Q1FY25
Persistent Systems Ltd

Result Update 24th July, 2024

Persistent Systems Ltd.

Q1FY25 in-line with estimates; Downgrade to Hold on valuations

CMP	Target	Potential Upside	Market Cap (INR Mn)	Recommendation	Sector
INR 4,819*	INR 4,901	1.7%	INR 7,39,354	HOLD	Internet Software & Services

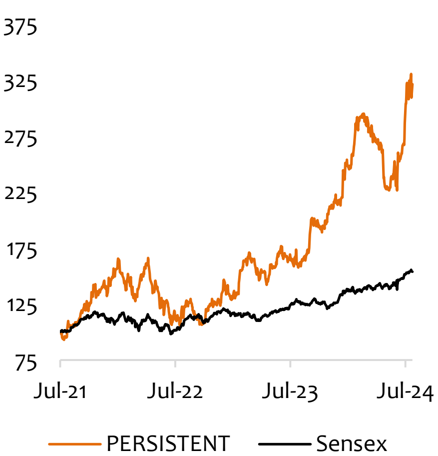
Result Highlights:

- Revenue of INR 27,372 Mn (+17.9% YoY/+5.7% QoQ) was driven by BFSI (+9.0% YoY), Healthcare & Lifesciences (+69.7% YoY), and Software, Hi-Tech, and emerging industries (+4.2% YoY), beating our estimate by 1.1%.
- EBIT of INR 3,840 Mn rose by 28.9% YoY (+2.6% QoQ), beating our projections by 0.5%; EBIT margins improved by 119bps YoY (-42bps QoQ).
- PAT jumped by 33.9% YoY (-2.8% QoQ) to INR 3,064 Mn, missing our projections by 0.9%; PAT margins improved by 134bps YoY (-98bps QoQ).
- **We lower our FY26E EPS to INR 104.3 (previously: INR 107.1) and raise our P/E multiple to 47.0x (previously: 36.0x) to arrive at a TP of INR 4,901 (previously: INR 3,857) reflecting strong performance and deal wins. Due to the recent price surge, we now view PSYS as fairly valued with limited upside, prompting us to downgrade our rating to "HOLD" from "ACCUMULATE".**

MARKET DATA

Shares outs (Mn)	154
Mkt Cap (INR Mn)	7,39,354
52 Wk H/L (INR)	4,925/1,158
Volume Avg (3m K)	725
Face Value (INR)	5.0
Bloomberg Code	PSYS IN

SHARE PRICE PERFORMANCE



MARKET INFO

SENSEX	80,149
NIFTY	24,414

KEY FINANCIALS

INR Millions	Q1FY25	Q4FY24	Q1FY24	QoQ	YoY
Revenue	27,372	25,905	23,212	5.7%	17.9%
EBIT	3,840	3,744	2,980	2.6%	28.9%
PAT	3,064	3,153	2,288	-2.8%	33.9%
OPM (%)	14.0%	14.5%	12.8%	-42bps	119bps
NPM (%)	11.2%	12.2%	9.9%	-98bps	134bps

Source: Company, KRChoksey Research

Healthcare & Life Sciences led the growth; BFSI vertical surpasses a milestone

- Revenue growth was led by North America showcasing a growth of 18.2% YoY. India region also saw a growth of 14.8% YoY, while the Rest of the World (ROW) experienced a commendable growth of 64.4%. However, Europe's revenue contribution declined by 6.7% YoY.
- The drop in revenue from Europe is partly attributed to decreased business in Salesforce-related operations and streamlining of underperforming customers in that sector.
- BFSI segment crossed the USD 100 Mn revenue mark for the first time.
- The TCV for Q1FY25 stood at USD 462.8 Mn with 67.2% being new booking and ACV stood at USD 337.3 Mn (58.7% net new).
- OPM stood at 14.0% in Q1FY25, QoQ headwinds contributing to OPM: i) 60bps from visa costs, ii) 210bps from increase in subcontractor cost, iii) 70bps from higher SG&A.
- Tailwinds impacting OPM in Q1FY25: i) 90bps from higher utilization, ii) 90bps from operational efficiencies, iii) 60bps from reversal of earnout credit, iv) 40bps from change in asset lifespan, v) 10bps from employee benefit.

New Deal Wins in Healthcare, acquisition announcement, new partnerships

- PSYS was selected by US-based insurance company and US-based diagnostic companies to undertake different projects.
- PSYS has announced its intent to acquire New Jersey-based Starfish Associates.
- In Q1FY25, the Company forged a strategic partnership with Google to strengthen AI-driven industry solutions and accelerate global enterprise digital transformation.

