

Industry	TECHNOLOGY
Bloomberg	PSYS IN
BSE CODE	533179

Challenges continues to hang over revenue growth in near term

RATING	BUY
CMP	565
Price Target	655
Potential Upside	16%

Rating Change	↔
Estimate Change	↓
Target Change	↓

Stock Info

52wk Range H/L	915/533
Mkt Capital (Rs Cr)	43178
Free float (%)	7%
Avg. Vol 1M (,000)	78
No. of Shares (Cr)	8
Promoters Pledged %	0%

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1QFY20 Result update

- ❑ Persistent reported weak set of numbers in its 1QFY20 result. Revenue stood at USD119.6 million(misses our estimates by 2%QoQ), a marginal growth of 1.1%QoQ led by steep decline in Digital (-5.9%) and Accelerite revenue (-39.7%QoQ).Even PAT for the quarter stood at Rs 82.4crore , de growth of 2.4%mainly supported by higher other income .
- ❑ EBIT for the quarter stood at Rs82crore, a decline of 1.7%QoQ.The margin declined 88 bps (210bps below our estimate) owing to higher employee cost, higher visa cost, slow IP growth and lower utilization. Also INR appreciation further aided the margin decline (30bps) during the quarter.
- ❑ The Company has made a provision of Rs10crore for exposure towards ILFS and cumulative provision now stands at Rs28.25crore which is 66% of the exposure.
- ❑ Business offering wise, Core services grew by a healthy 3.8% QoQ while Alliances revenue rose by 13.3% QoQ led by the top client. Major dip was seen in digital business which declined 5.9%QoQ after consistently growing for last two quarter.
- ❑ The company completed its share buyback program in June, buying back a total of >3.5mn shares for a total sum not exceeding Rs2.25bn.

View and Valuation

Persistent started the year with soft performance. Revenue grew marginally by 1.1%QoQ impacted by steep decline in Digital While margin dipped 88 bps owing to higher employee cost, higher visa cost and slow IP growth.

Going forward, we see concerns in revenue predictability for FY20 owing to inconsistent performance by digital business (declined 5.9% in 1QFY20) and continued softness in IP revenue .Digital business where most of IT companies are recording mid to high single digit QoQ growth in revenue, Persistent Digital business growth is dampening ever quarter. Also more dependency on its top client performance (deteriorating consecutively in last 6 quarter YoY) is raising concerns for the company performance in near term.

However, with the new leadership on board and new initiative we expect the challenges to gradually improve but it will take few quarters to start reflecting in the performanceWe expect the margin to remain under pressure with continued challenges. Thus factoring in near term challenges, we have cut down our revenue /PAT estimates by 3.6%/6.7% for FY20 and 4.1%/9.6% for FY21.

Despite revision our target price from Rs702 to Rs655, recent price correction in stock have made the stock look attractive. Thus we recommend Buy on stock with revised target price of Rs655.

Key Risks to our rating and target

- ❑ Delay in project execution .
- ❑ Slow momentum in Digital segment .

KEY FINANCIAL/VALUATIONS	FY17	FY18	FY19	FY20E	FY21E
Net Sales	2878	3034	3366	3436	3800
EBITDA	465	469	556	566	640
EBIT	316	310	399	405	465
PAT	302	323	352	360	388
EPS (Rs)	38	40	44	47	50
EPS growth (%)	1%	7%	9%	6%	8%
ROE (%)	17%	16%	16%	15%	15%
ROCE (%)	18%	15%	18%	17%	18%
BV	237	266	295	311	347
P/B (X)	2.5	2.7	2.1	1.8	1.6
P/E (x)	15.8	18.0	14.3	12.1	11.2

