



### Persistent Systems reported a strong Q3FY21 performance which marginally beat our estimates on the revenue front and a strong beat on our profitability estimates

- **\$ revenue:** \$ 146.45 Mn, +7.6% qoq / +13.1% yoy and +2.2% above our estimates
- **INR revenue:** INR 10,753.9 Mn, +6.7% qoq / +16.5% yoy and 3.2% above our estimates
- **EBITDA:** INR 1,825 Mn, +9.7% qoq / +47.8% yoy and +5.8% vs our estimates.
- **EBITDA for the quarter was robust due to a 27.2% qoq drop / 82.2% yoy drop in Travel Expenses**
- **EBITDA margins:** 17%, vs 16.5% / 13.4% in Q2FY21 / Q3FY20 respectively and 40 bps above our estimates
- **EBIT:** INR 1252 Mn, +11.4% qoq / +69% yoy and +8.9% vs our estimates
- **EBIT margins:** 12.7%, vs 12.1% / 8.7% in Q2FY21 / Q3FY20 respectively and 70 bps above our estimates
- **PAT:** INR 1,209 Mn, +18.5% qoq / +37.5% yoy and 15.8% above our estimates
- **EPS at INR 15.8 in Q3FY21 vs 13.3 / 11.5 in Q2FY21 / Q3FY20 respectively**

### Result Highlights

- **Technology Services** (76.3% of revenue) **grew by 6% qoq. Alliance business** (23.7% of revenue) **grew by 12.1% qoq**
- **TCV for Q3FY21 stood at \$302 Mn**, which included \$175 of new deals
- **Top Client (19% of revenue)** grew by 2.4% qoq whereas **Top 5-10 clients (9% of revenue)** grew by 11% qoq

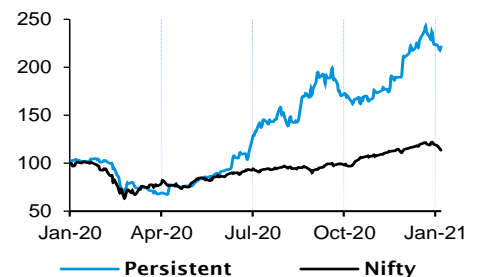
Rating	TP (Rs)	Up/Dn (%)
<b>BUY</b>	<b>1934</b>	<b>27</b>

### Market data

<b>Current price</b>	<b>Rs</b>	<b>1,526</b>
Market Cap (Rs.Bn)	(Rs Bn)	116
Market Cap (US\$ Mn)	(US\$ Mn)	1590
Face Value	Rs	10
52 Weeks High/Low	Rs	1690/420
Average Daily Volume	('000)	93
BSE Code		533179
Bloomberg		PSYS:IN

Source: Bloomberg

### One Year Performance



Source: Bloomberg

% Shareholding	Dec-20	Sep-20
Promoters	31.29	31.29
Public	65.95	65.85
Others	2.76	2.86
<b>Total</b>	<b>100</b>	<b>100</b>

Source: BSE

### Financial Summary

Y/E Mar (Rs mn)	FY19	FY20	FY21E	FY22E	FY23E
Net sales	33,659	35,658	41,863	47,293	52,883
EBITDA	5,506	4,923	6,868	7,737	8,861
Adjusted net profit	3,517	3,403	4,359	5,145	5,911
Free cash flow	7,821	(240)	3,063	7,165	5,592
EPS (Rs)	44.0	44.5	57.0	67.3	77.3
growth (%)	9%	1%	28%	18%	15%
P/E (x)	34.1	33.7	26.3	22.3	19.4
P/B (x)	34.1	33.7	26.3	22.3	19.4
EV/EBITDA (x)	20.3	22.4	16.0	13.8	11.6
ROCE (%)	12.5	10.2	14.1	13.9	14.4
RoE (%)	15.7	14.4	17.0	17.6	17.9
Dividend yield (%)	0.8	0.7	0.8	0.6	1.3

Source: Company

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## Conference Call Key Takeaways