SHARE HOLDING PATTERN (%)

Particulars (%)	Jun-24	Mar-24	Dec-23
Promoters	31.0	31.0	31.0
FIIs	22.6	25.0	24.6
DIIs	28.2	25.9	26.1
Others	18.2	18.1	18.3
Total	100.0	100.0	100.0

*Based on Today's closing

17.0%

Revenue CAGR between FY24 and FY26E

21.2%

Adj. PAT CAGR between FY24 and FY26E

Persistent Systems Ltd.

Key Concall Highlights:

- The Company has achieved a growth of 5.6% QoQ translating into a 16.0% YoY growth.
- The total contract value (TCV) for Q1FY25 stood at USD 462.8 Mn with the TCV of new booking being USD 310.8 Mn.
- The Annual contract value (ACV) of TCV is USD 337.3 Mn out of which ACV from new bookings contributed USD 198.1 Mn.
- The **drop in revenue from Europe is partly attributed to decreased business in Salesforce-related operations** and streamlining of underperforming customers in that sector.
- The Contribution from top 10 customers increased from 39.6% in Q1FY24 to 41.5% in Q1FY25.
- In the Company's strategic AI investments**, the focus is on two key areas: AI for technology and AI for business.**
- In the realm of AI for business, the Company has created proprietary IPs and accelerators such as iAURA and GenAI Hub. These innovations facilitate the rapid adoption of enterprise-grade generative AI applications that are secure and scalable for enterprises.
- The Company aims for robust revenue growth in FY25E and intends to maintain similar margins as FY24.
- PSYS **reaffirmed guidance of improving margins by 200 to 300 basis points over the next few years** as they expand operations.
- The Company noted that during challenging macroeconomic conditions, enterprises tend to reduce investments in new software licenses or additional modules, affecting the Company's customers' investment capabilities.
- PSYS has **implemented regular salary increases for its employees, effective July 2024.**
- The Company has created SASVA, a digital engineering platform that blends AI with human creativity to enhance customer value, accelerate time to market, and increase employee productivity.
- PSYS is harnessing AI in the contact center sector, aiming to integrate Starfish Associates' acquired contact center platform with its unified communications solutions.
- The Company **forged a strategic partnership with Google** to co-create industry-specific solutions aimed at fostering widespread AI adoption, leveraging Google's Cloud Gemini models and other advanced technologies.
- Persistent was chosen by a leading US technology giant to deliver engineering, deployment, and support services for its cloud offering on a Tier-1 virtual server platform.
- Persistent was also selected by a prominent US multinational health insurance firm to migrate its existing on-premises clinical and claims data warehouse to a cloud-based platform using Microsoft Azure Databricks and the Data Build Tool framework.
- Furthermore, the Company will **integrate and deploy Google Cloud solutions extensively** through its strategic collaboration with Google.
- The Company plans to utilize advanced AI solutions from its partner ecosystem, including Google Contact Center AI, AWS Connect, and Microsoft Teams, to enhance its efforts in modernizing contact centers.
- At the end of Q1, the Company's total workforce numbered 23,519, marking an increase of 389 compared to the same quarter last fiscal year.
- However, compared to the previous quarter headcount reduced by 331.
- The Company is leveraging subcontractors (subcons) for rapid scaling but intends to transition to its employees gradually, aiming to reduce costs and enhance margins in the long-term.
- PSYS' M&A strategy includes allocating a portion of the purchase price to the scalability of revenue and margin profiles over time, acting as a safeguard in case expected revenue and margin improvement do not materialize.
- **Two acquisitions by the Company did not meet initial expectations, resulting in a write-back of a portion of the consideration amount.**

Valuation and view:

PSYS reported Q1FY25 largely in line with our expectations. The Company announced an intent to acquire Starfish Associates and its partnership with Google. The Company also bagged new deals in Healthcare and BFSI in Q1FY25. PSYS aspires to maintain healthy growth and margin to be in the range of FY24. **Based on the recent developments, new deal wins, better growth in the BFSI sector, and robust pipeline, we increase our P/E multiple for FY26E to 47.0x (previously: 36.0x). However, we expect the announced partnerships and new deal wins to take some time before they materialize and are reflected in PSYS earnings. Therefore, we lower our FY26E EPS to INR 104.3 (previously: INR 107.1). Based on FY26E EPS and multiple, we increase the target price to INR 4,901 (previously: INR 3,857). Since the last time we valued the shares of Persistent Systems, the stock has rallied significantly (up 37.3%) leading to stretched valuations. We believe PSYS shares are adequately valued and offer limited potential for further upside from the current levels. Accordingly, we downgrade the shares of PSYS from "ACCUMULATE" to "HOLD".**

