



Research Report

PayGroup Limited

Buy

Price: \$0.70 | 12 Month Target: \$1.82 | Implied Return: 160% | 12 December 2019

Half-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 released its H1 result last week for the period ending 30 September 2019.

Results Summary

PYG reported statutory revenue of \$3.4m in the H1 period, an increase of 17.8% on H2 FY19 and an increase of 78.9% on previous corresponding period (pcp). \$2.8m in new contracts signings were added in the period, expressed as total contract value (TCV). 5,962 new client employees were implemented during the period, and total client employees (payslips) increased 18.2% to 57,048. We are pleased to report that client employees is currently trending above Lodge's forecast, and we expect this trend to continue for the full year period. This is partly due to the global channel partner program having contributed higher than expected sales. PYG has continued investing in growing this channel program, which contributed to the increase in employee and consulting expenses in H1. Due to these expenses, reported NPAT fell to a loss of \$1.4m in H1, versus a loss of \$1.1m in pcp. We understand these expenses are non-recurring and will not impact cash flow going forward. PYG is expected to be operating cash flow positive in H2 FY20. One-off costs associated with the Astute One acquisition further impacted the H1 result. The Astute One acquisition was completed on 14 November 2019 and is expected to materially increase the number of payslips processed to circa 4.7m annually, as well as increasing SaaS revenue based on the company's guidance of pro forma ARR (annual repetitive revenue) of \$17.5m in FY20.

Following the end of the period, PYG raised \$3m via a Placement of new shares to new and existing institutional investors. The Placement was priced at \$0.70, representing a 2.1% discount to the 5-day VWAP at the time. We also note that an existing institutional investor sold 3.85m shares to new institutional investors in conjunction with the placement, with this sell-down effectively removing an overhang in the stock.

Recommendation

Astute One, once integrated will add another 330 client entities to the current 450 base and more than \$7m in revenue. Astute is highly synergistic and will increase the group's SaaS revenue to over 45% of total revenue (currently 6%). We have adjusted our valuation to \$1.82, due principally to dilution, which represents 160% upside from current levels and accordingly maintain our **Buy Recommendation**.

H1 FY20 Results Commentary

The company reported H1 revenue of \$3.4m, an increase of 78.9% on pcp, and NPAT of \$(1.4)m. PYG's cash balance is currently \$7.8m, of which \$3.9m relates on balances held on behalf of clients for settlement of their payroll obligations.

Operational Highlights:

- Reported revenue increased 17.8% on H2 FY19 and 78.9% on pcp;
- 18.2% increase in payslips to 57,048, which is currently tracking above Lodge's estimates; and
- Reported NPAT of \$(1.4)m impacted by increased investment in channel partner program and increased headcount due to growth in Singapore, Indonesia and Thailand.

Company Data

Recommendation: BUY
Price (Date 12 December): \$0.70
ASX Code: PYG
Shares on Issue: 68.83m
Market capitalization: \$48.18m
Enterprise Value: \$45.2m

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^: 11.75%
JP Morgan Nominees: 5.7%
*escrowed for 24 months from IPO date
^escrowed for 24 months from 14/11/2019

Financial Highlights (with Astute)

\$m	FY19A*	FY20E*	FY21E*	FY22E*
Total Revenue	8.4	17.5	20.7	24.2
Operating Expenses	(5.7)	(12.1)	(13.4)	(15.5)
EBITDA	2.7	5.4	7.3	9.4
NPAT	2.3	4.98	6.76	8.8
Dividend yield	N/A	N/A	4.8%	6.0%
PE	15.4	9.6	7.0	5.4

