

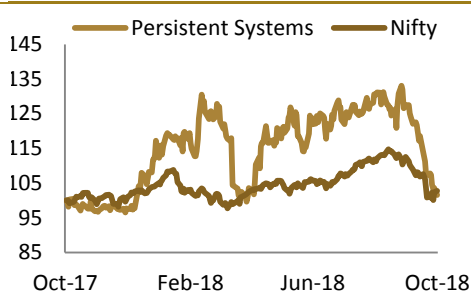
Market statistics

Current stock price (₹)	565
Shares O/S (cr.)	8.0
Mcap (₹ cr)	4,520
52W H/L (₹)	915/540
6m avg. volume	233,311
Bloomberg	PSYS IN

Shareholding pattern

Promoters	30.43
Domestic Institution	17.24
Foreign Institution	26.49
Non-institution	25.84
of which more than 1%	
Shridhar Bhalchandra Shukla	1.53
Ashutosh Vinayak Joshi	1.40

Persistent Systems vs Nifty



Capital efficiency & valuations

Particulars	FY18	FY19E	FY20E
RoE (%)	16.0	16.6	17.2
EPS (₹)	40.4	46.5	54.3
CEPS (₹)	60.2	66.7	76.1
P/E (x)	17.1	12.1	10.4
P/BV (x)	2.6	1.9	1.7
EV/EBITDA (x)	10.8	6.8	6.0
Income growth (%)	5.4	12.4	10.3
EBITDA growth (%)	0.1	25.4	10.6
PAT growth (%)	3.2	15.3	16.6

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Persistent Systems reported a decline of 4.3% QoQ in revenue in US\$ terms, while margins increased 40bps QoQ. The decrease in revenue was on account of 10.4% QoQ decrease in the IP revenue QoQ and the Europe business (down 38.8% QoQ), which PSYS management says is difficult to forecast. Persistent has been able to create a differentiated model through its early investment in digital technologies, and select acquisition of IP from its existing customers. However, there are multiple headwinds to the revenue and margins which play spoilsport. Hence, we maintain our Hold rating on the stock and await better entry points.

Revenue decline of 4.3% QoQ in US\$ terms: PSYS reported lower-than-expected revenue growth in Q2FY19, owing to short project closure due to mismatch with client expectations and adverse impact because of recent sales transformation initiative. EBITDA margin, surprised positively despite wage revisions. Revenue declined by 4.3% QoQ to US\$118.2mn, attributed to higher-than-anticipated fall in IP-led revenue, down 10.4% QoQ and a 2% QoQ decline in IT services revenue. The drop in IT services revenue was due to the 2.8% drop in realisation (whereas volumes continued to increase by 0.8% QoQ) and exit of one client (revenue impact of ~US\$300K). Higher-than-expected other income and forex gains during the quarter were partially offset by higher tax provisions. As a result, net profit grew by 0.9% QoQ.

EBITDA Margin increased by 40bps QoQ: EBITDA margin improved by 40bps QoQ to 17.2% (ahead of our expectations) despite wage revision, led by operational efficiencies, change in onshore mix and rupee tailwinds (110bps). PSYS had expected ~100bps improvement in margins in FY19 (from 15.5% in FY18) led by higher revenue, optimisation of operational efficiencies and a favourable onsite revenue mix in 1Q.

Structural weakness - Persistent's 2QFY19 performance continued to confirm structural weakness in ISV business (decreased 2.6% QoQ) after a series of QoQ declines, reflect our concerns on medium term challenges. Revenue from the Top client (IBM) was up 5.8% QoQ. Clients billed in both the segments, Services and IP-led business were lower by 5 and 3 QoQ respectively to 433 and 178 respectively.