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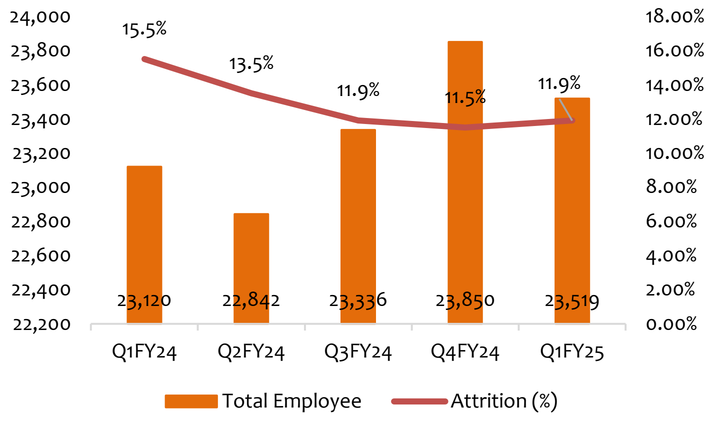
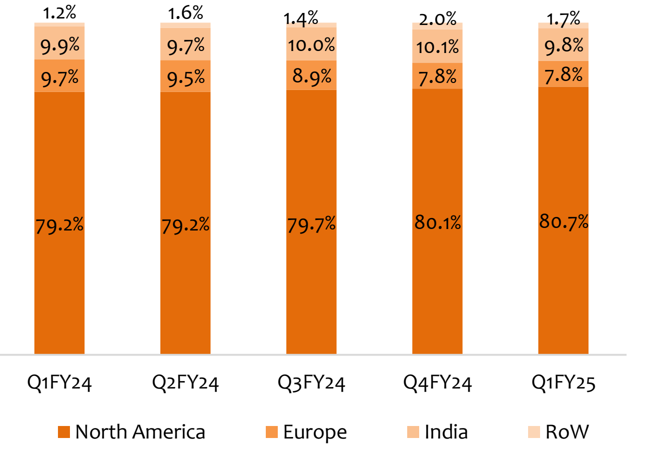
Persistent Systems Ltd.

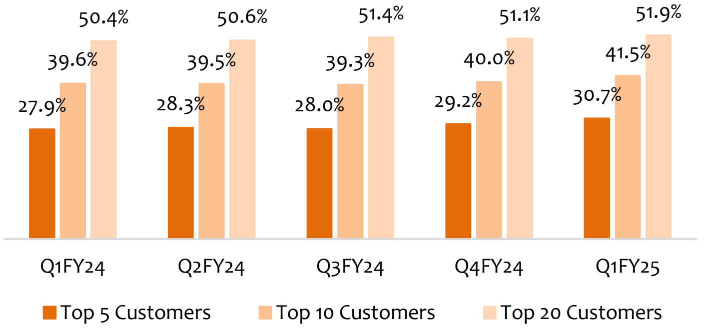
Consistent sequential increased sequentially after continous decline trend



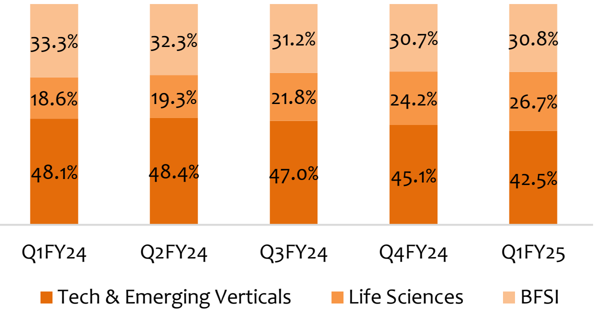
Revenue mix from North America increased QoQ



Revenue contribution continued to increase from top 5 and top 10 customers



The proportion of Healthcare & Life Sciences revenue has been increasing



Persistent Systems Ltd.

