

PAYCHEX

By The Asset Kickers



Company Overview

- Paychex (PAYX)
- Current Price \$76 per share
- Market Cap \$28 billion
- Founded in 1971
- Initial Public Offering (IPO) 1983
- Headquarter Rochester, New York
- Has 13,700 employees
- As of May 2020 Paychex had:
680,000 customer that had
over 12 million employees





Company Breakdown

What does Paychex do?

- PAYX is a Provider of Human Capital Management (HCM) solutions for
 - Payroll
 - Benefits
 - Human Resource (HR)
 - Insurance Services

For Small and Medium sized business (SMBs)

- Professional employer Organization (PEO)
- Administrative Service Organization (ASO)



Paychex Solutions

- What is HCM?
- Paychex Flex Software as a Service (SaaS)
- How do they solve problems?
- Outsource HR, Payroll, Retirement, Accounting, and Insurance services



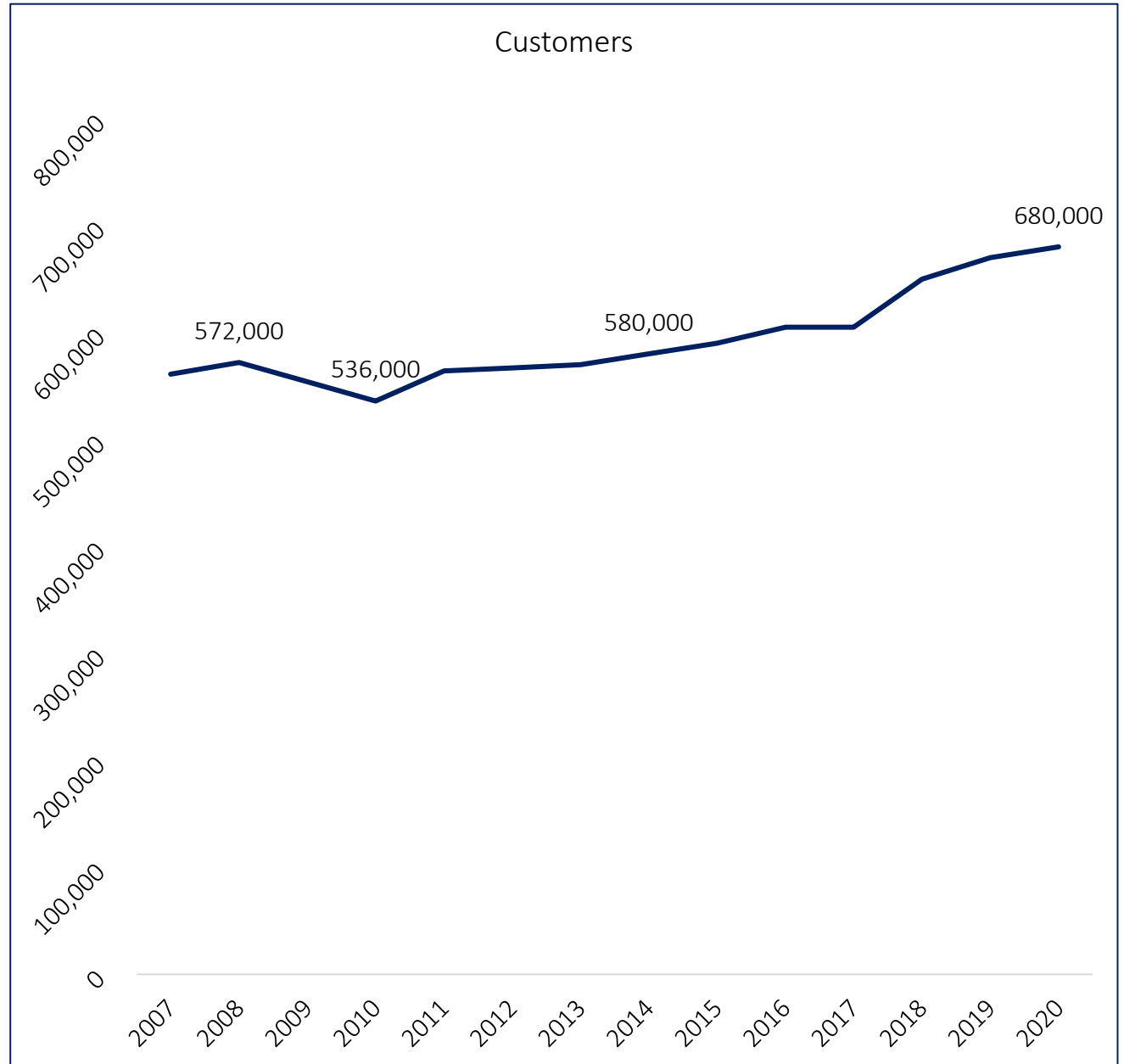
Paychex Solutions

- Professional Employer Organization (PEO)
- Administrative Service Organization (ASO)

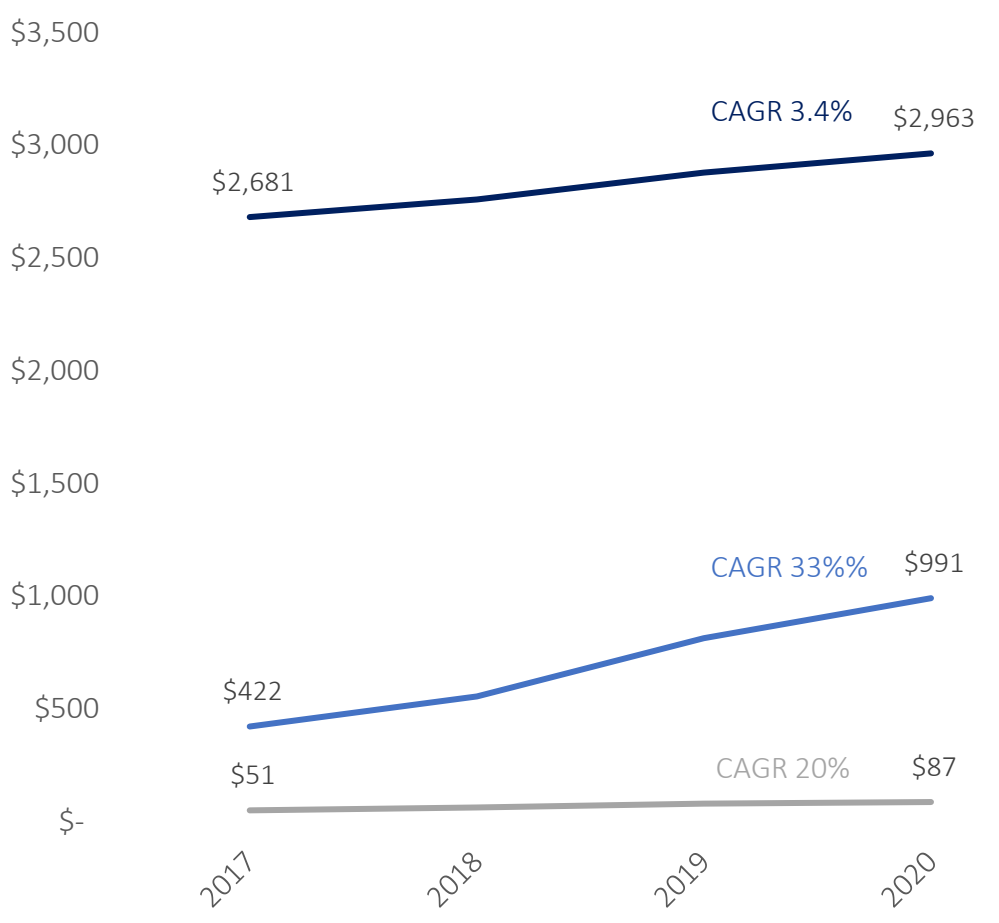


Customers

- Customer count
 - 10-year CAGR 2.41%, 5-year CAGR 3.23%
 - Historical retention rate 80%
- Average client employs 17 people
- Maximizes margins at 15-50 employees
- How do they make money?
 - Service processing fees
 - Interest on funds retained
 - 67% of payroll is from subscriptions, 33% is dependent upon headcount



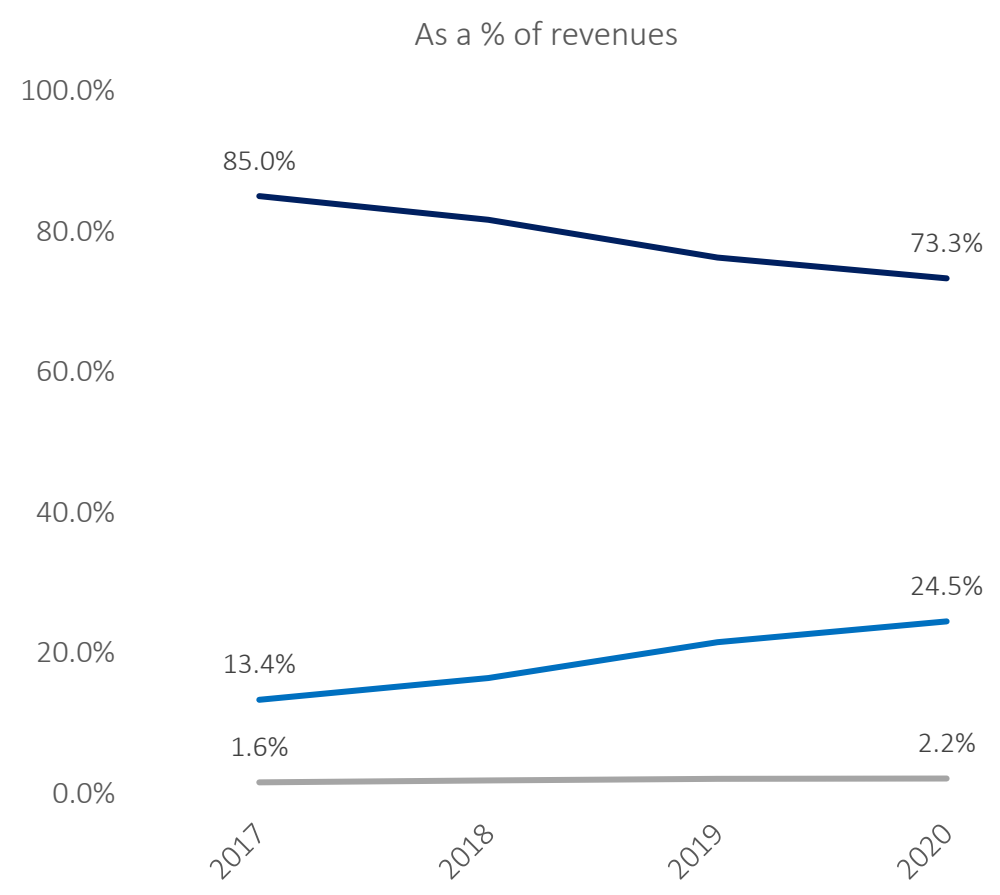
Revenue Breakdown



Management Solutions

PEO & Insurance Solutions

Interest on Funds Held for Clients



Company History

Realizing there was an opportunity for services catering to small businesses, B. Thomas Golisano started Paymaster (later Paychex) with \$3,000 and one employee.

1971

1979

Expands outside of Rochester, NY to have 18 franchises which are consolidated under one company.

Paychex has its IPO on the NASDAQ exchange.

1983

1989

Expands corporate headquarters and Rochester and reaches 100,000 clients/customers.

On 20th anniversary, Paychex launches Human Resources Services.

1991

1995

Acquires Pay-Fone and Payday and reaches over 200,000 clients.

On 25th anniversary, Paychex acquires Olsen Computer Systems and National Business Solutions, solidifying its movement into the tech space.

1996

1997

Launches Paychex Insurance agency with workers' comp, health insurance, and business insurance.

Adds 49,000 new clients by acquiring Advantage Payroll Services.

2002

Founder B. Thomas Golisano retires, replaced by former IBM executive Jonathan J. Judge.

2004

Expands retirement offering with Paychex Advisor Select 401(k). Also Paychex Mobile for iPhone, Android, and Blackberry.

2012

Announces the creation of Paychex Flex, SaaS platform which gives access to payroll, HR, benefits, and customer service all in one location.

2014

Returns to Shareholders

- Paychex is consistent in returning cash to shareholders via dividends.
 - Dividend yield: 3.5%
- Repurchasing stock opportunistically
 - New repurchase program of \$400 million (~1.5% of market cap)
- Dividend payout ratio: 80% consistently
 - May look bad at first glance but Paychex has consistent liquidity

Acquisitions

- **Oasis Outsourcing Group Holdings, L.P. (December 2018)** – industry leader in HR outsourcing services, \$1 billion (all cash) purchase price.
 - Contributed 4% to the 7% growth in revenue for FY2019
 - Drove an incremental amount of expense growth, notably compensation expenses and investment in product development.
 - Acquisition and integration costs related to Oasis were \$5.3 million during Fy2019.
- **Lessor Group (February 2018)** – market leading provider of payroll and human capital management (HCM) software solutions and is headquartered In Demark
 - \$162.5 million purchase price paid in call cash
- **HROI (August 2017)** – national Performance Employer Organization, serves small and medium sized business in more than 35 states (much like Paychex),
 - paid \$75.4 million, \$42.2 million in cash, \$33.2 million in PAYX stock.

Management



Thomas Golisano
 -Founder (1971)
 -Chairman of the Board (2004- Present)
 -Owns 10.4% of company (\$2.9B)



Martin Mucci
 -CEO/President (2011- Present)
 - Joined Paychex in 2002
 -Owns .5% of company (\$161M)



Efrain Rivera
 -CFO/SVP (2011- Present)
 - Joined Paychex as SVP in 2002
 -Owns .09% of company (\$26M)



Mark Bottini
 -SVP of Sales (2011- Present)
 -Joined Paychex in 2011
 -Owns .14% of company (\$39M)



John B. Gibson
 -SVP of Services (2013-Present)
 -Joined Paychex in 2013
 -Owns .11% of company (\$31M)



Michael Gioja
 -SVP of IT (2011-Present)
 -Joined Paychex in 2011
 Owns .09% of company (\$25M)

All together own 11.7%!

