

January 2, 2018

Paycom Software, Inc. : (PAYC)

Sam Gerardi

Sector: Information Technology

Industry: Software

Current Price: 136.51

Target Price: 144.33

Paycom Software, Inc. designs and develops software solutions. The Company provides data analytical software products to manage the employment life cycle from recruitment to retirement. Paycom Software serves customers in the United States.

BUY at \$125

Current Price: \$136.51

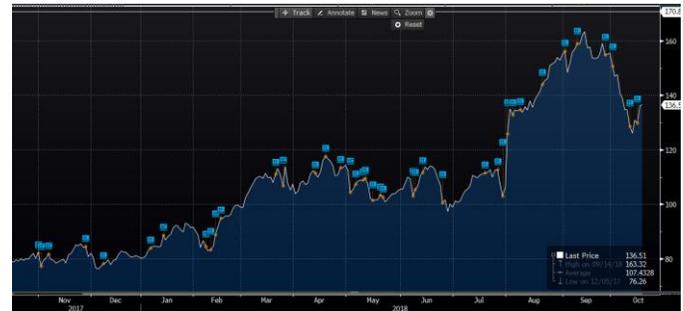
Target Price: \$150.93

Market Cap: 8.002 B

ROIC 1.66

Debt to common shares outstanding:

PAYC :26.07% Median: 53.67%



Thesis: Paycom is doubling down on expanding their business through organic growth. This places them in a position of vulnerability. Their company is very sensitive to any change in revenue or operational cost. With the opening of 2 new sales offices, this would allow them to generate ~50 million dollars in additional revenue in the first quarter if all goes according to plan. Due to the fact that they are so volatile, I suggest that we place a call at \$125. With my projections that the 1-year price is around \$145, this would allow us to get a 15% return.

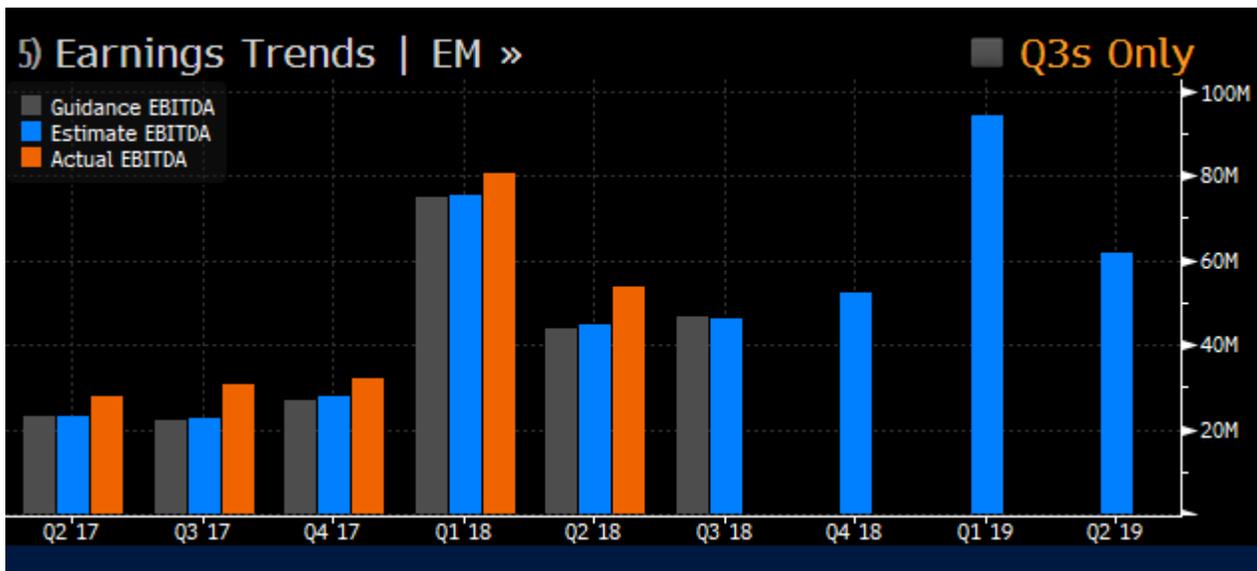
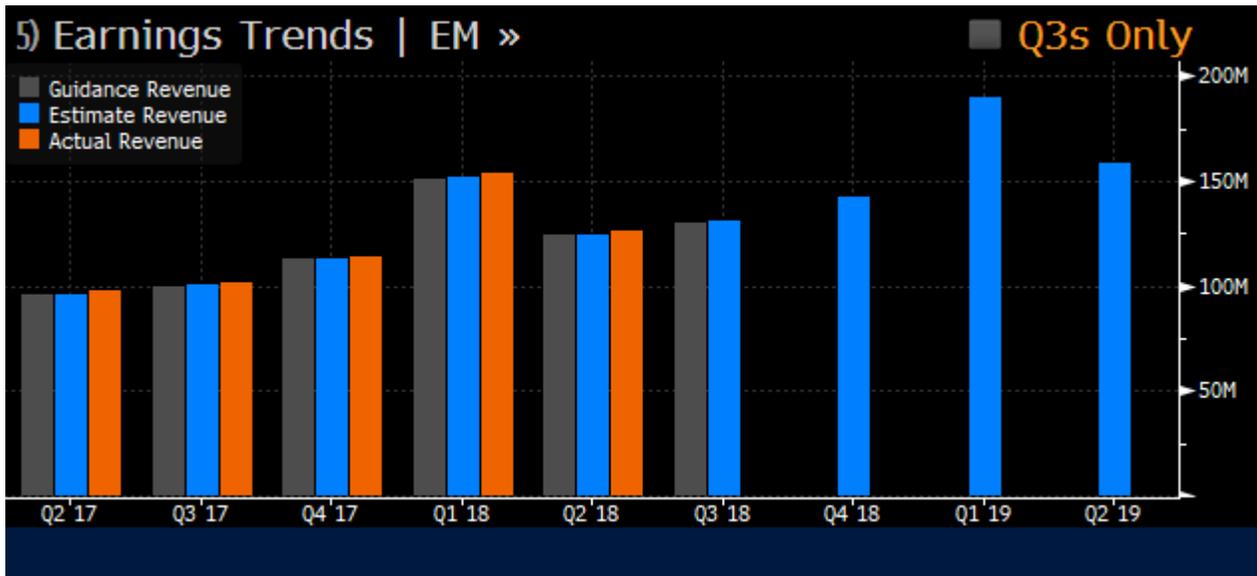
Catalysts:

