

**Stable performance but uncertain growth prospects;
not supporting rich valuations**

CMP: Rs 689

Rating: HOLD

Target Price: Rs 727

Stock Info

BSE	533179
NSE	PERSISTENT
Bloomberg	PERSISTENT IN
Reuters	PERSISTENT.BO
Sector	IT
Face Value (Rs)	10
Equity Capital (Rs mn)	764
Mkt Cap (Rs mn)	115,921
52w H/L (Rs)	2,059 / 1178
Avg Yearly Vol (in 000')	123

Shareholding Pattern %

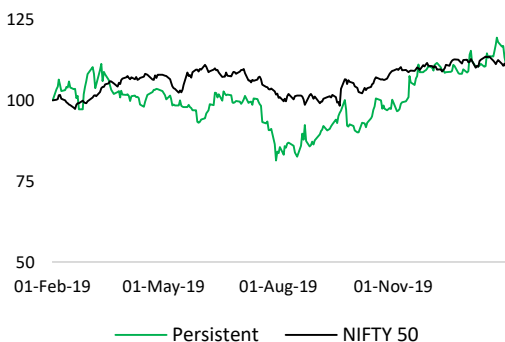
(As on Dec, 2019)

Promoters	31.91
FII	19.49
DII	23.49
Public & Others	25.11

Stock Performance (%)

	3m	6m	12m
Persistent	13.1	34.7	16.4
Nifty	2.3	7.7	13.1

Persistent Vs Nifty



Persistent Systems beat our Q3FY20 estimates but missed EBITDA and PAT estimates marginally. Consolidated revenue for the quarter stood at Rs 9,227 mn, registering +6.8% YoY/+4.3% QoQ growth. EBITDA fell to Rs 1,235 mn, (down) -15.5% YoY/+1.5% QoQ. EBITDA margins also fell by -353 bps YoY/-37 bps YoY to 13.4%. Contraction in margin came on the back of rising staff costs which increased by +13.4% YoY/+5.2% QoQ. Consolidated PAT for the quarter stood at Rs 879 mn falling marginally short of our estimate of Rs 935 mn, and down -4.1% YoY/ up 2.2% QoQ. We are of the opinion that it will take time for the new management to catapult the company to a new growth orbit as so far change in leadership has not yielded any perceptible result. We maintain our FY20E/21E estimates to build in stable margins, however due to inexpensive valuation maintain our Hold rating on the stock, with a revised target price of Rs 727.

Q3FY20 Highlights

USD Revenue stood at US\$129.4 mn, up by +3.1% QoQ/7.1% YoY. In Rupee terms, revenue was at Rs 9,227 mn, growing 4.3% QoQ/+6.8% YoY.

EBITDA stood at Rs 1,235 mn, de-growth of -15.5% YoY/ up +1.5% QoQ. EBITDA margin was at 13.8% v/s 17.2% YoY and 14% QoQ.

PAT stood at Rs 879 mn, down -4.1% YoY /+2.2% QoQ. PAT margins fell to 9.5% v/s 10.6% in Q3FY19 and 9.7% QoQ.

During the quarter contribution from top 10 clients increased to 53.4% against 52.4% in Q2FY19. However top client contribution continued to remain muted at 23.7% in Q2FY20 against 25.7% in Q2FY19.

The blended utilization stood at 79.8% while that of global delivery centres stood at 84.0% for Q3FY20. The attrition rate also came down to 14.9% with 92.4% of employees counted in technical workforce. North America still contributed 80.1% of the revenue contribution for the quarter despite this being weak quarter seasonally.

Valuations

At CMP of Rs 689, Persistent trades at FY20E and FY21E, P/E of 13.1x and 11.6x respectively. Factoring in Q3FY20 results, we maintain our FY20E/FY21E estimates to build in stable margin for FY20E/FY21E. We marginally raised our target P/E multiple from 12.0x to 14.0x its FY21E earnings and arrive at a target price of 727 per share, and maintain our **HOLD** rating.