Why Paychex?

Why Paychex?

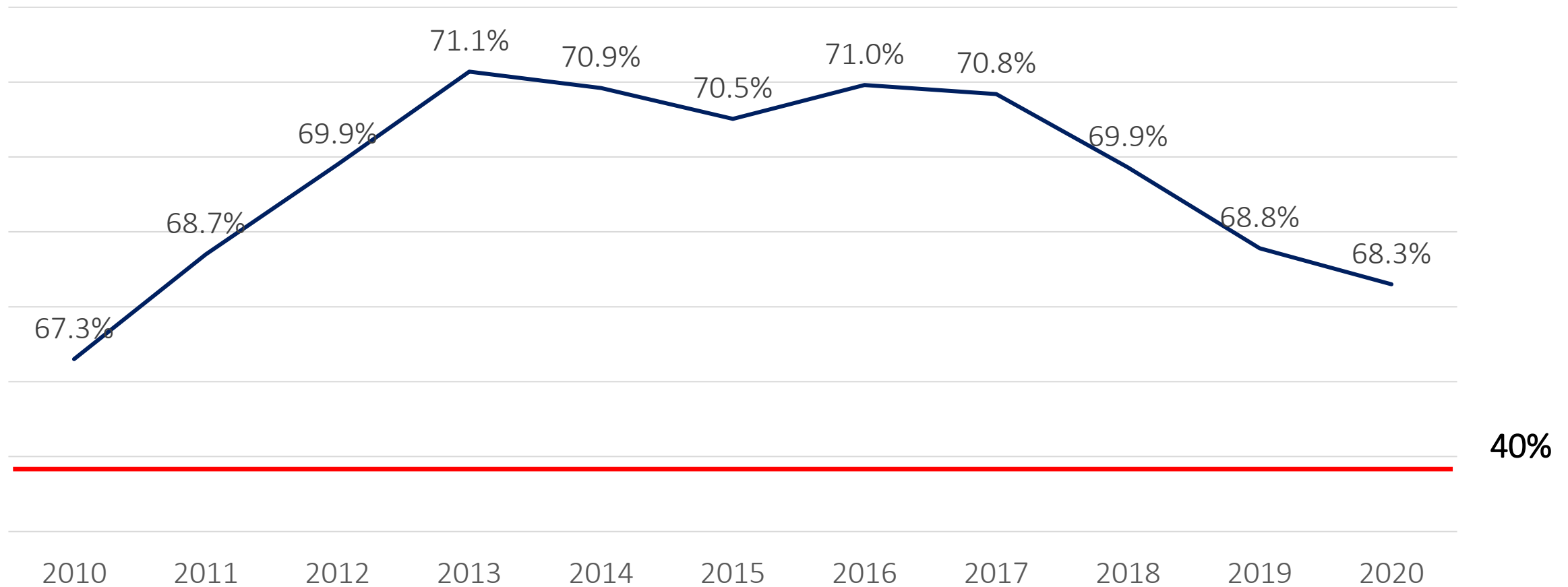
- Wide moat company
- Great business economics
- High quality financials
- Predictable and consistent
- Strong growth opportunities
- Conservative management team
- Fairly valued



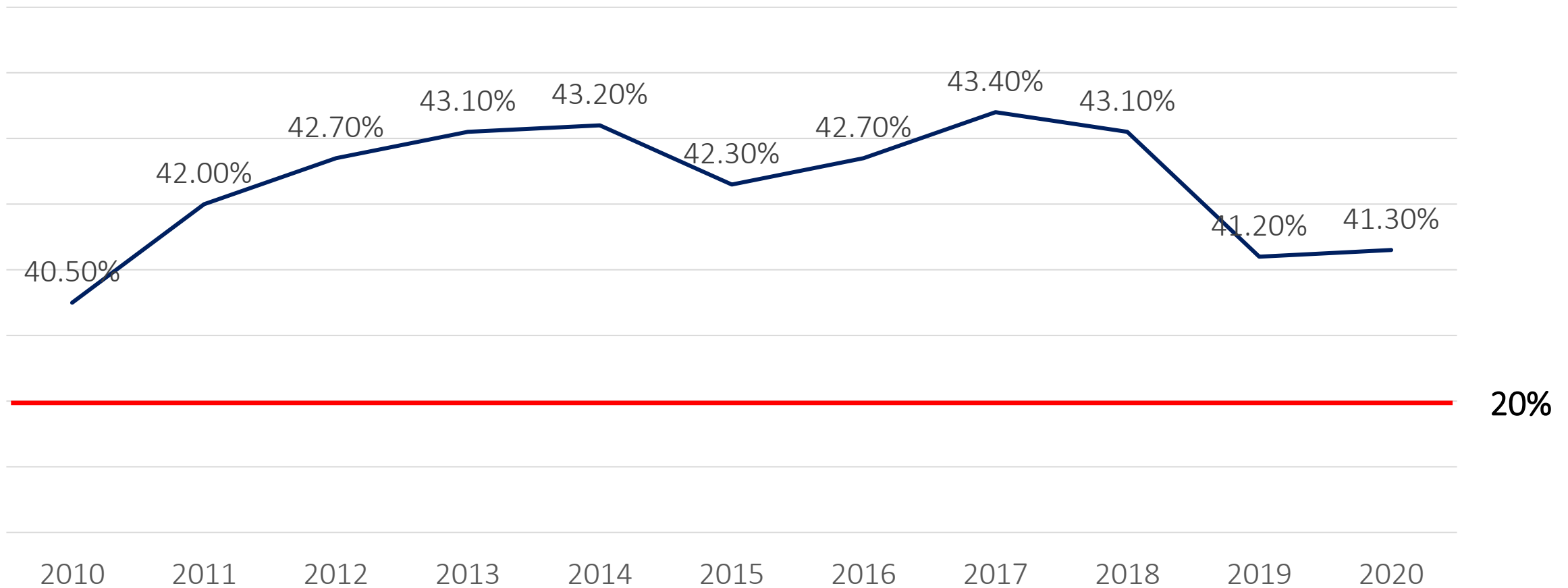


Interpretations of Financial Statements (IOFS)

