

Paycom Software, Inc.
NASDAQ:PAYC

Analyst: Thomas Marano
Sector: Information
Technology

BUY

Price Target: \$51.62

Key Statistics as of 11/11/2016

Market Price: \$41.60
Industry: Software
Market Cap: \$2,681.57M
52-Week Range: \$22.42-52.93
Beta: 1.98

Catalysts:

- Presidential Election
- Equal employment compliance

Company Description:

Paycom Software, Inc. (Paycom) is a United States based online payroll and human resources technology provider located in Oklahoma City, Oklahoma. Paycom is known for their multiple online services in areas such as talent acquisitions, time and labor management, payroll, talent management, and human resources. Paycoms broad cloud based HR system helps corporations manage many aspects of their company. With ISO 27001 and ISO 9001 certificates, Paycom Software has extreme security standards.



Thesis

Paycom Software Inc., is a growth company who has continued to grow revenue year after year. Providing evidence that demand for their product is growing. The main reasons corporations' partner with Paycom is due to their on-site implementation, to improve talent and retention, customize and create a communication channel to employees, work efficiency with strategic organizations, and compliance by design. Plus Paycom is one of the only human resource software that is together on a single database. Which provides extreme ease to payroll and human capital management.

Industry Outlook

Continuing through 2016, the software industry and information technology sector continue to grow.

Labor within the software industry has grown since 2015 by nearly 40% with overall confidence of continuous growth going forward into 2017. In the aggregate the US IT sector employs approximately 5.9 million workers in technical and non-technical roles. Spanning from jobs such as software developers, network administrators, human resources, and marketing.

Globally revenue within the IT industry is expected to reach 3.8 trillion, up from 2015's 3.7 trillion, with the United States accounting for nearly 31%.

The driving force within the industry is the cloud computing software. Paycom's Cloud computing software increases efficiency, has a disaster recovery system, and allows associates to work from anywhere. Paycom has many well-known competitors of similar size and revenue that provide a similar service.

COMPETITORS	SYMBOL
Cornerstone OnDemand, Inc.	NasdaqGS:CSOD
The Ultimate Software Group, Inc.	NasdaqGS:ULTI
Paylocity Holding Corporation	NasdaqGS:PCTY
RealPage, Inc.	NasdaqGS:RP
Synchronoss Technologies, Inc.	NasdaqGS:SNCR
Zendesk, Inc.	NYSE:ZEN
Mentor Graphics Corp	NYSE:MENT

Business Model

Paycom Software Inc. provides a comprehensive, cloud oriented payroll and human resources software solution that was created for companies as a software service. With Paycom's key advantage being that their software operates on a single server base. Allowing their customers to access all their data in one area, rather than multiple databases.

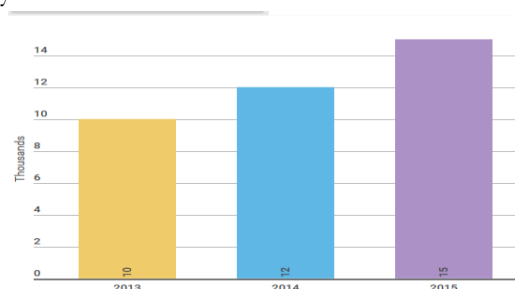
Paycom currently has 39 sales offices across the country that act as their main source of communication for demos or any errors. They plan to open more storefronts within 2017 and increase overall client numbers. Headquarters strategically places Paycom in areas where the software is highly used.

Paycom's target market is mid-size corporations with approximately 2000-8000 employees.

Product Differentiation

With the IT sector and Software industry growing rapidly each year it is extremely crucial that Paycom Software differentiates itself from their competition. Most of Paycom's competition have a similar payroll processing software but not all of them have an HCM (Human Capital Management) solution. Paycom software offers a software program that "Truly Completes Employment Life Cycle Management". Making the everyday tasks of running a business much more efficient and easier. With talent acquisition, which provides convenience when screening for new employees. Payroll, time & labor management which aid in clocking employee hours and their duties. Talent management and HR Management. Many of Paycom's competitors do not offer all of these services and because of this Paycom easily differentiates itself from its competition.