- Opening of new headquarters and new office in Texas
- Launching new ad campaign in the beginning of 2019
- How quickly their new sales teams can reach their operational capacity

Earnings Performance:

Over the Past 2 years, Paycom has outperformed revenue and net income estimates. They have been able to deliver for their shareholders and place a focus on client retention and creating value for their clients. This has allowed them to see a 51.2% increase in year-to-year growth of EBITDA and a 28.9% increase in revenue year to year. Their gross profit margin is consistently between 81% and 84% over the past 4 years, which demonstrates that they have a very lucrative product. Paycom's net income has increased dramatically in the same period. In 2014, they had a net income margin of 6.1% and this year their net income margin is now at 21%. This shows that the company is starting to effectively cut cost and produce enough revenue to have a

more breathing room. Although their stock has gone down from a 52 week high of 164.08, their ambitious marketing campaign set for 2019 and the opening of new sales offices in Texas will allow their sales capacity to increase by a sizable amount. The stock price dropped in late September due to analysts ranking was downgraded from a buy to hold. This caused a substantial reaction in the market, causing the stock price to drop \$30 dollars. Recently in the last quarter, Paycom emphasized returning value to their shareholders by repurchasing 400,000 shares of stock.



Competitive advantage

When comparing to similar software companies, Paycom has some significant advantages to their competitors. The companies used to evaluate this were Cadence Design Sys Inc, Athenahealth Inc, Ptc Inc, Ss&C Technologies Holdings, Realpage Inc, Guidewire Software Inc And Tableau Software Inc-Cl A. They

all develop software that have to do with data collection and analyzation. These companies value depend upon their ability to generate revenue from sales and retain those clients they capture. This is where Paycom thrives. They place enormous value returning value to their clients and this has resulted in a 91% client retention rate. Another important point is Paycom's growth is organic. This is why their advertisement campaign and how quickly they can get their new sales teams up to operational capacity is pivotal to the revenue growth. Paycom offers an HR solution that covers the employee's life from first hire to retirement. For example, their solution offers things such as candidate and application tracker, background checks and talent acquisition. Also included in the software is payroll, government compliance, employee performance analysis, time clock and scheduling. Their product is design to enable companies to improve their efficiency in all aspects of business instead of just doing say payroll or government compliance. This allows their product to stand out from their competitors.