### Operational Highlights

- **Margin walk:** Revenue expansion and cost control enabled Persistent to absorb Pay hike impact of 200 bps, adverse currency movement impacted margins by 20 bps + Lower provisions helped margin by 0.4% (lower Other Expenses) + lower CSR (COVID contribution)
- Higher amortization due to CAPIOT acquisition.
- **Work-From-Home Update:** Hybrid working model - employees partially coming to office. As vaccines are rolled out, number of employees returning to office will increase
- **Offshore:** Linear Revenue grew by 8.9% - Volumes increased 11.5%, billing rate was down 2.3% down
- **Onsite:** Linear Revenue dropped by 1% Volumes increased 0.2%, billing rate was down 1.2% down High collections resulted in lower DSOs
- **Cash at \$258 Mn or INR 18,880 Mn**
- Completed the acquisition of Capiot Software in the 1st week of November. Persistent rebadged 200 employees.

**Margin expansion came in despite wage hikes and was supported by cost control measures.**

### Deal Win & Hiring

- **Order bookings:** TCV stood at \$302 Mn which is the highest in the last 5 quarters and includes new deals and renewal deals (\$175 Mn out of this were new deal wins)
- **Robust employee addition (1,532 heads) for fulfillment of earlier large deal wins and anticipation strong growth momentum.** 70% of addition were lateral hires. Company also increased hiring due to overall spike in industry demand and therefore preparing for any supply-side issues.

**Deal-win continued momentum with TCV of \$302 Mn in Q3FY21, highest in last 5 quarters.**

### Vertical Highlights

- **BFSI performance was subdued during the quarter due to cost control by few top clients and intermediate ramp downs.** Management expects BFSI to recover in forthcoming quarters. Lot of banks looking at modernization through Hyperscalers (Hybrid, Private and Public cloud) + Digital + Compliance & Security services
- PES, Cloud, Salesforce and Security led the growth in terms of Services
- Capiot contributed \$1 Mn to Technology Services
- **Alliance business reported a strong sequential growth due to seasonality in IP revenue and uptick in reseller business.** Seeing good traction and therefore will return to significant growth in the coming FY on the back of strong alignment with the top client's new leadership's vision in Cloud.

### Partnerships & Investments

- Expanded IBM cloud partnership to Teleco Cloud (until last year, Persistent had a partnership for Financial Services Cloud) + Persistent is development partner for Cloud packs, namely Cloud Pack for Data, Integration and Multi-cloud Management + deployment partner with IBM + continue to grow key IBM businesses such AI, Automation Security and WatsonHealth + Red Hat partner for modernization across ISV and Enterprise markets.
- **Capital Allocation:** Actively looking at inorganic acquisitions, specifically in the industries Persistent is present in and in Europe

## Outlook

- **EBITDA margin trend:** have some operating levers such as utilization even after travel and facility expenses return. Deal wins and pipeline ensure that revenue momentum will continue which will also aid margins.
- **Expect Alliance business to report healthy growth going ahead (in all segments – ‘sell-with’, ‘sell-through’ and ‘sell-to’) as see traction in large deal pipeline in Alliance business** and won few large deals which are lined up for ramp up. One can expect revenue booking of these deals from Q1FY22.
- M&A will be in Cloud, Security or Data. Organic and inorganic focus will be on these technology lines and Europe for the next 4-6 quarters.
- Looking to reduce volatility of Top Account by scaling up ‘sell-with’, ‘sell-through’ and ‘sell-to’ of Services side of the Alliance business which will compensate for the volatility in the IP side of the Alliance business

**Margin will continue to expand supported by operating levers and strong deal pipeline. Alliance Business will continue with the healthy growth.**