*Normalised Pro Forma results



Source: Iress

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

Year ending Mar	2019A	2020E	2021E	2022E	2023E
Proforma profit	2,293	5,025	6,900	8,864	10,962
EPS_{adj} (¢)	0.044	0.073	0.100	0.129	0.159
EPS growth	N/A	64.5%	37.3%	28.5%	23.7%
P/E ratio	15.8 x	9.6 x	7.0 x	5.4 x	4.4 x
Enterprise Value (m)	31,404	29,310	29,122	28,371	39,270
EV/Sales (x)	3.74 x	1.67 x	1.41 x	1.17 x	1.40 x
EV / EBIT (x)	13.7 x	5.9 x	4.3 x	3.2 x	3.6 x
EV / EBITDA (x)	11.8 x	5.4 x	4.0 x	3.0 x	3.4 x
DPS (¢)	0.00	0.0	5.0	6.4	8.0
Dividend Yield	0.0%	0.0%	7.2%	9.2%	11.4%
Payout Ratio	0.0%	0.0%	50.0%	50.0%	50.0%
Franking	0.0%	0.0%	0.0%	0.0%	0.0%
FCFPS	0.06	0.07	0.11	0.13	0.16
P/FCFPS	11.56	9.33	6.51	5.43	4.43

Cashflow (A\$'000's)

Year ending Mar	2019A	2020E	2021E	2022E	2023E
EBIT	2,293	4,944	6,815	8,833	10,974
Dep'n and amort'n	376	441	493	534	467
Deferred tax benefit	(41)	(155)	(213)	(274)	(339)
Share option expenses	0	0	0	0	1
Change in Work cap	568	196	217	233	0
Operating cashflow	2,670	6,034	7,589	9,615	11,662
Investing cashflows					
Capex	(500)	(500)	(500)	0	0
Acquisitions/Divestments	0	0	0	0	0
Other	0	0	0	0	0
Free Cash Flow	2,170	5,534	7,089	9,615	11,662
Equity	7,760	3,000	0	0	0
Other	(2,100)	0	0	0	0
Dividends paid	0	0	(3,450)	(4,432)	(5,481)
Net cashflow	7,830	8,534	3,639	5,183	6,181
Cash at beginning 01/04	5	7,866	9,960	10,148	10,899
Cash at end 31/03	7,866	9,960	10,148	10,899	11,600

Revenue Split (A\$'000's)

Year ending Mar	2019A	2020E	2021E	2022E	2023E
Payroll Services	8,067	9,811	12,105	14,737	18,036
Other	320	320	320	320	320
Group Revenue	8,387	17,547	20,707	24,208	27,965

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

Year ending Mar	2019A	2020E	2021E	2022E	2023E
Operating revenue	8,387	17,547	20,707	24,208	27,965
EBITDA	2,669	5,385	7,308	9,367	11,441
D&A	(376)	(441)	(493)	(534)	(467)
EBIT	2,293	4,944	6,815	8,833	10,974
Net interest income	0	236	299	304	327
NPBT	2,293	5,180	7,114	9,138	11,301
Tax Expense (benefit)	0	(155)	(213)	(274)	(339)
NPAT	2,293	5,025	6,900	8,864	10,962
Significant Items	0	0	0	0	1
NPAT (Proforma)	2,293	5,025	6,900	8,864	10,962
EBITDA Margin	31.8%	30.7%	35.3%	38.7%	40.9%
EBIT Margin	27.3%	28.2%	32.9%	36.5%	39.2%
NPAT Margin	27.3%	28.6%	33.3%	36.6%	39.2%

Balance sheet (A\$'000's)

Year ending Mar	2019A	2020E	2021E	2022E	2023E
Bank Balance	7,866	9,960	10,148	10,899	11,600
Receivables	1,700	3,556	4,197	4,907	5,668
Prepayments	0	0	0	0	0
Other	3,150	3,150	3,150	3,150	3,150
Current assets	12,716	16,666	17,495	18,956	20,418
Net PPE	85	85	85	85	85
Intangibles	1,204	1,463	1,671	1,336	1,069
Deferred Tax Assets	0	0	0	0	0
Other	0	0	0	0	0
Non-current assets	1,289	1,548	1,756	1,421	1,154
Total assets	14,005	18,214	19,251	20,378	21,572
Trade payables	4,644	5,481	6,408	7,402	0
Borrowings	0	0	0	0	0
Employee entitlements	0	0	0	0	0
Deferred Revenue	0	0	0	0	0
Total liabilities	5,520	7,944	8,781	9,708	10,702
NET ASSETS	8,485	10,270	10,470	10,670	10,870

