

**BUY**

TP: Rs 5,330 | ▲ 19%

**PERSISTENT SYSTEMS**

Technology & Internet

26 April 2023

**Growth resilient**

- Q4 revenue up 3.9% QoQ CC to US\$ 275mn, backed by services and top-client business
- EBIT margin flat QoQ at 15.4% with some drag visible from the healthcare and tech/emerging verticals
- Management confident of above-industry growth in FY24; we assume coverage with BUY and a TP of Rs 5,330, set at 30x FY25E EPS

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**Top client drives growth:** PSYS reported 3.9% QoQ CC revenue growth in Q4FY23 – similar to Q3 – at US\$ 275mn led by (i) its top client (T1) where incremental revenue grew 58.5% QoQ to US\$ 26mn, and (ii) the services business which increased by 5.5% QoQ. Excluding T1, growth slips to 1.7% QoQ, impacted by a decline in IP-led revenue and project ramp-down at hyperscale clients (-1.1% QoQ impact). For FY23, revenue increased 35% YoY (incl. ~9% inorganic growth).

**Sustainability of deal wins key in the near term:** Deal TCV/ACV increased by 17%/18% YoY to US\$ 422mn/US\$ 310mn in Q4 with the new deal component at its highest ever. After four straight quarters of decline, the top client’s growth rebounded to 30.5% QoQ backed by a US\$ 100mn TCV win. PSYS’s ability to maintain its revenue run-rate at FY22 levels of US\$ 31mn/quarter (vs. US\$ 25.5mn in Q4FY23) will be a key monitorable.

ACV fell 5% QoQ and the book-to-bill ratio remained at 1.13x (vs. 1.15x in Q3). Organic growth slowed further to 19.6% YoY. We see improvement in client mining, cross-sell and annuity business, which is reflected in higher revenue per client in the services segment (~1.6x in the last two years vs. a flat trend during FY15-FY21).

**EBIT margin flat QoQ:** PSYS’s EBIT margin stood at 15.4% in Q4FY23 and 14.9% in FY23, supported by growth in the offshore mix and in T1 business, offset to some extent by a decline in segmental margins in the healthcare and tech & emerging verticals. Attrition continued to trend lower, and the company added 291 employees to its headcount in Q4 with plans for 850-1,000 fresher adds in FY24 together with wage hike plans for Q2FY24.

**Relatively bullish outlook:** PSYS aspires to achieve above-industry growth of 7-10% for FY24 and is confident of clocking quarterly growth of 3-5%. The stock is currently trading at 25x FY25E EPS. We assume coverage with BUY and a TP of Rs 5,330 based on 30x FY25E EPS (vs. historical average of 34.4x over FY20-FY23).

**Key changes**

Target	Rating
▲	▲

Ticker/Price	PSYS IN/Rs 4,472
Market cap	US\$ 4.4bn
Free float	70%
3M ADV	US\$ 21.1mn
52wk high/low	Rs 5,135/Rs 3,092
Promoter/FPI/DII	30%/26%/44%

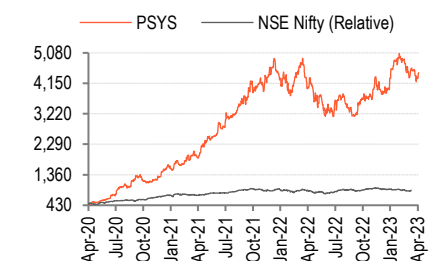
Source: NSE | Price as of 25 Apr 2023

**Key financials**

Y/E 31 Mar	FY23P	FY24E	FY25E
Total revenue (Rs mn)	83,506	96,822	1,11,253
EBITDA (Rs mn)	15,191	18,155	21,063
Adj. net profit (Rs mn)	9,507	11,422	13,574
Adj. EPS (Rs)	124.4	149.4	177.6
Consensus EPS (Rs)	124.4	146.7	174.8
Adj. ROAE (%)	27.4	30.8	33.7
Adj. P/E (x)	35.9	29.9	25.2
EV/EBITDA (x)	23.5	19.9	17.0
Adj. EPS growth (%)	43.7	20.1	18.8

