

HOLD

TP: Rs 2,920 | ▼ 4%

PERSISTENT SYSTEMS | IT Services

| 24 July 2021

An all-round growth beat; upgrade to HOLD

- PSYS reported stellar Q1FY22 numbers with dollar revenue growth of 9.1% QoQ (incl. Capiot) driven by BFSI and healthcare
- EBIT margin at 13.5% was broadly in line with our/consensus estimates. TCV stood at a robust US\$ 245mn
- We upgrade to HOLD (V/s SELL earlier) and roll over to a new Jun'22 TP of Rs 2,920 (vs. Rs 1,340), set at a higher 30x P/E

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Stellar growth: PSYS reported 9.1% QoQ USD revenue growth, ahead of our estimate of 5.9%. This was the company's best first-quarter growth rate, albeit aided by Capiot acquisition revenue. EBIT margin stood at 13.5%, up 40bps QoQ, in line with our estimate of 13.6%. Increased visa costs and higher attrition limited further margin gains. Offshore revenue share increased 80bps QoQ to 55.5%.

Broad-based traction across markets and verticals: Geography-wise, revenue growth was fuelled by India/North America at 17.2%/8.7% QoQ. The strong performance in India was backed by multi-year transformation deals with mid-tier NBFCs. Among verticals, BFSI and healthcare & life science both grew in double digits at 11.7% and 15.9% respectively. Alliance business performed well as the top client grew 3.7% QoQ. PSYS's top 10 clients grew 10.1% QoQ.

Strong TCV maintained: TCV stood at US\$ 244.8mn, including new contracts worth US\$ 147.7mn. ACV was at US\$ 188.8mn. The company saw key wins across verticals such as software, hi-tech & emerging industries, BFSI and healthcare & life sciences. Most of these deals have a long tenure and are centered around core transformation and cloud migration.

Attrition shoots up amid supply constraints: A total of 1,224 employees (400 freshers) were hired in Q1FY22. Attrition surged to 16.6% vs. 11.7% in Q4FY21 given increased demand for digital skills in the industry. PSYS has launched several initiatives to combat the rising attrition, including flexible working hours and salary hikes (due in Q2), besides ramping up hiring with plans to recruit 2,000 freshers in FY22. Utilisation remained high at 80%+ levels.

Upgrade to HOLD: Incorporating the stellar Q1 print and all-round positive outlook, we raise FY22/FY23 EPS estimates by 15%/31% and increase our target one-year forward P/E from 19x to 30x (inline with target valuation multiple for LTI) – this yields a higher Jun'22 TP of Rs 2,920 (vs. Rs 1,340). With stellar start in Q1, PSYS is in strong position to clock industry leading growth in FY22. Upgrade to HOLD V/s SELL earlier.

Key changes

Target	Rating
▲	▲

Ticker/Price	PSYS IN/Rs 3,039
Market cap	US\$ 3.3bn
Free float	70%
3M ADV	US\$ 7.7mn
52wk high/low	Rs 3,130/Rs 725
Promoter/FPI/DII	30%/26%/44%

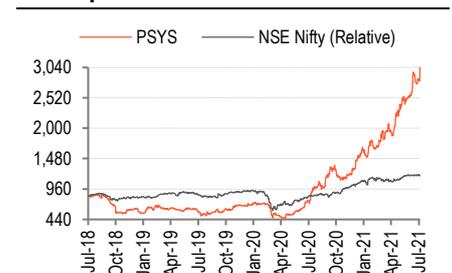
Source: NSE | Price as of 23 Jul 2021

Key financials

Y/E 31 Mar	FY21P	FY22E	FY23E
Total revenue (Rs mn)	41,879	54,654	64,905
EBITDA (Rs mn)	6,830	8,765	11,084
Adj. net profit (Rs mn)	4,507	5,899	7,294
Adj. EPS (Rs)	56.5	74.0	91.4
Consensus EPS (Rs)	56.5	76.3	91.7
Adj. ROAE (%)	17.1	19.9	21.5
Adj. P/E (x)	53.8	41.1	33.2
EV/EBITDA (x)	35.4	27.5	21.7
Adj. EPS growth (%)	32.4	30.9	23.6