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1QFY20 Results

Weak quarter

Financials	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	YoY %	QoQ%	FY18	FY19	YoY %
Net Sales	834	836	864	832	832	-0.3%	0.0%	3,034	3,366	11.0%
Other Income	19	23	(1)	28	30	60.7%	5.6%	119	88	-26.4%
Employee Exp	462	486	491	486	492	6.5%	1.2%	1,832	1,925	5.1%
Other Expenses	232	206	203	225	220	-5.2%	-2.2%	733	885	20.6%
EBITDA	140	144	170	121	120	-14.3%	-0.4%	469	556	18.7%
Depreciation	40	40	40	38	39	-3.5%	2.5%	158	157	-0.8%
EBIT	100	104	131	83	82	-18.6%	-1.7%	310	399	28.6%
Interest	0	0	0	0	2	9150%	1696%	0	0	286.1%
PBT	119	127	130	111	110	-7.7%	-1.4%	429	486	13.3%
Tax	31	39	38	27	27	-12.5%	1.7%	106	135	26.9%
Exceptional	-	-	-	-	-			-	-	
PAT	88	88	92	84	82	-5.9%	-2.4%	323	352	8.9%

1QFY20 performance: Weak revenue growth

- Revenue for the quarter stood at USD119.6 million, a growth of 1.1% QoQ mainly led by steep decline in digital business and Accelerite revenue (-39.7%QoQ).
- In rupee term, revenue stood at Rs 832 crore, a muted performance. From volume perspective, service volume rose by 1.8% QoQ, while blended billing rate declined by 0.5% QoQ. Onsite volume fell by 1.2% QoQ, while offshore volume rose by 2.3% QoQ. Onsite billing rate declined 0.6% QoQ, while offshore rate rose 1% QoQ.

Digital and Accelerite dragging the overall growth

SERVICE(USD Mn)	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	QoQ%	YoY%
Services	51	53	51	51	51	53	55	3.9%	6.5%
Digital	27	28	27	26	28	29	27	-5.9%	2.4%
Alliance	36	28	40	35	36	29	33	13.4%	-16.4%
Accelerite	8	7	6	6	7	7	4	-39.6%	-28.6%

- Core services grew by a healthy 3.8% QoQ while Alliances revenue rose by 13.3% QoQ led by the top client. Major dip was seen in digital business which declined 5.9%QoQ after consistently growing for last two quarter. Accelerite declined 39.6% owing to softness in IP revenue
- Service wise, Enterprise (35.3% of revenue) rose by a decent 3% QoQ, ISV (39.8% of the overall revenue)declined by 0.6% QoQ, while IP revenue rose by a subdued 0.6% QoQ.
- Vertical-wise, BFSI revenue grew healthy by growing 3.7% QoQ and Tech & Emerging Verticals by 1.1% QoQ, while Healthcare & Life Sciences declined by 2.5% QoQ.

IP revenue washed way the overall revenue growth

Industry Wise(USD Mn)	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	QoQ%	YoY%
ISV	47	47	48	47	48	49	49	-0.3%	1.0%
Enterprise	43	43	42	41	43	44	45	3.1%	8.3%
IP Led	33	26	34	30	30	26	26	0.7%	-24.2%

Barring Healthcare, other segment grew moderately

Vertical (in crore)	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	QoQ%	YoY%
BFSI	-	-	29	29	31	32	33	3.8%	12.8%
Healthcare & Life Science	-	-	22	21	22	23	23	-2.4%	3.7%
Technology Cos. &	-	-	73	67	68	63	64	1.2%	-12.2%

Wage hike and INR appreciation impacted margins

- EBIT for the quarter 82crore, a decline of 1.7%QoQ.The margin declined 88 bps (210bps below our estimate) owing to higher employee cost, higher visa cost, slow IP growth and lower utilization. Also INR appreciation further aided the margin decline (30bps) during the quarter.
- The Company has made a provision of Rs10crore for exposure towards ILFS and cumulative provision now stands at Rs28.25crore which is 66% of the exposure.
- PAT for the quarter stood at Rs 82.4crore , de growth of 2.4%mainly supported by higher other income .