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

**Stock performance**



Source: NSE

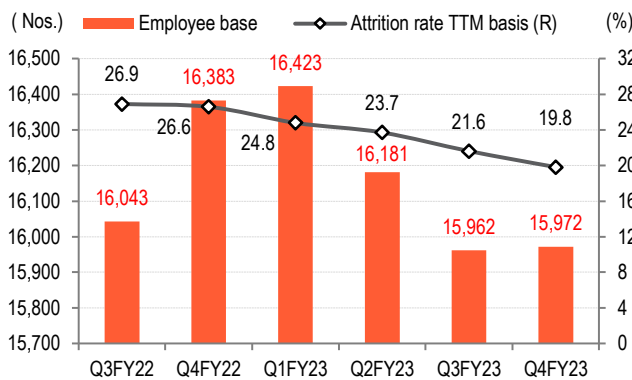


**Fig 1 – Quarterly performance**

(Rs mn)	Q4FY23	Q3FY23	Q4FY22	QoQ (%)	YoY (%)
US\$ Revenue	275	264	217	3.9	26.3
INR Revenue	22,545	21,694	16,379	3.9	37.6
EBIT	3,466	3,332	2,300	4.0	50.7
PAT	2,515	2,380	2,010	5.7	25.1
EBIT Margin (%)	15.4	15.4	14.0	1bps	133bps
PAT Margin (%)	11.2	11.0	12.3	19bps	(112bps)