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

Stock performance



Source: NSE



Fig 1 – Quarterly performance

(Rs mn)	Q1FY22	Q1FY21	YoY (%)	Q4FY21	QoQ (%)	FY21	FY20	YoY (%)
Revenue (US\$ mn)	166.8	131.0	27.3	152.8	9.1	587	502	17.0
Revenue	12,299	9,914	24.1	11,134	10.5	43,424	35,658	21.8
Operating Expenditure	10,284	8,449	21.7	9,250	11.2	36,404	30,729	18.5
Cost of revenues	8,173	6,646	23.0	7,363	11.0	28,759	23,494	22.4
as % of sales	66.5	67.0	-	66.1	-	66.2	65.9	-
SG&A expenses	2,111	1,803	17.1	1,887	11.9	7,644	7,234	5.7
as % of sales	17.2	18.2	-	17.0	-	17.6	20.3	-
EBITDA	2,015	1,464	37.6	1,883	7.0	7,021	4,930	42.4
Depreciation	350	436	(19.6)	419	(16.5)	1,645	1,660	(0.9)
EBIT	1,665	1,029	61.9	1,464	13.7	5,376	3,270	64.4
Other Income	366	192	-	385	-	1,020	1,254	-
PBT	2,031	1,220	66.4	1,849	9.8	6,396	4,523	41.4
Total Tax	518	320	61.7	471	9.9	1,665	1,121	48.6
Adjusted PAT	1,513	900	68.1	1,378	9.8	4,731	3,403	39.0
(Profit)/loss from JV's/Ass/MI	-	-	-	-	-	0	0	-
APAT after MI	1,513	900	68.1	1,378	9.8	4,731	3,403	39.0
Extra ordinary items	0	0	-	0	-	0	0	-
Reported PAT	1,513	900	68.1	1,378	9.8	4,731	3,403	39.0
Reported EPS	18.9	11.3	68.1	17.2	9.8	56.3	43	32.4
Margins (%)			(bps)		(bps)			
EBITDA	16.4	14.8	161	16.9	(53)	16.2	13.8	234
EBIT	13.5	10.4	316	13.2	39	12.4	9.2	321
EBT	16.5	12.3	420	16.6	(9)	14.7	12.7	204
PAT	12.3	9.1	322	12.4	(7)	10.9	9.5	135
Effective Tax Rate	25.5	26.2	(74)	25.5	2	26.0	24.8	126

Source: Company, BOBCAPS Research

Fig 2 – Operating metrics

(in US\$ terms)	Q1FY22 (% Contr. to Revenue)	Growth	
		QoQ (%)	YoY (%)
Revenue by Geography			
North America	78.9	8.7	24.9
Europe	9.5	3.7	18.6
India, APAC	11.6	17.2	57.1
Client Concentration			
Top Client	17.0	3.7	(4.0)
Top 5 Clients	36.5	9.4	(10.5)
Top 10 Clients	46.7	10.1	(4.7)
Non-Top 10 Clients	53.3	8.3	4.5
Revenue by Vertical			
BFSI	30.8	11.7	23.3
Healthcare and Lifesciences	20.5	15.9	32.5
Tech. Cos. & Emerging Verticals	48.7	5.0	27.8
	Q1FY22	Q4FY21	Q1FY21
Onsite-Offshore mix (%)			
Onsite	31.4	30.4	33.7
Offshore	55.5	54.7	48.9
IP-led	13.1	14.9	17.4
Utilisation	80.1	79.1	78.5
Headcount	14,904	13,680	10,829