Balance Sheet Ratios

Year ending Mar	2019A	2020E	2021E	2022E	2023E
Net Debt	(7,866)	(9,960)	(10,148)	(10,899)	(11,600)
NTA	0.14	0.13	0.13	0.14	0.14
Price / NTA (x)	5.0 x	5.5 x	5.5 x	5.2 x	4.9 x
Return on assets	18.6%	7.2%	26.1%	33.9%	41.1%
Return on equity	13.9%	34.7%	32.3%	29.3%	26.6%

Valuation

Year ending Mar	2019A	2020E	2021E	2022E	2023E
Discounted Cash Flow			WACC		9.84%
Beta	0.9		Discount Period		9 years
Cost of Equity	9.84%		DCF/Price Target		\$1.82

Table 1: Earnings estimates. Source: Lodge

Comparable analysis

PayGroup trades at a deep discount relative to its listed international peers with a comparable analysis detailed in Table 4 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 forecast PE basis, PayGroup currently trades at an 85.1% discount relative to other listed international BPO Payroll and HCM Software providers (67.2 times average) and an 80.6% discount to HCM Software providers (51.5 times average).

We would also note that in 2018, the NASDAQ listed Ultimate Software Group, Inc. was acquired by a private equity group led by Hellman & Friedman for US\$11 billion, representing a 32% premium to its then 30-day VWAP and 52.69 times net earnings.

A summary of 8 domestic and internationally listed comparable companies and multiple analysis is detailed in Table 2 below.

CODE	COMPANY	STOCK EXCHANGE	PRICING	MARKET CAP	PRICE	P/E	EV/EBITDA	EV/REV	SOLUTION
ADP	Automatic Data Processing	U.S.	USD\$	72.88B	168.43	31.03	19.92	5.20	BPO Payroll and HCM Software
WDAY	Workday	U.S.	USD\$	37.5B	163.22	97.73	61.55	12.28	HCM Software
PAYX	Paychex	U.S.	USD\$	30.1B	84.51	28.94	16.75	6.92	BPO Payroll and HCM Software
PAYC	Paycom	U.S.	USD\$	16B	265.5	93.03	38.64	16.46	BPO Payroll and HCM Software
PCTY	Paylocity	U.S.	USD\$	6.44B	120.43	115.8	39.12	11.12	BPO Payroll and HCM Software
CSOD	Cornerstone OnDemand	U.S.	USD\$	3.56B	58.67	39.92	25.07	5.41	HCM Software
ZAL	Zalaris	OSL (Norway)	NOK	490m	25.00	16.86	6.98	0.97	HCM Software
ELO	Elmo Software	ASX	AUD\$	487m	6.50	N/A	N/A	7.6	BPO Payroll and Software
PYG	Paygroup*	ASX	AUD\$	48.2m	0.70	9.6	8.4	2.58	BPO Payroll and Software

Table 2: Market comparables Source: Thomson Reuters Consensus and Lodge Research, 12 December 2019. *Forward P/E, EV/EBITDA and EV/Revenue based on FY20 pro-forma forecasts including Astute

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Contact Lodge Partners

Melbourne

Lodge Partners Pty Ltd
ABN: 25 053 432 769 AFSL: 246271
Level 6, 90 Collins Street, Melbourne VIC 3000
T +61 3 9200 7000

lodgepartners.com.au

Sydney

Lodge Partners Pty Ltd
ABN: 25 053 432 769 AFSL: 246271
Lvl 22, 227 Elizabeth Street
+61 2 9225 4433