It's proven that Paycom differentiates itself from their competition by maintaining their 91% retention rate year after year and increasing their total clients year after year. As you can see from the chart below, Paycom continues to increase their number of clients year after year.



Strong 3rd Quarter Results

Paycom Software's Q3 earnings came out on November 1st 2016 and shows huge signs of success.

-Third quarter revenue of \$77.3 million up from prior year Q3 by 40%.

-Third quarter GAAP net income up \$6.2 million, 61% from prior year's quarter.

- Third Quarter adjusted EBITDA up 68% to \$18.2 million from Q3 2015.

-Projections for quarter ending December 31st 2016 are revenues between \$85 million to \$87 million and adjusted EBITDA between \$14 and \$16 million.

Ownership

According to the graph below showing short interest you can see Paycom's short interest began to severely plunge from their all-time high in October. The decline is an indication that investors are beginning to sell their short positions, meaning investors possibly believe that the share price may pick up traction and raise again. This supports my thought for purchasing shares of Paycom Software Inc.



The CEO, Chad Richardson and his leadership team together own approximately 20% of shares outstanding. This shows that internal sources within the company believe in the future and success of the company.

Profit Margins

Paycom Software is financially healthy. They've continued to increase return on invested capital from 2013-2015 and has continued to grow each quarter of 2016. Gross margin has steadily increase year after year and although EBITDA margin took a dip in 2013,

they're on track and continue to grow going in the final quarter of 2016. Paycom has also increased their operating margin year after year showing that Paycom is earning more per dollar of sales.

			4.83	9.79	19.10
Return on Invested Capital					
Margins					
Gross Margin	76.80	78.74	80.58	81.90	84.21
EBITDA Margin	11.79	15.07	13.90	15.15	19.52
Operating Margin	2.55	7.88	8.80	10.40	15.33

Financials and Multiples

Paycom Software has continued to increase revenue year and after a very strong 2016 Q3 they're predicted to continue this trend through 2016 and into 2017.

ROIC		
	History	LFY
PAYC	16.6%	25.7%
Competitors	8.1%	4.5%

ROIC /WACC		
	History	LFY
PAYC	1.80	1.69
Competitors	0.79	0.30

As you can see from the ratio comparison above, in comparison to their top competitors Paycom Software has been demonstrating value creation at a much greater pace. 1.69 LFY compared to the competitors .30 LFY.

Historically the WACC of Paycom has been lower than their competitors but recently they're had a higher value. However due to their very high ROIC value of 25.7% they're still creating value (ROIC/WACC>1 shows value creation). Whereas their competitors have been destroying value.

According to Bloomberg. Paycom has LF Net debt less than 0 million of -\$44.41 Million which is significantly less than their competitors.

Long Term Plan

-Increase relationship with current software users and seek new clients.

-Develop more storefronts throughout the country.

-Increase employment; One of Paycom's biggest issue is their number of software engineers. Paycom has a great staff however most of the employees installing the software through the country are not developers. They're just associates. By increasing the number of software developers this will increase the efficiency of the installment of the software in corporations. Providing their customers with ease and adding to their accredited name.

Important Dates and Catalysts

I believe that due to the outcome of the presidential election the market is going to do great. According to CNBC the Trump presidency has already brought the Dow to all-time highs. Showing a promising future for investors. I believe that due to Trump's tax and job creation plan more corporations will take on more employees. Hopefully leading to the use of Paycom's software.

As industries grow they're required to file an Equal Employment Opportunity report annually. As corporations throughout the country continue to grow they'll need to employ and categorize their employees based on race/ethnicity, job category, and gender. As more rules and regulations come into effect I believe that more users will seek a simplified solution to keeping these records, like Paycom Software. The software helps scan potential employees which will provide ease to human resources.

Summary

In conclusion I believe that Paycom Software is undervalued and is a very useful single server software that provides an extremely useful system to many complicated problems. They're financially stable and have met past quarter goals and are on track to exceeding goals for quarter 4. As we move into the future, I expect the corporation to grow and take on larger clients leading to an increase in value and revenue.