# Quarterly Performance Analysis

## Exhibit 1

YE March (Rs. Mn)	Q3 FY21	Q2 FY21	Q-o-Q change %	Q3 FY20	Y-o-Y change %	Q3 FY21 estimates	Deviation %
Net Sales (US\$ Mn)	146.2	136.1	7.4%	129	12.9%	143.3	2.0%
Net Sales (INR Mn)	10,754	10,077	6.7%	9,227	16.5%	10,416	3.2%
Less:							
Employees Remuneration & Benefits	7,741	7,448	3.9%	6,593	17.4%	7,674	0.9%
SG&A Expenses	1,188	965	23.1%	1,399	(15.1%)	1,016	17.0%
<b>Total Operating Expenditure</b>	<b>8,929</b>	<b>8,413</b>	<b>6.1%</b>	<b>7,992</b>	<b>11.7%</b>	<b>8,690</b>	<b>2.8%</b>
EBITDA	1,825	1,664	9.7%	1,235	47.7%	1,726	5.7%
EBIT	1,364	1,224	11.4%	807	69.0%	1,252	8.9%
Less: Depreciation	461	440	4.8%	428	7.6%	474	(2.6%)
Less: Interest	14	14	(3.2%)	15	(6.8%)	15	
Add: Other income	300	165	81.9%	348	(13.7%)	171	76.0%
<b>Profit Before Tax</b>	<b>1,650</b>	<b>1,375</b>	<b>20.0%</b>	<b>1,140</b>	<b>44.8%</b>	<b>1,407</b>	<b>17.2%</b>
<b>Adjusted Profit s</b>	<b>1,650</b>	<b>1,375</b>	<b>20.0%</b>	<b>1,140</b>	<b>44.8%</b>	<b>1,407</b>	
Less: Total Tax	441	355	24.1%	260	69.2%	364	
<b>PAT</b>	<b>1,209</b>	<b>1,020</b>	<b>18.6%</b>	<b>879</b>	<b>37.5%</b>	<b>1,044</b>	<b>15.9%</b>
<b>Adjusted PAT</b>	<b>1,209</b>	<b>1,020</b>	<b>18.6%</b>	<b>879</b>	<b>37.5%</b>	<b>1,044</b>	<b>15.9%</b>
<b>Reported Diluted EPS (Rs.)</b>	<b>15.8</b>	<b>13.3</b>	<b>18.6%</b>	<b>11.5</b>	<b>37.5%</b>	<b>13.7</b>	
Adjusted Diluted EPS (Rs.)	15.8	13.3	18.6%	12	37.5%	13.7	15.9%
No of Shared Diluted (mn)	76	76		76		76	
<b>Margin Analysis %</b>			<b>Change in bps</b>		<b>Change in bps</b>		<b>Deviation in bps</b>
EBIT margin	12.7%	12.1%	53	8.7%	394	12.0%	66
EBIDTA Margin	17.0%	16.5%	46	13.4%	358	16.6%	40
NPM	11.2%	10.1%	112	9.5%	172	10.0%	122
Adjusted NPM	11.2%	10.1%	112	9.5%	172	10.0%	122
Effective Tax Rate %	26.7%	25.8%	88	22.9%	386	25.8%	88
<b>Cost Analysis %</b>			<b>Change in bps</b>		<b>Change in bps</b>		<b>Deviation in bps</b>
Employee Cost/Net Sales	72.0%	73.9%	(193)	71.5%	53	73.7%	(170)
SG&A/Net sales	11.1%	9.6%	147	15.2%	(411)	9.8%	130

Source: Dalal & Broacha Research, Company

Growth was largely driven by Alliance business which had a seasonally strong quarter and solid execution of past deal wins

EBITDA margin was impacted by almost 200 bps due to wage hikes which was absorbed by revenue growth, lower bad debt provisions and lower CSR spends

## Exhibit 2

Services (% Terms)	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21
Services (Technology Services)	45.8%	45.2%	46.5%	48.4%	77.1%	77.3%	76.3%
Alliance	27.8%	28.1%	26.7%	22.2%	22.9%	22.7%	23.7%
<b>Services Revenues (\$ Terms)</b>							
Services (Technology Services)	55	57	60	61	101	105	112
Q-o-Q Growth	3.8%	3.5%	6.1%	2.2%	64.3%	4.1%	6.0%
Y-o-Y Growth	6.8%	11.6%	18.9%	16.5%	84.4%	85.4%	85.3%
Alliance	33	35	35	28	30	31	35
Q-o-Q Growth	13.3%	6.1%	-2.0%	-18.4%	6.4%	3.0%	12.1%
Y-o-Y Growth	-16.2%	1.1%	-2.7%	-3.9%	-9.8%	-12.4%	0.2%

