

Persistent Systems

Preparing for the big league

NEUTRAL

22 December 2014

BSE Sensex: 27702

Sector: IT Services

Stock data

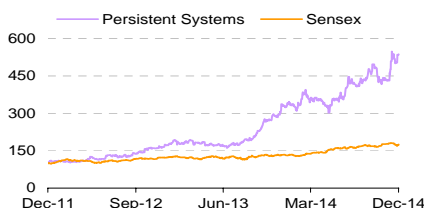
CMP (Rs)	1,604
Mkt Cap (Rsbn/US\$bn)	64.2 / 1.0
Target Price (Rs)	1,660
Change in TP (%)	+23.0
Potential from CMP (%)	+3.5
Earnings change (%)	
FY15E	↔
FY16E	↔
FY17E	↔
Bloomberg code	PSYS IN
1-yr high/low (Rs)	1917/880
6-mth avg. daily volumes (m)	0.06
6-mth avg. daily traded value (Rsm/US\$m)	83.7 / 1.32
Shares outstanding (m)	40.0
Free float (%)	61.1
Promoter holding (%)	39.0

Persistent Systems' (Persistent) management, during the Investor Day, showcased its 'ahead of the curve' technological prowess and strategy to create market position in Enterprise Digital Transformation (EDT) space. Key highlights:

- ◆ **Persistent striving to be the chosen vendor in EDT:** Enterprises globally are spending on digital transformation in addition to IT modernization. As per Zinnov, it is a ~US \$70bn market with ~26% CAGR estimated by 2020E. Despite competition, Persistent hopes to gain scale in this rapidly growing market.
- ◆ **From me-too player to a leader in a niche category:** Based on its superior technological capabilities and association of two decades with global software vendors in product development, Persistent aspires to emerge as a preferred vendor for enterprises in the latter's digital transformation journey.
- ◆ **Acquisitions to drive IP business growth:** Persistent would continue to innovate and build own intellectual properties. However, growth would be driven by acquisition of non-strategic products (end-of-life) of partners. Product upgrades and re-positioning should help Persistent cross-sell and extend product life.
- ◆ **FY15 growth guidance re-affirmed:** The management reiterated the ~15% revenue growth guidance for FY15, which implies ~6% CQGR for the next two quarters. The focus is to optimize PBT margins even as investments in sales and technology would continue to ensure long-term growth.

We believe the management has set its sights on getting into the big league with enterprises investing in digital transformation over the next decade. We build in ~19% CAGR for both USD revenue and INR EPS over FY14-17E and value Persistent at Rs1,660 (based on 16x FY17E EPS). Maintain Neutral as valuations leave limited upside in the near term even as we like the business model.

Price performance – relative and absolute



(%)	3-mth	6-mth	1-yr
Persistent Systems	13.3	45.9	59.2
BSE Sensex	1.8	10.3	31.4

Key financials

As on 31 March	FY13	FY14	FY15E	FY16E	FY17E
Net sales (Rs m)	12,945	16,692	19,026	23,334	28,270
Adj. net profit (Rs m)	1,876	2,493	2,970	3,593	4,153
Shares in issue (m)	40	40	40	40	40
Adj. EPS (Rs)	46.9	62.3	74.2	89.8	103.8
% change	32.3	32.9	19.1	21.0	15.6
PE (x)	34.2	25.7	21.6	17.9	15.5
Price/ Book (x)	6.3	5.2	4.5	3.8	3.2
EV/ EBITDA (x)	18.1	13.8	13.9	10.7	8.7
RoE (%)	20.2	22.3	22.4	22.9	22.2
RoCE (%)	26.6	27.9	24.4	27.7	28.2

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Income statement

Year to 31 Mar (Rs m)	FY13	FY14	FY15E	FY16E	FY17E
Net sales	12,945	16,692	19,026	23,334	28,270
% growth	29.4	28.9	14.0	22.6	21.2
Operating expenses	9,593	12,389	14,776	17,964	21,895
EBITDA	3,352	4,303	4,250	5,370	6,375
% change	44.2	28.4	(1.2)	26.3	18.7
Other income	283	299	458	531	657
Net interest	(0)	-	-	-	-
Depreciation	783	1,026	947	998	1,072
Pre-tax profit	2,630	3,427	4,150	5,102	5,961
Current tax	754	934	1,180	1,509	1,808
Profit after tax	1,876	2,493	2,970	3,593	4,153
Net profit after non-recurring items	1,876	2,493	2,970	3,593	4,153
% change	32.3	32.9	19.1	21.0	15.6