Paycom Software, Inc.
(PAYC)

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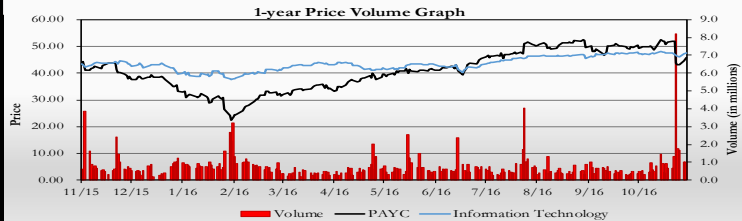
BULLISH

Analysis by Thomas Marano
11/11/2016

Current Price: \$41.60
Divident Yield: 0.1%

Intrinsic Value: \$43.74
Target Price: \$51.62

Target 1 year Return: 24.21%
Probability of Price Increase: 98.4%

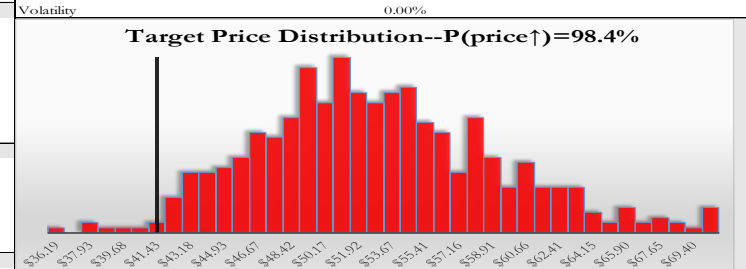


Description	
Paycom Software, Inc. provides cloud-based human capital management (HCM) software solutions delivered as Software-as-a-Service for small to mid-sized companies in the United States.	
General Information	
Sector	Information Technology
Industry	Software
Last Guidance	November 3, 2015
Next earnings date	February 9, 2017
Estimated Country Risk Premium	6.25%
Effective Tax rate	40%
Effective Operating Tax rate	41%

Market Data	
Market Capitalization	\$2,365.98
Daily volume (mil)	1.03
Shares outstanding (mil)	60.11
Diluted shares outstanding (mil)	58.69
% shares held by institutions	72%
% shares held by investments Managers	64%
% shares held by hedge funds	19%
% shares held by insiders	23.53%
Short interest	14.19%
Days to cover short interest	10.19
52 week high	\$52.93
52-week low	\$22.42
Levered Beta	1.98
Volatility	0.00%

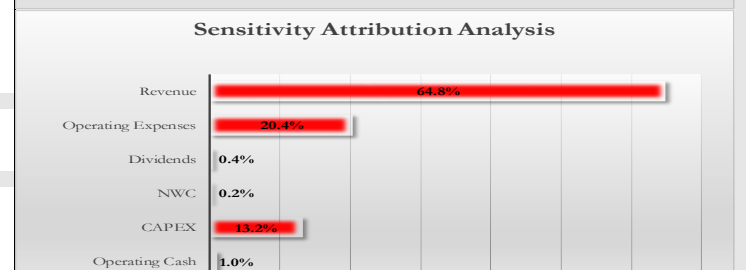
Past Earning Surprises		
Quarter ending	Revenue	EBITDA
9/30/2015	6.33%	-8.92%
12/31/2015	5.52%	-36.06%
3/31/2016	0.03%	34.73%
6/30/2016	3.33%	16.51%
9/30/2016	-0.13%	-74.16%
Mean	3.02%	-13.58%
Standard error	1.3%	19.3%

Peers	
Cornerstone OnDemand, Inc.	
The Ultimate Software Group, Inc.	
Paylocity Holding Corporation	
Workday, Inc.	
HubSpot, Inc.	
Zendesk, Inc.	
Ellie Mae, Inc.	
Bottomline Technologies (de), Inc.	



