

**HOLD**

TP: Rs 4,580 | ▲ 6%

**PERSISTENT SYSTEMS**

Technology & Internet

21 January 2022

### Stellar quarter

- Above-expected Q3 with revenue growth of 9.2% QoQ USD led by IP business
- TCV robust at US\$ 334mn. EBIT margin flat QoQ at 14% but ahead of our estimate of 13.4%
- We raise FY22-FY24 EPS by 5-9% and retain HOLD with a revised TP of Rs 4,580 (vs. Rs 4,240)

Ruchi Burde | Seema Nayak  
researchreport@bobcaps.in

**Soaring growth led by IP:** PSYS reported stellar Q3FY22 growth of 9.2% QoQ USD, ahead of our estimate of 7.4%. Adjusted for its acquisitions (SCI and Shree Partners), growth stood at 6.7% QoQ USD. Services were up 8.3% QoQ and IP-led revenues increased 16.2% led by traction in 'Accelerite' and higher royalty. The BFSI vertical led the way aided by acquisitions, rising 14.6% QoQ. Healthcare and emerging verticals were up 6-7%. The growth was also broad-based across geographies. Client addition was strong with two clients being added QoQ in the US\$ 5mn+ bucket and six in the US\$ 1mn-5mn bucket due to better account mining.

**Beat on margins:** EBIT margin at 14% was up 10bps QoQ, outperforming our estimate of 13.4%. Employee cost and SG&A increased 10-11% QoQ each. Onsite revenue share grew 100bps QoQ to 31.4% due to employee addition in North America from the SCI acquisition.

**Strong deal wins:** PSYS reported TCV of US\$ 334.3mn, up 18% QoQ. This is the company's fifth quarter of US\$ 200mn+ in contract wins. However, new business TCV at US\$ 157.6mn formed only 47% share (vs. 53% in Q2). ACV was at US\$ 291.3mn, up 45% QoQ.

**Attrition soars:** Attrition stood at 26.9%, up 330bps QoQ. PSYS added 1,110 employees during the quarter (including those from acquired entities). Annualised attrition has started to moderate on account of the base effect and improving supply situation. Fresh graduates constituted a fourth of the Q3 net additions. Linear utilisation improved 20bps QoQ. Career planning, a stronger value proposition and salary hikes were a few of the initiatives taken by PSYS to arrest attrition.

**Robust outlook:** Per management, demand remains healthy, especially in the BFSI and HLS verticals. PSYS will continue scouting for more acquisition targets such as SCI and Shree Partners to fill in its white spaces. Factoring in the Q3FY22 performance, we raise FY22/FY23/FY24 EPS by 5%/6%/9% and revise our TP to Rs 4,580 (vs. Rs 4,240) based on an unchanged one-year forward target P/E of 40x. Maintain HOLD given limited upside at current valuations of 49.8x FY23E EPS.

### Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	PSYS IN/Rs 4,302
Market cap	US\$ 4.6bn
Free float	70%
3M ADV	US\$ 18.7mn
52wk high/low	Rs 4,988/Rs 1,482
Promoter/FPI/DII	30%/26%/44%

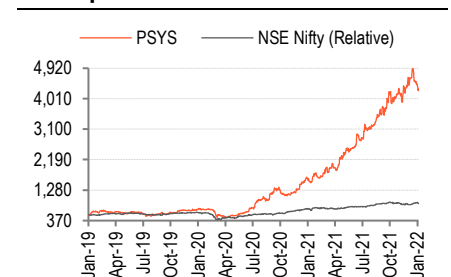
Source: NSE | Price as of 21 Jan 2022

### Key financials

Y/E 31 Mar	FY21A	FY22E	FY23E
Total revenue (Rs mn)	41,879	56,927	72,519
EBITDA (Rs mn)	6,830	9,297	11,823
Adj. net profit (Rs mn)	4,507	6,563	7,843
Adj. EPS (Rs)	56.5	82.3	98.3
Consensus EPS (Rs)	56.5	83.7	101.7
Adj. ROAE (%)	17.1	22.0	22.7
Adj. P/E (x)	76.1	52.3	43.8
EV/EBITDA (x)	50.2	36.8	28.9
Adj. EPS growth (%)	32.4	45.6	19.5

Source: Company, Bloomberg, BOBCAPS Research

### Stock performance



Source: NSE



## Other highlights

- PSYS' acquisition of SCI and Shree Partners was closed in Q3FY22. SCI gives the company access to market-leading US banking clients and also strengthens its dedicated payments business unit. Shree Partners consolidates PSYS' position in strategic BFSI accounts.
- The company is planning to expand its presence in Mexico and Canada.
- New leadership has been inducted across several departments.
- ESOPs have been given to 80% of employees and a few among senior management as well. ESOP costs formed 8.9% of quarterly revenue.
- The board declared interim dividend of Rs 10/sh.
- DSO increased to 58 days vs. 55 days in Q2FY22 due to higher invoicing in the IP business.