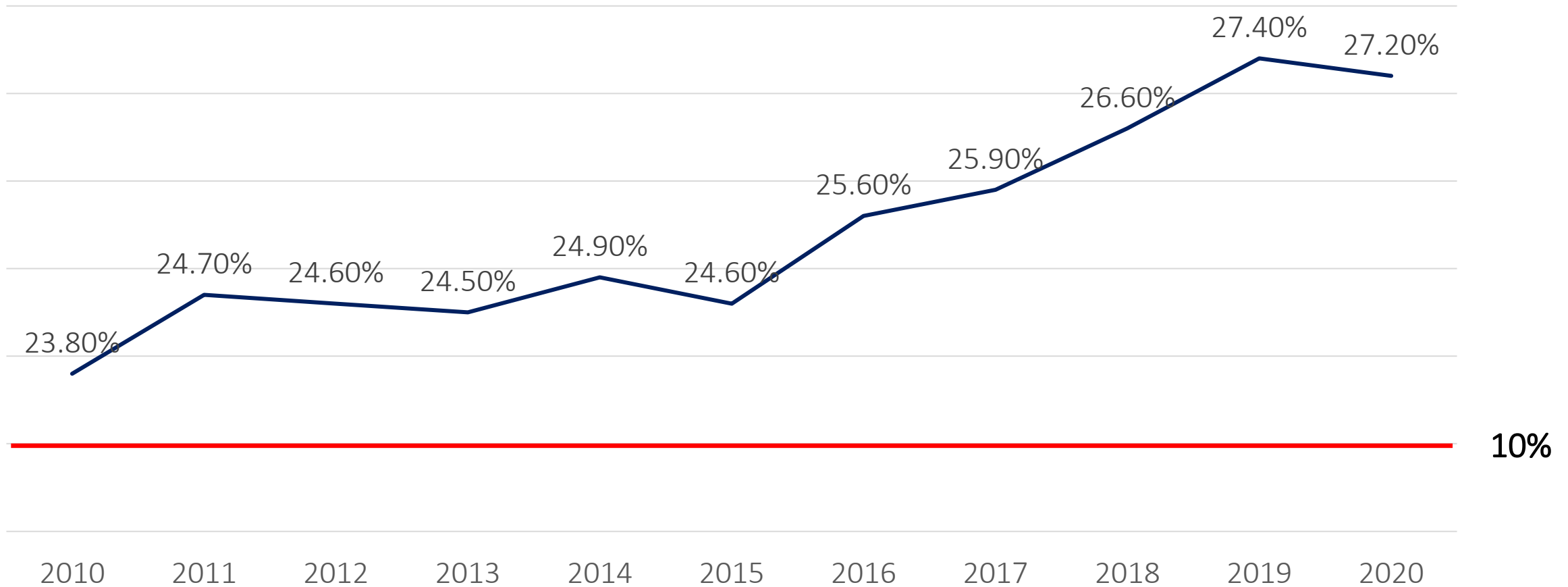
Gross Margin



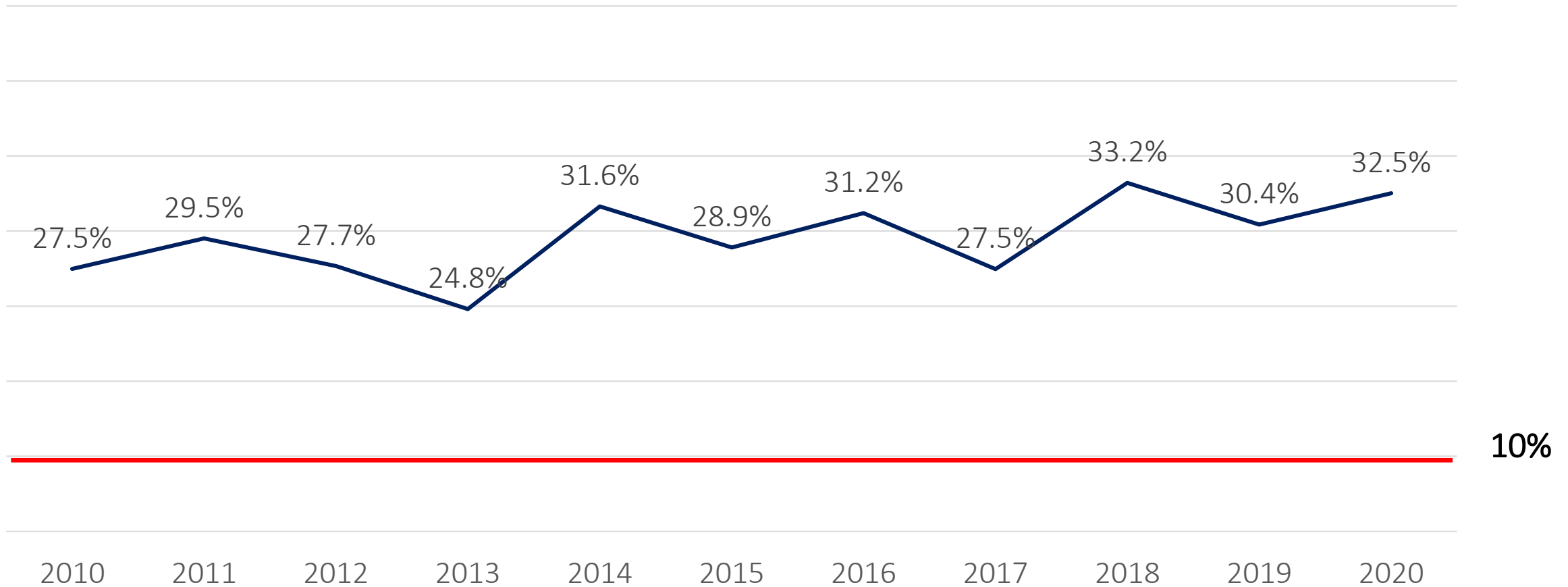
Operating Margin



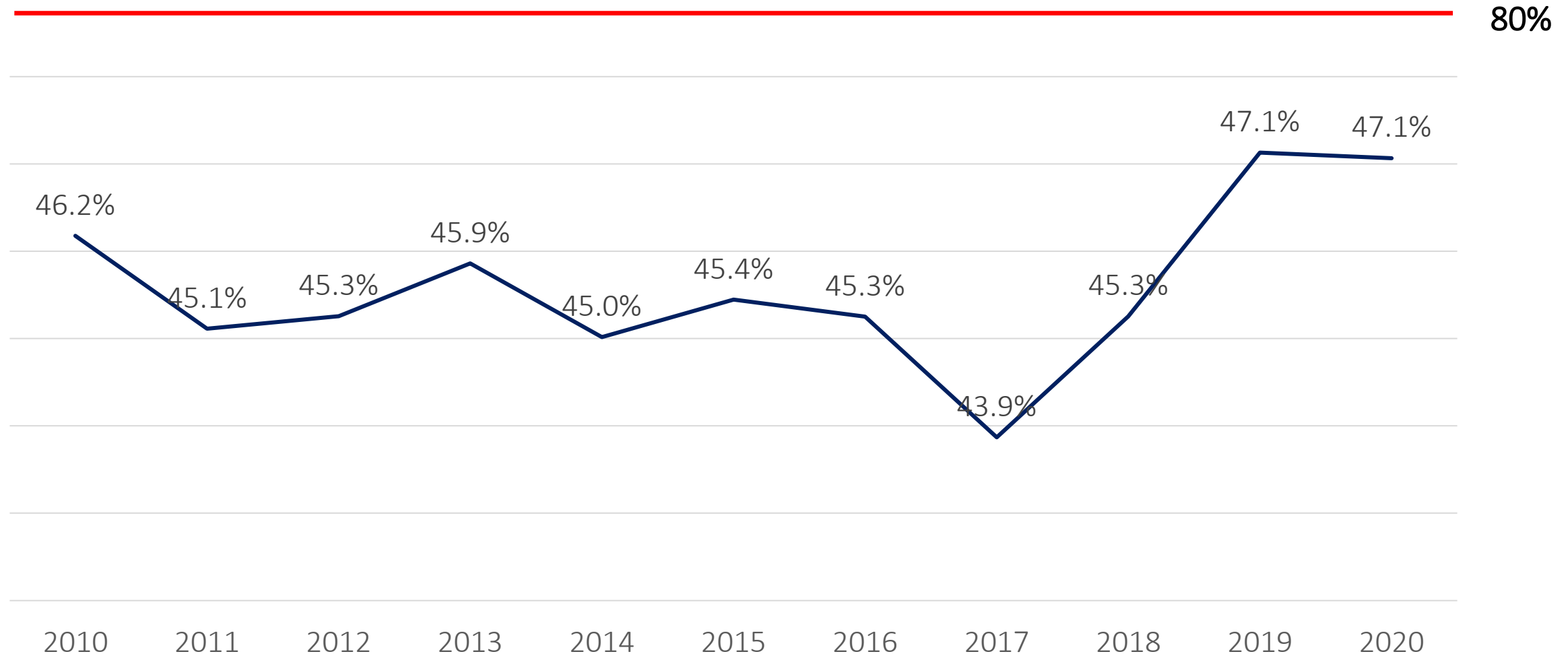
Net Margin



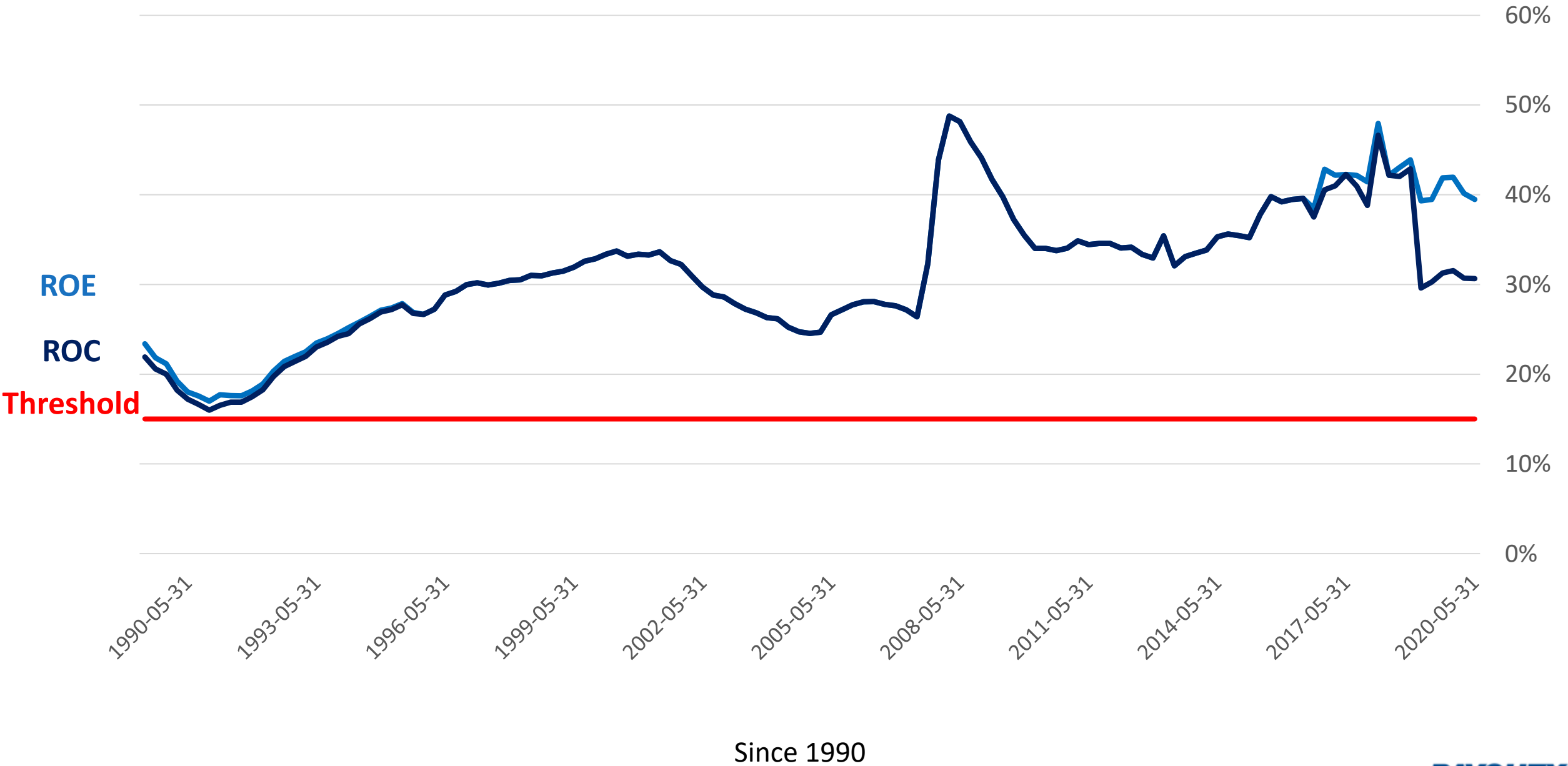
Free Cash Flow Margin



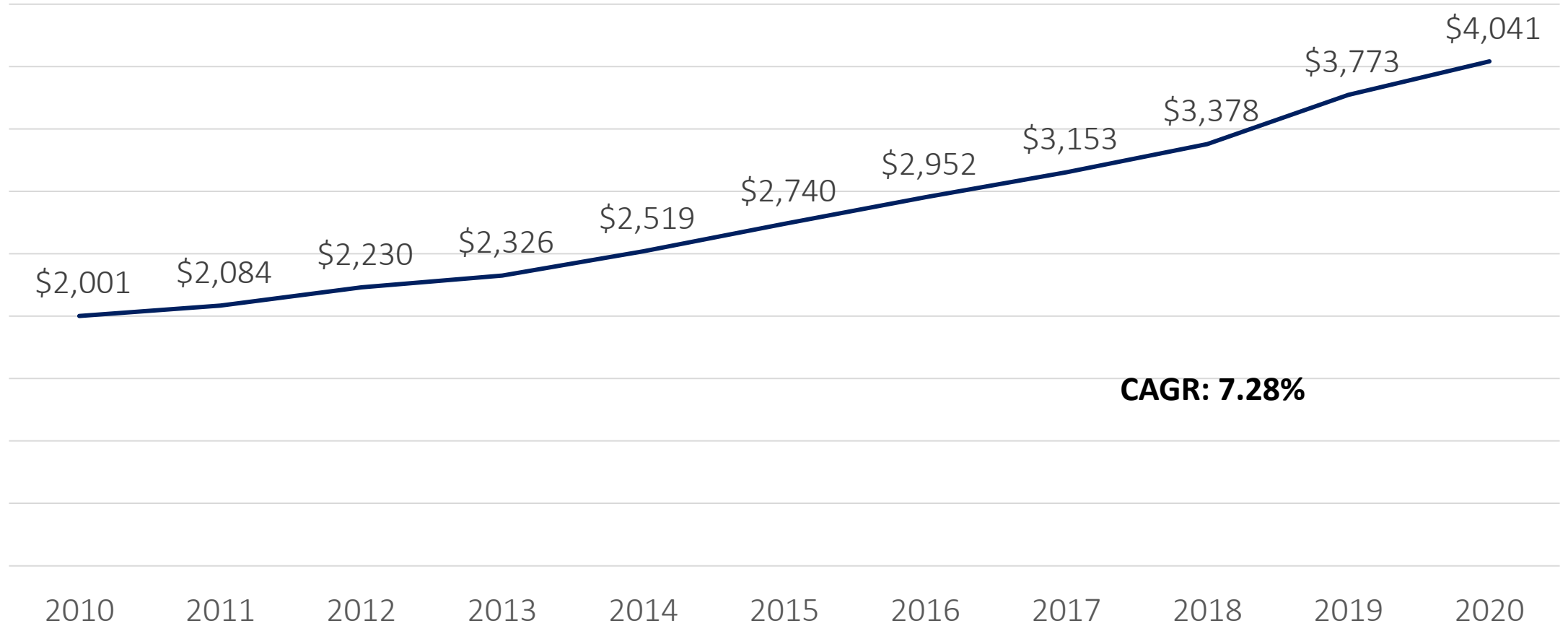
Selling General & Admin as % of Gross Profit