Digital revenue down in Q2, expect it to be back on track in FY19: Digital revenue declined by 1.7% QoQ owing to short closure of one of its projects and shift in the business mix as some projects moved offshore. Alliance revenue declined by 12.1% QoQ owing to weak seasonality. After the decline in revenue in the past three quarters, Accelerite revenue grew by 5.2% QoQ. However, management remains optimistic - digital business is placed well to be back on the growth trajectory in FY19, led by closure of new deals (including in the healthcare and financial services vertical), signing of partnerships, ramping-up of digital spending from clients and improving demand environment. Management hopes that revenue in 2HFY19 would bounce back, driven by anticipated strong growth in alliance business (Q3 is usually a strong quarter for IBM), good revenue visibility in the re-seller business, and recovery in digital revenue on a sequential basis in the coming quarters.

Other details: #2-5 and #6-10 clients declined 13.8% and 10% QoQ. 400 employees on a net basis joined PSYS QoQ taking total head-count to 9,302. Attrition was up 60bps QoQ at 15.4%. DSO days were down 5 days QoQ to 63. Geographically, North America was up 1.5%, APAC was up 16.8%, while Europe decreased 38.8%. The company lost 2 clients QoQ in the US\$1mn-US\$3mn bracket QoQ to take the list to 56.

Outlook & Valuation: There are multiple headwinds to the margins which plays spoilsport. Hence, we maintain our Hold rating on the stock and await better entry points. PSYS is trading at a PE(x) of 12.1x/10.4x FY19E/FY20E earnings.

**Exhibit 1: Quarterly details**

` mn	2QFY18	1QFY19	2QFY19	QoQ (%)	YoY (%)	Comments
Revenues (in US\$ mn)	118.1	123.6	118.2	(4.3)	0.1	Volume up 0.8% QoQ in Services (onsite: -5.4% QoQ and offshore: +2%). IP-led solutions was down 10.4%
Revenues	7,613	8,343	8,356	0.2	9.8	
- Operating costs	6,455	6,942	6,919	(0.3)	7.2	
EBITDA	1,158	1,401	1,436	2.5	24.0	
EBITDA margin (%)	15.2	16.8	17.2	40bps	198bps	EBITDA margin improved by despite wage revision, led by operational efficiencies, change in onshore mix and rupee tailwinds (110bps).
- Interest expense	0	0	1	282.1	568.8	
- Depreciation	379	401	399	(0.6)	5.0	
+ Other income, net (incl forex)	336	187	232	24.3	(30.8)	
PBT	1,114	1,186	1,269	7.0	13.9	
- Taxes	288	313	387	23.9	34.4	
Effective tax rate (%)	25.9	26.4	30.5	417bps	465bps	Effective tax rate for FY19 to be between ~27-28%
PAT	826	873	881	0.9	6.8	
Net Margin	10.8	10.5	10.5	8bps	(30)bps	

Source: Company

Exhibit 2: Change in estimates

` mn	FY19E			FY20E		
	Old	New	%Chg	Old	New	%Chg
Revenue (US\$ mn)	518	490	(5.4)	569	537	(5.6)
Revenue	34,788	34,092	(2.0)	38,101	37,613	(1.3)
EBITDA margin (%)	16.7	17.1	35bps	17.0	17.2	15bpw
EPS (`)	47.1	46.5	(1.3)	54.6	54.3	(0.5)

Source: Trust Research

Exhibit 3: Geographical wise Performance

Geographical mix	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19
US	85.4	86.6	86.5	85.5	83.4	84.4	80.9	79.7	82.6
Europe	6.1	5.3	5.3	5.9	8.5	7.3	8.2	12.0	7.5
APAC	8.5	8.1	8.2	8.6	8.1	8.3	10.9	8.3	9.9
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Company

Exhibit 4: Client details

Client concentration	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19
Top client (%)	28.4	29.5	26.5	27.9	25.9	28.0	21.7	23.8	25.7
Top 5 clients (%)	44.3	46.0	43.3	45.7	43.8	46.3	40.9	43.8	43.3
Top 10 clients (%)	52.8	54.6	52.4	55.2	53.5	55.3	49.9	53.7	52.4
Large >US\$3mn	15	15	15	18	19	19	18	18	18
Medium > US\$1m <US\$3m	51	50	55	52	49	51	53	58	56
Clients billed (Services)	314	315	313	303	419	431	426	438	433
Clients billed (IP Led)	335	338	308	306	277	268	177	181	178

Source: Company



Human Resources: 400 employees on a net basis joined PSYS QoQ taking total head-count to 9,302. Attrition was up 60bps QoQ at 15.4%.