Management		
Management	Position	Total compensations growth
Richison, Chad	Founder, Chairman of the Boa	36.19% per annum over 3y
Boelte, Craig	Chief Financial Officer	50.03% per annum over 3y
Pezold, Stacey	Chief Operating Officer	N/M
Kerber, William	Chief Information Officer	46.93% per annum over 3y
York, Jeffrey	Chief Sales Officer	42.27% per annum over 3y
Oden-Hall, Kathy	Chief Marketing Officer	N/M

Total return to shareholders	
N/M	
N/M	
0% per annum over 0y	
N/M	
N/M	
N/M	



Profitability		
Profitability	PAYC (LTM)	Industry (LTM)
ROIC	39.0%	9.06%
NOPAT Margin	20%	12.9%
Revenue/Invested Capital	1.90	0.70
ROE	49.1%	10.12%
Adjusted net margin	20%	11.0%
Revenue/Adjusted Book Value	2.46	0.92

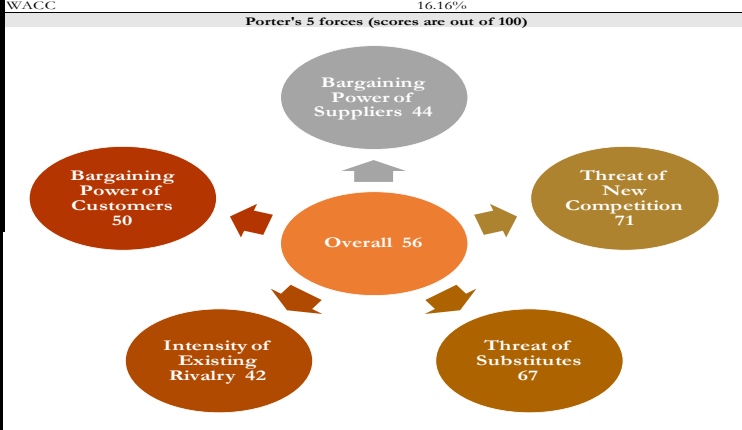
PAYC (5 years historical average)	
30.11%	
17.28%	
1.74	
-5.32%	
14.62%	
-0.36	

Invested Funds		
Invested Funds	PAYC (LTM)	Industry (LTM)
Total Cash/Total Capital	23.8%	53%
Estimated Operating Cash/Total Capital	17.4%	N/A
Non-cash working Capital/Total Capital	-7.9%	-27%
Invested Capital/Total Capital	76.3%	63%

PAYC (5 years historical average)	
18.1%	
12.0%	
-6.5%	
64.8%	

Capital Structure		
Capital Structure	PAYC (LTM)	Industry (LTM)
Total Debt/Common Equity (LTM)	0.02	0.15
Cost of Existing Debt	5.18%	3.00%
Estimated Cost of new Borrowing	6.13%	3.00%
CGFS Risk Rating	D	CCC
Unlevered Beta (LTM)	1.95	1.17
WACC	16.16%	10.92%

Industry (LTM)	
9.06%	
12.9%	
0.70	
10.12%	
11.0%	
0.92	



Revenue growth	
Period	Revenue growth
Base Year	50.5%
9/30/2017	46.3%
9/30/2018	42.1%
9/30/2019	37.9%
9/30/2020	33.6%
9/30/2021	29.4%
9/30/2022	25.2%
9/30/2023	21.0%
9/30/2024	16.7%
9/30/2025	12.5%
9/30/2026	8.3%
Continuing Period	4.1%

Valuation	
Valuation	ROIC/WACC
NOPAT margin	2.41
20.5%	2.68
22.5%	2.71
22.5%	2.65
22.4%	2.60
22.3%	2.55
22.2%	2.50
22.1%	2.44
21.9%	2.37
21.6%	2.29
21.2%	2.19
20.8%	2.07

Invested Capital	
Period	Invested Capital
Base Year	\$49.04
9/30/2017	\$57.09
9/30/2018	\$77.68
9/30/2019	\$100.24
9/30/2020	\$160.95
9/30/2021	\$239.09
9/30/2022	\$346.83
9/30/2023	\$502.80
9/30/2024	\$703.87
9/30/2025	\$953.54
9/30/2026	\$1,251.27
Continuing Period	

Net Claims	
Net Claims	Price per share
\$37.44	\$43.75
-\$12.20	\$51.68
-\$85.68	\$61.01
-\$186.89	\$71.62
-\$322.71	\$83.55
-\$499.63	\$96.74
-\$722.71	\$111.04
-\$994.20	\$126.21
-\$1,312.31	\$141.91
-\$1,670.37	\$157.73
-\$2,056.57	\$173.23