\$0 Treasury Stock

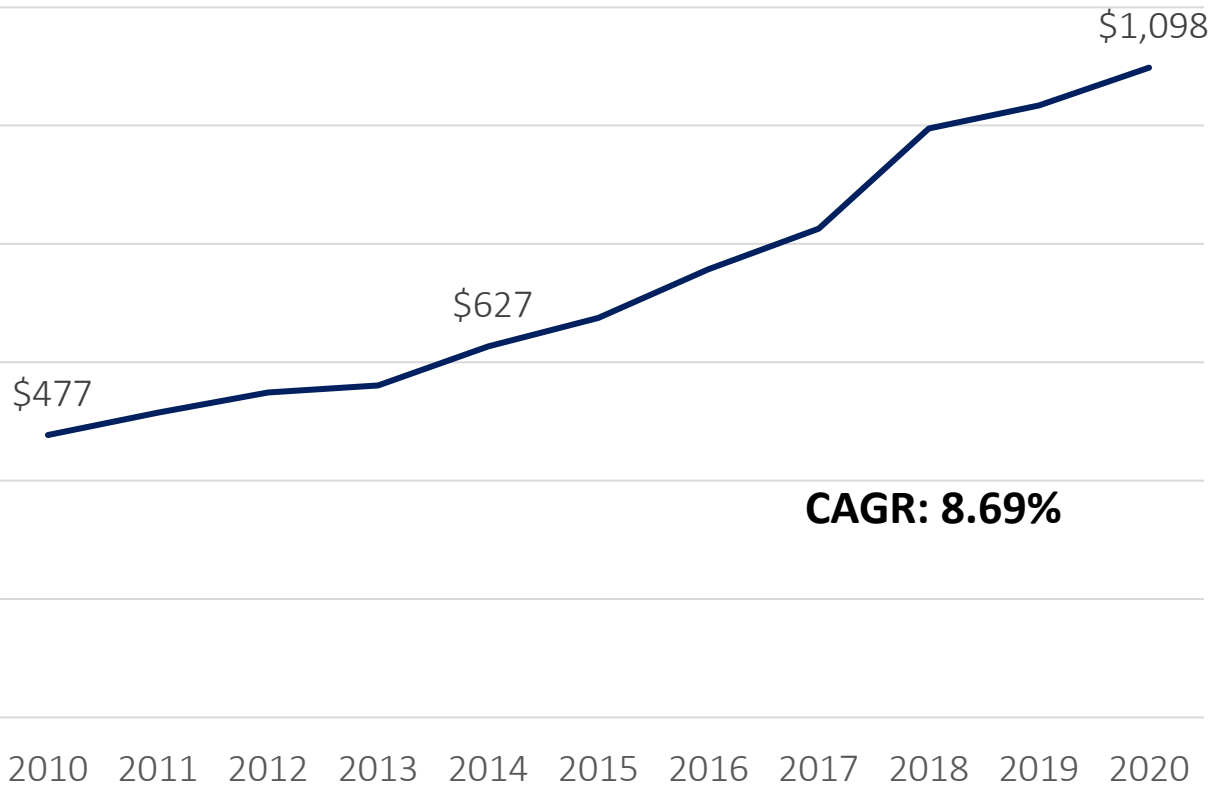


Revenue

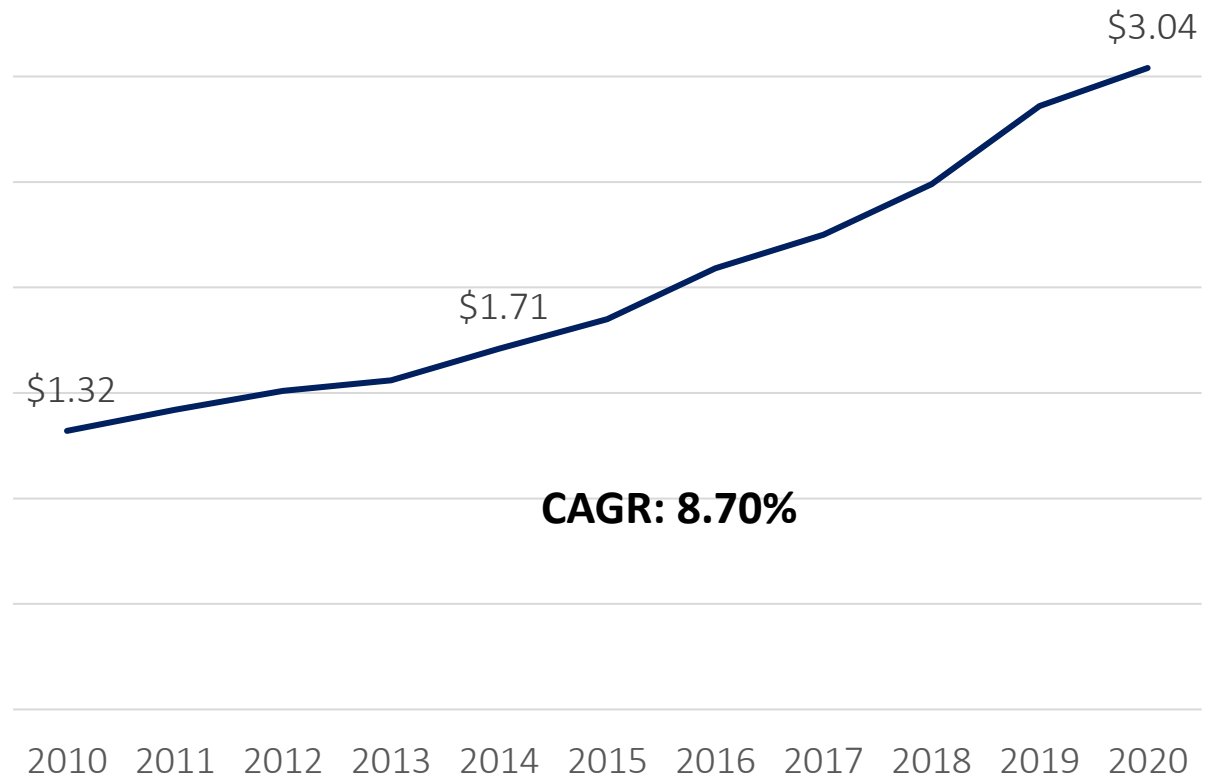


Net Income + EPS

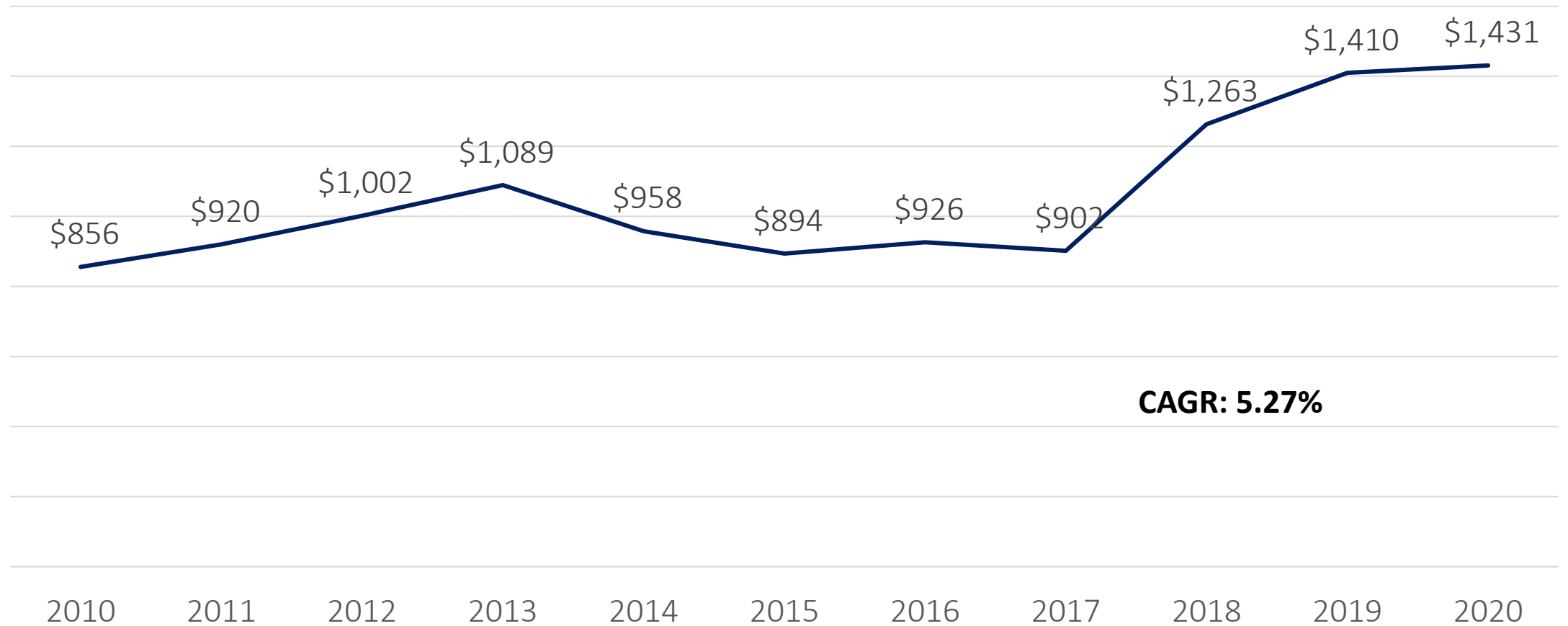
Net Income



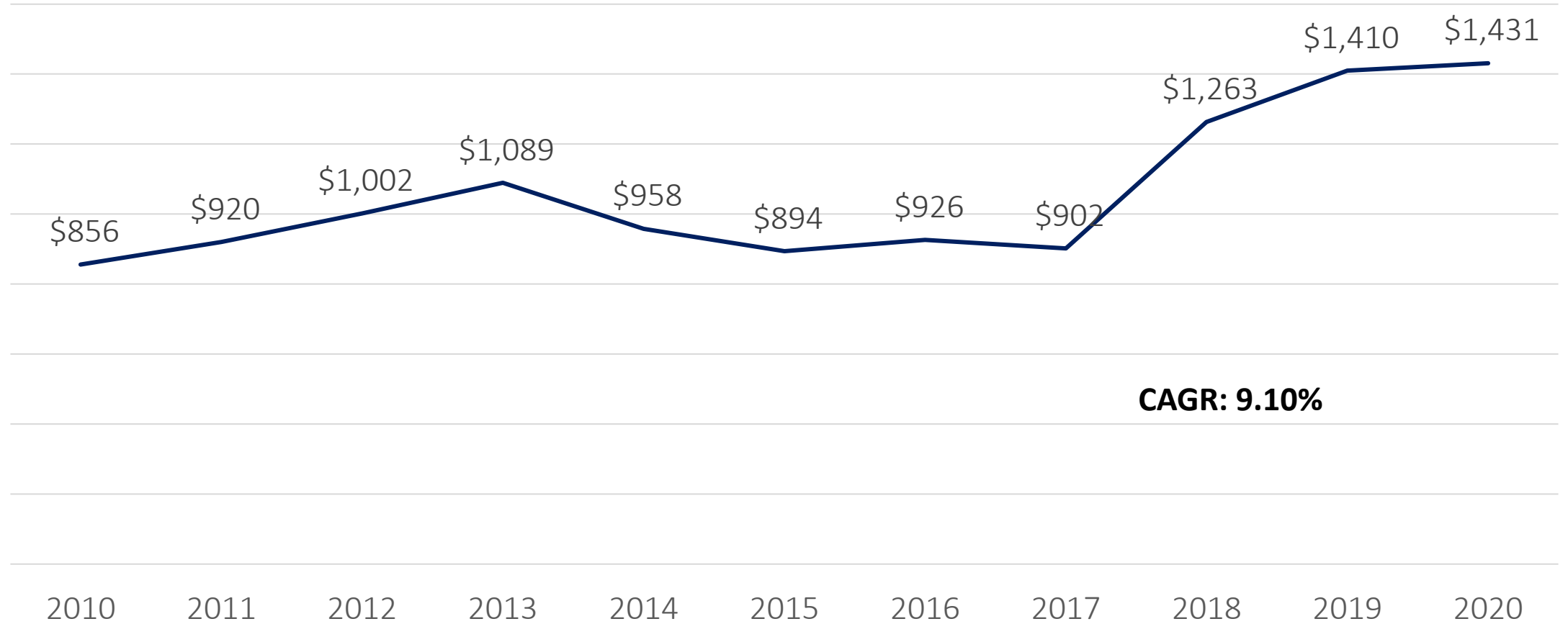
Earnings per Share (EPS)