Balance sheet

As on 31 Mar (Rs m)	FY13	FY14	FY15E	FY16E	FY17E
Paid-up capital	400	400	400	400	400
Reserves & surplus	9,783	11,823	13,951	16,655	19,919
Total shareholders' equity	10,183	12,223	14,351	17,055	20,319
Total current liabilities	1,835	2,785	2,953	3,383	3,877
Total debt	14	32	-	-	-
Other non-current liabilities	639	394	107	107	107
Total liabilities	2,489	3,210	3,059	3,490	3,984
Total equity & liabilities	12,671	15,434	17,410	20,545	24,303
Net fixed assets	4,677	4,362	4,378	4,917	5,494
Investments	173	823	1,651	1,651	1,651
Total current assets	6,908	9,368	10,941	13,537	16,717
Deferred tax assets	190	260	263	263	263
Other non-current assets	723	620	177	177	177
Working capital	5,073	6,584	7,988	10,154	12,840
Total assets	12,671	15,434	17,410	20,545	24,303

Cash flow statement

Year to 31 Mar (Rs m)	FY13	FY14	FY15E	FY16E	FY17E
Pre-tax profit	2,630	3,427	4,150	5,102	5,961
Depreciation	783	1,026	947	998	1,072
Chg in Working capital	(839)	(57)	(831)	(686)	(786)
Total tax paid	(754)	(934)	(1,180)	(1,509)	(1,808)
Ext ord. Items & others	568	(245)	(287)	-	-
Operating cash Inflow	2,388	3,216	2,799	3,905	4,439
Capital expenditure	(1,735)	(711)	(963)	(1,537)	(1,649)
Free cash flow (a+b)	653	2,505	1,836	2,369	2,790
Chg in investments	(1,251)	(1,606)	(796)	-	-
Debt raised/(repaid)	8	18	(32)	-	-
Dividend (incl. tax)	(409)	(562)	(702)	(889)	(889)
Misc	227	40	(143)	-	-
Net chg in cash	(772)	395	163	1,480	1,901

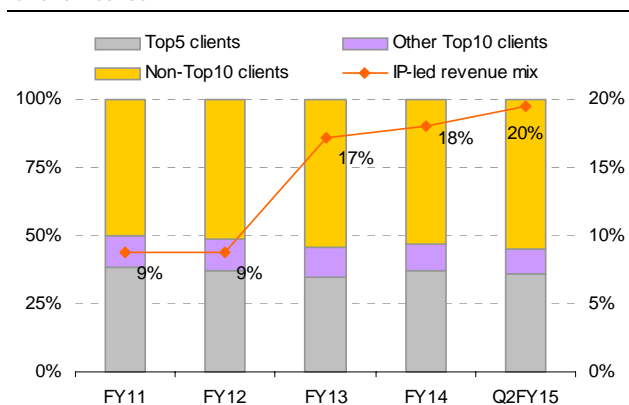
Key ratios

Year to 31 Mar	FY13	FY14	FY15E	FY16E	FY17E
EBITDA margin (%)	25.9	25.8	22.3	23.0	22.6
EBIT margin (%)	19.8	19.6	17.4	18.7	18.8
PAT margin (%)	14.5	14.9	15.6	15.4	14.7
RoE (%)	20.2	22.3	22.4	22.9	22.2
RoCE (%)	26.6	27.9	24.4	27.7	28.2
Gearing (x)	(0.4)	(0.4)	(0.4)	(0.4)	(0.4)

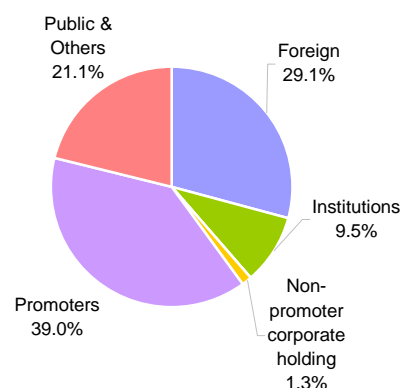
Valuations

Year to 31 Mar	FY13	FY14	FY15E	FY16E	FY17E
Reported EPS (Rs)	46.9	62.3	74.2	89.8	103.8
Adj. EPS (Rs)	46.9	62.3	74.2	89.8	103.8
PE (x)	34.2	25.7	21.6	17.9	15.5
Price/ Book (x)	6.3	5.2	4.5	3.8	3.2
EV/ Net sales (x)	4.7	3.5	3.1	2.5	2.0
EV/ EBITDA (x)	18.1	13.8	13.9	10.7	8.7
EV/ CE (x)	5.6	4.7	4.1	3.4	2.7

Client metrics



Shareholding pattern



As of September 2014

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1. Outperformer : More than 5% to Index
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