Particulars (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	14.8
FY19	33,660	5,806	3,517	44.5	17.2	15.0	13.5
FY20E	35,500	4,935	3,515	46.0	13.9	13.8	13.1
FY21E	37,800	5,859	3,969	51.9	15.5	14.9	11.6

Source: Arihant Research, Company Filings, Ace Equity, Bloomberg

Q3 FY20 - Quarterly Performance (Consolidated)

Rs Mn (consolidated)	Q3FY20	Q2FY20	Q3FY19	Q-o-Q	Y-o-Y	9MFY20	9MFY19	Y-o-Y
Net Revenue	9,227	8,846	8,642	4.3%	6.8%	26,394	25,341	4.2%
Employee Cost	6,593	6,267	5,815	5.2%	13.4%	18,636	17,018	9.5%
Other Expenses	1,399	1,363	1,365	2.7%	2.5%	4,105	3,968	3.5%
EBITDA	1,235	1,216	1,462	1.5%	-15.5%	3,653	4,355	-16.1%
<i>EBITDA Margin %</i>	<i>13.4%</i>	<i>13.8%</i>	<i>16.9%</i>	<i>-37bps</i>	<i>-353bps</i>	<i>13.8%</i>	<i>17.2%</i>	<i>-335bps</i>
Depreciation	428	425	396	0.8%	8.1%	1,239	1,196	3.7%
EBIT	807	792	1,066	1.9%	-24.3%	2,414	3,160	-23.6%
Other Income	348	382	230	-9.1%	51.2%	1,031	593	73.9%
Finance Cost	15	18	1	NA	NA	52	2	NA
Exceptional Item	-	-	-	-	-	-	-	-
PBT	1,140	1,156	1,295	-1.4%	-12.0%	3,393	3,750	-9.5%
Tax Expense	260	295	378	-11.7%	-31.1%	828	1,078	-23.2%
Effective Tax Rate %	22.9%	25.5%	29.2%	-266bps	-633bps	24.4%	28.7%	-434bps
PAT	879	861	917	2.2%	-4.1%	2,565	2,672	-4.0%
MI & Associates	-	-	-	-	-	-	-	-
Consolidated PAT	879	861	917	2.2%	-4.1%	2,565	2,672	-4.0%
<i>PAT Margin %</i>	<i>9.5%</i>	<i>9.7%</i>	<i>10.6%</i>	<i>-20bps</i>	<i>-108bps</i>	<i>9.7%</i>	<i>10.5%</i>	<i>-83bps</i>
EPS (Rs)	11.50	11.26	11.46	2.2%	0.4%	33.41	33.40	0.0%

Source: Arianth Research, Company Filings, Ace Equity, Bloomberg

Key Concall Highlights

- The management attributed the flat EBITDA margin to the transition cost involved in 2 out of 4 large deal won in Q3FY20. The company also expects the margins to improve going through Q4FY20 and ahead.
- The management also expects to maintain the Off-site revenue a around 65% which blipped by 200 bps to 64%.
- The management maintained positivity on rebounding revenues from BFSI sector in next few quarters since the BFS segment remains weak in general during Q3FY20.
- The company's firm business over next 12 months stood at USD 424 mn while the addition of a another BFS client will help its growth.
- Under the broader leadership talent acquisition program, the company appointed 3 new executive Vice Presidents during the quarter.
- The company saw an increase of 49 in headcount during the quarter. The employee utilization stood at 79.3% from 80.7% last quarter while the attrition rate also improved to 11.9%.