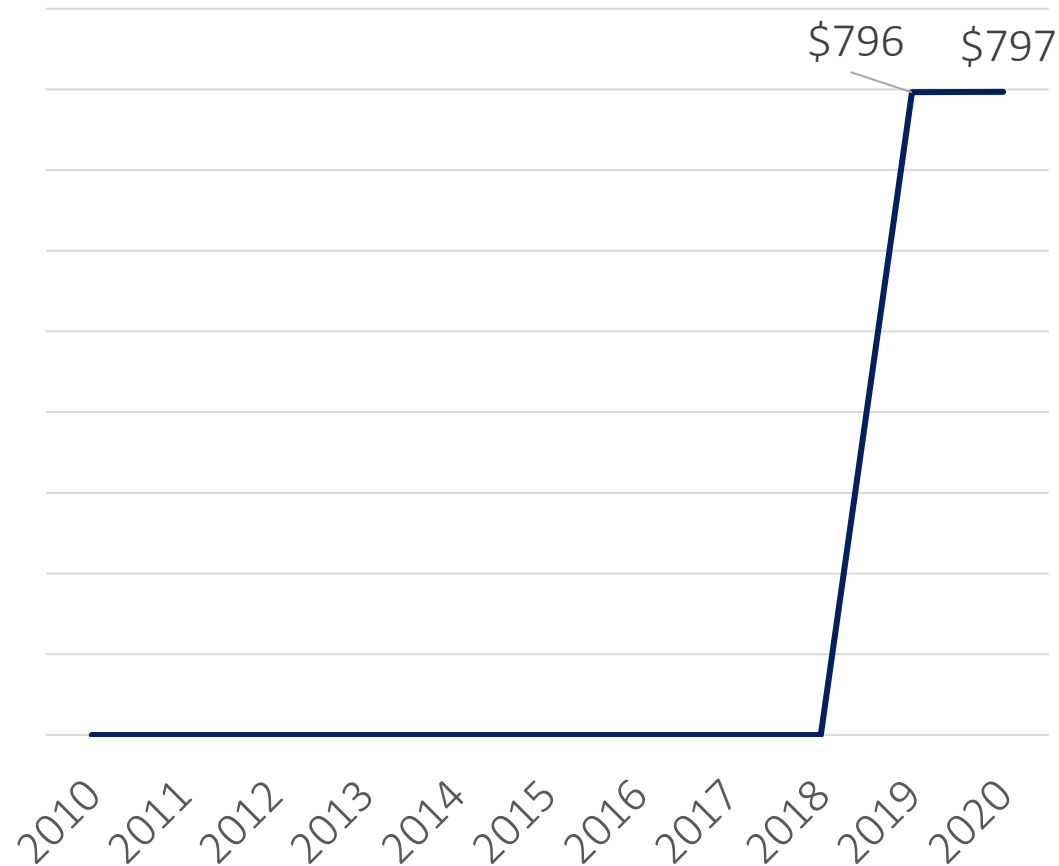
Retained Earnings



Free Cash Flow



Long Term Debt + Obligation Ratio



(+) Total Debt: \$801.9 million

(+) Pension Shortfall: N/A

(+) Preferred Stock: N/A

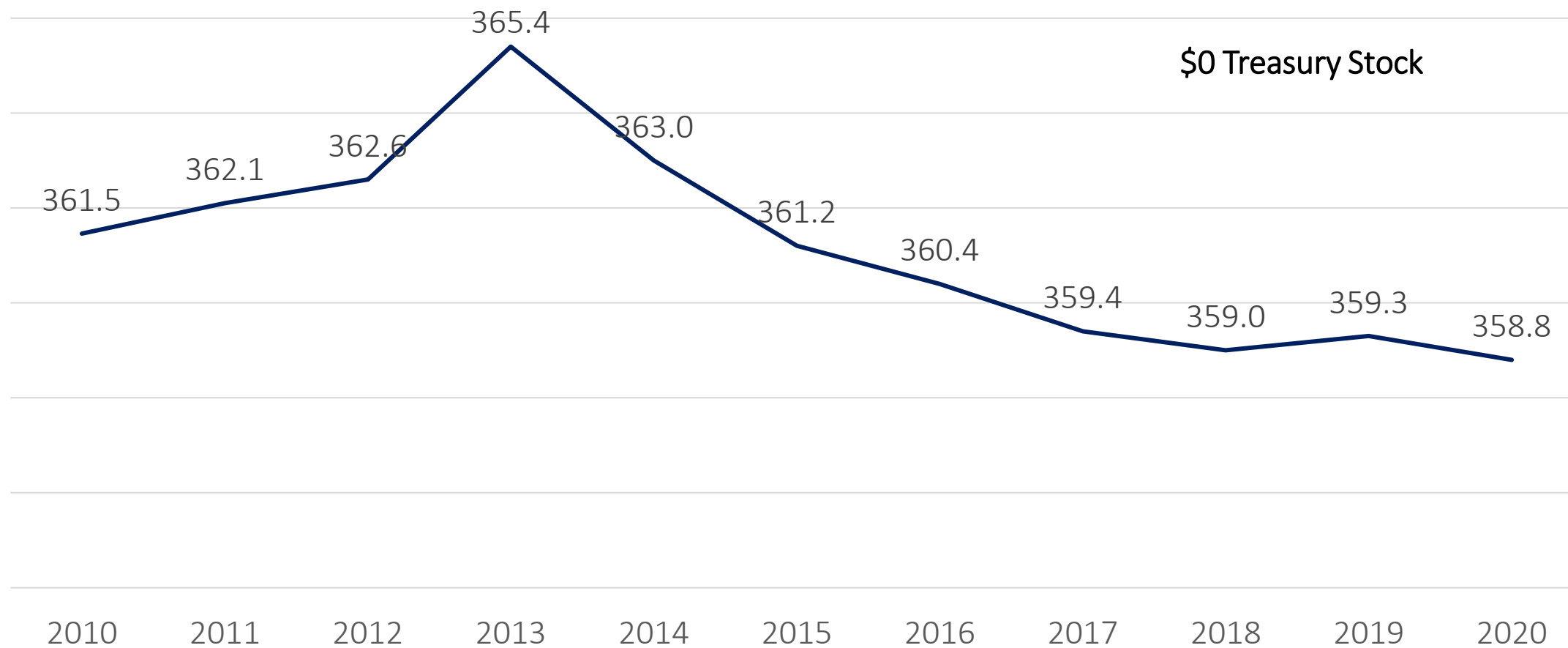
(+) Leases x 7: \$275.8 million

(-) Cash Assets: \$905.2 million

(/) Net Income: \$1098 million

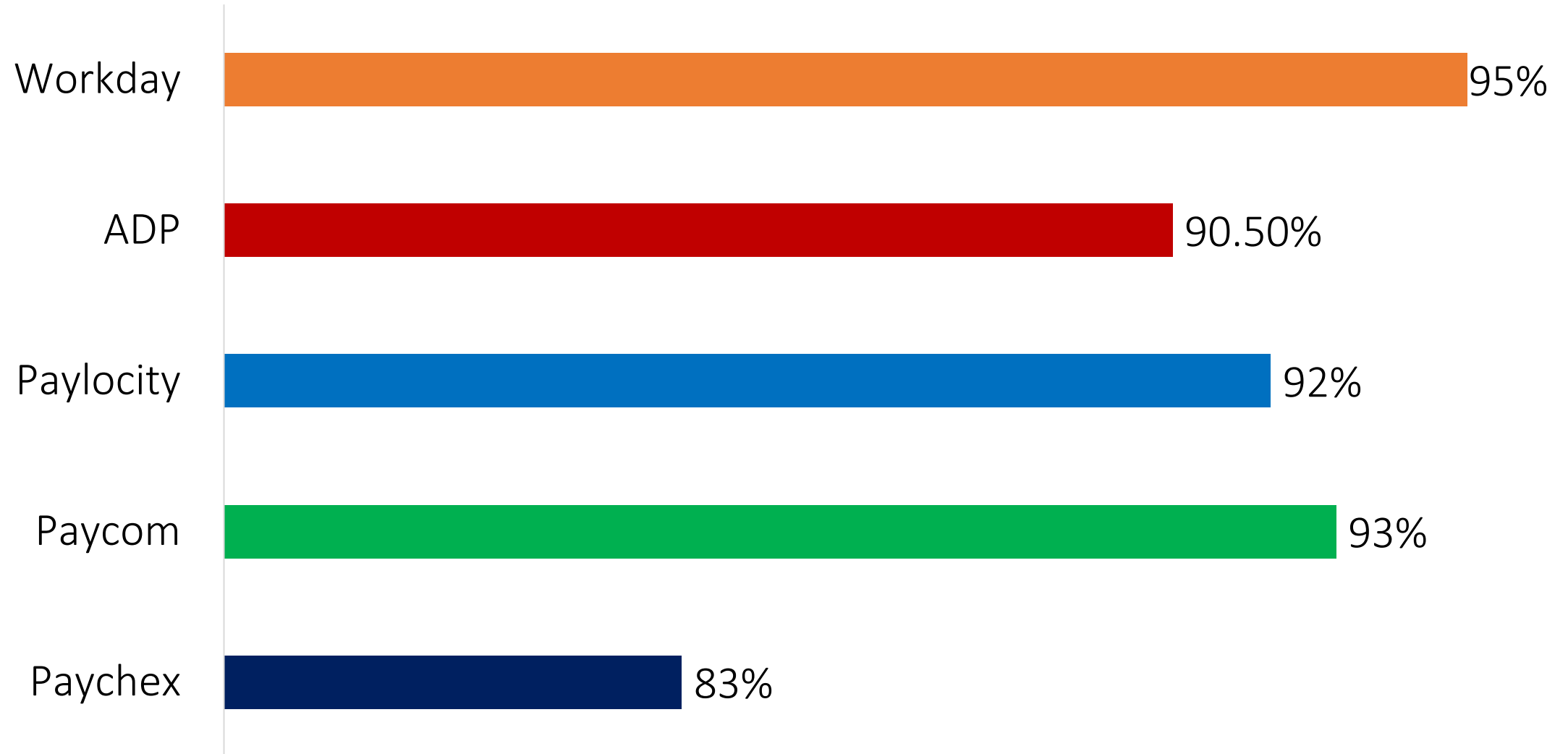
= **0.16** < 5 = **PASSES**

Shares Outstanding

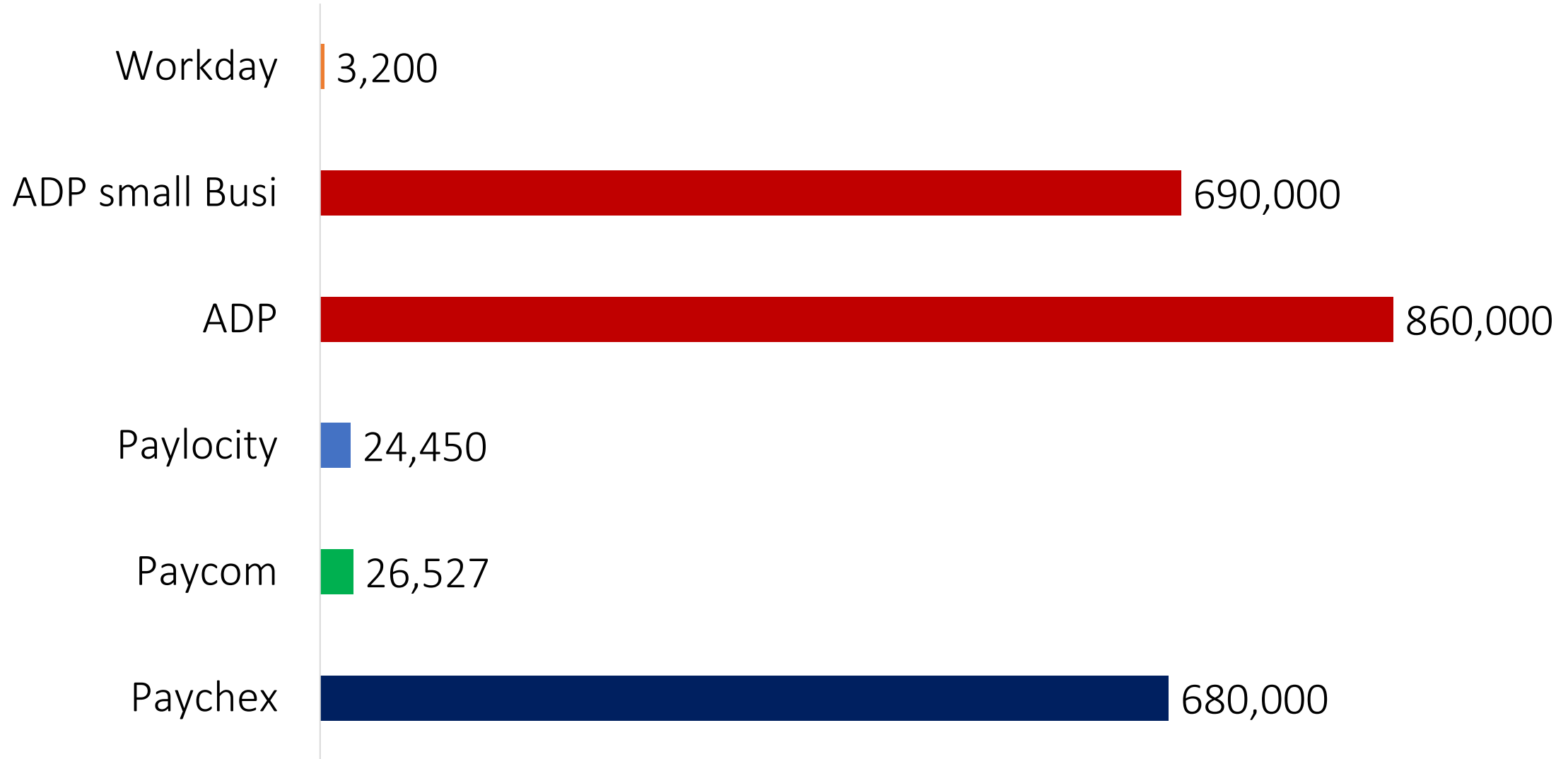


Competitors Metrics






2019-2020 Retention Rate



Client Count



Paychex vs Competitors

					
Market Cap (\$M)	\$27330	\$56200	\$15920	\$7800	\$49500
Revenue (\$M)	\$4041	\$14590	\$780	\$555	\$4300
Net Margin	27.2%	16.9%	25.6%	13.5%	NMF (-)
ROE	39.5%	43.0%	27.5%	20.0%	NMF (-)
ROC	31.0%	33.5%	26.5%	20.0%	NMF (-)
P/E	25.0	22.9	80.4	107.5	NMF (-)
EV/EBIT	18.5	17.2	70.2	115.6	NMF (-)
Employees (#)	15,800	58,000	3,765	3,050	12,200
Customers (#)	680,000	740,000	26,500	24,450	2,100
Retention	83%	91%	93%	92%	99%



Moat Analysis

The reason for good business economics

High Switching Costs

- Complex regulations
- Outsource departments through ASO and PEO
- Co-employment through PEO
- The more applications customers add the higher the switching costs

Cost Advantages

- Scale
- Large initial fixed investment
- Add additional services at minimal cost
- Able to spread out fixed costs

Wide Moat

Growth Opportunities

Growth Opportunities

- Paychex Flex (SaaS)
- Additional applications
- Higher demand due to COVID-19 Remote Working
- Professional Employer Organization (PEO) faster growing and moatier business



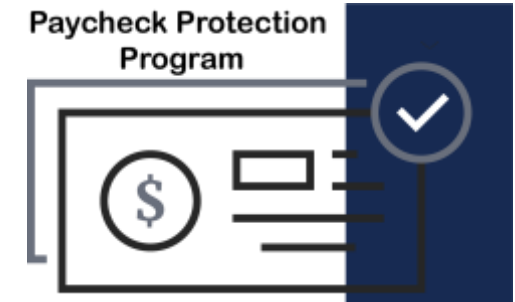
PAYCHEX FLEX

Oasis
A **PAYCHEX** company



Growth Opportunities

- Geographical Expansion via Acquisition
- Affordable Cares Act increase in required information
- Paycheck Protection Program facilitated over \$28 billion worth of loans
- Can add additional products and services at minimal extra cost



Risk Factors

Risk Factors

- COVID-19 layoffs
- Small and Medium sized businesses Exposure
- 83% retention rates
- Loses customer due to bankruptcies or acquisitions

- During the Great Recession revenue fell only 4%.
- 2009 retention rates fell to 77%.
- Low interest rates on "Interest on fund held for clients"

Risk Factors

- Faster growing competitors
- Threat of superior technology
- Cloud based solution
- Developed in house



Valuation

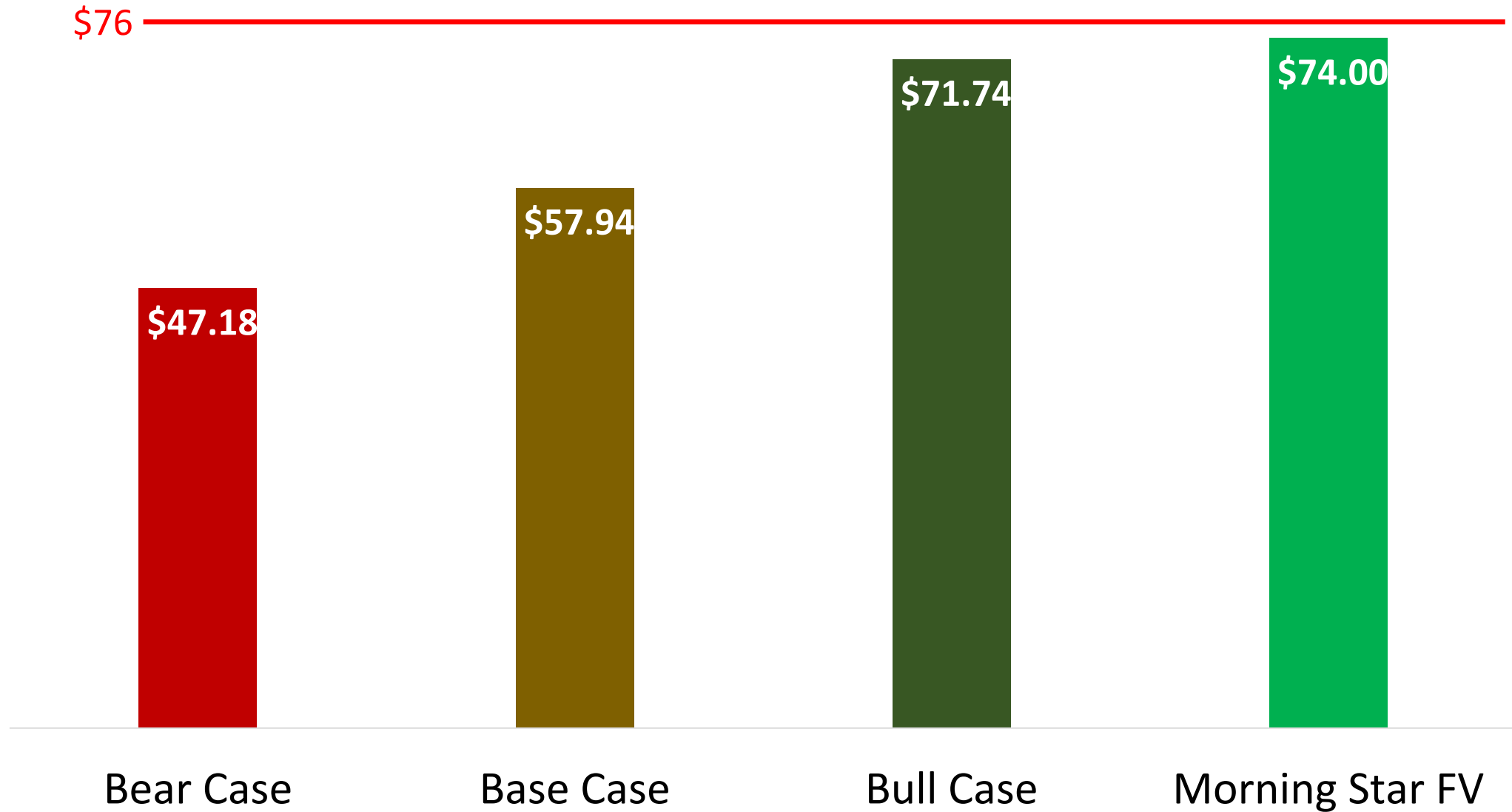
Bear Case	
Current Price	\$76.07
Fair Value	\$47.18
MOS	-61.23%
EPS	\$3.04
GR	7.0%
DR	9%
Years	10
Terminal	4%

Base Case	
Current Price	\$76.07
Fair Value	\$57.94
MOS	-31.29%
EPS	\$3.04
GR	10.0%
DR	9%
Years	10
Terminal	4%

