

Muted numbers; it will take time for the new management to catapult Persistent to new growth orbit, maintain Hold with a revised TP of Rs 614

Current	Previous
CMP: Rs 564	
Rating: Hold	Rating: Hold
Target: Rs 614	Target: Rs 697

(NR-Not Rated)

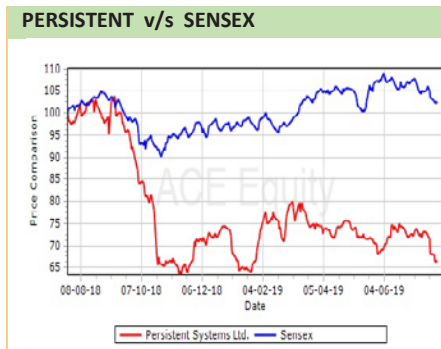
Stock Info	
INDEX	
BSE	533179
NSE	PERSISTENT
Bloomberg	PERSISTENT IN
Reuters	PERSISTENT.BO
Sector	Information Technology
Face Value (Rs)	10
Equity Capital (Rs Mn)	764
Market Cap (Rs Mn)	43104
52w H/L (Rs)	915 / 532
Avg Weekly Vol (BSE+NSE)	294,940

Shareholding Pattern	%
(As on June, 2019)	
Promoters	31.7
Public & Others	68.3

Source: NSE, Arihant Research

Stock Performance (%)	3m	6m	12m
PERSISTENT	-11.9	0.6	-33.4
SENSEX	-3.0	5.2	2.4

Source: ACE Equity, Arihant Research



Source: ACE Equity, Arihant Research

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Persistent Systems came out with muted set of numbers in Q1FY20, which were a tad below our estimate. Revenue was flat (-0.3% YoY) at Rs 8321 mn against our estimate of Rs 8460 mn. EBITDA stood at Rs 1202 mn against our estimate of Rs 1360 mn. PAT for the quarter stood at Rs 825 mn, slightly below our estimate of Rs 865 mn. Due to management transition and client specific (IBM) issues, we already toned down our estimate post last quarter result. As expected, this quarter was lacklustre for Persistent and Q1FY20 numbers mostly matched our estimate. We are of the opinion that it will take time for the new management to catapult the company in a new growth orbit and till that time stock price might remain under pressure. We have neutral view on the stock in absence of any near term trigger, however due to inexpensive valuation maintain our Hold rating with a revised target price of Rs 614.

Q1FY20 Highlights

- USD Revenue stood at US\$119.6 mn, growth of 1.1% QoQ and decline of 3.2% YoY. In Rupee terms, revenue stood at Rs 8321 mn, which was flat sequentially and suffered a de-growth of 0.3% YoY.
- EBITDA stood at Rs 1202 mn, de-growth of 14.2% YoY and 0.4% QoQ. EBITDA margins stood at 14.4%, v/s 16.8% YoY and 14.5% QoQ.
- PAT stood at Rs 825 mn, decline of 5.6% YoY and 2.4% QoQ. PAT margins stood at 9.9% v/s 10.5% YoY and 10.2% QoQ.
- In USD terms, digital revenues for the quarter declined 5.9% QoQ, unlike its peers which showed strong digital growth in this quarter. The slow digital growth can clearly be attributed to company specific inefficiency, as it is in sharp contrast to industry wide trend of strong digital growth.
- During the quarter the company acquired youperience, bringing it together with PARX to create Europe's leading boutique Salesforce partner.

Valuations

At CMP of Rs 564, Persistent is trading at FY20E and FY21E, P/E of 11.6x and 10.6x respectively, which is inexpensive. However despite comfortable valuation, after factoring in muted Q1FY20 results, we have reduced our target P/E multiple from 12.5x to 11.5x, and now value the stock at a target P/E of 11.5x its FY21E earnings, which yields a price of Rs 614 per share. **We maintain our Hold rating on the stock purely on valuation comfort.**

Financial Performance

YE March (Rs Mn)	Net Sales	EBITDA	PAT	EPS (Rs)	EBITDA Margin %	RoE (%)	P/E (x)
FY18	30,337	4,687	3,231	40.8	15.5	15.2	13.8
FY19	33,660	5,806	3,517	44.5	17.2	15.0	12.7
FY20E	35,500	6,177	3,732	48.8	17.4	14.7	11.6
FY21E	37,800	6,615	4,082	53.4	17.5	15.3	10.6