Name (BICS Best Fit)	Mkt Cap (USD)	Rev - 1 Yr Gr:Y	EPS - 1 Yr Gr:Y	P/E	WACC Cost of Debt	Adj ROIC AR	Rtrn on CE Adj:Y	EBITDA Adj T12M	Debt/Com Eq:Y	Adj Net Sales T12M
Median	7.21B	12.69%	45.75%	60.74	3.67%	7.52	4.82%	151.96M	54.10%	774.29M
100) PAYCOM SOFTWARE INC	7.68B	31.57%	54.69%	73.47	3.67%	45.79	53.67%	148.13M	26.07%	498.03M
101) SS&C TECHNOLOGIES HO...	12.05B	13.09%	56.87%	42.29	4.62%	8.14	10.29%	748.41M	76.13%	2.17B
102) CERIDIAN HCM HOLDING...	4.99B	6.60%	90.13%	--	5.48%	--	-1.00%	90.50M	123.63%	750.70M
103) ZENDESK INC	6.13B	37.98%	1.95%	--	4.41%	-4.04	-34.93%	-86.05M	0.00%	507.89M
104) PTC INC	10.88B	2.06%	27.48%	222.69	5.02%	9.17	1.84%	170.77M	80.46%	1.24B
105) REALPAGE INC	5.23B	18.10%	64.91%	121.41	1.68%	6.91	7.79%	151.96M	119.27%	774.29M
106) CADENCE DESIGN SYS INC	11.34B	6.99%	36.80%	34.20	3.93%	22.85	35.29%	487.75M	73.73%	2.02B
107) ATHENAHEALTH INC	4.94B	12.69%	117.09%	37.56	3.40%	9.87	8.90%	325.80M	34.47%	1.29B

(Accounting Adjustments: Adjusted for Abnormal Items When Applicable)

10) Analyze List

Growth potential

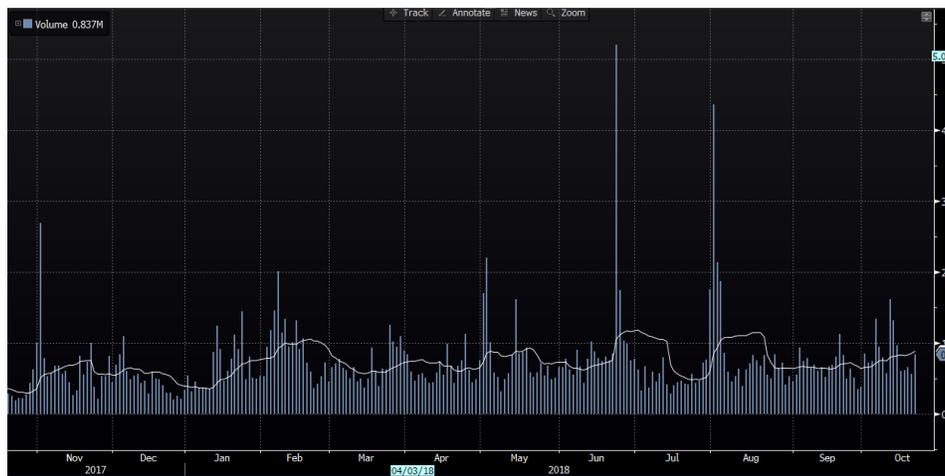
As stated before, Paycom is going all in on expanding their company with the purchase of their new headquarters in Oklahoma City and a new sales department in Texas. If their ad campaign works as intended this would allow them to generate ~50 million dollars in additional revenue in the first quarter of 2019 if they meet their projections. This company has very little debt and a large amount of free cash flows, so they are positioning themselves to expand and definitely have the means to do so.

Threats and drawbacks:

This is an internet based company, things such as data breaches are a real threat for this company. If they have a breach, this could give their perception that their company is not safe, thus reduce sales, and potentially lower their retention rate. In addition to that, if the server network they rely on goes down, they would not be able to provide for their clients. Another important thing to note is their industry is extremely competitive so maintaining their competitive advantage is paramount. They have to adapt to changes in law and technology to stay ahead of the curve and deliver the same value to their customers.