Bull Case	
Current Price	\$76.07
Fair Value	\$71.14
MOS	-6.78%
EPS	\$3.04
GR	13.0%
DR	9%
Years	10
Terminal	4%



DCF Scenarios

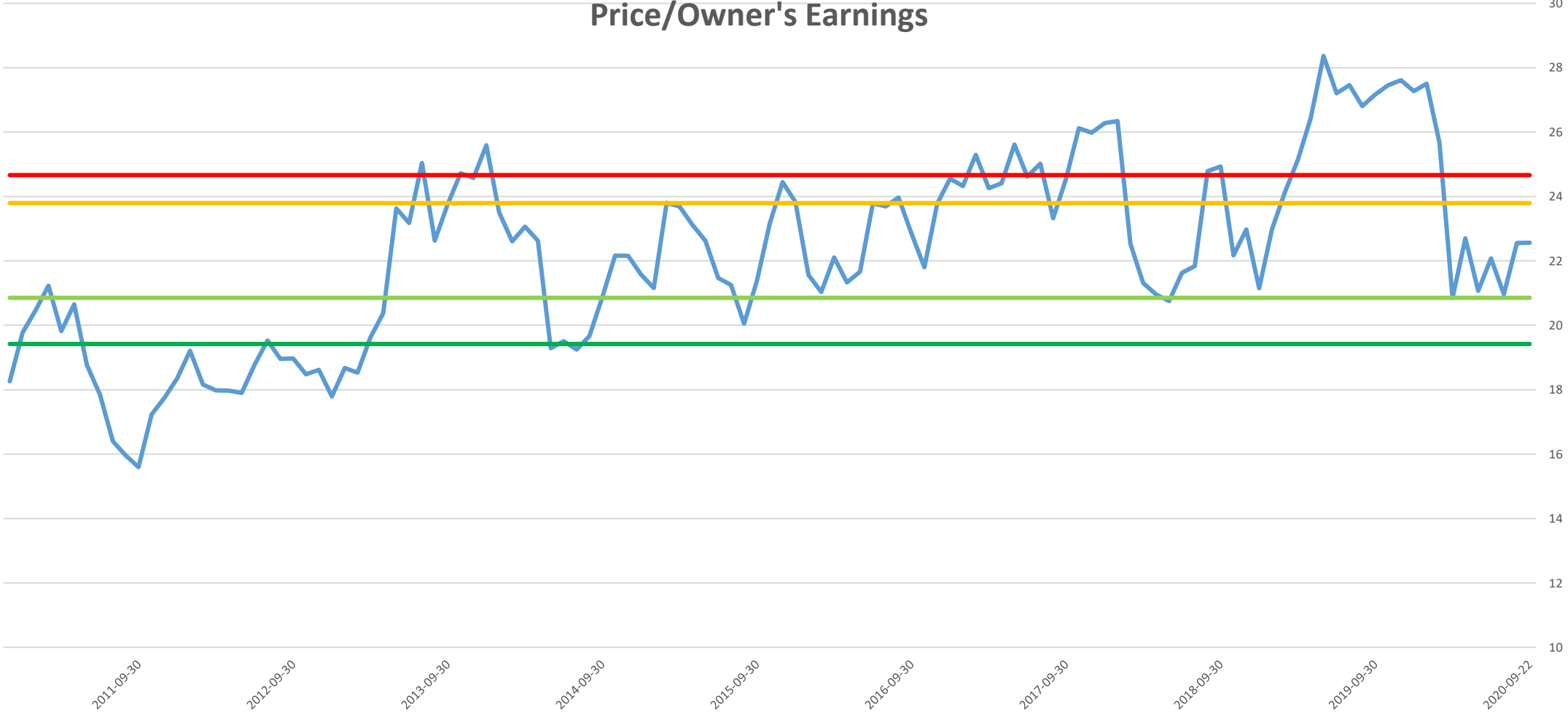


10-year Value Bands

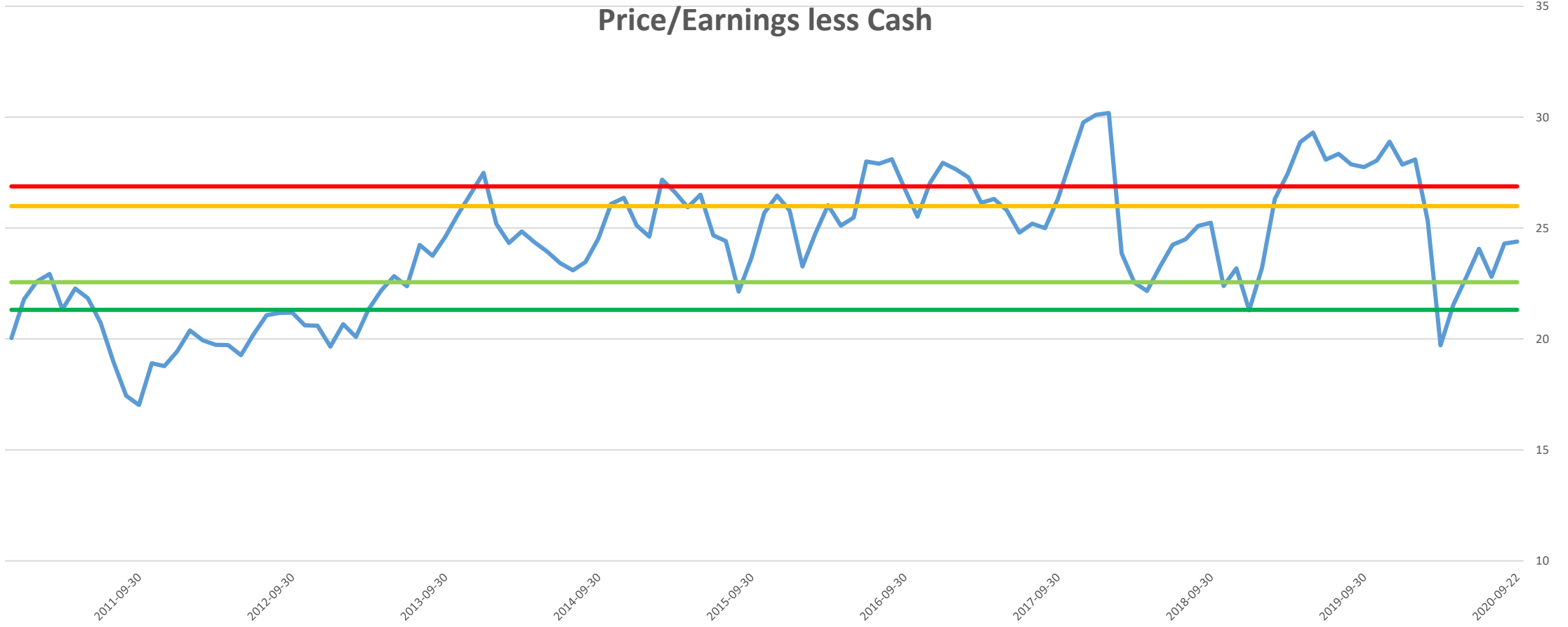
Price/Sales



Price/Owner's Earnings



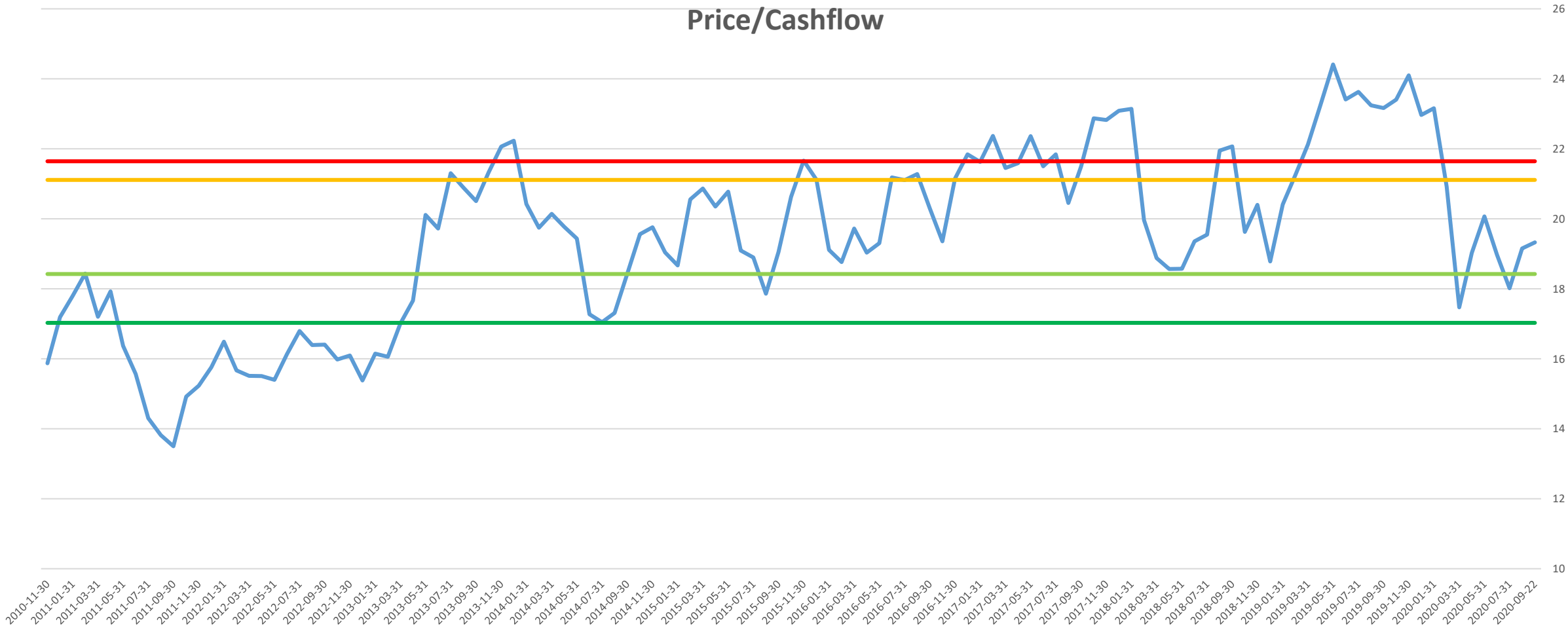
Price/Earnings less Cash



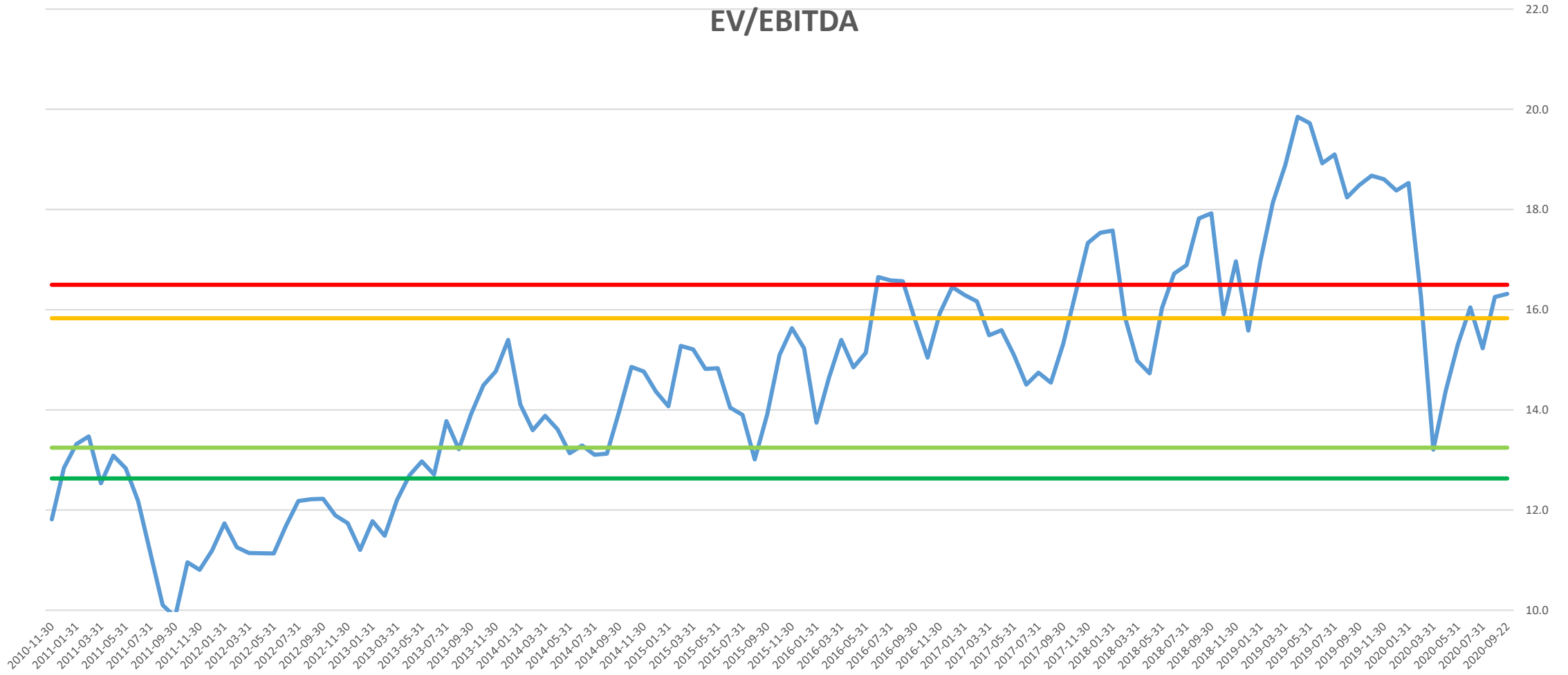
Price/Earnings



