



# Research Update

## PayGroup Limited – FY20 update

### Buy

Price: \$0.70 | 12 Month Target: \$1.82 | Implied Return: 160% | 3 June 2020

#### Full Yearly Update

Multi-Country Software with a Service (SaaS) Payroll Solutions and APP enabled Cloud Software as a Service (SaaS) Human Capital Management (HCM) provider PayGroup Limited (PYG) recently released its FY20 result for the period ending 31 March 2020.

#### Results Summary

PYG reported its second successive quarter of positive cash flows and this showed in the full-year FY20 results with the company reporting a strong improvement in operating cash flow from a loss of \$4.8m in FY19 to a marginal loss of 0.1m for FY20. The cash flow does not include a '13<sup>th</sup> month' of billing which is year-end billing undertaken in Asia, which will be recognized this quarter.

Statutory revenue increased 110.4% to \$10.9m and this includes 5 months of Astute One Limited, which PYG acquired in November 2019. Statutory NPAT fell 19% to a loss of \$1.9m. There was a slight increase in the cost base due to one-off costs associated with the Astute acquisition, investment in growth initiatives, integration costs of Astute systems and new service lines, and continued investments in growth initiatives such as the Global Partner Program.

When accounting for the Astute business for the whole financial year, PYG saw pro-forma revenue increase 112% to \$17.8m of which \$8.8m is from Astute. This is slightly higher than our previous estimate of \$17.5m however we had expected pro-forma NPAT to equal \$5m while PYG reported an NPAT of \$3.9m. This is mainly due to higher than expected depreciation costs of \$1.4m due to software intangibles from Astute and adoption of AASB16 accounting standards regarding lease payments.

	Our forecast	Actual	Comment
Pro-forma revenue	\$17.5m	\$17.8m	Stronger Astute contribution
Pro-forma EBITDA	\$5.3m	\$5.3m	In line
Pro-forma NPAT	\$5.0m	\$3.9m	We forecasted depreciation of \$300k versus actual \$1.4m

#### Recommendation

Despite the coronavirus situation, PYG has seen steady growth and we feel confident the growth pattern will continue beyond the current period. The APAC addressable market, comprised of both BPO and HCM software, is estimated at US\$28.1bn. PYG has increased its proportion of SaaS revenue and the HCM Software market in APAC is expected to grow by 14.5% CAGR beyond 2021 to US\$3.06bn by 2024. The current COVID-19 pandemic has placed higher reliance on PYG's software and services which we expect to continue post-COVID-19. **We maintain our buy recommendation on PYG with a price target of \$1.82** and we have slightly updated our earnings forecast to reflect stronger Astute contributions with a slightly higher cost base, higher run-rate in payslips, and taking into account higher depreciation due to changes in accounting standards and software intangibles. PYG continues to increase the number of processed payslips, new contracts wins remain strong, the global partner program continues to expand, and the Astute acquisition has provided PYG a strong foothold into the Australian market.

#### Company Data

Recommendation: BUY  
 Price (Date 3 June): \$0.70  
 ASX Code: PYG  
 Shares on Issue: 68.83m  
 Market capitalization: \$48.2m  
 Enterprise Value: \$46.2m

#### Board Structure

Ian Basser: Non-Exec Chairman  
 Mark Samlal: Managing Director  
 Franck Neron-Bancel: Exec Director  
 David Fagan: Non-Exec Director

#### Major Shareholders

Samantha Samlal: 32.08%  
 Lawrence Pushpam: 10.25%  
 Marcus Webb & Associates<sup>^</sup>: 11.75%  
 JP Morgan Nominees: 5.7%  
<sup>^</sup>escrowed for 24 months from 14/11/2019

#### Financial Highlights (with Astute)

\$m	FY20A*	FY21E*	FY22E*	FY23E*
Total Revenue	17.8	20.8	24.1	28.0
Operating Expenses	(12.5)	(13.6)	(14.8)	(16.2)
EBITDA	5.3	7.2	9.2	11.8
NPAT	3.9	5.44	7.34	9.8
Dividend yield	N/A	N/A	N/A	N/A
PE	12.3	8.9	6.6	4.9