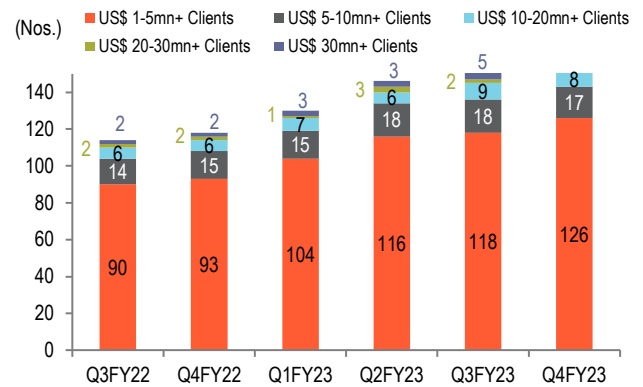
Source: Company, BOBCAPS Research

**Fig 2 – Employee base and Attrition**



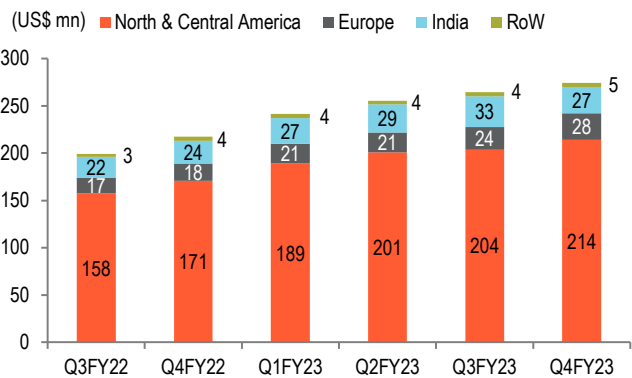
Source: Company, BOBCAPS Research

**Fig 3 – Client revenue contribution**



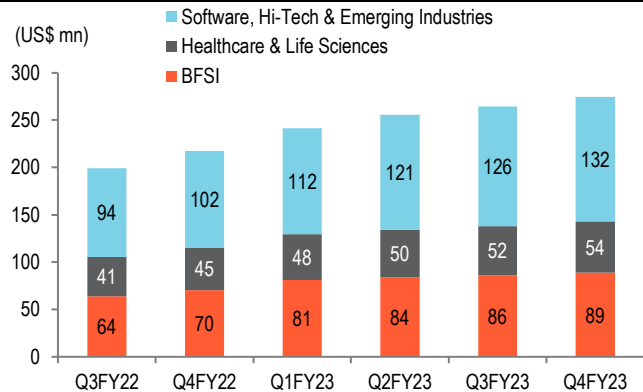
Source: Company, BOBCAPS Research

**Fig 4 – Revenue by geography**



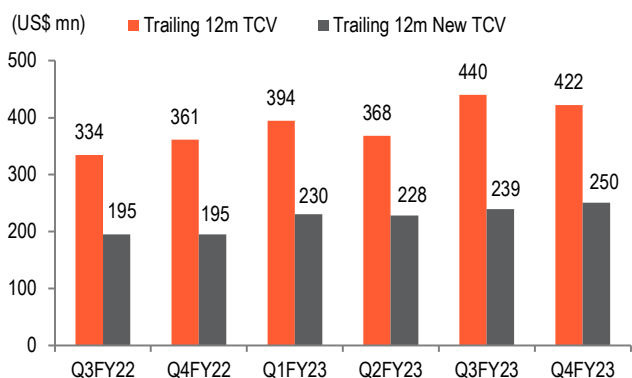
Source: Company, BOBCAPS Research

**Fig 5 – Revenue by vertical**



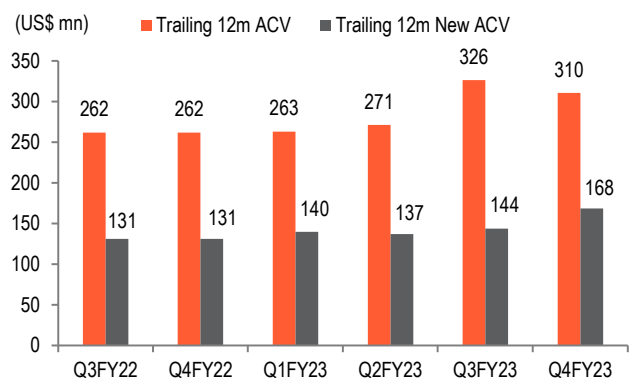
Source: Company, BOBCAPS Research

**Fig 6 – Deal TCV**



Source: Company, BOBCAPS Research

**Fig 7 – Deal ACV**



Source: Company, BOBCAPS Research

**Fig 8 – Acquisition summary**

Acquisition	Domain	Consideration (US\$ mn)	Revenue-run rate (US\$ mn)	Year
MediaAgility	Cloud Transformation	72	25	2022
Data Glove	Microsoft Product Suite	90	50	2022
Shree Partners LLC	ADM, Cloud Data & Analytics	7	8	2021
SCI (Software Corporation International & Fusion360 LLC)	Consulting in Payment Domain	53	17	2021
Capiot Software Inc	IT Services (Mulesoft)	6	1.1	2020
Youperience	Salesforce Consulting	2	1	2019
Park Werk	Salesforce Consulting	15	8	2017

Source: Company, BOBCAPS Research

**Fig 9 – Recent deal wins**

Vertical	Subsegment	Scope
BFSI	Bank (Leading US-based)	Transforming legacy check platform
BFSI	Bank	CX and application development
BFSI	Bank (Large bank)	Digital banking platform
BFSI	Payroll Services	HR application development
BFSI	Fintech	Salesforce services
BFSI	Bank	Platform development
BFSI	Fintech	Risk & Pricing platform development
Healthcare & Life Science	Health Tech	Cloud migration
Healthcare & Life Science	Medical Devices	Enterprise integration services
Healthcare & Life Science	Lab Equipment Provider	Modernise tech stack
Healthcare & Life Science	Pharma	Automation services
Healthcare & Life Science	Healthcare Insurer	Application design
Healthcare & Life Science	Bio Tech	Data platform
Tech & Emerging	Online Retailer (USD 70mn TCV)	Cost optimisation, data integration, Google Cloud services
Tech & Emerging	Software	Software migration
Tech & Emerging	Software (Canadian Company)	Product development services
Tech & Emerging	Hi-tech (Software AG, USD 100mn+ TCV)	Application modernisation
Tech & Emerging	Hi-tech	Setup of professional services
Tech & Emerging	Media Tech	Software product development
Tech & Emerging	Hi-tech	OTT video streaming application development

