

PERSISTENT SYSTEMS

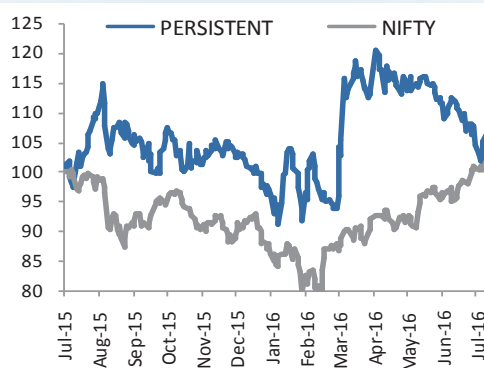
Result Update	
CMP	689
Target Price	660
Previous Target Price	-
Upside	-4%
Change from Previous	-

Market Data	
BSE Code	533179
NSE Symbol	PERSISTENT
52wk Range H/L	798/575
Mkt Capital (Rs Cr)	55.00B
Av. Volume	16230
Nifty	8,635.65

Stock Performance			
	1Month	1Year	YTD
Absolute	-5.6	4.1	2.1
Rel.to Nifty	-12.3	4.0	1.8

Share Holding Pattern-%			
	Jun-16	Mar-16	Dec-15
Promoters	38.2	38.5	38.5
Public	57.2	56.8	56.49
Others	4.6	4.7	
Total	100.0	100.0	100.0

Company Vs NIFTY



Persistent Systems: Performance at a glance:

Persistent System's performance beat out estimate on growth prospectus. In 1QFY17, Net Revenue grew 4.3% QoQ to \$104.76 Mn with noticeable growth in IP-Led business as compared to \$100.43 Mn in the previous quarter of the same year. EBITDA Margin grew from 14.7% to 15.1% QoQ. Net profit margin declined from 10.7% to 10.4% QoQ.

Organic and Inorganic Growth:

During the quarter, the IBM-Watson IoT deal had revenue of \$11.5 Mn and Citrix reported \$2 Mn. Excluding the incremental addition from these two, organic revenue was flat during the quarter i.e. \$91.6 Mn. In 1QFY17, ISV Segment grew 3.4% QoQ from \$46.0 Mn to \$47.6 Mn. Enterprise grew 5.9% QoQ from \$26.1 Mn to \$27.7 Mn. IP-Led revenue grew 4.3% QoQ from \$28.3 Mn to \$29.5 Mn.

Margins to remain a pain-point:

Management said costs associated with the IBM deal are expected to weigh upon margins to the tune of 200bps in FY17. Margins to remain volatile QoQ. In 2QFY17, wage hike would impact the margin by 0.7-0.8%. Although more of it set off by traditional levers.

See improved profitability in IBM-IoT alliance over next few years

- 1) In FY17, Management said IBM IoT partnership contribute about \$50 - 55 mn revenue.
- 2) Investment in this alliance could effect the margins by 200 bps in FY17.
- 3) Enterprise revenue growth traction remains strong, will bounce back in the coming quarters.
- 4) Will do more local hirings in foreign geographies, visa cost will similar to last quarters

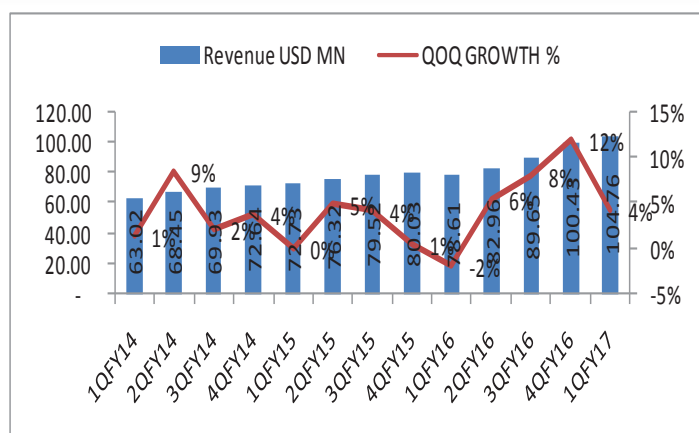
Outlook and Valuation

As management stated that IBM partnership will be revenue accretive and has a potential to add 15-20% revenue of FY16 to FY17. So our estimate for FY17 will be around 338 - 450 crore in FY17. However, investment in this alliance will affect the company's operating profit margin by 200 - 250bps in FY17. Hence we recommend "Neutral" to this stock with target price of Rs 660.