Source: Dalal & Broacha Research, Company

Technology services unit had \$1 Mn of contribution from Capiot, which was integrated from November 2020. Alliance business had strong uptick due to seasonality and healthy reseller business

## Exhibit 3

Geography	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21
North America	82.5%	81.4%	80.1%	80.2%	80.4%	82.9%	81.1%
Europe	8.5%	9.9%	10.6%	8.8%	10.2%	7.6%	8.8%
India	6.7%	6.7%	7.4%	9.0%	7.9%	8.1%	8.6%
ROW	2.3%	2.0%	1.9%	2.0%	1.5%	1.4%	1.5%
<b>Geography Revenues</b>							
North America	99	102	104	102	105	113	119
Q-o-Q Growth	3.1%	3.5%	1.5%	-1.7%	3.4%	7.1%	5.1%
Y-o-Y Growth	0.2%	4.6%	2.5%	6.5%	6.7%	10.4%	14.3%
Europe	10	12	14	11	13	10	13
Q-o-Q Growth	8.8%	22.2%	10.4%	-18.5%	19.5%	-22.6%	24.3%
Y-o-Y Growth	-31.4%	40.1%	49.4%	19.6%	31.4%	-16.8%	-6.3%
India	8	8	10	11	10	11	13
Q-o-Q Growth	-12.0%	4.9%	13.9%	19.4%	-9.5%	6.5%	14.0%
Y-o-Y Growth			16.6%	25.5%			31.2%
Rest of the world	3	3	2	3	2	2	2
Q-o-Q Growth	-33.6%	-8.8%	-2.0%	3.3%	-22.7%	-3.1%	15.1%
Y-o-Y Growth	1.2%	-18.3%	7.1%	-38.6%	-28.6%	-24.1%	-10.9%

Source: Dalal & Broacha Research, Company

North America led the growth pack at 5.1% qoq

Europe bounced back during the quarter at 24.3% qoq growth

Europe remains Persistent's main focus area as it plans to expand presence in the region

## Exhibit 4

EMPLOYEE METRICS	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21
Total Employees	10,167	10,543	10,532	10,632	10,829	10,820	12,438
Additions	205	376	-11	100	197	-9	1,618
Technical	9,363	9,726	9,729	9,835	10,027	10,001	11,533
Additions	178	363	3	106	192	-26	1,532
Sales & Marketing	272	285	266	263	274	268	277
Additions	-1	13	-19	-3	11	-6	9
Others	532	532	537	534	528	551	628
Additions	28	0	5	-3	-6	23	77

Persistent had the highest ever quarterly headcount addition during the quarter – in light of higher expected demand and supply-side shortage therein

Source: Dalal & Broacha Research, Company

## Valuation & Outlook

Persistent is currently trading at 22.3x / 19.4x FY22e / FY23e EPS. Management continues to give a strong outlook for Services as well Alliance business on the back of a robust pipeline and order book. Highest quarterly net additions also indicate that management is preparing for surge in broad-based demand which is not only from Persistent's top clients but a sector-wide phenomenon. Management has further indicated that it has managed to reduce volatility in the alliance business by balancing the services part of the alliance business relative to the IP part – which is highly seasonal and volatile in nature.

Based on 2<sup>nd</sup> consecutive strong results and commentary, Persistent remains an undervalued stock reporting one of the highest growths in the midcap space.

Taking all the above factors into consideration, we upgrade our target price on Persistent to INR 1,934 (earlier TP INR 1,120), based on 25x FY23e EPS estimates.