Ownership

Compare Current Stats Against 10/14/18				Institutional - Based on Current Filings				Insider - Based on Last 6 Months			
	10/14/18	Curr	Change		10/14/18	Curr	Change				
51) Institutional				52) Insider							
11) % of Shares Held	109.92	109.92	0.00%	21) % of Shares Held	17.25	17.25	0.00%				
12) % of Float Held	132.84	132.84	0.00%	22) % Chg Insider Positions	-2.64	-2.10	+0.54%				
13) # of Institutions	474	478	+0.84%	23) # of Insiders	15	15	0.00%				
14) # of Buyers	143	143	0.00%	24) # of Buyers Opn Mkt	0	0					
15) # of Sellers	143	142	-0.70%	25) # of Sellers Opn Mkt	8	7	-12.50%				
16) # of New Buyers	104	106	+1.92%	26) # of Shrs Bought Opn Mkt	0	0					
17) # of Selloffs	67	65	-2.99%	27) # of Shrs Sold Opn Mkt	255,982	197,982	-22.66%				
18) % Chg in Inst Positions	+2.34	+2.72	+0.38%	28) Avg Opn Mkt Buy Price	0	0					
				29) Avg Opn Mkt Sell Price	121.48	124.49	+2.48%				
Top Geographic Ownership (%)				Top Ownership Type (%)							
	10/14/18	Curr	Change		10/14/18	Curr	Change				
53) Geographic				54) Ownership Type							
31) UNITED STATES	81.73	81.72	-0.01%	41) Investment Advisor	76.73	76.81	+0.08%				
32) Unknown	13.57	13.57	0.00%	42) Individual	13.57	13.57	0.00%				
33) UNITED KINGDOM	2.16	2.16	0.00%	43) Hedge Fund Manager	4.97	4.97	0.00%				
34) AUSTRALIA	0.59	0.59	0.00%	44) Pension Fund	2.50	2.50	0.00%				
35) CANADA	0.53	0.53	0.00%	45) Bank	0.64	0.64	0.00%				
36) GERMANY	0.39	0.39	0.00%	46) Insurance Company	0.51	0.51	0.00%				
37) SWITZERLAND	0.32	0.32	0.00%	47) Brokerage	0.45	0.45	0.00%				
38) NORWAY	0.29	0.29	0.00%	48) Sovereign Wealth Fund	0.29	0.29	0.00%				
39) JAPAN	0.10	0.10	0.00%	49) Government	0.27	0.18	-0.09%				



This company was founded and based in the US, so this is why a majority of the ownership is in the US. A thing to note is the daily trade volume. This demonstrates the volatility of this stock; all the major peaks were either earnings announcements or a change advisor rating. For example, the reason for the last major spike was when the rating moved to a buy. The trading volume of this company is around 1 million shares, which makes it a fairly liquid stock. The short interest is down from the beginning of the year with its peaks at 22%, but has recently had a slight uptick due to the announcement of the new building purchases. Companies such as Paycom have to be strategic with their capital allocation. Biting off more than you can chew is often kiss of

death for expanding tech companies such as Paycom. With the short interest being around 5%, that demonstrates that market believes there is growth potential due to the lack of people willing to bet against it.

Base case/ Bull case / Bear case

My intrinsic value from my pro forma is 133.24. That is only less than a dollar from what it is currently valued. I believe with the new initiatives and constant product improvement will allow the company to grow and exceed the analysis projections. The main driver of stock price for this company is revenue, so that is what I manipulated to get the bear and bull case.

Base case: 133.24 | Bear case: revenue decreases by 5% =126.53 | Bull case with 5% increase revenue: 139.94

Conclusion:

Paycom is a rapidly growing company that is putting its money where its mouth is. They are going all in by buying new buildings in Oklahoma and Texas. If it works out how it is predicted, we are positioned in the perfect time to jump in and ride the revenue increase that is expected in 2019, but at its current price, the reward is not worth the risk. That is why I believe a call at 125 could allow us to get the type of margin we are looking for. If the call works in our favor, my estimates say that we could see a 15%-20% return. Paycom is a best-in-class stock that has great growth potential and I believe if the price falls just a bit more, it would be a worthwhile investment.

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(PAYC)

CENTER FOR GLOBAL FINANCIAL STUDIES

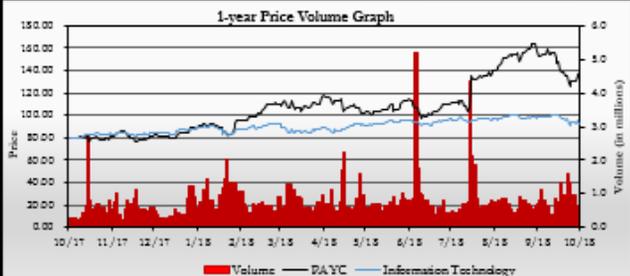
NEUTRAL

Analysis by Al Capone
10/19/2018

Current Price: \$133.64
Dividend Yield: 0.0%

Intrinsic Value: \$137.60
Target Price: \$150.62

Target 1 year Return: 12.71%
Probability of Price Increase: 97%



Description
Paycom Software, Inc. provides cloud-based human capital management (HCM) software service for small to mid-sized companies in the United States.