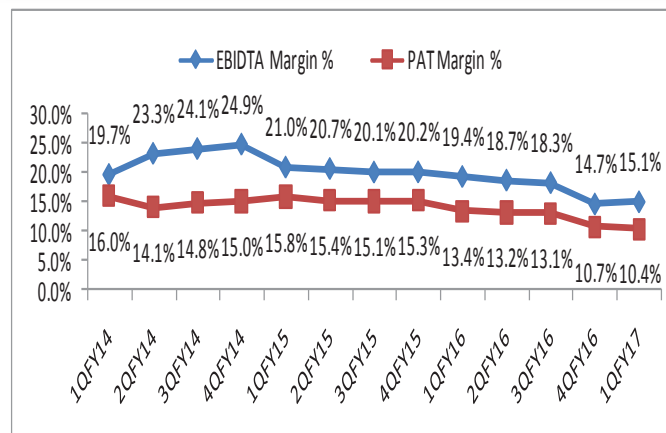
Financials	FY13	FY14	FY15	FY16	FY17E
Sales	1295	1669	1891	2312	3025
EBITDA	313	414	390	414	469
Net Profit	188	249	291	297	330
EBITDA%	24.2%	24.8%	20.6%	17.9%	15.5%
P/E	5.8	8.4	19.7	19.5	19.8

(Source: Company/Eastwind)

Revenue growth QoQ



Key Trend in Margin

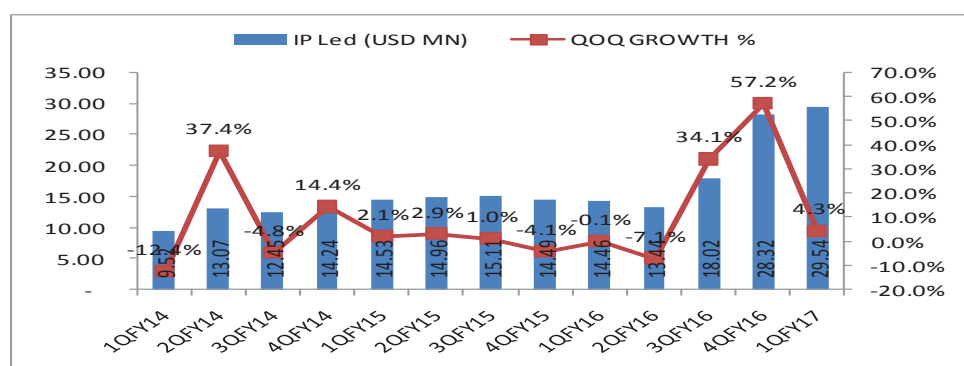


Industry Segment Classification (In \$ mn)

Segment Revenue	1QFY15	2QFY15	3QFY15	4QFY15	1QFY16	2QFY16	3QFY16	4QFY16	1QFY17
ISV (\$mn)	43.81	44.49	46.04	46.26	44.81	47.45	45.99	46.00	47.56
Enterprise (\$ mn)	14.39	16.87	18.37	19.29	19.34	22.07	25.64	26.11	27.66
IP Led (\$ mn)	14.53	14.96	15.11	14.49	14.46	13.44	18.02	28.32	29.54
Total	72.73	76.32	79.52	80.03	78.61	82.96	89.65	100.43	104.76

- Management seeing the challenging environment for ISV clients of the company especially the 'pre-Internet and pre-cloud' clients.
- The total contribution from the IBM-Watson IoT deal during the quarter was \$11.5 Mn (versus \$8 Mn in 4QFY16). The contribution from Citrix was USD2m in 1Q. Excluding this IP-Led revenue declined by 13% QoQ.
- Enterprise grew by 5.9% QoQ compared to 4QFY16 growth of 1.8% QoQ. Traction in this segment has relatively weakened over the last two quarters.

Aggressive foray in IP led revenue



Excluding IBM's revenue, IP-Led revenue declined by 13% QoQ

Management Commentary:

>>> In FY17, IBM Deal : expects ~USD50m of revenue
 >>> In FY17, IBM deal to put 200 bps pressure on PAT margins
 >>> In FY17, Management seeing the challenging environment for ISV clients of the company especially the 'pre-Internet and pre-cloud' clients.