# Financial

Profit & Loss A/c						Balance Sheet (Consolidated)					
YE March (Rs. mn)	FY19	FY20	FY21E	FY22E	FY23E	YE March (Rs. mn)	FY19	FY20	FY21E	FY22E	FY23E
<b>Net Sales</b>	<b>33,659</b>	<b>35,658</b>	<b>41,863</b>	<b>47,293</b>	<b>52,883</b>	<b>Liabilities</b>					
<i>Growth %</i>	<i>11.0%</i>	<i>5.9%</i>	<i>17.4%</i>	<i>13.0%</i>	<i>11.8%</i>	Equity Capital	791	764	764	764	764
<b>Total Revenue</b>	<b>33,659</b>	<b>35,658</b>	<b>41,863</b>	<b>47,293</b>	<b>52,883</b>	Reserves & Surplus	22,656	23,093	26,701	30,189	34,197
Employee Cost & Related Expenses	22,740	25,475	30,298	33,638	36,883	<b>Equity</b>	<b>23,447</b>	<b>23,858</b>	<b>27,465</b>	<b>30,953</b>	<b>34,961</b>
Miscellaneous Expenses	5,413	5,260	4,697	5,918	7,139	<b>Net Worth</b>	<b>23,447</b>	<b>23,858</b>	<b>27,465</b>	<b>30,953</b>	<b>34,961</b>
<b>Total Operating Expenditure</b>	<b>28,153</b>	<b>30,735</b>	<b>34,995</b>	<b>39,555</b>	<b>44,022</b>	<b>Total Loans</b>	<b>12</b>	<b>407</b>	<b>407</b>	<b>407</b>	<b>407</b>
EBIDTA	5,506	4,923	6,868	7,737	8,861	<b>Capital Employed</b>	<b>23,712</b>	<b>24,448</b>	<b>28,128</b>	<b>31,656</b>	<b>35,708</b>
<i>Growth %</i>	<i>18.2%</i>	<i>-10.6%</i>	<i>39.5%</i>	<i>12.7%</i>	<i>14.5%</i>	<b>Assets</b>					
Less: Depreciation	1,573	1,660	1,841	2,142	2,327	Gross Block	7,390	7,370	9,370	10,370	11,370
<b>EBIT</b>	<b>3,934</b>	<b>3,263</b>	<b>5,027</b>	<b>5,595</b>	<b>6,534</b>	Less: Depreciation	5,059	5,145	6,986	9,128	11,455
<i>Growth %</i>	<i>27.9%</i>	<i>-17.1%</i>	<i>54.0%</i>	<i>11.3%</i>	<i>16.8%</i>	<b>Net Block</b>	<b>2,331</b>	<b>2,225</b>	<b>2,384</b>	<b>1,242</b>	<b>-85</b>
Interest Paid	3	63	57	61	0	<b>Investments</b>	<b>4,763</b>	<b>5,311</b>	<b>5,707</b>	<b>5,912</b>	<b>6,120</b>
Non-operating Income	933	1,324	955	1,419	1,454	Intangible Assets	1,980	1,661	1,950	2,203	2,463
<b>Profit Before tax</b>	<b>4,864</b>	<b>4,523</b>	<b>5,924</b>	<b>6,953</b>	<b>7,988</b>	Right of Use Assets		567	709	630	0
Tax	1,347	1,121	1,565	1,808	2,077	<b>Current Assets</b>					
<b>Net Profit</b>	<b>3,517</b>	<b>3,403</b>	<b>4,359</b>	<b>5,145</b>	<b>5,911</b>	Sundry Debtors	4,923	5,922	7,455	7,774	8,693
<b>Adjusted Profit</b>	<b>3,517</b>	<b>3,403</b>	<b>4,359</b>	<b>5,145</b>	<b>5,911</b>	Current Investments	3,296	5,165	6,063	6,850	7,660
<b>Reported Diluted EPS Rs</b>	<b>44.0</b>	<b>44.5</b>	<b>57.0</b>	<b>67.3</b>	<b>77.3</b>	Cash and Bank Balance	6,724	4,572	4,855	8,438	12,466
<i>Growth %</i>	<i>8.9%</i>	<i>1.3%</i>	<i>28.1%</i>	<i>18.0%</i>	<i>14.9%</i>	<b>Total Current Assets</b>	<b>19,064</b>	<b>20,032</b>	<b>23,531</b>	<b>28,889</b>	<b>35,335</b>