Concall Highlights

- **1QFY20 performance:** the company started with a weak growth of 1.1%QoQ despite 1Q being strong quarter. IP revenue came in below company's internal expectation .In YoY variation in IP revenue was because of one reseller deal which was there in 1Q last year and it is also reflecting the purchase royalty cost which is seen YoY. Service revenue as portfolio grew 1.2%QoQ.Linear revenue grew by 1.2% while IP revenue grew 0.8% in 1QFY20.
- **Completed the buyback:** Persistent completed its share buyback program in June, buying back a total of >3.5mn shares for a total sum not exceeding Rs2.25bn.
- **Acquisition:** The company announced the acquisition of European Sales force consulting partner youperience. Together with previously acquired Sales force Platinum Consulting Partner PARX, the professionals from these two boutique Sales force shops combined with Persistent existing Sales force experts will further strengthen the company's ability to provide exceptional Sales force outcomes to its global customers.
- **Deal wins:** The Company won significant deal during the quarter. Won a deal with India's one of largest BFSI company for implementation process and company will be involved in doing non core banking work .Also the company won a global deal based out of US , It is multimillion multiyear deal .In Healthcare segment , the company continue to make progress winning multiple deal in this segment .For technology segment, the company signed a project engagement deal with a inception leading hardware manufacturer in area of thrust and security and block chain deployments.
- **Restructuring process:** With the new leadership on board and changes that will be going ahead, the company will be focusing not only getting historic business but working for large annuity based business .The company is also forming a large deal team which will be working on the seeking advisors, getting to get RFP from there and also working with PE firms on their portfolio opportunities. All initiatives are expected to inflow larger deal specially annuity deals which support revenue acceleration for the company.
- **Margin performance:** Gross margin came at 34.7% as against 36.8% in previous quarter. The key reason for the impact 1)softness in IP revenue;2) coupled with increase in headcount and slightly lower utilization (77.9% in 1Q vs 79.7% in 4Q).Utilization impact the margin by 50bps.Also seasonality of higher visa cost impacted the margins by 70bps.Currency softness further impacted 30 bps to margins.
- **Provision for ILFS:** The Company has made a provision of Rs10crore for exposure towards ILFS and cumulative provision now stands at Rs28.25crore which is 66% of the exposure.
- **ETR:** Effective tax rate is pegged at 26-27% for FY20.
- **Outlook on margins:** The Company expects the Utilization to improve in coming quarters however sees margin improvement when the IP revenue comes back. For 2QFY20 wage hike will impact margins by 250bps to 275bps however some margins will be recouped through hedge gains. Overall the investment the company is making , the approach the markets in terms of deepening the client relationship , as it plays out over period for next few quarters , the company will see the conversion happening to the margins.

Exhibit: Revenue trend

Steep decline in IP and Digital revenue impacted the revenue growth.

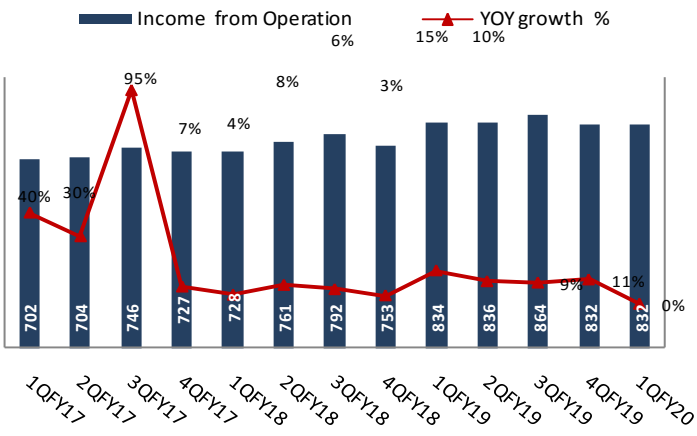


Exhibit: Digital revenue

Discouraging performance in 1QFY20(declined 5.9%QoQ).

