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FIRST LIGHT

29 April 2022

RESEARCH

Persistent Systems | Target: Rs 4,880 | +13% | HOLD

Stellar, all-round performance

Power

Expert call – Power shortage to persist near term

Daily macro indicators

Indicator	26-Apr	27-Apr	Chg (%)
US 10Y yield (%)	2.72	2.83	11bps
India 10Y yield (%)	7.05	7.08	3bps
USD/INR	76.58	76.53	0.1
Brent Crude (US$/bbl)	105	105.3	0.3
Dow	33,240	33,302	0.2
Hang Seng	19,935	19,946	0.1
Sensex	57,357	56,819	(0.9)
India FII (US$ mn)	**25-Apr**	**26-Apr**	**Chg ($ mn)**
FII-D	(91.4)	(57.2)	34.2
FII-E	(344.6)	13.6	358.2

Source: Bank of Baroda Economics Research

SUMMARY

Persistent Systems

- Q4 revenue growth of 9.1% QoQ USD outperformed estimates led by services business; TCV at US$ 361mn rose 8% QoQ
- EBIT margin flattish QoQ at 14% and guided to remain at this level in FY23. Attrition under control, declining 30bps QoQ
- We raise FY23/FY24 EPS ~8% to bake in the strong services growth and margin beat; on rollover, our TP rises to Rs 4,880 (vs. Rs 4,580) – HOLD

Click here for the full report.

Power

- India's ongoing power crisis stems from a coal shortage due to inadequate planning; situation to continue till hydropower ramps up
- Long-term, renewables' share in the power mix must rise from the current 9%; critical to address issues of battery and supply storage
- No viable near-term solution for distribution woes given socio-political challenges to distribution reforms

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RESULT REVIEW

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HOLD
TP: Rs 4,880 | ⮝ 13%

PERSISTENT SYSTEMS | Technology & Internet | 28 April 2022

Stellar, all-round performance

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Performance beats estimates: PSYS reported Q4FY22 revenue growth of 9.1% QoQ USD (6.8% organic growth), ahead of consensus as well as our optimistic estimate of 7.7%. Growth was led by the services segment while IP volatility continued (-27%). The company did well across verticals, with revenue from major segments rising by high single digits QoQ. BFSI led the way (+9.8% QoQ USD), aided by the SCI and Shree Partners' acquisitions. However, top client revenue contracted 12.7% QoQ USD due to IP contract restructuring. Overall, top-5 client revenues contracted 1.7%. TCV at US$ 361mn grew 8% QoQ. New business formed 54% of TCV, up from 47% in Q3, pointing to a strong demand climate.

Margin flattish: EBIT margin at 14% was flat QoQ (vs. our estimate of 13.3%) despite the widespread talent supply crunch. Employee cost increased slightly but was offset by reduction in SG&A expense as % of revenue. Strong employee addition caused utilisation to moderate to 80.6%, after two quarters of high prints.

Attrition stable: Attrition at 26.6% was down 30bps QoQ. PSYS is the first company to report lower sequential attrition rates in Q4. Management believes employee churn will be elevated for the next few quarters before tapering down. The company hired 1,610 employees QoQ (700 from inorganic additions).

Acquisition update: PSYS acquired five companies in FY22, viz. SCI, Shree Partners, Data Glove, MediaAgility and Sureline, which will drive enhanced cloud capabilities and stronger partnerships with cloud hyperscalers. Integration of Data Glove is proceeding per expectations. The SCI and Shree Partners buyouts have already opened up multiple new leads in the payments segment. PSYS will continue to target tuck-in acquisitions that strengthen any of its verticals, geographies or service lines.

Maintain HOLD: Management expects EBIT margin to remain at 14% in FY23 due to high employee costs, pay hikes and rising amortisation cost (from multiple acquisitions). We raise FY23/FY24E EPS estimates by ~8% each to bake in the Q4 outperformance and roll valuations forward to Jun'23, leading to a new TP of Rs 4,880 (vs. Rs 4,580), set at an unchanged 40.1x P/E. Retain HOLD.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	PSYS IN/Rs 4,309
Market cap	US$ 4.5bn
Free float	70%
3M ADV	US$ 18.0mn
52wk high/low	Rs 4,988/Rs 1,926
Promoter/FPI/DII	30%/26%/44%

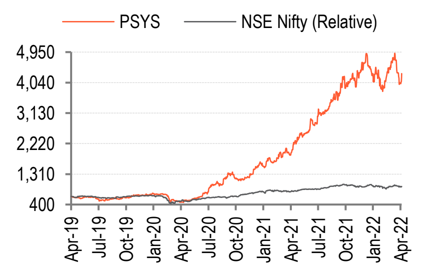
Source: NSE | Price as of 28 Apr 2022

Key financials

Y/E 31 Mar	FY22A	FY23E	FY24E
Total revenue (Rs mn)	57,108	76,929	86,553
EBITDA (Rs mn)	9,582	13,121	14,475
Adj. net profit (Rs mn)	6,904	8,486	9,994
Adj. EPS (Rs)	86.6	106.4	125.3
Consensus EPS (Rs)	83.7	101.7	124.4
Adj. ROAE (%)	22.4	23.2	23.2
Adj. P/E (x)	49.8	40.5	34.4
EV/EBITDA (x)	35.8	26.3	24.0
Adj. EPS growth (%)	53.2	22.9	17.8

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE

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POWER

28 April 2022

Expert call – Power shortage to persist near term

- **India's ongoing power crisis stems from a coal shortage due to inadequate planning; situation to continue till hydropower ramps up**
- **Long-term, renewables' share in the power mix must rise from the current 9%; critical to address issues of battery and supply storage**
- **No viable near-term solution for distribution woes given socio-political challenges to distribution reforms**

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We hosted a call with power sector expert Arun Kumar to discuss the current challenges facing the sector. Key takeaways:

Power deficit to continue in short term: India's current power shortage has arisen because coal production has not kept pace with the growing demand – FY21 production levels were similar to those in FY17. Power demand had been weak since 2019 owing to reduced economic activity during two years of Covid-19 lockdowns. However, with the economy reopening in full swing, heatwaves across various regions of India and no new coal plant additions, supply is falling short of demand. Spot prices have soared amid the current shortage, with the regulator intervening to cap prices at Rs 12/unit. This deficit will continue till June when the monsoon begins and hydro capacities enter into the mix. With normal monsoons forecast this year, hydro output is expected to be healthy.

Higher renewables in the mix the only way forward: From a medium-to-long-term perspective, the share of renewables in India's power mix must rise from the current 9%. Solar currently dominates the green energy mix with a 48% share followed by wind at 38%. The key challenge with renewables is the variable supply curve, even as load patterns have changed from evening peak load to peaks during the day. Hence, it is critical to address the issues of battery and supply storage to ensure uninterrupted power supply.

No near-term solution for distribution woes: Despite a series of revival schemes and bailout packages, distribution remains a problem area for the power sector as it lacks payment discipline. This is primarily because states don't want to cede control and there is a lack of political will to reform the segment. Moreover, previous privatisation and PPP attempts have often failed to meet desired parameters as, political will aside, public support is also lacking for many of the changes needed in the distribution space.

Disclaimer: The information in this report represents the personal views and opinions of the power sector expert and does not necessarily reflect the views and opinions of his past or present employers.

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Recommendation scale: Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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