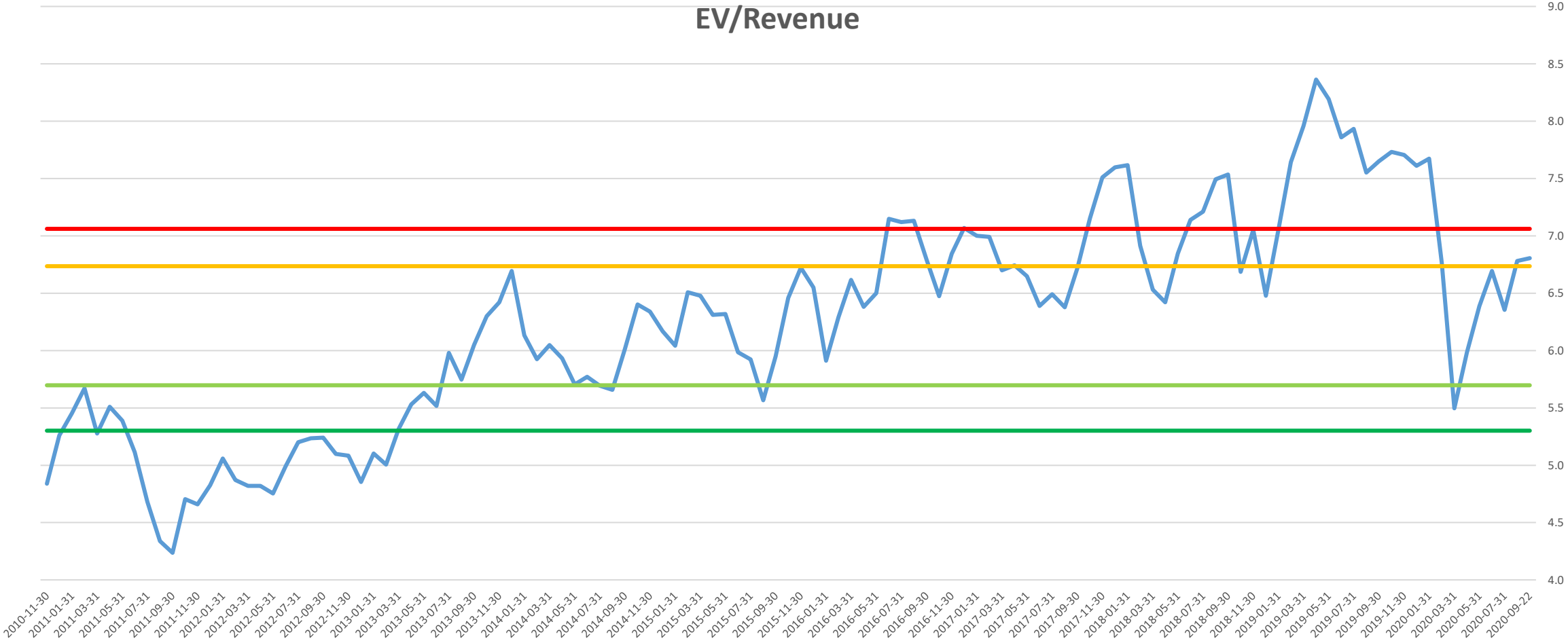
Price/Cashflow



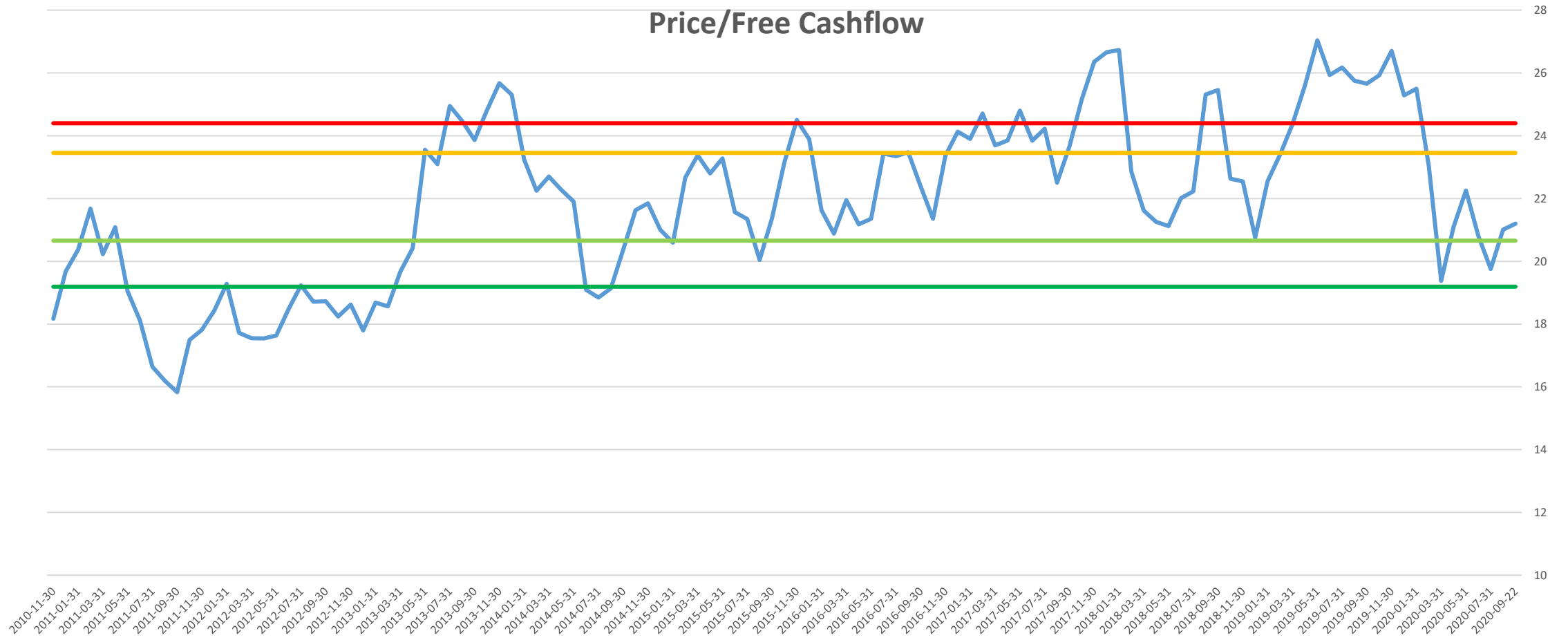
EV/EBITDA



EV/Revenue



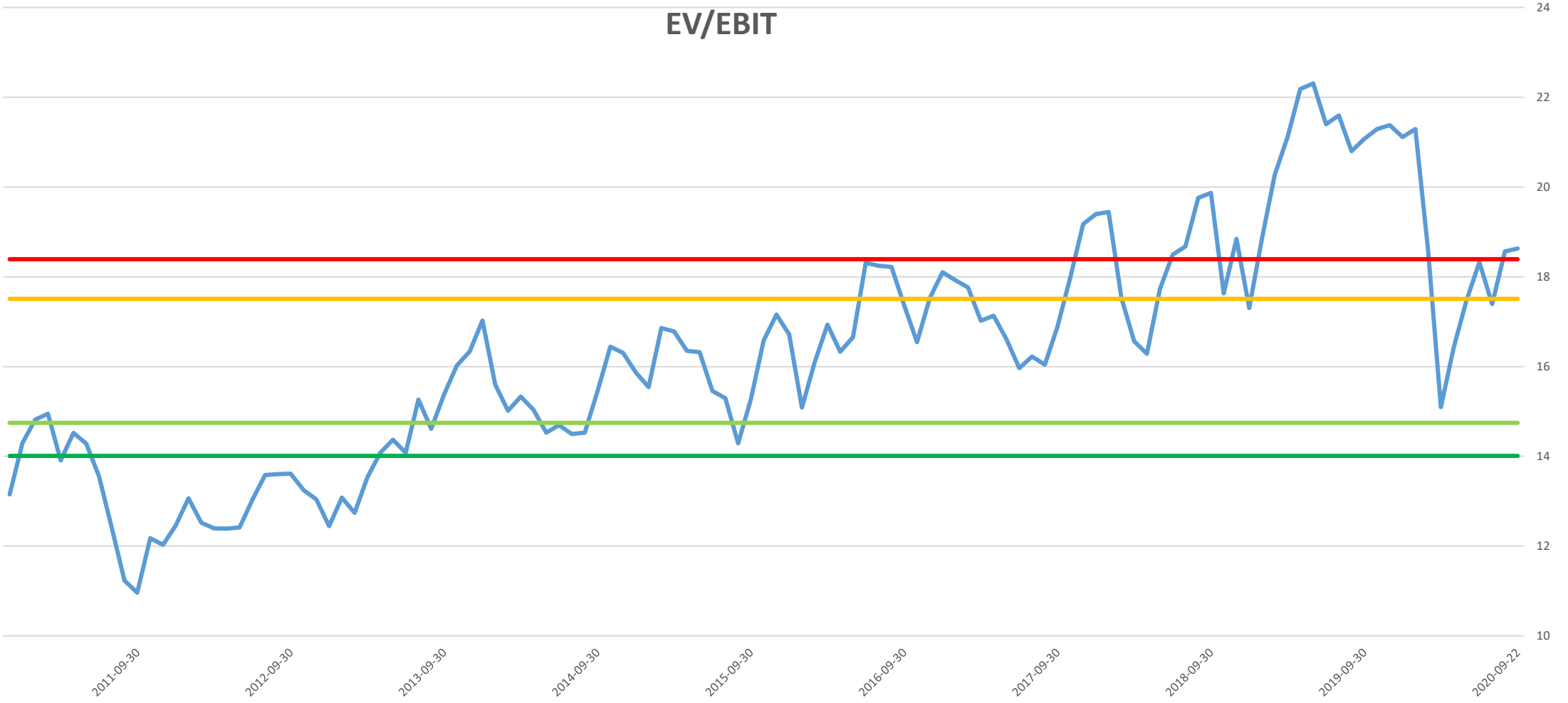
Price/Free Cashflow



Price/Book



EV/EBIT



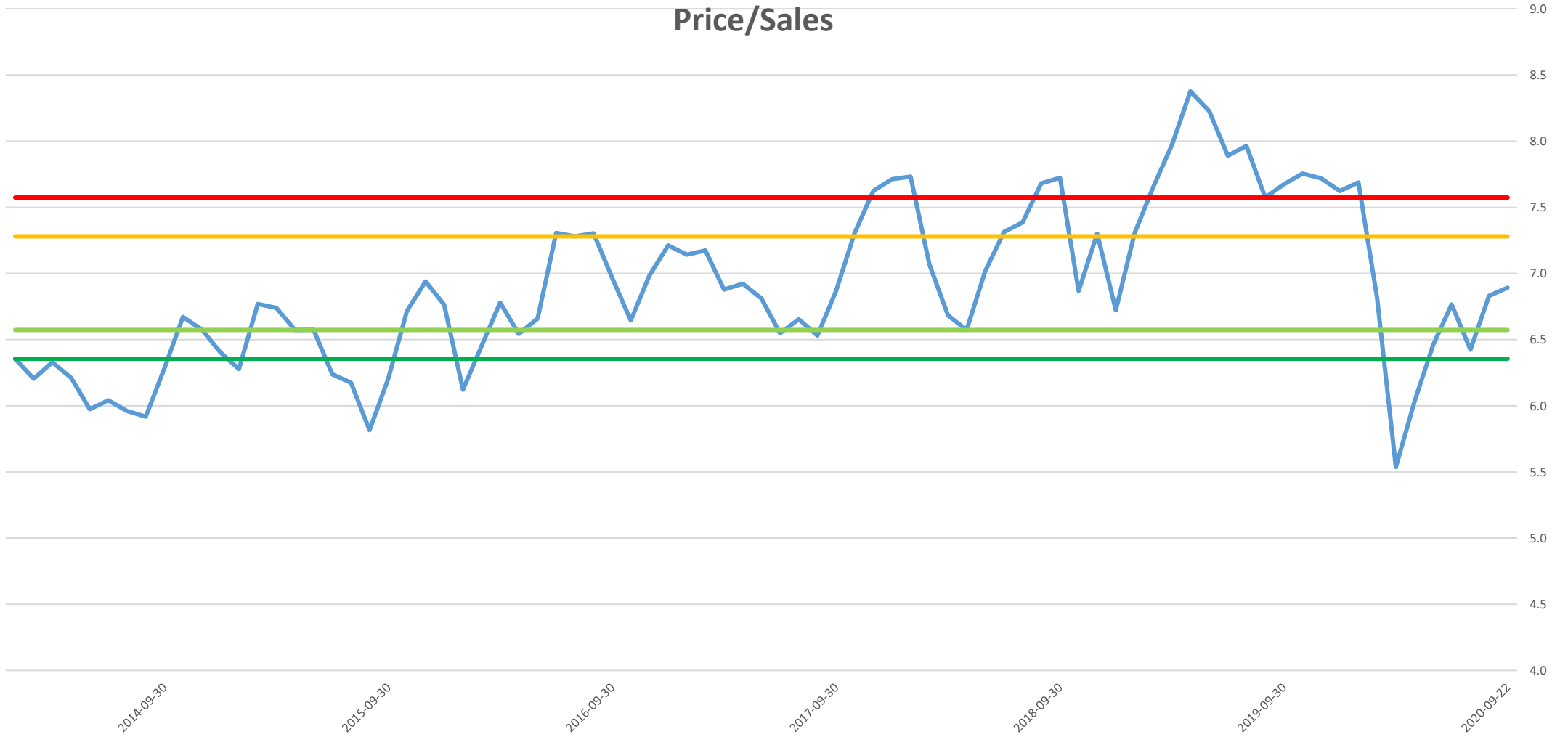
Based on Paychex's 10-year Historical Metrics

- Seems to be Fairly Valued
- However, over the last 10-years the company has changed substantially
- Business Shift