Exhibit 5: Employee strength at PSYS

(Nos)	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19
Billable Personnel – onsite	2,048	2,109	2,236	2,431	2,689	2,777	2,713	2,757	2,656
Billable Personnel - offshore	15,426	14,968	14,942	15,205	15,556	15,166	14,669	14,836	14,827
Total billable employees	17,474	17,077	17,178	17,636	18,245	17,943	17,382	17,593	17,483
Billed Personnel - onsite	1,720	1,867	1,907	2,104	2,346	2,413	2,391	2,348	2,221
Billed Personnel - offshore	11,246	11,610	11,459	11,507	11,994	11,922	11,728	11,857	12,097
Total billed employees	12,966	13,477	13,366	13,611	14,340	14,335	14,119	14,205	14,318
Utilisation details									
Utilisation (blended, %)	74.2	78.9	77.8	77.2	78.6	79.9	81.2	80.7	81.9
Utilisation (onsite, %)	84.0	88.5	85.3	86.5	87.2	87.2	88.1	85.2	83.6
Utilisation (offshore, %)	72.9	77.6	76.6	75.7	77.1	77.1	80.0	79.9	81.6
Employees									
Technical	8,612	8,562	8,808	8,744	8,599	8,460	8,329	8,196	8,566
Sales & Business Development	207	200	193	210	208	206	211	237	247
Others	486	467	459	447	439	443	436	469	489
Total	9,305	9,229	9,460	9,401	9,246	9,109	8,976	8,902	9,302

Source: Company

Exhibit 6: Billing rates

US\$/ppm	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19
Onsite	16,101	15,704	15,914	16,307	16,023	16,314	16,662	16,360	15,787
Offshore	4,288	4,257	4,244	4,212	4,148	4,220	4,349	4,333	4,372

Source: Company

Exhibit 7: Other details

Revenue mix	Q2FY17	Q3FY17	Q4FY17	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19
Onsite	26.3	26.7	27.8	29.9	31.9	32.1	34.1	31.1	29.7
Offshore	45.9	44.9	44.6	42.9	42.1	41.1	43.6	41.5	44.7
IP Led	27.8	28.4	27.6	27.2	26.0	26.8	22.3	27.4	25.6
Total	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
DSO	66	70	65	64	66	66	66	68	63
Attrition (%)	15.9	15.8	15.7	15.5	15.5	14.7	14.7	14.8	15.4

Source: Company



Financials

Income Statement (` mn)

Year End-March	FY16	FY17	FY18	FY19E	FY20E
Revenues	23,123	28,784	30,337	34,092	37,613
Op. Expenses	18,985	24,131	25,677	28,247	31,151
EBITDA	4,138	4,654	4,660	5,845	6,462
Other Income	784	958	1,217	958	1,158
Depreciation	965	1,490	1,585	1,610	1,750
EBIT	3,957	4,122	4,293	5,193	5,870
Interest	1	1	1	3	3
PBT	3,956	4,121	4,292	5,189	5,867
Tax	983	992	1,062	1,466	1,525
PAT	2,974	3,129	3,230	3,724	4,341
Minority	-	-	-	-	-
Adj Pat	2,974	3,129	3,230	3,724	4,341