Source: Company, Arihant Research

Q1FY20 Financial Performance

Rs Mn (consolidated)	Q1FY20	Q4FY19	Q1FY19	Q-o-Q	Y-o-Y
Net Revenue	8,321	8,319	8,343	0.0%	-0.3%
Employee Cost	5,776	5,722	5,463	0.9%	5.7%
Other Expenses	1,343	1,389	1,479	-3.3%	-9.2%
EBITDA	1,202	1,207	1,401	-0.4%	-14.2%
<i>EBITDA Margin %</i>	<i>14.4%</i>	<i>14.5%</i>	<i>16.8%</i>	<i>-7bps</i>	<i>-234bps</i>
Depreciation	386	377	401	2.5%	-3.7%
EBIT	816	830	1,000	-1.7%	-18.4%
Other Income	300	284	187	5.8%	60.8%
Finance Cost	19	1	0	NA	NA
Exceptional Item	-	-	-	-	-
PBT	1,098	1,113	1,186	-1.4%	-7.5%
Tax Expense	273	268	313	1.7%	-12.7%
Effective Tax Rate %	24.9%	24.1%	26.4%	+75bps	-150bps
PAT	825	845	873	-2.4%	-5.6%
MI & Associates	-	-	-	-	-
Consolidated PAT	825	845	873	-2.4%	-5.6%
<i>PAT Margin %</i>	<i>9.9%</i>	<i>10.2%</i>	<i>10.5%</i>	<i>-24bps</i>	<i>-56bps</i>
EPS (Rs)	10.8	10.7	10.9	1.1%	-1.2%

Source: Company, Arianth Research

Post Result Conference Call Highlights

- IP led revenue was soft during Q1FY20, constituting 21.5% of total revenue compared to 27.4% in Q1FY19, which impacted gross margin.
- EBITDA margin had negative impact of -50bps due to utilisation level and -30bps due to cross currency headwinds.
- Persistent has completed its buyback process on June 27, 2019 and have brought back 3.575 mn shares bringing the equity capital to Rs 764 mn.
- The company incurred operational capex of Rs 172 mn during the quarter and had Rs 80 mn of forex gain.
- Client engagement showed some improvement during the quarter with large (USD >3 mn) clients being 22 in numbers compared to 18 in Q1FY19.
- Wanted Deloitte as auditor for 2-years and not 5-years, but since shareholders has not approved the 2-year period, so Deloitte declined the offer. The company will approach shareholders in an EGM for appointment of fresh auditor, till that time Deloitte will continue as auditor for the company.
- Hiring has been strong in last few months in Persistent.
- Enough appetite for services offering in the advisory side.

Future Outlook

We believe going forward, for Persistent, the focus will be to accelerate revenue growth by 1) monetizing and optimizing IP assets, 2) forging partnerships with more platforms, apart from those of top clients and 3) deploying cash for a few acquisitions.

Consolidated Financials

Income Statement

Y/E March (Rs Mn)	FY18	FY19	FY20E	FY21E
Revenues	30,337	33,660	35,500	37,800
<i>Change (%)</i>	5.4%	11.0%	5.5%	6.5%
Total Expenses	25,650	27,854	29,323	31,185
EBITDA	4,687	5,806	6,177	6,615
Other Income	1,190	630	710	869
Depreciation	1,585	1,573	1,704	1,814
Interest	0	0	0	0
PBT	4,293	4,863	5,183	5,670
Extra-ordinary	0	0	0	0
PBT after ext-ord.	4,293	4,863	5,183	5,670
Tax	1,062	1,347	1,451	1,588
<i>Rate (%)</i>	24.7%	27.7%	28.0%	28.0%
PAT	3,231	3,517	3,732	4,082
MI & Associates	0	0	0	0
Consolidated PAT	3,231	3,517	3,732	4,082
<i>Change (%)</i>	7.2%	8.8%	6.1%	9.4%