Recent Aquisition :

Persistent Systems Limited signed an agreement to acquire assets of PRM Cloud Solutions Pty Ltd., an Australia based company engaged in Salesforce implementation services

Revenue : FY15 AUD 946 k FY14 : 875 K FY13: 873 K

Cost of acquisition :

- 1) payment of AUD 500 K adjustment for prepaid work and employee liabilities on completion of transaction
- 2) additional payment of up to AUD 280 K on the first anniversary of the completion of the transaction

Consideration : In Cash

Deal closed on 8th april,2016

Key Triggers

>>> Better-than-estimated margins from aggressive exercise of levers.
 >>> Sharper growth in IBM Watson IoT
 >>> Strong rebound in Enterprise growth

Key Risk

>>> Continued revenue sluggishness in ISV segment (ex-IBM)
 >>> Pressure on margins from higher S&M to sell products/investments in latest collaboration with top customer
 >>> Decline in discretionary activity

About Company

Persistent Systems (PSYS) began its operations in 1990 and is engaged in software development services for software product companies and enterprises in verticals such as infrastructure & systems (51% of revenue) financial services (20% of revenue), telecom (16% of revenue) and lifescience (14% of revenues). It is a leading global player in offshore software product development with revenue across geographies; Americas (85% of revenue), Europe (6% of revenue) and Australia & APAC and ~20% of its revenue is product-based under the brand 'Accelerite'.

Financials Snap Shot

INCOME STATEMENT				
	FY13	FY14	FY15	FY16
Revenue (Net of Excise D	1295	1669	1891	2312
Other Income	29	31	94	78
Total Revenue	1323	1700	1985	2391
COGS	0	0	0	0
GPM	0%	0%	0%	0%
Other Expenses	209	255	281	357
EBITDA	313	414	390	414
EBITDA Margin (%)	24%	25%	21%	18%
Depreciation	78	103	94	97
EBIT	234	312	296	317
Interest	0	0	0	0
PBT	263	343	390	396
Tax	75	93	99	98
Tax Rate (%)	29%	27%	25%	25%
Reported PAT	188	249	291	297
Dividend Paid	39	51	67	68
No. of Shares (In crore)	4	4	8	8

Souce: Eastwind/Company

BALANCE SHEET				
	FY13	FY14	FY15	FY16
Share Capital	40	40	80	80
Reserves	978	1182	1326	1559
Net Worth	1018	1222	1406	1639
Long term Debt	1	3	2	3
Short term Debt	0	0	0	0
Deferred Tax	56	30	0	0
Total Capital Employed	1020	1226	1408	1642
Net Fixed Assets	468	438	412	445
Capital WIP	117	31	4	0
Debtors	56	96	142	143
Cash & Bank Balances	35	41	42	81
Trade payables	32	43	53	165
Total Provisions	113	130	187	135
Net Current Assets	507	658	753	862
Total Assets	1267	1543	1775	2107

Souce: Eastwind/Company

RATIOS				
	FY13	FY14	FY15	FY16E
EPS	46.9	62.3	36.3	37.2
Book Value	254.6	305.6	175.7	204.9
DPS	9.9	12.9	8.3	8.5
Payout (incl. Div. Tax.)	21%	21%	23%	23%
Valuation(x)				
P/E	5.8	8.4	19.7	19.5
Price / Book Value	1.1	1.7	4.1	3.5
Dividend Yield (%)	3.63%	2.45%	1.17%	1.18%
Profitability Ratios				
RoE	18%	20%	21%	18%
RoCE	23%	25%	21%	19%
Turnover Ratios				
Asset Turnover (x)	1.0	1.1	1.1	1.1
Debtors (No. of Days)	74.1	77.7	80.8	67.5
Inventory (No. of Days)				
Creditors (No. of Days)	9.0	9.5	10.2	26.1
Net Debt/Equity (x)	0.00	0.00	0.00	0.00

Souce: Eastwind/Company

	FY13	FY14	FY15	FY16E
OP/(Loss) before Tax	263	343	390	396
Depreciation	78	103	94	97
Direct Taxes Paid	60	98	100	101
Operating profit before w	323	430	439	439
CF from Op. Activity	216	281	312	254
	5	65	1	32
Capital expenditure on fix	116	58	96	166
CF from Inv. Activity	171	196	232	116
Repayment of Long Term Borrowings				
Interest Paid	0	0	(0)	(0)
Divd Paid (incl Tax)	39	51	67	125
CF from Fin. Activity	39	50	66	127
Inc/(Dec) in Cash	6	35	14	11
Add: Opening Balance	43	50	83	99
Closing Balance	50	83	99	140

Souce: Eastwind/Company