**Fig 1 – Quarterly performance**

(Rs mn)	Q3FY22	Q3FY21	YoY (%)	Q2FY22	QoQ (%)	9MFY22	9MFY21	YoY (%)
<b>Revenue (US\$ mn)</b>	<b>199.1</b>	<b>146.2</b>	<b>36.2</b>	<b>182.3</b>	<b>9.2</b>	<b>548</b>	<b>413</b>	<b>32.7</b>
Revenue	14,917	10,754	38.7	13,512	10.4	40,729	30,745	32.5
Operating Expenditure	12,406	8,929	38.9	11,268	10.1	33,959	25,798	31.6
Cost of revenues	9,880	7,064	39.9	8,982	10.0	27,035	20,287	33.3
as % of sales	66.2	65.7	-	66.5	-	66.4	66.0	-
SG&A expenses	2,526	1,865	35.4	2,286	10.5	6,923	5,511	25.6
as % of sales	16.9	17.3	-	16.9	-	17.0	17.9	-
<b>EBITDA</b>	<b>2,511</b>	<b>1,825</b>	<b>37.6</b>	<b>2,244</b>	<b>11.9</b>	<b>6,770</b>	<b>4,947</b>	<b>36.9</b>
Depreciation	428	461	(7.2)	371	15.4	1,149	1,336	(14.0)
<b>EBIT</b>	<b>2,083</b>	<b>1,364</b>	<b>52.7</b>	<b>1,873</b>	<b>11.2</b>	<b>5,621</b>	<b>3,610</b>	<b>55.7</b>
Other Income	281	286	-	303	-	950	635	-
PBT	2,364	1,650	43.3	2,176	8.6	6,571	4,246	54.8
Total Tax	600	441	36.1	559	7.4	1,677	1,116	50.2
<b>Adjusted PAT</b>	<b>1,764</b>	<b>1,209</b>	<b>45.9</b>	<b>1,618</b>	<b>9.0</b>	<b>4,894</b>	<b>3,129</b>	<b>56.4</b>
(Profit)/loss from JV's/Ass/MI	-	-	-	-	-	0	0	-
APAT after MI	1,764	1,209	45.9	1,618	9.0	4,894	3,129	56.4
Extra ordinary items	0	0	-	0	-	0	0	-
<b>Reported PAT</b>	<b>1,764</b>	<b>1,209</b>	<b>45.9</b>	<b>1,618</b>	<b>9.0</b>	<b>4,894</b>	<b>3,129</b>	<b>56.4</b>
Reported EPS	22.0	15.1	45.9	20.2	9.0	61	39	56.4
<b>Margins (%)</b>			<b>(bps)</b>		<b>(bps)</b>			<b>(bps)</b>
EBIDTA	16.8	17.0	(14)	16.6	22	16.6	16.1	53
EBIT	14.0	12.7	128	13.9	10	13.8	11.7	206
EBT	15.8	15.3	50	16.1	(26)	16.1	13.8	233
PAT	11.8	11.2	58	12.0	(15)	12.0	10.2	184
Effective Tax rate	25.4	26.7	(133)	25.7	(29)	25.5	26.3	(78)