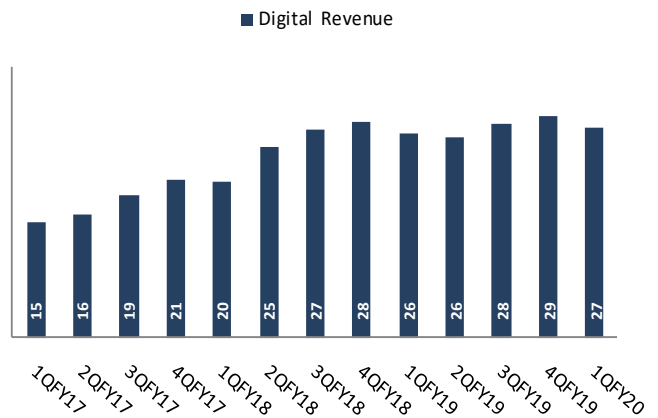


Exhibit: EBITDA and EBITDA margin

Wage hike and INR appreciation washed away the overall margins.

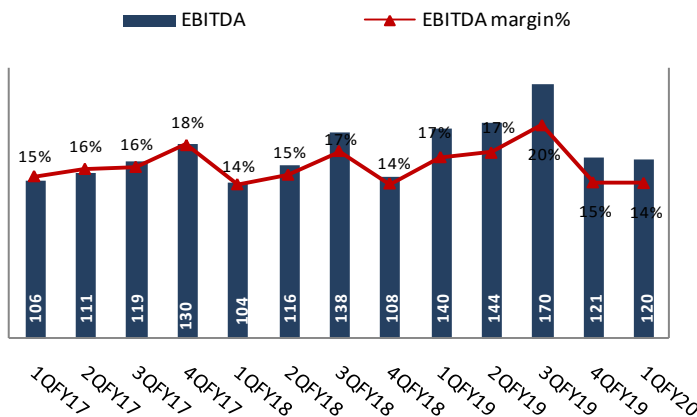


Exhibit: Utilization

Continued decline in Utilization rate

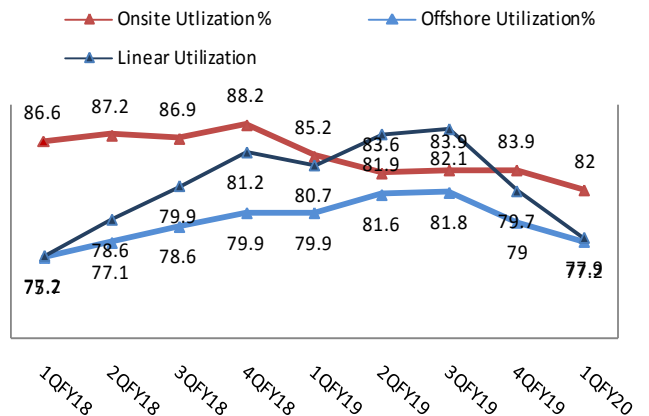
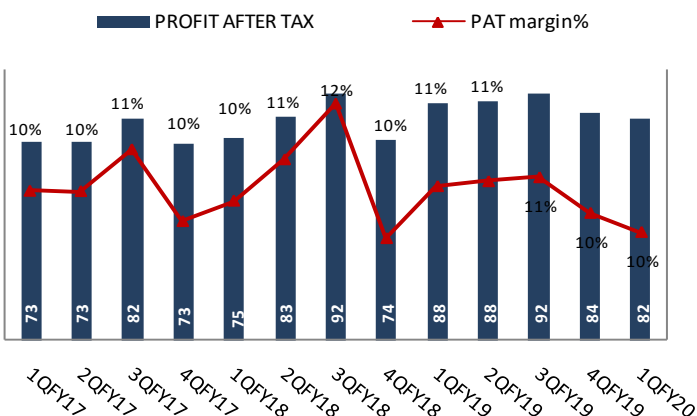


Exhibit: PAT and PAT Margin

Higher Other income supported the PAT decline.