Source: Company, BOBCAPS Research | OTT: Over-The-Top

## Earnings call highlights

- Growth moderated in Q4FY23 due to ramp-down in a key hyperscaler account, amounting to ~US\$ 3mn for Q4 and US\$ 10mn on an annualised basis for FY23. PSYS's second-largest client (BFSI segment) witnessed sequential growth of 7.6% during the quarter as the company gained from the absence of furloughs in this account.
- Tailwinds of better billing rates were offset by employee engagement events (-30bps) and higher travel costs. Management expects fresher billing to start aiding margins in FY24. The quantum of wage hikes is guided to be lower than last year (~8%/~5% offshore/onsite in FY23) and is expected to take place in Q2FY24.
- The company stated that it has partnered with its top client for new opportunities and collaborations, leading to a TCV win of US\$ 100mn in Q4FY23, with healthy revenue growth likely going forward. In the shorter run, salesforce services can slow down but management expects it to form 10% of revenue when the company reaches the US\$ 2bn mark.
- TCV/ACV stood at US\$ 1.6bn/US\$ 1.2bn, taking the book-to-bill ratio to 1.6x/1.13x of FY23 revenue on TTM basis.
- On a quarterly basis, PSYS aspires to achieve dollar revenue growth of 3-5% QoQ. The company also guided for EBIT margin improvement by 200-300bps over the next 2-3 years (FY23 margin at 14.9%).
- Management stated that layoffs in the US are an opportunity for greater offshoring which augurs well for Indian IT and engineering services, and expects an improved demand environment in the next 1-2 quarters. Further, the company affirmed that all the acquired businesses are fully integrated and showing good growth.
- For FY24, PSYS indicated that lateral hiring will be a function of revenue growth, while fresher addition would be between 850-1,000 employees.
- Blended utilisation saw a mild dip to 77.3% as compared to 77.6% in Q3FY23. Onsite (Global Development Center) utilisation rose to 87.9% from 86.8%.
- Management stated that it would resume looking for M&A opportunities in FY24 to add capabilities in the areas of consumer tech, cybersecurity, selective financial services and generative AI.
- PSYS announced final dividend of Rs 12/sh and special dividend of Rs 10/sh, taking the total to Rs 50/sh for full-year FY23.

## Valuation methodology

PSYS aspires to achieve above-industry growth of 7-10% for FY24 and is confident of clocking quarterly growth of 3-5%. The stock is currently trading at 25x FY25E EPS. We assume coverage with BUY and a TP of Rs 5,330 based on 30x FY25E EPS (vs. historical average of 34.4x over FY20-FY23).

## Key risks

- A further rise in interest rates would be a key downside risk to our estimates as deal wins could soften due to longer client decision-making cycles, especially in the financial services, retail, hi-tech and telecom verticals

## Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
HCL Technologies	HCLT IN	34.9	1,053	1,240	BUY
Infosys	INFO IN	62.9	1,225	1,760	BUY
Persistent Systems	PSYS IN	4.4	4,472	5,330	BUY
Tata Consultancy Services	TCS IN	141.9	3,176	3,580	HOLD
Tech Mahindra	TECHM IN	10.6	997	1,160	HOLD
Wipro	WPRO IN	25.2	376	440	HOLD

Source: BOBCAPS Research, NSE | Price as of 25 Apr 2023

## Financials

### Income Statement

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23P	FY24E	FY25E
<b>Total revenue</b>	<b>41,879</b>	<b>57,108</b>	<b>83,506</b>	<b>96,822</b>	<b>1,11,253</b>
EBITDA	6,830	9,582	15,191	18,155	21,063
Depreciation	1,756	1,660	2,719	3,052	3,169
EBIT	5,075	7,922	12,472	15,103	17,894
Net interest inc./(exp.)	0	0	0	0	0
Other inc./(exp.)	1,020	1,322	233	228	204
Exceptional items	0	0	0	0	0
EBT	6,094	9,243	12,705	15,331	18,098
Income taxes	1,588	2,339	3,198	3,909	4,525
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
<b>Reported net profit</b>	<b>4,507</b>	<b>6,904</b>	<b>9,507</b>	<b>11,422</b>	<b>13,574</b>
Adjustments	0	0	0	0	0
<b>Adjusted net profit</b>	<b>4,507</b>	<b>6,904</b>	<b>9,507</b>	<b>11,422</b>	<b>13,574</b>