Source: Company, BOBCAPS Research

**Fig 2 – Operating metrics**

(in USD terms)	Q3FY22 (% Contr. to Revenue)	Growth	
		QoQ (%)	YoY (%)
<b>Revenue by Geography</b>			
North America	79.2	9.9	33.1
Europe	8.3	3.0	28.5
India, APAC	12.5	9.2	68.6
<b>Client Concentration</b>			
Top Client	17.5	13.1	(5.4)
Top 5 Clients	36.1	10.1	(4.5)
Top 10 Clients	45.0	8.3	(4.3)
Non Top 10 Clients	55.0	10.0	3.8
<b>Revenue by Vertical</b>			
BFSI	32.2	14.6	48.7
Healthcare and Lifesciences	20.7	6.7	47.7
Tech. Cos. & Emerging Verticals	47.1	7.0	24.8
	<b>Q3FY22</b>	<b>Q2FY22</b>	<b>Q3FY21</b>
<b>Onsite- Offshore mix (%)</b>			
Onsite	31.4	30.4	30.5
Offshore	55.3	57.1	51.4
IP-led	13.3	12.5	18.1
Utilisation	83.0	82.8	81.0
Headcount	16989	15879	12438

Source: Company, BOBCAPS Research

## Valuation methodology

Incorporating the stellar Q3FY22 print, we raise FY22/FY23/FY24 EPS estimates by 5%/6%/9%, baking in higher revenue growth assumptions and contribution from acquired entities. The increase in EPS estimates is relatively muted given management's conservative margin outlook. PSYS's sustained growth momentum coupled with stable margins and regular TCV gives us confidence on earnings.

Based on our revised estimates, we have a new TP of Rs 4,580 (vs. Rs 4,240 earlier), set at an unchanged Dec'23E target P/E of 40x. While we expect PSYS to maintain its strong growth momentum, we see limited upside at current valuations of 49.8x FY23E EPS and hence retain HOLD.

**Fig 3 – Revised estimates**

(Rs mn)	New			Old			Change (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenues (US\$ mn)	758.6	926.7	1049.7	746.9	881.1	996.5	1.6	5.2	5.3
YoY growth (%)	34.0	22.2	13.3	31.9	18.0	13.1	-	-	-
Revenues	56,927	72,519	82,404	56,441	68,957	78,224	0.9	5.2	5.3
EBITDA	9,297	11,823	13,599	9,034	11,259	12,686	2.9	5.0	7.2
EBITDA margin (%)	16.3	16.3	16.5	16.0	16.3	16.2	-	-	-
Net profits	6,563	7,843	9,220	6,260	7,422	8,482	4.8	5.7	8.7
EPS (Rs)	82.0	98.0	115.2	78.2	92.8	106.0	4.8	5.7	8.7

Source: BOBCAPS Research

**Fig 4 – Key assumptions**

Parameter	FY21	FY22E	FY23E	FY24E
Revenues (US\$ mn)	566	759	927	1,050
Revenues growth YoY (%)	12.9	34.0	22.2	13.3
EBIT (%)	12.1	13.5	13.7	14.2

Source: Company, BOBCAPS Research

**Fig 5 – Peer comparison**

Ticker	Rating	Target Price (Rs)	US\$ revenue CAGR FY21-23E (%)	EPS (Rs)		RoE (%)		P/E (x)	
				FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
TCS IN	BUY	4,770	14.1	104.0	120.3	39.6	37.5	36.8	31.9
INFO IN	BUY	2,250	17.1	54.4	62.3	29.8	32.0	32.8	28.7
WPRO IN	BUY	850	18.2	22.6	26.9	20.5	21.6	26.8	22.5
HCLT IN	BUY	1,610	12.6	49.0	56.2	20.3	20.9	23.8	20.8
TECHM IN	BUY	1,970	16.1	65.5	81.1	21.5	23.6	24.3	19.7
LTI IN	BUY	8,490	23.2	131.1	166.8	28.9	30.9	48.8	38.4
MPHL IN	HOLD	3,470	19.1	75.7	90.1	20.9	23.1	39.9	33.6
MTCL IN	BUY	5,610	23.9	97.9	105.3	34.2	31.0	42.1	39.1
PSYS IN	HOLD	4,580	27.9	82.3	98.3	22.0	22.7	52.3	43.7
COFORGE IN	BUY	7,040	27.5	123.4	173.2	27.9	33.1	42.1	30.0
ECLX IN	BUY	3,690	22.9	125.8	143.6	27.0	28.4	20.5	17.9