Key Financials

Income Statement (Rs Mn)	FY18	FY19	FY20E	FY21E	Cash Flow Statement (Rs Mn)	FY18	FY19	FY20E	FY21E
Revenues	30,337	33,660	35,500	37,800	PBT	4,293	4,863	4,687	5,292
<i>Change (%)</i>	5.4%	11.0%	5.5%	6.5%	Depreciation	1,585	1,573	1,598	1,701
Total Expenses	25,650	27,854	30,566	31,941	Interest & others	-496	-417	-1,349	-1,132
EBITDA	4,687	5,806	4,935	5,859	Cash flow before WC changes	5,381	6,018	4,936	5,861
Other Income	1,190	630	1,350	1,134	(Inc)/dec in working capital	44	207	1,765	0
Depreciation	1,585	1,573	1,598	1,701	Operating CF after WC changes	5,426	6,226	6,700	5,861
Interest	0	0	0	0	Less: Taxes	-1,214	-1,347	-1,172	-1,323
PBT	4,293	4,863	4,687	5,292	Operating Cash Flow	4,212	4,879	5,529	4,538
Extra-ordinary	0	0	0	0	(Inc)/dec in F.A + CWIP	-651	438	-500	-500
PBT after ext-ord.	4,293	4,863	4,687	5,292	(Pur)/sale of investment	-2,822	1,156	0	0
Tax	1,062	1,347	1,172	1,323	Cash Flow from Investing	-3,474	1,594	-500	-500
<i>Rate (%)</i>	24.7%	27.7%	25.0%	25.0%	Free Cash Flow (FCF)	3,560	4,505	5,029	4,038
PAT	3,231	3,517	3,515	3,969	Loan raised/(repaid)	-5	-5	0	0
MI & Associates	0	0	0	0	Equity raised	0	-9	-27	0
Consolidated PAT	3,231	3,517	3,515	3,969	Interest & others	1,120	-3,153	-6,438	-4,662
<i>Change (%)</i>	7.2%	8.8%	0.0%	12.9%	Dividend	-950	1,004	1,004	1,004
					Cash Flow from Financing Activities	166	-2,163	-5,461	-3,658
					Net inc /(dec) in cash	904	4,310	-432	380
					Opening balance of cash	1,510	2,414	6,724	6,292
					Closing balance of cash	2,414	6,724	6,292	6,672

Balance Sheet (Rs Mn)	FY18	FY19	FY20E	FY21E	Key Ratios	FY18	FY19	FY20E	FY21E
Sources of Funds					Per share (Rs)				
Share Capital	800	791	764	764	EPS	40.8	44.5	46.0	51.9
Reserves & Surplus	20,472	22,656	24,704	25,836	CEPS	63.0	66.6	66.9	74.2
Net Worth	21,272	23,447	25,468	26,600	BVPS	278.3	306.8	333.2	348.1
Loan Funds	17	12	12	12	DPS	10.0	11.0	11.0	11.0
MI, Deferred Tax & other Liab.	270	0	0	0	Div. Payout (%)	23.7%	23.9%	23.9%	21.2%
Capital Employed	21,559	23,459	25,480	26,612	Valuation (x)				
Application of Funds					P/E	14.8	13.5	15.0	13.3
Net Block	2,581	2,331	2,831	3,331	P/CEPS	9.6	9.0	10.3	9.3
CWIP	52	316	316	316	P/BV	2.2	2.0	2.1	2.0
Other Non-current Assets	2,669	2,094	2,094	2,094	EV/EBITDA	9.3	6.8	9.4	7.9
Deferred Tax Assets	642	405	405	405	Dividend Yield (%)	1.7%	1.8%	1.6%	1.6%
Net Fixed Assets	5,945	5,146	5,646	6,146	Return Ratio (%)				
Investments	8,797	7,641	7,641	7,641	EBIDTA Margin	15.5%	17.2%	13.9%	15.5%
Debtors	4,847	4,923	4,863	5,178	PAT Margin	10.6%	10.4%	9.9%	10.5%
Inventories	0	0	0	0	ROE	15.2%	15.0%	13.8%	14.9%
Cash & Bank Balance	2,414	6,724	6,292	6,672	ROCE	14.4%	18.0%	13.1%	15.6%
Loans & Advances & other CA	4,705	4,122	7,840	8,092	Leverage Ratio (x)				
Total Current Assets	11,966	15,769	18,995	19,942	Total D/E	0.0	0.0	0.0	0.0
Current Liabilities	3,390	3,158	4,863	5,178	Net D/E	-0.1	-0.3	-0.2	-0.3
Provisions	1,759	1,939	1,939	1,939	Turnover Ratios				
Net Current Assets	6,817	10,671	12,193	12,825	Asset Turnover (x)	1.4	1.4	1.4	1.4
Total Assets	21,559	23,459	25,480	26,612	Receivable Days	58	53	50	50
					Payable days	62	55	50	50

Source: Arianth Research, Company Filings, Ace Equity, Bloomberg

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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% to -12%
SELL	<-12%

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