\*Normalised Pro Forma results



Source: Iress

**FY20 Results Commentary**

Payslips processed during the period continue to grow despite the downturn experienced due to the COVID-19 pandemic. Total combined payslips processed (SaaS and SaaS) increased by 26.5% to 61,054. SaaS contributes nearly 50% to revenue. Astute contributed an additional 327,657 payslips, which itself represents an increase of 3% on FY19. The growth in payslips has come not only from organic growth but also through PYG's channel partners which have increased to 7 partners. Treasury services contributed an additional 3,653 payslips and 5% to pro-forma revenue and we expect this to increase significantly in the future. The company added \$5.5m (\$4.9m from PayAsia and \$0.6m from Astute) in new contracts wins in FY20, expressed as total contract value (TCV), representing an increase of 12% on FY19's TCV of \$4.9m. Pleasingly, the initial two months of FY21 have started well with \$2.7m in new contracts won. The company reported statutory revenue of \$10.9m and a full year statutory loss of \$1.9m. Pro-forma revenue increased 112% to \$17.8m which is slightly higher than our previous estimate of \$17.5m due to higher than expected contribution from Astute. Pro-forma NPAT increased 69% to \$3.9m. This was slightly lower than our forecast due to higher than expected depreciation.

**Operational Highlights:**

- Reported cash receipts increase from a loss of \$4.8m to a loss of \$0.1m;
- 26.5% increase in payslips to 61,054, despite the coronavirus pandemic causing widespread business downturns
- \$2.7m in new contracts, expressed as total contract value (TCV), in the first two months of FY21, more than half of the total new contracts of \$5.5m PYG won in FY20.



**Valuation Ratios (A\$'000's) Proforma**

Year ending Mar	2020A	2021E	2022E	2023E	2024E
Proforma profit	3,915	5,440	7,347	9,802	11,953
<b>EPS<sub>adj</sub> (¢)</b>	<b>0.057</b>	<b>0.079</b>	<b>0.107</b>	<b>0.142</b>	<b>0.174</b>
<b>EPS growth</b>	<b>29.3%</b>	<b>39.0%</b>	<b>35.0%</b>	<b>33.4%</b>	<b>21.9%</b>
<b>P/E ratio</b>	<b>12.3 x</b>	<b>8.9 x</b>	<b>6.6 x</b>	<b>4.9 x</b>	<b>4.0 x</b>
Enterprise Value (m)	30,229	26,028	22,012	39,270	39,270
EV/Sales (x)	1.69 x	1.25 x	0.92 x	1.40 x	1.23 x
EV / EBIT (x)	7.8 x	4.5 x	2.8 x	3.8 x	3.1 x
EV / EBITDA (x)	5.7 x	3.6 x	2.4 x	3.3 x	2.8 x
DPS (¢)	0.0	0.0	0.0	0.0	0.0
<b>Dividend Yield</b>	<b>0.0%</b>	<b>0.0%</b>	<b>0.0%</b>	<b>0.0%</b>	<b>0.0%</b>
Payout Ratio	0.0%	0.0%	0.0%	0.0%	0.0%
Franking	0.0%	0.0%	0.0%	0.0%	100.0%
FCFPS	0.08	0.08	0.11	0.14	0.17
P/FCFPS	9.09	8.51	6.43	4.97	4.02