### Balance Sheet

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23P	FY24E	FY25E
Accounts payables	0	0	0	0	0
Other current liabilities	4,607	9,911	9,151	9,284	10,668
Provisions	2,719	4,195	4,118	4,775	5,486
Debt funds	44	6,004	6,004	6,004	6,004
Other liabilities	0	0	0	0	0
Equity capital	764	764	764	764	764
Reserves & surplus	27,192	32,918	35,065	37,550	41,540
Shareholders' fund	27,957	33,682	35,830	38,315	42,304
<b>Total liab. and equities</b>	<b>35,327</b>	<b>53,792</b>	<b>55,103</b>	<b>58,378</b>	<b>64,463</b>
Cash and cash eq.	2,419	2,978	3,405	5,934	10,716
Accounts receivables	5,709	9,484	10,295	11,937	13,716
Inventories	0	0	0	0	0
Other current assets	4,945	5,355	6,497	7,003	8,046
Investments	17,853	18,445	18,445	18,445	18,445
Net fixed assets	3,277	13,617	12,548	11,146	9,627
CWIP	122	1,071	1,071	1,071	1,071
Intangible assets	86	2,790	2,790	2,790	2,790
Deferred tax assets, net	1,038	1,123	1,123	1,123	1,123
Other assets	0	0	0	0	1
<b>Total assets</b>	<b>35,327</b>	<b>53,792</b>	<b>55,103</b>	<b>58,378</b>	<b>64,463</b>

### Cash Flows

Y/E 31 Mar (Rs mn)	FY21A	FY22A	FY23P	FY24E	FY25E
<b>Cash flow from operations</b>	<b>5,679</b>	<b>8,448</b>	<b>9,204</b>	<b>12,888</b>	<b>15,812</b>
Capital expenditures	(392)	(3,808)	(1,650)	(1,650)	(1,650)
Change in investments	(362)	(212)	0	0	0
Other investing cash flows	1,020	(5,754)	(4,267)	(5,272)	(5,296)
<b>Cash flow from investing</b>	<b>266</b>	<b>(9,773)</b>	<b>(5,917)</b>	<b>(6,922)</b>	<b>(6,946)</b>
Equities issued/Others	0	0	0	0	0
Debt raised/repaid	(324)	3,928	0	0	0
Interest expenses	0	(118)	0	0	0
Dividends paid	(1,627)	(1,987)	(2,861)	(3,436)	(4,084)
Other financing cash flows	0	0	0	0	1
<b>Cash flow from financing</b>	<b>(1,951)</b>	<b>1,823</b>	<b>(2,861)</b>	<b>(3,436)</b>	<b>(4,083)</b>
<b>Chg in cash &amp; cash eq.</b>	<b>3,995</b>	<b>497</b>	<b>426</b>	<b>2,529</b>	<b>4,783</b>
<b>Closing cash &amp; cash eq.</b>	<b>5,456</b>	<b>2,979</b>	<b>3,405</b>	<b>5,934</b>	<b>10,716</b>

### Per Share

Y/E 31 Mar (Rs)	FY21A	FY22A	FY23P	FY24E	FY25E
Reported EPS	56.5	86.6	124.4	149.4	177.6
Adjusted EPS	56.5	86.6	124.4	149.4	177.6
Dividend per share	16.9	26.0	31.1	37.4	44.4
Book value per share	350.5	422.3	468.8	501.3	553.5

### Valuations Ratios

Y/E 31 Mar (x)	FY21A	FY22A	FY23P	FY24E	FY25E
EV/Sales	8.5	6.2	4.3	3.7	3.2
EV/EBITDA	52.1	37.0	23.5	19.9	17.0
Adjusted P/E	79.2	51.7	35.9	29.9	25.2
P/BV	12.8	10.6	9.5	8.9	8.1