KEY FINANCIALS

Exhibit 1: Profit & Loss Statement

INR Millions	FY22	FY23	FY24	FY25E	FY26E
Revenue	57,107	83,506	98,216	116,002	134,479
Total Operating expenses	47,526	68,315	81,459	95,582	110,322
EBITDA	**9,582**	**15,191**	**16,757**	**20,420**	**24,157**
Depreciation	1,660	2,719	3,094	3,679	3,607
EBIT	**7,922**	**12,472**	**13,664**	**16,741**	**20,550**
Finance Cost & Extra Ordinary- Expense	**118**	**770**	**467**	**523**	**586**
Other income, net	1,440	706	1,280	1,370	1,748
Pre-tax Income	**9,243**	**12,409**	**14,477**	**17,588**	**21,713**
Income tax expense	2,339	3,198	3,541	4,405	5,645
Net profit	**6,904**	**9,211**	**10,935**	**13,183**	**16,067**
Diluted EPS (INR)	45.2	60.3	71.5	85.6	104.3
Shares in Mn	153	153	153	154	154

Source: Company, KRChoksey Research

Exhibit 2: Cash Flow Statement

INR Millions	FY22	FY23	FY24	FY25E	FY26E
Net Cash Generated From Operations	8,500	9,558	12,214	12,824	16,048
Net Cash Flow from/(used in) Investing Activities	-9,773	-4,213	-4,695	-10,334	-5,091
Net Cash Flow from Financing Activities	1,823	-4,039	-5,937	-6,589	-7,978
Net Inc/Dec in cash equivalents	549	1,305	1,582	-4,099	2,978
Opening Balance	2,419	2,978	4,670	6,625	2,525
Adjustments	9	387	373	0	0
Closing Balance Cash and Cash Equivalents	2,978	4,670	6,625	2,525	5,504

Source: Company, KRChoksey Research

Exhibit 3: Key Ratios

Key Ratio	FY22	FY23	FY24	FY25E	FY26E
EBITDA Margin (%)	13.9%	14.9%	13.9%	14.4%	15.3%
Tax rate (%)	25.3%	25.8%	24.5%	25.0%	26.0%
Net Profit Margin (%)	12.1%	11.0%	11.1%	11.4%	11.9%
RoE (%)	21.7%	24.9%	26.1%	27.7%	28.2%
RoCE (%)	21.7%	25.5%	26.6%	28.2%	28.7%
Current ratio	2.9	3.4	3.6	3.2	3.2
EPS (INR)	45.2	60.3	71.5	85.6	104.3

Source: Company, KRChoksey Research

Persistent Systems Ltd.

Exhibit 4: Balance Sheet

INR Millions	FY22	FY23	FY24	FY25E	FY26E
Property, Plant and Equipment	2,918	4,860	4,420	5,033	6,132
Right-of-use Asset	1,358	2,198	2,307	2,446	2,592
CWIP	1,071	161	335	235	166
Goodwill	2,790	7,184	10,913	10,913	10,913
Intangible Assets	8,270	9,171	4,575	11,097	12,207
Non-current Investments	4,750	6,847	7,865	8,715	9,661
Deferred Tax Assets	1,123	1,134	1,360	1,360	1,360
Loans and Advances	3,522	709	730	730	730
Total non-current assets	12,259	14,193	9,330	16,366	43,761
Current Investments	4,347	1,880	2,727	3,054	3,420
Trade Receivables	9,484	15,253	16,761	21,189	24,564
Cash & Bank Balances	9,145	9,033	10,229	6,130	9,096
Other current Assets	5,414	8,300	11,515	13,473	15,763
Total current assets	28,389	34,466	41,232	43,845	52,844
Total Assets	54,191	66,731	73,736	84,374	96,604
Equity Share Capital	764	764	770	770	770
Other Equity	32,918	38,887	48,807	55,862	64,461
Total Equity	33,682	39,651	49,577	56,633	65,232
Long term borrowings	2,801	2,058	99	99	99
Other Long-term liabilities	1,114	1,592	1,653	2,092	2,342
Long term Provisions	246	373	547	591	638
Total non-current liabilities	6,249	6,951	2,317	2,801	3,098
Trade Payables	4,299	5,689	8,139	9,716	11,303
Other Current Liabilities	3,795	6,571	7,021	8,215	9,611
Short-term Provisions	3,950	4,649	3,331	3,597	3,885
Current tax liabilities (net)	349	294	547	547	547
Total Current Liabilities	14,260	20,129	21,842	24,941	25,346
Total liabilities	54,191	66,731	73,736	84,374	96,604

Source: Company, KRChoksey Research

Persistent Systems Ltd.

Persistent Systems Ltd.			
Date	CMP (INR)	TP (INR)	Recommendation
24-Jul-24	4,819	4,901	HOLD
24-Apr-24	3,466	3,857	ACCUMULATE
23-Jan-24	4,127	4,204	HOLD
02-Nov-23	3,113	3,308	ACCUMULATE
21-Jul-23	2,375	2,765	BUY

Rating Legend (Expected over a 12-month period)	
Our Rating	Upside
Buy	More than 15%
Accumulate	5% – 15%
Hold	0 – 5%
Reduce	-5% – 0
Sell	Less than – 5%

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