Operational Details

By Geography (%)	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
North America	83%	84%	81%	80%	83%	84%	81%	83%
Europe	9%	7%	8%	12%	8%	8%	8%	9%
India	6%	6%	8%	6%	7%	7%	8%	7%
ROW	3%	3%	3%	2%	3%	2%	4%	2%

Revenue by Service(%)	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
Services	44%	42%	46%	42%	43%	42%	45%	46%
Digital	21%	22%	24%	21%	22%	23%	24%	23%
Alliance	27%	30%	24%	32%	30%	29%	25%	28%
Accelerite	8%	7%	6%	5%	6%	6%	6%	4%

Revenue by Industry(%)	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
ISV	40%	39%	41%	39%	40%	40%	41%	41%
Enterprise	34%	35%	37%	34%	35%	35%	37%	38%
IP Led	26%	27%	22%	27%	26%	25%	22%	22%

Client	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
Top 1	26%	28%	22%	24%	26%	26%	20%	24%
Top 5	44%	46%	41%	44%	43%	45%	40%	45%
Top 10	54%	55%	50%	54%	52%	55%	50%	53%
Large > \$ 3Mn	19	19	18	18	18	20	20	22
Medium > \$1Mn, < \$ 3Mn	49	51	53	58	56	56	57	56

Revenue Mix	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
Onsite	31.9	32.1	34.1	31.1	29.7	29.9	31.4	30.5
Offshore	42.1	41.1	43.6	41.5	44.7	45.1	47	48
IP Led	26	26.8	22.3	27.4	25.6	25	21.6	21.5

Yield	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
yield	5096	5355	5225	5497	5329	5386	5082	4953

People Number	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
Technical	8599	8460	8329	8196	8566	8761	9185	9363
Sales & Business	208	206	211	237	247	266	273	272
Rest	439	443	436	469	489	503	504	532

Business offering	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
Services	74%	73%	78%	73%	74%	75%	78%	79%
IP Led	26%	27%	22%	27%	26%	25%	22%	22%

Utilization	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
Linear Utilization(%)	79	80	81	81	82	82	80	78
Onsite Utilization %	87	87	88	85	84	84	84	82
Offshore Utilization%	77	79	80	80	82	82	79	77

Financial Details

Balance Sheet

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Share Capital	40	80	80	80	80	80	77	77
Reserves	1,182	1,326	1,559	1,819	2,047	2,266	2,320	2,598
Networth	1,222	1,406	1,639	1,899	2,127	2,345	2,397	2,675
Debt	3	2	3	2	2	1	1	1
Other Non Current Liab	39	12	13	28	43	25	25	25
Total Capital Employed	1,226	1,408	1,642	1,901	2,129	2,346	2,398	2,676
Net Fixed Assets (incl CWIP)	436	409	445	557	509	424	335	263
Non Current Investments	82	212	135	234	288	435	435	435
Other Non Cur Asst	46	1	87	7	9	7	7	7
Non Current Assets	478	456	571	701	599	524	435	363
Debtors	303	359	428	475	485	492	503	556
Cash & Bank	96	142	143	151	242	672	652	793
Other Curr Assets	90	104	179	86	156	139	142	157
Current investments	407	462	483	450	592	330	488	676
current tax asset	-	-	-	9	11	19	19	19
Short-term loans and advances	41	41	81	1	1	1	1	1
Curr Assets	937	1,106	1,314	1,404	1,763	1,890	2,041	2,438
Trade payables	43	53	165	121	167	152	155	171
Provisions	121	176	122	139	160	169	172	190
Other Curr Liab	114	127	164	111	120	112	115	127
Other financial liability	-	-	-	45	40	44	44	44
Curr Liabilities	278	355	452	417	487	484	493	540
Net Current Assets	658	751	861	987	1,276	1,406	1,547	1,897
Total Assets	1,543	1,775	2,107	2,346	2,659	2,856	2,917	3,242

Income Statement

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Revenue from Operation	1,669	1,891	2,312	2,878	3,034	3,366	3,436	3,800
Change (%)	29%	13%	22%	24%	5%	11%	2%	11%
EBITDA	414	390	414	465	469	556	566	640
Change (%)	32%	-6%	6%	12%	1%	19%	2%	13%
Margin (%)	25%	21%	18%	16%	15%	17%	16%	17%
Depr & Amor.	103	94	97	149	158	157	161	175
EBIT	312	296	317	316	310	399	405	465
Int. & other fin. Cost	0	0	0	-	0	0	7	7
Other Income	31	94	78	96	119	88	91	71
EBT	343	390	396	412	429	486	488	529
Exp Item	-	-	-	11	-	-	-	-
Tax	93	99	98	99	106	135	127	140
Minority Int & P/L share of Ass.	-	-	-	-	-	-	-	-
Reported PAT	249	291	297	302	323	352	360	388
Adjusted PAT	249	291	297	302	323	352	360	388
Change (%)	33%	17%	2%	1%	7%	9%	2%	8%
Margin(%)	15%	15%	13%	10%	11%	10%	10%	10%