**Cashflow (A\$'000's)**

Year ending Mar	2020A	2021E	2022E	2023E	2024E
Receipts	11,305	20,809	24,056	28,041	31,884
Payments	(11,331)	(14,051)	(17,423)	(21,604)	(26,789)
Interest received	15	(168)	(227)	(303)	(370)
Interest paid	-129	-129	-129	-129	-129
Change in Work cap	8,111	1,346	1,476	1,811	1,747
<b>Operating cashflow</b>	<b>(140)</b>	<b>6,462</b>	<b>6,277</b>	<b>6,005</b>	<b>4,597</b>
<b>Investing cashflows</b>					
Intangibles	(2,261)	(2,261)	(2,261)	(2,261)	(2,261)
Acquisitions/Divestments	(99)	(99)	(99)	(99)	(99)
Net cash inflow	262	0	0	0	0
<b>Financing activities</b>					
Equity	3,000	0	0	0	0
Other	(436)	0	0	0	0
Dividends paid	0	0	0	0	0
<b>Net cashflow</b>	<b>425</b>	<b>4,201</b>	<b>4,016</b>	<b>3,744</b>	<b>2,336</b>
Cash at beginning 01/04	1,429	9,041	13,242	17,258	21,002
<b>Cash at end 31/03*</b>	<b>9,041</b>	<b>13,242</b>	<b>17,258</b>	<b>21,002</b>	<b>23,338</b>

**Revenue Split (A\$'000's)**

Year ending Mar	2020A	2021E	2022E	2023E	2024E
Payroll Services	8,165	10,074	12,265	15,010	17,834
Other	853	853	853	853	853
<b>Group Revenue</b>	<b>17,847</b>	<b>20,809</b>	<b>24,056</b>	<b>28,041</b>	<b>31,884</b>

**Profit and loss (A\$'000's) Proforma**

Year ending Mar	2020A	2021E	2022E	2023E	2024E
Operating revenue	17,847	20,809	24,056	28,041	31,884
EBITDA	5,300	7,177	9,202	11,808	14,093
D&A	(1,400)	(1,400)	(1,400)	(1,400)	(1,400)
<b>EBIT</b>	<b>3,900</b>	<b>5,777</b>	<b>7,802</b>	<b>10,408</b>	<b>12,693</b>
Net interest income	15	(168)	(227)	(303)	(370)
NPBT	3,915	5,609	7,574	10,105	12,323
Tax Expense (benefit)	0	(168)	(227)	(303)	(370)
<b>NPAT</b>	<b>3,915</b>	<b>5,440</b>	<b>7,347</b>	<b>9,802</b>	<b>11,953</b>
Significant Items	0	0	0	1	2
<b>NPAT (Proforma)</b>	<b>3,915</b>	<b>5,440</b>	<b>7,347</b>	<b>9,802</b>	<b>11,953</b>
EBITDA Margin	29.7%	34.5%	38.3%	42.1%	44.2%
EBIT Margin	21.9%	27.8%	32.4%	37.1%	39.8%
NPAT Margin	21.9%	26.1%	30.5%	35.0%	37.5%

**Balance sheet (A\$'000's)**

Year ending Mar	2020A	2021E	2022E	2023E	2024E
Bank Balance	9,041	13,242	17,258	21,002	23,338
Receivables	4,451	5,190	6,000	6,994	7,952
Prepayments	165	165	165	165	165
Other	1,315	1,315	1,315	1,315	1,315
<b>Current assets</b>	<b>14,973</b>	<b>19,912</b>	<b>24,738</b>	<b>29,476</b>	<b>32,770</b>
Net PPE	182	83	(16)	(115)	(214)
Intangibles	11,973	11,973	11,973	11,973	11,973
Deferred Tax Assets	0	0	0	0	0
Other	0	0	0	0	0
<b>Non-current assets</b>	<b>12,155</b>	<b>12,056</b>	<b>11,957</b>	<b>11,858</b>	<b>11,758</b>
<b>Total assets</b>	<b>27,127</b>	<b>31,968</b>	<b>36,695</b>	<b>41,334</b>	<b>44,529</b>
Trade payables	14,647	16,932	19,738	22,443	0
Borrowings	0	0	0	0	0
Employee entitlements	0	0	0	0	0
Deferred Revenue	0	0	0	0	0
<b>Total liabilities</b>	<b>15,998</b>	<b>18,076</b>	<b>20,361</b>	<b>23,166</b>	<b>25,872</b>
<b>NET ASSETS</b>	<b>13,895</b>	<b>13,892</b>	<b>16,333</b>	<b>18,167</b>	<b>18,657</b>