General Information
Sector: Information Technology
Industry: Software
Last Guidance: May 8, 2018
Next earnings date: October 30, 2018

Market Assumptions
Estimated Equity Risk Premium: 5.08%
Effective Tax rate: 21%

Market Data

Market Capitalization	\$7,834.67
Daily volume (mil)	0.56
Shares outstanding (mil)	58.63
Diluted shares outstanding (mil)	58.76
% shares held by institutions	86%
% shares held by investments Managers	75%
% shares held by hedge funds	4%
% shares held by insiders	15.95%
Short interest	6.51%
Days to cover short interest	4.78
52 week high	\$164.08
52-week low	\$74.35
Volatility	0.00%

Past Earning Surprises

Quarter ending	Revenue	EBITDA
6/30/2017	2.32%	0.00%
9/30/2017	0.78%	-14.88%
12/31/2017	0.91%	-8.16%
3/31/2018	1.64%	-19.86%
6/30/2018	3.62%	11.85%
Mean	1.85%	-6.21%
Standard error	1.0%	4.6%

Market and Credit Scores

Recommendation (STAR3) Value--0
Recommendation (STAR3) Description--0
Quality Ranking Value--NR
Quality Ranking Description--Not Ranked
Short Score--2
Market Signal Probability of Default % (Non-Ratings)--0.19%
CreditModel Score (Non-Ratings)--bb

Industry and Segment Information

LTM Revenues by Geographic Segment	LTM Revenues by Business Segments
United States--82%	Internet Software & Services--100%
United Kingdom--2%	--
Australia--1%	--
Canada--1%	--
Germany--0%	--

Management

Management	Position	Total Compensation Growth
Richison, Chad	Founder, Chairman, President & CEO	34.68% per annum over 5y
Boelte, Craig	CFO, Treasurer & Corporate Secretary	39.39% per annum over 5y
York, Jeffrey	Chief Sales Officer	34.55% per annum over 5y
Evans, Jon	Chief Operating Officer	
Smith, Bradley	Chief Information Officer	
Niedermer, David	Investor Relations Professional	

Stock Price Growth During Tenure

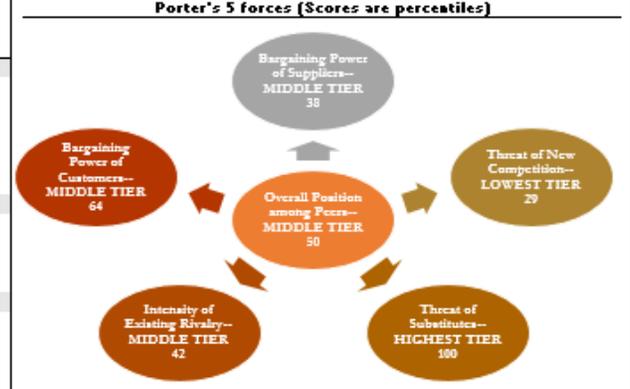
Peers

Guidewire Software, Inc.	Coridian HCM Holding Inc.
Aspen Technology, Inc.	athenshealth, Inc.
Tableau Software, Inc.	Cadence Design Systems, Inc.
Zendesk, Inc.	--
RealPage, Inc.	--

Profitability

	PAYC (LTM)	PAYC Historical	Peers' Median (LTM)
Return on Capital (GAAP)	82.0%	24.34%	19.81%
Operating Margin	34%	12.44%	20.05%
Revenue/Capital (GAAP)	2.43	1.36	0.93
ROE (GAAP)	62.6%	40.4%	8.3%
Net margin	20.2%	15.9%	13.1%
Revenue/Book Value (GAAP)	3.104082867	2.53	0.68

Peers' Median (LTM)



Invested Funds

	PAYC (LTM)	PAYC Historical	Peers' Median (LTM)
Cash/Capital	15.6%	19.3%	29.3%
NWC/Capital	-15.7%	-1.9%	-6.4%
Operating Assets/Capital	79.7%	40.7%	56.8%
Goodwill/Capital	20.4%	35.9%	18.2%

Capital Structure

	PAYC (LTM)	PAYC Historical	Peers' Median (LTM)
Total Debt/Market Capitalization	0.24	0.30	0.26
Cost of Debt	3.0%	7.1%	3.3%
CGFS Rating (F-score, Z-score, and default Probability)	BB		
WACC	10.0%	11.4%	8.0%

Peers' Median (LTM)

Forecast Assumptions

	Explicit Period (13 years)	Continuing Period
Revenue Growth CAGR	13%	2.5%
Average Operating Margin	34%	34%
Average Net Margin	30%	27%
Growth in Capital CAGR	22%	3%
Growth in Claims CAGR	0%	3%
Average Return on Capital	22%	3%
Average Return on Equity	22%	3%
Average Cost of Capital	3%	3%
Average Cost of Equity	3%	3%