Key Parameters

Year End-March	FY16	FY17	FY18	FY19E	FY20E
Per share (`)					
EPS	37.2	39.1	40.4	46.5	54.3
CEPS	49.2	57.7	60.2	66.7	76.1
BVPS	204.9	237.4	265.9	295.9	335.0
DPS	8.0	9.0	10.0	12.0	13.0
Payout (%)	25.2	26.9	29.0	30.2	28.0
Valuation (x)					
P/E	20.5	15.3	17.1	12.1	10.4
P/BV	3.7	2.5	2.6	1.9	1.7
EV/EBITDA	12.6	9.4	10.8	6.8	6.0
Dividend Yield (%)	1.0	1.5	1.4	2.1	2.3
Return ratio (%)					
EBITDA Margin	17.9	16.2	15.4	17.1	17.2
PAT Margin	12.9	11.3	10.6	10.9	11.5
ROAE	19.5	17.7	16.0	16.6	17.2
ROACE	25.9	23.3	21.3	23.1	23.2
Leverage Ratios (x)					
Long Term D/E	0.0	0.0	0.0	0.0	0.0
Net Debt/Equity	(0.4)	(0.3)	(0.3)	(0.4)	(0.4)
Debt/EBITDA	0.0	0.0	0.0	0.0	0.0
Interest Coverage	-	-	-	-	-
Current ratio	2.9	3.8	3.9	4.2	4.4
Growth Ratios (%)					
Income growth	22.3	24.5	5.4	12.4	10.3
EBITDA growth	6.9	18.9	0.1	25.4	10.6
PAT growth	2.3	12.8	3.2	15.3	16.6
Turnover Ratios					
F.A Turnover x	7.1	10.2	11.7	13.0	13.1
Debtors Days	74	67	65	64	63
Payable days	35	20	23	24	24

Balance Sheet (` mn)

Year End-March	FY16	FY17	FY18	FY19E	FY20E
Sources of Funds					
Equity Share Capital	800	800	800	800	800
Reserves & Surplus	15,593	18,193	20,472	23,072	26,197
Total Shareholders Fund	16,393	18,993	21,272	23,872	26,997
Non- current liabilities	(77)	445	201	217	235
Long term Borrowings	26	22	17	17	17
Deferred tax liabilities	(228)	277	25	25	25
Other LT liabilities & prov	126	146	160	176	193
Current Liabilities	4,517	3,720	4,474	4,953	5,462
Trade payables	1,651	1,210	1,673	1,857	2,048
Other cur liabilities & Prov	2,866	2,510	2,801	3,096	3,414
Total Liabilities	20,833	23,157	25,947	29,042	32,694
Assets					
Non- current Assets					
Fixed assets	3,273	2,817	2,589	2,614	2,864
Non-current investments	2,703	5,172	5,466	5,466	5,466
Long-term loans & adv	851	131	143	187	206
Other non-current assets	870	994	129	187	206
Current assets	13,136	14,043	17,620	20,589	23,952
Current investments	4,828	4,500	5,916	5,916	5,916
Trade receivables	4,275	4,754	4,847	5,417	5,977
Cash & bank balances	1,432	1,461	1,344	3,081	5,247
Short-term loans & adv	812	14	7	9	10
Other current assets	1,788	3,314	5,506	6,165	6,801
Total Assets	20,833	23,157	25,947	29,042	32,694

Cash flow Statement

Year End-March	FY16	FY17	FY18	FY19E	FY20E
PBT	3,956	4,121	4,292	5,189	5,867
Depreciation	1,050	1,995	1,333	1,610	1,750
Interest expense	1	1	1	3	3
CF before W.cap	5,007	6,117	5,626	6,803	7,620
Inc/dec in W.cap	2,455	1,387	657	838	709
Op CF after W.cap	2,552	4,730	4,969	5,965	6,911
Less Taxes	983	992	1,062	1,466	1,525
Net CF From Operations	1,569	3,738	3,907	4,500	5,386
Inc/(dec) in F.A + CWIP	1,141	1,034	1,357	1,635	2,000
(Pur)/sale of investments	(224)	2,141	1,711	-	-
Others	(1)	(1)	(1)	(3)	(3)
CF from Invst Activities	(918)	(3,176)	(3,069)	(1,639)	(2,003)
Loan raised	1	(4)	(5)	-	-
Equity Raised	113	313	(15)	(0)	0
Dividend	749	842	936	1,123	1,217
CF from Fin Activities	(635)	(533)	(956)	(1,123)	(1,217)
Net inc /(dec) in cash	16	29	(118)	1,738	2,166
Op. bal of cash	1,416	1,432	1,461	1,344	3,081
Cl. balance of cash	1,432	1,461	1,344	3,081	5,247



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