Financial Details

Key Ratios

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
ROE	22%	22%	20%	17%	16%	16%	15%	15%
ROCE	28%	23%	21%	18%	15%	18%	17%	18%
Asset Turnover	1	1	1	1	1	1	1	1
Current Ratio	3	3	2.9	3.4	3.6	3.9	4.1	4.5
Debtor Days	66	69	67	60	58	53	53	53
Payable Days	9	10	26	15	20	16	16	16
Book Value Per Share	306	171	207	237	266	295	311	347
Earnings Per Share	62	36	37	38	40	44	47	50
P/E	17	20	20	16	18	14	12	11
Price / Book Value	3	4	4	3	3	2	2	2
EV/EBITDA	10	14	14	10	12	9	7	6
EV/Sales	2	3	3	2	2	1	1	1

Cash Flow Statement

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
PBT	343	390	396	401	429	486	488	529
(inc)/Dec in Working Capital	51	28	84	106	106	106	106	106
Non Cash Op Exp	87	49	43	97	108	115	162	175
Int Paid (+)	-	-	-	-	-	-	-	-
Tax Paid	98	100	101	105	121	141	127	140
others	-	-	-	-	-	-	-	-
CF from Op. Activities	281	312	254	286	421	432	519	542
(inc)/Dec in FA & CWIP	(58)	(96)	(166)	(218)	(65)	(38)	(72)	(103)
Free Cashflow	223	216	88	69	356	394	446	439
(Pur)/Sale of Inv	(1,239)	-	46	-	-	(14)	(158)	(188)
others	1,099	(126)	44	(4)	(278)	168	-	-
CF from Inv. Activities	(196)	(232)	(116)	(222)	(347)	(226)	(230)	(291)
inc/(dec) in NW	-	-	-	-	-	-	(3)	-
inc/(dec) in Debt	2	1	(1)	(0)	(0)	(0)	-	-
Int. Paid	(44)	(0)	(0)	(0)	(0)	(0)	-	-
Div Paid (inc tax)	(7)	(67)	(125)	(58)	(95)	(102)	(111)	(111)
others	-	-	-	-	-	-	-	-
CF from Fin. Activities	(50)	(66)	(127)	(58)	(96)	(160)	(308)	(111)
Inc(Dec) in Cash	35	14	11	6	(22)	47	(20)	140
Add: Opening Balance	48	84	129	140	156	127	174	154
Closing Balance	83	99	140	146	135	174	154	294

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A graph of daily closing prices of securities is available at www.nseindia.com, www.bseindia.com.

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Registration Details of Group entities: G. Raj & Company Consultants Ltd (G RAJ)-BSE Broker INZ260010731; NSDL DP: IN-DP-NSDL-371-2014 || Narnolia Commerze Limited (Formerly Microsec Commerze Ltd.)-MCX/NCDEX Commodities Broker: INZ000051636 || NarnoliaVeloX Advisory Ltd.- SEBI Registered PMS: INP000005109 || Eastwind Capital Advisors Pvt Ltd. (EASTWIND)-SEBI Registered Investment Adviser: INA300005439 || Narnolia Insurance Brokers Limited (Formerly Microsec Insurance Brokers Ltd.)-IRDA Licensed Direct Insurance Broker (Life & Non-Life) Certificate No. 134, License No. DB046/02 || Narnolia Securities Ltd. (NSL)-AMFI Registered Mutual Fund distributor: ARN 20558, PFRDA NPS POP: 27092018 || Narnolia Capital Advisors Pvt. Ltd. - RBI Registered NBFC:B.05.02568.

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