Source: Company, BOBCAPS Research

Valuation methodology

Incorporating the stellar Q1FY22 print, we raise FY22/FY23 EPS estimates by 15%/31%, baking in higher revenue and margin assumptions. PSYS's sustained growth momentum coupled with stable margin outlook and regular TCV reporting gives us confidence on earnings. We roll valuations over and increase our target one-year forward P/E from 19x to 27.6x, which is inline with target valuation multiple for LTI– this yields a new Jun'22 TP of Rs 2,920 (vs. Rs 1,340). We upgrade PSYS to HOLD (V/s SELL earlier) on back of strong growth momentum. Its Q1 head start growth sets PSYS in strong position to claim industry leading growth in FY22.

Fig 3 – Revised estimates

(Rs mn)	FY22E			FY23E			FY24E
	Old	New	Change (%)	Old	New	Change (%)	New
Revenues (US\$ mn)	671.6	719.2	7.1	748.8	829.4	10.8	941.2
YoY growth (%)	18.6	27.0	-	11.5	15.3	-	13.5
Revenues	52,231	54,654	4.6	58,596	64,905	10.8	73,882
EBITDA	8,174	8,765	7.2	9,124	11,084	21.5	12,519
EBITDA margin (%)	15.6	16.0	-	15.6	17.1	-	16.9
Net profits	5,132	5,899	15.0	5,553	7,294	31.4	8,308
EPS (Rs)	64.3	74.0	15.0	69.6	91.4	31.4	104.2

Source: BOBCAPS Research

Fig 4 – Peer comparison

Company	Ticker	Rating	Target Price (Rs)	US\$ revenue CAGR FY21-23E (%)	EPS (Rs)		P/E (x)		ROE (%)	
					FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
Tata Consultancy Services	TCS IN	BUY	3,890	15.1	109.8	127.0	29.3	25.3	41.4	43.1
Infosys	INFO IN	BUY	1,860	14.3	54.1	61.1	29.4	26.0	33.8	33.8
Wipro	WPRO IN	HOLD	590	18.4	23.5	27.1	24.9	21.6	7.1	7.5
HCL Technologies	HCLT IN	BUY	1,260	11.3	52.2	59.0	18.8	16.6	31.9	38.4
Tech Mahindra	TECHM IN	BUY	1,190	14.7	63.4	75.7	18.1	15.2	20.9	22.2
L&T Infotech	LTI IN	BUY	4,990	18.7	134.1	158.4	32.9	27.8	37.1	42.6
Mphasis	MPHL IN	HOLD	2,500	14.0	82.0	95.7	29.2	25.0	22.3	25.5
Mindtree	MTCL IN	SELL	2,270	15.8	87.7	93.9	31.5	29.4	50.5	55.7
Persistent Systems	PSYS IN	SELL	2,620	21.0	74.0	89.6	38.2	31.6	19.6	22.1
Coforge	COFORGE IN	BUY	4,080	23.3	131.3	163.3	35.5	28.6	25.1	26.3
eClerx Services	ECLX IN	BUY	1,620	16.8	120.3	135.1	18.4	16.4	38.3	41.6

Source: BOBCAPS Research

Key risks

Key upside risks to our estimates are:

- increase in annuity business, and
- above-expected operating margin improvement.

Sector recommendation snapshot

Stock	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
HCL Technologies	HCLT IN	36	994	1,260	BUY
Info Edge	INFOE IN	9	5,143	2,880	SELL
Infosys	INFO IN	91	1,590	1,860	BUY
L&T Infotech	LTI IN	10	4,361	4,990	BUY
Mindtree	MTCL IN	6	2,721	2,270	SELL
Mphasis	MPHL IN	6	2,530	2,500	HOLD
Persistent Systems	PSYS IN	3	3,039	2,920	HOLD
Tata Consultancy Services	TCS IN	162	3,213	3,890	BUY
Tech Mahindra	TECHM IN	13	1,131	1,190	BUY
Wipro	WPRO IN	44	599	590	HOLD