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

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Coforge	COFORGE IN	4.4	5,200	7,040	BUY
eClerx Services	ECLX IN	1.3	2,563	3,690	BUY
HCL Technologies	HCLT IN	42.6	1,168	1,610	BUY
Infosys	INFO IN	102.2	1,786	2,250	BUY
L&T Infotech	LTI IN	15.1	6,394	8,490	BUY
Mindtree	MTCL IN	9.1	4,119	5,610	BUY
Mphasis	MPHL IN	7.6	3,025	3,470	HOLD
Persistent Systems	PSYS IN	4.6	4,302	4,580	HOLD
Tata Consultancy Services	TCS IN	193.5	3,834	4,770	BUY
Tech Mahindra	TECHM IN	18.7	1,594	1,970	BUY
Wipro	WPRO IN	45.0	605	850	BUY

Source: BOBCAPS Research, NSE | Price as of 21 Jan 2022

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Total revenue</b>	<b>35,658</b>	<b>41,879</b>	<b>56,927</b>	<b>72,519</b>	<b>82,404</b>
EBITDA	4,930	6,830	9,297	11,823	13,599
Depreciation	1,660	1,756	1,588	1,854	1,938
EBIT	3,270	5,075	7,709	9,969	11,660
Net interest inc./(exp.)	0	0	0	0	0
Other inc./(exp.)	1,254	1,020	1,102	629	715
Exceptional items	0	0	0	0	0
EBT	4,523	6,094	8,811	10,598	12,375
Income taxes	1,121	1,588	2,248	2,755	3,156
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
<b>Reported net profit</b>	<b>3,403</b>	<b>4,507</b>	<b>6,563</b>	<b>7,843</b>	<b>9,220</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>3,403</b>	<b>4,507</b>	<b>6,563</b>	<b>7,843</b>	<b>9,220</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Accounts payables	0	0	0	0	0
Other current liabilities	3,810	4,607	6,083	7,749	8,805
Provisions	1,954	2,719	3,119	3,974	4,515
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	31,075	36,558	43,004
Shareholders' fund	24,793	27,957	31,839	37,322	43,768
<b>Total liab. and equities</b>	<b>30,569</b>	<b>35,327</b>	<b>41,085</b>	<b>49,089</b>	<b>57,132</b>
Cash and cash eq.	1,461	2,419	3,172	4,029	9,463
Accounts receivables	5,862	5,709	9,358	11,921	13,546
Inventories	0	0	0	0	0
Other current assets	5,373	4,945	6,551	9,338	10,611
Investments	13,304	17,853	17,853	19,853	19,853
Net fixed assets	4,083	3,277	3,339	3,135	2,846
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
<b>Total assets</b>	<b>30,569</b>	<b>35,327</b>	<b>41,085</b>	<b>49,088</b>	<b>57,132</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY20A	FY21A	FY22E	FY23E	FY24E
<b>Cash flow from operations</b>	<b>2,025</b>	<b>5,679</b>	<b>3,671</b>	<b>6,237</b>	<b>9,143</b>
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	1,102	629	715
<b>Cash flow from investing</b>	<b>(247)</b>	<b>(3,094)</b>	<b>(548)</b>	<b>(3,021)</b>	<b>(935)</b>
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)	(2,370)	(2,360)	(2,774)
Other financing cash flows	0	0	0	0	0
<b>Cash flow from financing</b>	<b>(2,057)</b>	<b>(1,627)</b>	<b>(2,370)</b>	<b>(2,360)</b>	<b>(2,774)</b>
<b>Chg in cash &amp; cash eq.</b>	<b>(278)</b>	<b>958</b>	<b>753</b>	<b>857</b>	<b>5,434</b>
<b>Closing cash &amp; cash eq.</b>	<b>1,461</b>	<b>2,419</b>	<b>3,172</b>	<b>4,029</b>	<b>9,463</b>

### Per Share

Y/E 31 Mar (Rs)	FY20A	FY21A	FY22E	FY23E	FY24E
Reported EPS	42.7	56.5	82.3	98.3	115.6
Adjusted EPS	42.7	56.5	82.3	98.3	115.6
Dividend per share	12.8	16.9	24.7	24.6	28.9
Book value per share	310.8	350.5	399.2	467.9	548.7

### Valuations Ratios

Y/E 31 Mar (x)	FY20A	FY21A	FY22E	FY23E	FY24E
EV/Sales	9.6	8.2	6.0	4.7	4.1
EV/EBITDA	69.4	50.2	36.8	28.9	25.0
Adjusted P/E	100.8	76.1	52.3	43.8	37.2
P/BV	13.8	12.3	10.8	9.2	7.8

