of 16,556. The company reported total revenue of \$689mn in the 12 months period ended 30 September, 2010. Thus, the combined entity will have a total revenue of around \$1 bn which will make it eligible to bid for larger and long-term projects. We also believe that Patni's focus on micro-verticals as well as its experience in execution will go a long way in strengthening iGate solutions in the banking as well as other space where it has presence.

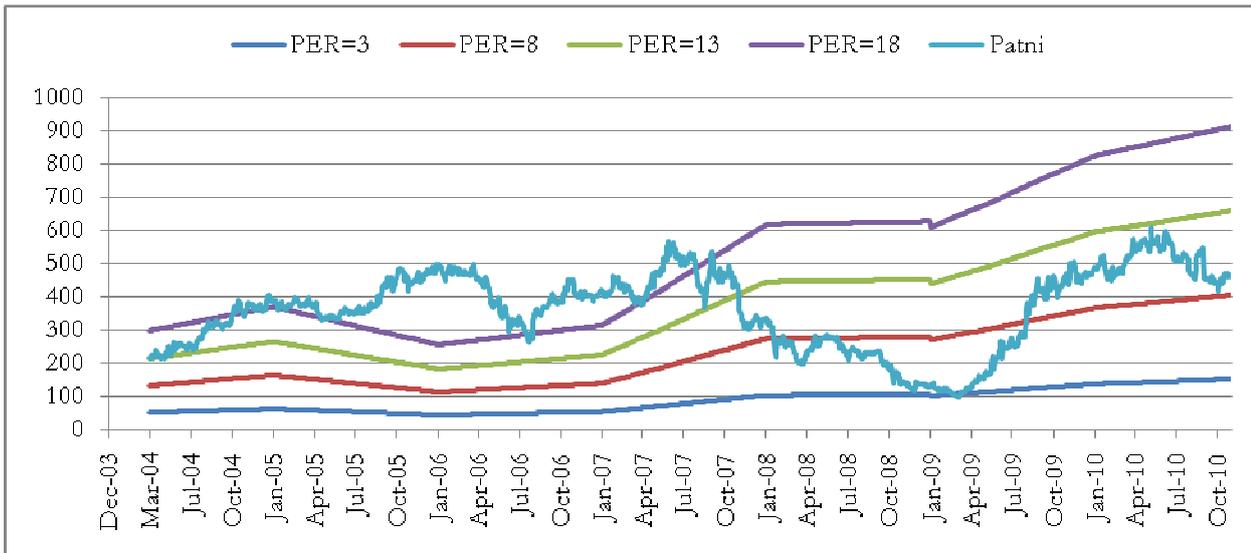
Any worries?: As we have mentioned previously, this is the first instance in the Indian IT sector that a small company is taking over a bigger one and therefore it remains to be seen how things pan out specially on the attrition front. With attrition at its' peak and uncertainty looming large on how well the two companies gets integrated, one has to keep an eye on what steps the management takes to retain talent.

Our view: We believe that the deal is positive for Patni in the medium to long-term. The merged entity will be in a position to grab a larger share of its' clients' wallet and compete better with larger peers. iGate will also bring a certain level of aggressiveness as well as stability into Patni which has long been missing, which we believe can be partly attributed to the uncertainty on the ownership front. Though, there are headwinds in the form of integration issues and employee adjustments, we believe at the same time, that a number of positives like higher cross-selling opportunities will also come in. We are therefore maintaining our target price at Rs.583 per share and reiterate our "Buy" call on the stock as at current market price it is available at cheap valuations. We have arrived at the target price by assigning a PE multiple of 13x to our CY11E EPS estimates.



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

PE Band



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>
<i>EPS</i>	<i>32.3</i>	<i>45.7</i>	<i>43.2</i>	<i>44.9</i>

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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