Source: BOBCAPS Research, NSE | Price as of 23 Jul 2021

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21P	FY22E	FY23E	FY24E
Total revenue	35,658	41,879	54,654	64,905	73,882
EBITDA	4,930	6,830	8,765	11,084	12,519
Depreciation	1,660	1,756	1,668	1,854	1,938
EBIT	3,270	5,075	7,098	9,230	10,581
Net interest inc./(exp.)	0	0	0	0	0
Other inc./(exp.)	1,254	1,020	821	627	723
Exceptional items	0	0	0	0	0
EBT	4,523	6,094	7,919	9,857	11,304
Income taxes	1,121	1,588	2,019	2,563	2,996
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	3,403	4,507	5,899	7,294	8,308
Adjustments	0	0	0	0	0
Adjusted net profit	3,403	4,507	5,899	7,294	8,308

Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21P	FY22E	FY23E	FY24E
Accounts payables	0	0	0	0	0
Other current liabilities	3,810	4,607	5,840	6,935	7,894
Provisions	1,954	2,719	2,995	3,556	4,048
Debt funds	12	44	44	44	44
Other liabilities	0	0	0	0	0
Equity capital	791	764	764	764	764
Reserves & surplus	24,002	27,192	30,651	35,750	41,559
Shareholders' fund	24,793	27,957	31,415	36,515	42,323
Total liab. and equities	30,569	35,327	40,294	47,050	54,310
Cash and cash eq.	1,461	2,419	3,095	4,302	9,219
Accounts receivables	5,862	5,709	8,984	10,669	12,145
Inventories	0	0	0	0	0
Other current assets	5,373	4,945	6,289	8,358	9,514
Investments	13,304	17,853	17,853	19,853	19,853
Net fixed assets	4,083	3,277	3,259	3,055	2,767
CWIP	316	122	122	122	122
Intangible assets	81	86	86	86	86
Deferred tax assets, net	405	1,038	727	727	727
Other assets	0	0	0	0	0
Total assets	30,569	35,327	40,294	47,050	54,310

Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21P	FY22E	FY23E	FY24E
Cash flow from operations	2,025	5,679	3,635	6,424	8,343
Capital expenditures	(1,500)	(392)	(1,650)	(1,650)	(1,650)
Change in investments	0	(3,722)	0	(2,000)	0
Other investing cash flows	1,254	1,020	821	627	723
Cash flow from investing	(247)	(3,094)	(829)	(3,023)	(927)
Equities issued/Others	(828)	0	0	0	0
Debt raised/repaid	0	0	0	0	0
Interest expenses	0	0	0	0	0
Dividends paid	(1,229)	(1,627)	(2,130)	(2,195)	(2,500)
Other financing cash flows	0	0	0	0	0
Cash flow from financing	(2,057)	(1,627)	(2,130)	(2,195)	(2,500)
Chg in cash & cash eq.	(278)	958	676	1,207	4,916
Closing cash & cash eq.	1,461	2,419	3,095	4,302	9,219

Per Share

Y/E 31 Mar (Rs)	FY20A	FY21P	FY22E	FY23E	FY24E
Reported EPS	42.7	56.5	74.0	91.4	104.2
Adjusted EPS	42.7	56.5	74.0	91.4	104.2
Dividend per share	12.8	16.9	22.2	22.9	26.0
Book value per share	310.8	350.5	393.8	457.8	530.6

Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21P	FY22E	FY23E	FY24E
EV/Sales	6.8	5.8	4.4	3.7	3.2
EV/EBITDA	48.9	35.4	27.5	21.7	19.1
Adjusted P/E	71.2	53.8	41.1	33.2	29.2
P/BV	9.8	8.7	7.7	6.6	5.7

DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21P	FY22E	FY23E	FY24E
Tax burden (Net profit/PBT)	75.2	73.9	74.5	74.0	73.5
Interest burden (PBT/EBIT)	138.3	120.1	111.6	106.8	106.8
EBIT margin (EBIT/Revenue)	9.2	12.1	13.0	14.2	14.3
Asset turnover (Rev./Avg TA)	120.6	127.1	144.5	148.6	145.8
Leverage (Avg TA/Avg Equity)	1.2	1.2	1.3	1.3	1.3
Adjusted ROAE	14.1	17.1	19.9	21.5	21.1

Ratio Analysis

Y/E 31 Mar	FY20A	FY21P	FY22E	FY23E	FY24E
YoY growth (%)					
Revenue	5.9	17.4	30.5	18.8	13.8
EBITDA	(15.1)	38.6	28.3	26.5	12.9
Adjusted EPS	(2.9)	32.4	30.9	23.6	13.9
Profitability & Return ratios (%)					
EBITDA margin	13.8	16.3	16.0	17.1	16.9
EBIT margin	9.2	12.1	13.0	14.2	14.3
Adjusted profit margin	9.5	10.8	10.8	11.2	11.2
Adjusted ROAE	14.1	17.1	19.9	21.5	21.1
ROCE	10.9	15.3	19.6	22.5	23.8
Working capital days (days)					
Receivables	55	50	49	55	56
Inventory	0	0	0	0	0
Payables	41	44	42	43	44
Ratios (x)					
Gross asset turnover	8.6	11.4	16.7	20.6	25.4
Current ratio	2.2	1.8	2.1	2.2	2.6
Net interest coverage ratio	NA	NA	NA	NA	NA
Adjusted debt/equity	(0.1)	(0.1)	(0.1)	(0.1)	(0.2)

Source: Company, BOBCAPS Research | Note: TA = Total Assets

Disclaimer

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

BUY – Expected return >+15%

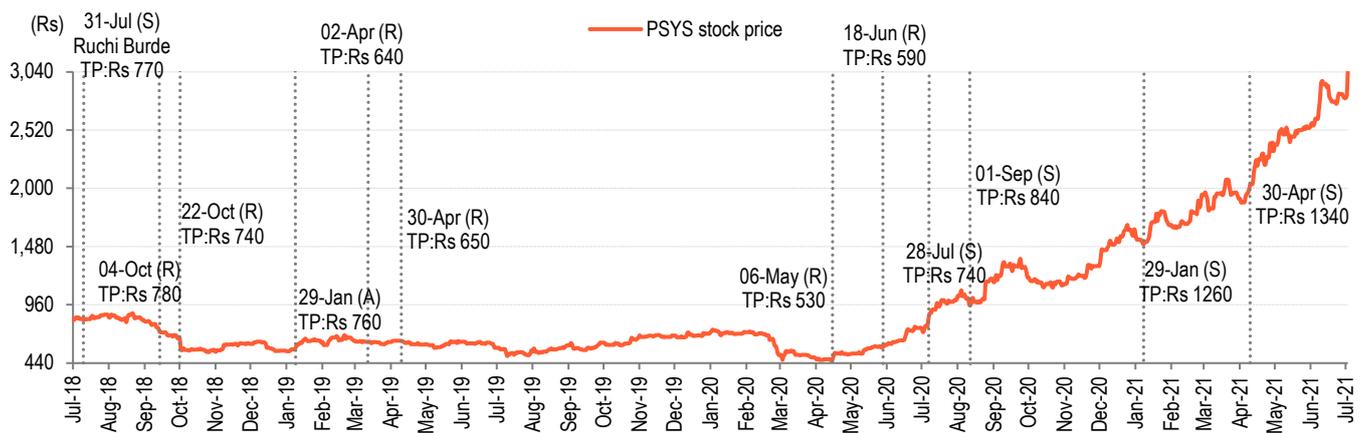
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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Ratings and Target Price (3-year history): PERSISTENT SYSTEMS (PSYS IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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