Source: Company, Arian Research

Balance Sheet

Y/E March (Rs Mn)	FY18	FY19	FY20E	FY21E
Sources of Funds				
Share Capital	800	791	764	764
Reserves & Surplus	20,472	22,656	24,704	25,836
Net Worth	21,272	23,447	25,468	26,600
Loan Funds	17	12	12	12
MI, Deferred Tax & other Liabilities	270	0	0	0
Capital Employed	21,559	23,459	25,480	26,612
Application of Funds				
Net Block	2,581	2,331	2,831	3,331
CWIP	52	316	316	316
Other Non-current Assets	2,669	2,094	2,094	2,094
Deferred Tax Assets	642	405	405	405
Net Fixed Assets	5,945	5,146	5,646	6,146
Investments	8,797	7,641	7,641	7,641
Debtors	4,847	4,923	4,863	5,178
Inventories	0	0	0	0
Cash & Bank Balance	2,414	6,724	6,292	6,671
Loans & Advances & other CA	4,705	4,122	7,840	8,092
Total Current Assets	11,966	15,769	18,995	19,942
Current Liabilities	3,390	3,158	4,863	5,178
Provisions	1,759	1,939	1,939	1,939
Net Current Assets	6,817	10,671	12,193	12,824
Total Assets	21,559	23,459	25,480	26,612

Source: Company, Arian Research

Cash Flow Statement

Y/E March (Rs Mn)	FY18	FY19	FY20E	FY21E
PBT	4,293	4,863	5,183	5,670
Depreciation	1,585	1,573	1,704	1,814
Interest & others	-496	-417	-709	-867
Cash flow before WC changes	5,381	6,018	6,178	6,617
(Inc)/dec in working capital	44	207	1,765	0
Operating CF after WC changes	5,426	6,226	7,943	6,617
Less: Taxes	-1,214	-1,347	-1,451	-1,588
Operating Cash Flow	4,212	4,879	6,492	5,029
(Inc)/dec in F.A + CWIP	-651	438	-500	-500
(Pur)/sale of investment	-2,822	1,156	0	0
Cash Flow from Investing	-3,474	1,594	-500	-500
Free Cash Flow (FCF)	3,560	4,505	5,992	4,529
Loan raised/(repaid)	-5	-5	0	0
Equity raised	0	-9	-27	0
Interest & others	1,120	-3,183	-7,401	-5,154
Dividend	-950	1,004	1,004	1,004
Cash Flow from Financing Activities	166	-2,193	-6,424	-4,150
Net inc/(dec) in cash	904	4,280	-432	379
Opening balance of cash	1,510	2,414	6,724	6,292
Closing balance of cash	2,414	6,694	6,292	6,671

Source: Company, Arianth Research

Key Ratios

Y/E March	FY18	FY19	FY20E	FY21E
Per share (Rs)				
EPS	40.8	44.5	48.8	53.4
CEPS	63.0	66.6	71.1	77.2
BVPS	278.3	306.8	333.2	348.1
DPS	10.0	11.0	11.0	11.0
Div. Payout (%)	23.7%	23.9%	22.5%	20.6%
Valuation (x)				
P/E	13.8	12.7	11.6	10.6
P/CEPS	9.0	8.5	7.9	7.3
P/BV	2.0	1.8	1.7	1.6
EV/EBITDA	8.7	6.3	6.0	5.5
Dividend Yield (%)	1.8%	2.0%	2.0%	2.0%
Return Ratio (%)				
EBIDTA Margin	15.5%	17.2%	17.4%	17.5%
PAT Margin	10.6%	10.4%	10.5%	10.8%
ROE	15.2%	15.0%	14.7%	15.3%
ROCE	14.4%	18.0%	17.6%	18.0%
Leverage Ratio (x)				
Total D/E	0.0	0.0	0.0	0.0
Net D/E	-0.1	-0.3	-0.2	-0.3
Turnover Ratios				
Asset Turnover (x)	1.4	1.4	1.4	1.4
Receivable Days	58	53	50	50
Payable days	62	55	50	50

Source: Co, Arianth Research

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Stock Rating Scale

	Absolute Return
BUY	>20%
ACCUMULATE	12% to 20%
HOLD	5% to 12%
NEUTRAL	-5% to 5%
REDUCE	<-5%

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