### DuPont Analysis

Y/E 31 Mar (%)	FY20A	FY21A	FY22E	FY23E	FY24E
Tax burden (Net profit/PBT)	75.2	73.9	74.5	74.0	74.5
Interest burden (PBT/EBIT)	138.3	120.1	114.3	106.3	106.1
EBIT margin (EBIT/Revenue)	9.2	12.1	13.5	13.7	14.2
Asset turnover (Rev./Avg TA)	120.6	127.1	149.0	160.8	155.2
Leverage (Avg TA/Avg Equity)	1.2	1.2	1.3	1.3	1.3
<b>Adjusted ROAE</b>	<b>14.1</b>	<b>17.1</b>	<b>22.0</b>	<b>22.7</b>	<b>22.7</b>

### Ratio Analysis

Y/E 31 Mar	FY20A	FY21A	FY22E	FY23E	FY24E
<b>YoY growth (%)</b>					
Revenue	5.9	17.4	35.9	27.4	13.6
EBITDA	(15.1)	38.6	36.1	27.2	15.0
Adjusted EPS	(2.9)	32.4	45.6	19.5	17.6
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	13.8	16.3	16.3	16.3	16.5
EBIT margin	9.2	12.1	13.5	13.7	14.2
Adjusted profit margin	9.5	10.8	11.5	10.8	11.2
Adjusted ROAE	14.1	17.1	22.0	22.7	22.7
ROCE	10.9	15.3	21.2	23.8	25.7

### Working capital days (days)

	FY20A	FY21A	FY22E	FY23E	FY24E
Receivables	55	50	48	54	56
Inventory	0	0	0	0	0
Payables	41	44	41	42	44

### Ratios (x)

	FY20A	FY21A	FY22E	FY23E	FY24E
Gross asset turnover	8.6	11.4	17.2	22.4	27.6
Current ratio	2.2	1.8	2.1	2.2	2.5
Net interest coverage ratio	NA	NA	NA	NA	NA
<b>Adjusted debt/equity</b>	<b>(0.1)</b>	<b>(0.1)</b>	<b>(0.1)</b>	<b>(0.1)</b>	<b>(0.2)</b>

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

## Disclaimer

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

**BUY** – Expected return >+15%

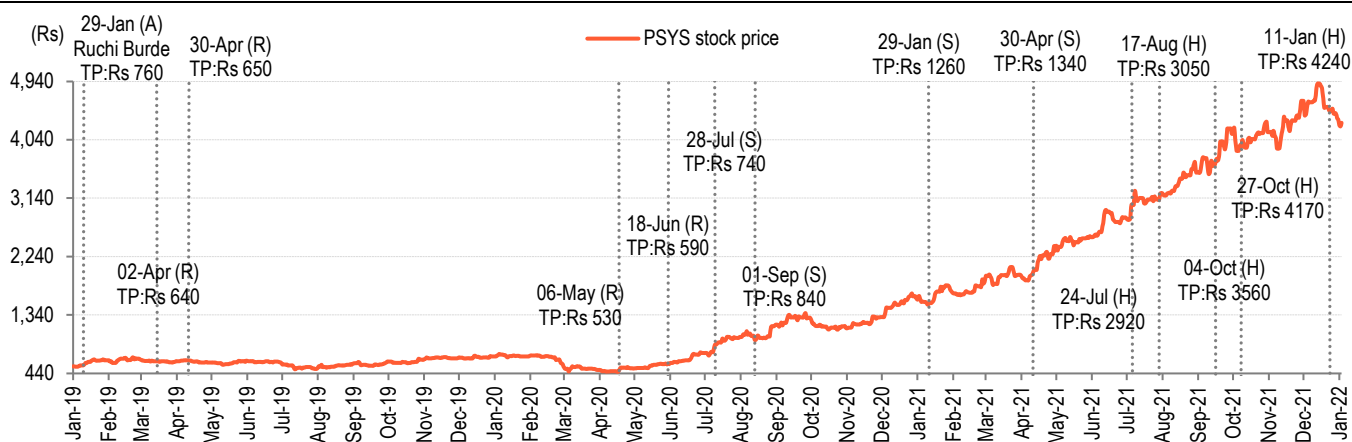
**HOLD** – Expected return from -6% to +15%

**SELL** – Expected return <-6%

**Note:** Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

### 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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