<b>Adjusted Diluted EPS Rs</b>	<b>44.0</b>	<b>44.5</b>	<b>57.0</b>	<b>67.3</b>	<b>77.3</b>	<b>Less: Current Liabilities &amp; Provisions</b>					
<i>Growth %</i>	<i>8.9%</i>	<i>1.3%</i>	<i>28.1%</i>	<i>18.0%</i>	<i>14.9%</i>	Sundry Creditors	1,517	2,247	2,589	3,143	3,498
						<b>Total Current Liabilities &amp; Provision:</b>	<b>4,844</b>	<b>6,474</b>	<b>7,475</b>	<b>8,713</b>	<b>9,796</b>
						<b>Capital Applied</b>	<b>23,712</b>	<b>24,448</b>	<b>28,128</b>	<b>31,656</b>	<b>35,708</b>
Key Ratios						Cash Flows (Consolidated)					
YE March (Rs. mn)	FY19	FY20	FY21E	FY22E	FY23E	YE March (Rs. Mn)	FY19	FY20	FY21E	FY22E	FY23E
EBIDTA (%)	16.4%	13.8%	16.4%	16.4%	16.8%	PAT	3,517.0	3,402.9	4,359.5	5,145.1	5,911.4
NPM (%)	10.4%	9.5%	10.4%	10.9%	11.2%	Add: Depreciation	1,572.5	1,659.6	1,840.9	2,142.1	2,326.8
RoE (%)	15.7%	14.4%	17.0%	17.6%	17.9%	Add: Interest Paid	3.1	63.3	57.4	61.2	0.0
RoCE (%)	12.5%	10.2%	14.1%	13.9%	14.4%	<b>Operating Profit before WC Changes</b>	<b>4,159.7</b>	<b>3,802.1</b>	<b>5,302.5</b>	<b>5,929.6</b>	<b>6,784.0</b>
Tax Rate %	27.7%	24.8%	26.4%	26.0%	26.0%	(Inc)/Dec in Current Assets	3,127.9	(3,119.3)	(3,216.8)	(1,774.8)	(2,417.3)
Book Value Per share (Rs.)	293.1	312.2	359.4	405.0	457.5	(Inc)/Dec in Current Liabilities	(145.0)	1,629.4	1,001.5	1,237.6	1,082.7
						<b>Net Cash Generated From Operations</b>	<b>7,142.6</b>	<b>2,312.2</b>	<b>3,087.2</b>	<b>5,392.5</b>	<b>5,449.4</b>
						<b>Cash Flow from Investing Activities</b>					
						(Inc)/Dec in Fixed Assets	(66.3)	20.1	(2,000.0)	(1,000.0)	(1,000.0)
						Add: Non Operating Income	932.9	1,323.8	955.3	1,418.8	1,454.3
						<b>Cash Flow from Investing Activities</b>	<b>(49.5)</b>	<b>406.0</b>	<b>(1,925.1)</b>	<b>(210.8)</b>	<b>(190.9)</b>
						<b>Cash Flow from Financing Activities</b>					
						Dividend Paid	(869.3)	(917.1)	(653.9)	(1,440.6)	(1,655.2)
						<b>Net Cash Flow from Financing Activities:</b>	<b>(2,783.3)</b>	<b>(4,303.1)</b>	<b>(736.9)</b>	<b>(1,678.3)</b>	<b>(1,859.6)</b>
						<b>Net Inc/Dec in cash equivalents</b>	<b>4,309.8</b>	<b>(1,585.0)</b>	<b>425.2</b>	<b>3,503.3</b>	<b>3,399.0</b>
						<b>Opening Balance</b>	<b>2,414.0</b>	<b>6,723.8</b>	<b>4,572.1</b>	<b>4,855.1</b>	<b>8,437.9</b>
						<b>Closing Cash Balance</b>	<b>6,723.8</b>	<b>5,138.9</b>	<b>4,997.3</b>	<b>8,358.4</b>	<b>11,836.9</b>

Source: Dalal & Broacha Research, Company

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