### DuPont Analysis

Y/E 31 Mar (%)	FY21A	FY22A	FY23P	FY24E	FY25E
Tax burden (Net profit/PBT)	73.9	74.7	74.8	74.5	75.0
Interest burden (PBT/EBIT)	120.1	116.7	101.9	101.5	101.1
EBIT margin (EBIT/Revenue)	12.1	13.9	14.9	15.6	16.1
Asset turnover (Rev./Avg TA)	127.1	128.2	153.4	170.6	181.1
Leverage (Avg TA/Avg Equity)	1.2	1.4	1.6	1.5	1.5
<b>Adjusted ROAE</b>	<b>17.1</b>	<b>22.4</b>	<b>27.4</b>	<b>30.8</b>	<b>33.7</b>

### Ratio Analysis

Y/E 31 Mar	FY21A	FY22A	FY23P	FY24E	FY25E
<b>YoY growth (%)</b>					
Revenue	17.4	36.4	46.2	15.9	14.9
EBITDA	38.6	40.3	58.5	19.5	16.0
Adjusted EPS	32.4	53.2	43.7	20.1	18.8
<b>Profitability &amp; Return ratios (%)</b>					
EBITDA margin	16.3	16.8	18.2	18.8	18.9
EBIT margin	12.1	13.9	14.9	15.6	16.1
Adjusted profit margin	10.8	12.1	11.4	11.8	12.2
Adjusted ROAE	17.1	22.4	27.4	30.8	33.7
ROCE	15.3	19.0	24.8	29.3	35.3
<b>Working capital days (days)</b>					
Receivables	50	49	43	42	42
Inventory	0	0	0	0	0
Payables	44	56	51	43	40
<b>Ratios (x)</b>					
Gross asset turnover	11.4	6.8	6.4	8.2	10.7
Current ratio	1.8	1.3	1.5	1.8	2.0
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>0.0</b>	<b>(0.1)</b>

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

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

**BUY** – Expected return >+15%

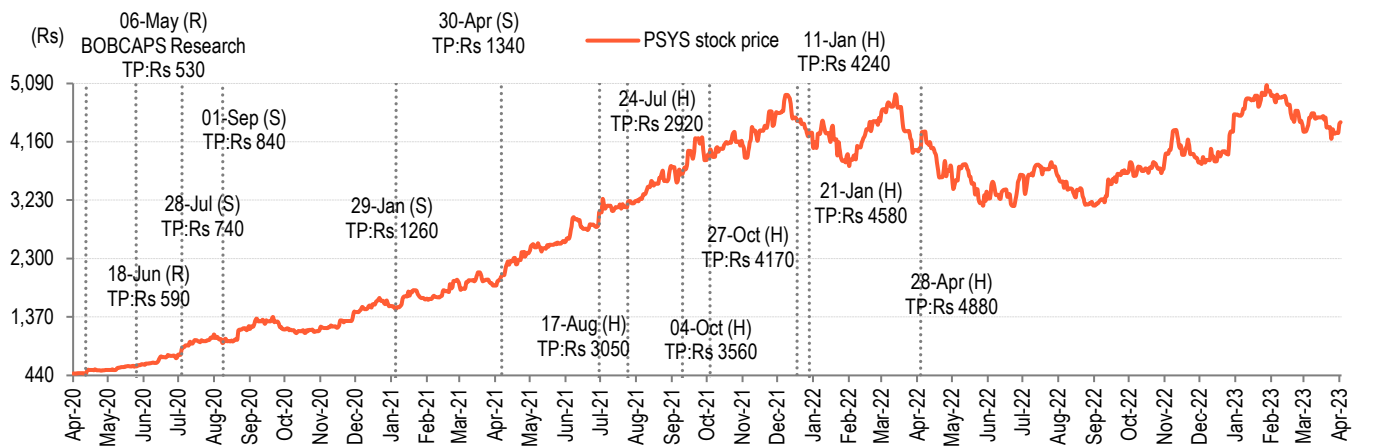
**HOLD** – Expected return from -6% to +15%

**SELL** – Expected return <-6%

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

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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