**Balance Sheet Ratios**

Year ending Mar	2020A	2021E	2022E	2023E	2024E
Net Debt	(7,945)	(12,146)	(16,162)	(19,906)	(22,242)
NTA	0.03	0.03	0.06	0.09	0.10
Price / NTA (x)	25.1 x	25.1 x	11.0 x	7.8 x	7.2 x
Return on assets	4.4%	12.2%	14.8%	17.8%	22.0%
Return on equity	28.2%	39.2%	45.0%	54.0%	64.1%

**Valuation**

Year ending Mar	2020A	2021E	2022E	2023E	2024E
Discounted Cash Flow			WACC		9.84%
Beta	0.9		Discount Period		9 years
Cost of Equity	9.84%		DCF/Price Target		\$1.82

\*Includes client moneys

Table 1: Earnings estimates. Source: Lodge

		WACC			
		8%	9.84%	12%	14%
Growth	2%	2.43	1.82	1.39	1.14
	3%	2.74	1.97	1.47	1.18
	4%	3.21	2.17	1.56	1.23
	5%	4.00	2.46	1.68	1.30
	6%	5.57	2.89	1.85	1.38

## Comparable analysis

PayGroup trades at a deep discount relative to its listed international peers with a comparable analysis detailed in Table 2 below. Comparable valuation analysis does not presently form part of our valuation model for PayGroup, however we believe it is important to note the material discount which the company trades at relative to listed international BPO Payroll and HCM Software providers. On a forecasted PE basis, PayGroup currently trades at an 79.9% discount relative to other listed international BPO Payroll and HCM Software providers (43.96 times average) and an 82.8% discount to HCM Software providers (51.5 times average).

CODE	COMPANY	STOCK EXCHANGE	PRICING	MARKET CAP	PRICE	P/E	EV/EBITDA	EV/REV	SOLUTION
<b>ADP</b>	Automatic Data Processing	U.S.	USD\$	62.55B	145.55	25.78	19.92	5.20	BPO Payroll and HCM Software
<b>WDAY</b>	Workday	U.S.	USD\$	41.82B	177.96	97.73	61.55	12.28	HCM Software
<b>PAYX</b>	Paychex	U.S.	USD\$	25.81B	71.95	28.94	16.75	6.92	BPO Payroll and HCM Software
<b>PAYC</b>	Paycom	U.S.	USD\$	17.55B	305.61	87.35	38.64	16.46	BPO Payroll and HCM Software
<b>PCTY</b>	Paylocity	U.S.	USD\$	7.24B	134.84	108.8	39.12	11.12	BPO Payroll and HCM Software
<b>CSOD</b>	Cornerstone OnDemand	U.S.	USD\$	2.53B	39.65	39.92	25.07	5.41	HCM Software
ZAL	Zalaris	OSL (Norway)	NOK	686m	34.1	16.86	6.98	0.97	HCM Software
ELO	Elmo Software	ASX	AUD\$	568m	6.59	N/A	N/A	7.6	BPO Payroll and Software
<b>PYG</b>	<b>Paygroup*</b>	<b>ASX</b>	<b>AUD\$</b>	<b>46.8m</b>	<b>0.68</b>	<b>8.60</b>	<b>6.4</b>	<b>2.22</b>	<b>BPO Payroll and Software</b>

Table 2: Market comparables Source: Thomson Reuters Consensus and Lodge Research, 2 June 2020.

\*Forward P/E, EV/EBITDA and EV/Revenue based on FY21 pro-forma forecasts including Astute

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I verify that I, Sven Restel, have prepared this research report accurately and that any financial forecasts and recommendations that are expressed are solely my own personal opinions. In addition, I certify that no part of my compensation is or will be directly or indirectly tied to the specific recommendation or financial forecasts expressed in this report. I do not currently own any shares in the Company.

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