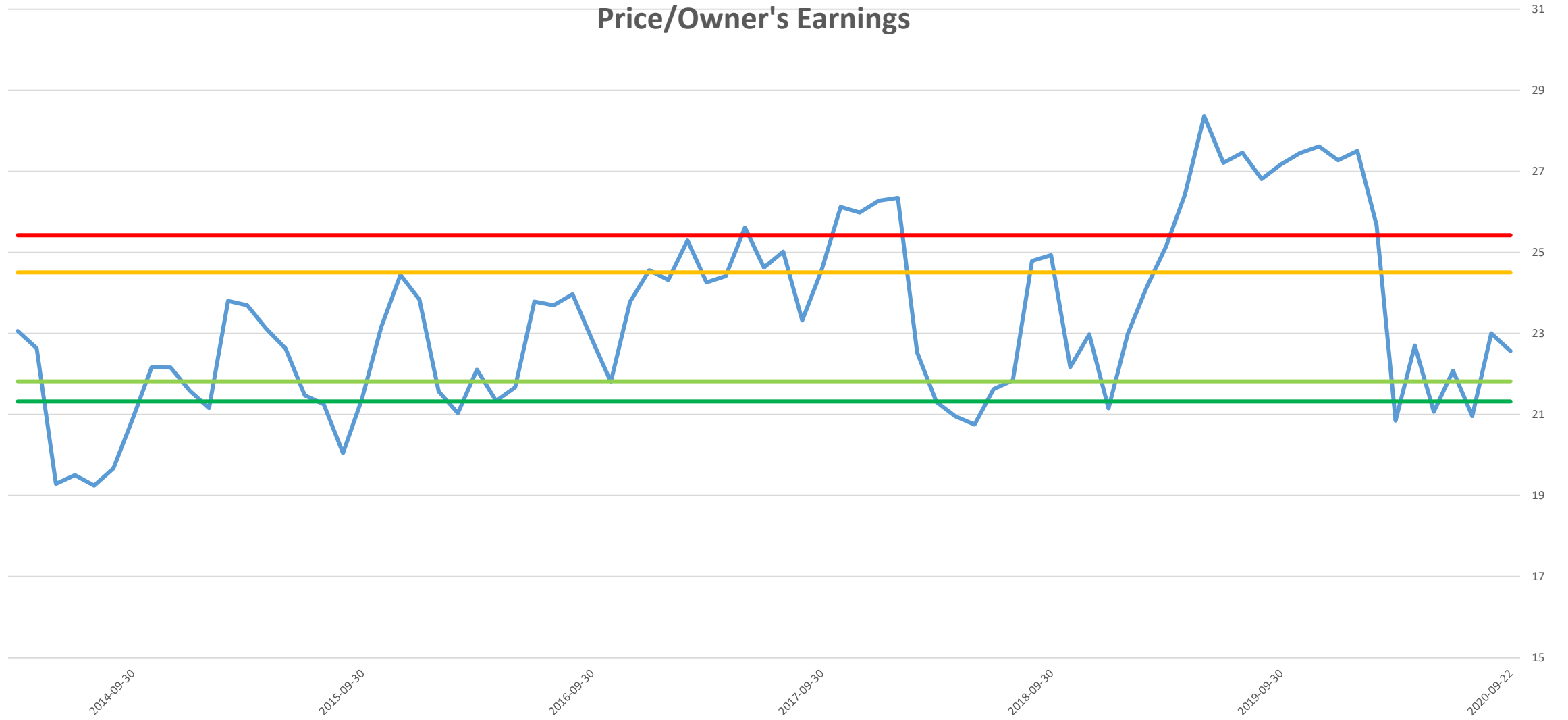
- Their Professional Employer Organization and Insurance segment accounts for 24% of revenues
- Growing at a faster rate
- And introduced their cloud-based solutions

5-year Value Bands

Price/Sales



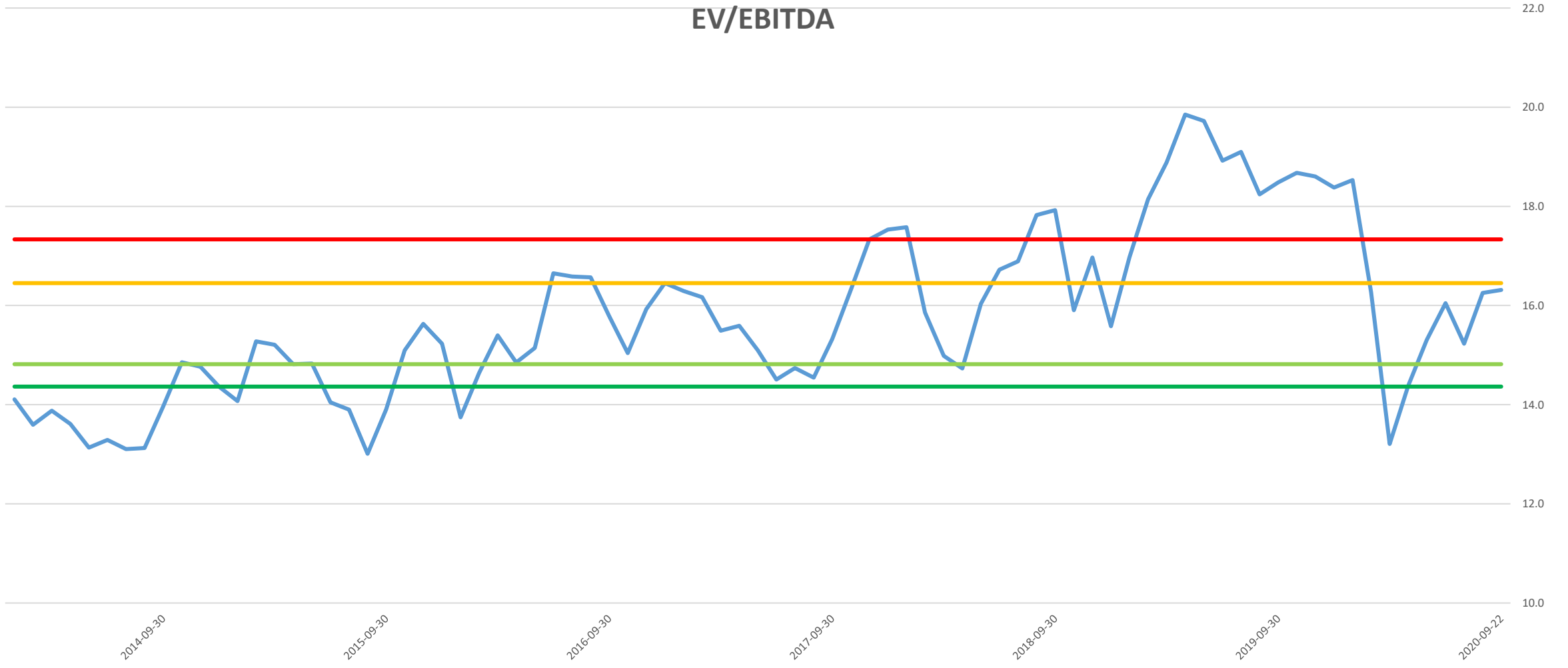
Price/Owner's Earnings



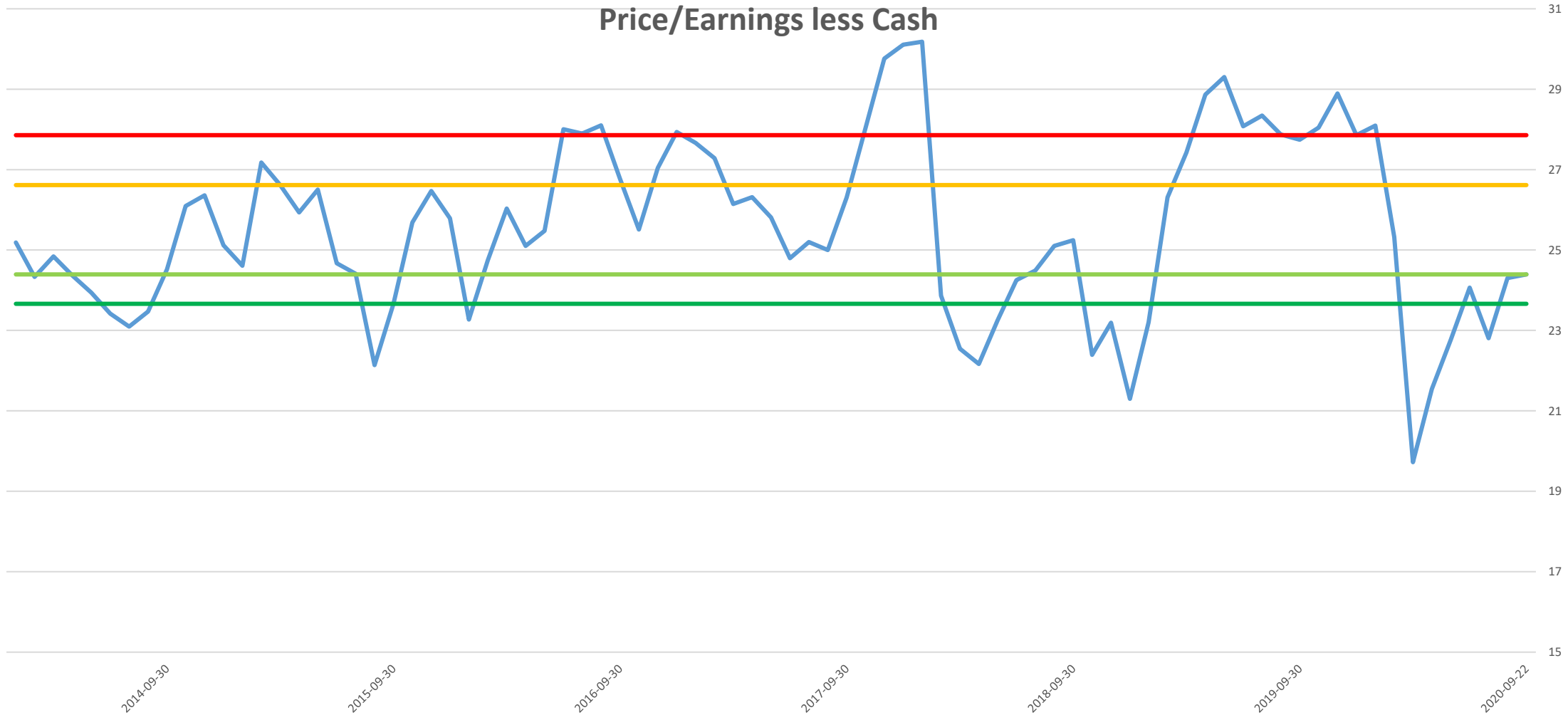
Price/Earnings



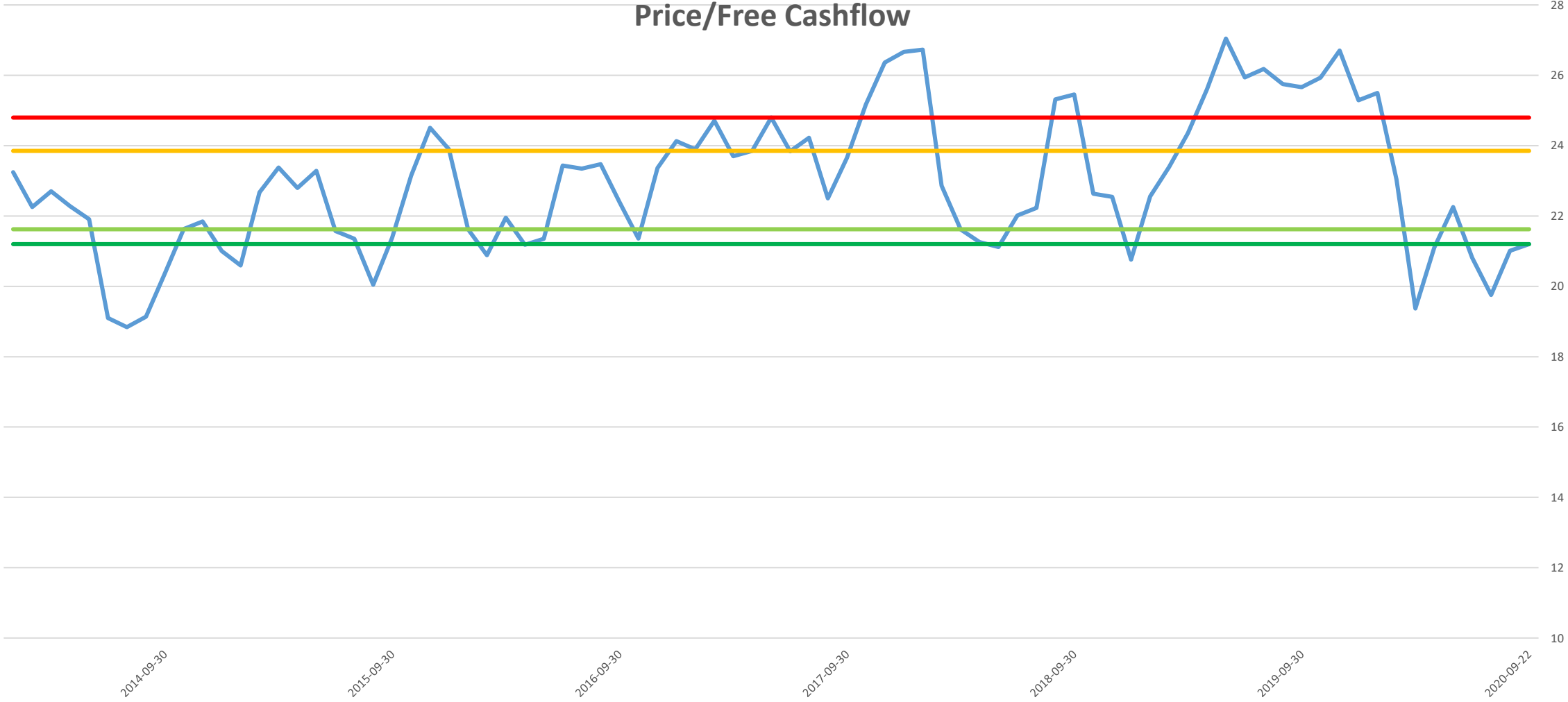
EV/EBITDA



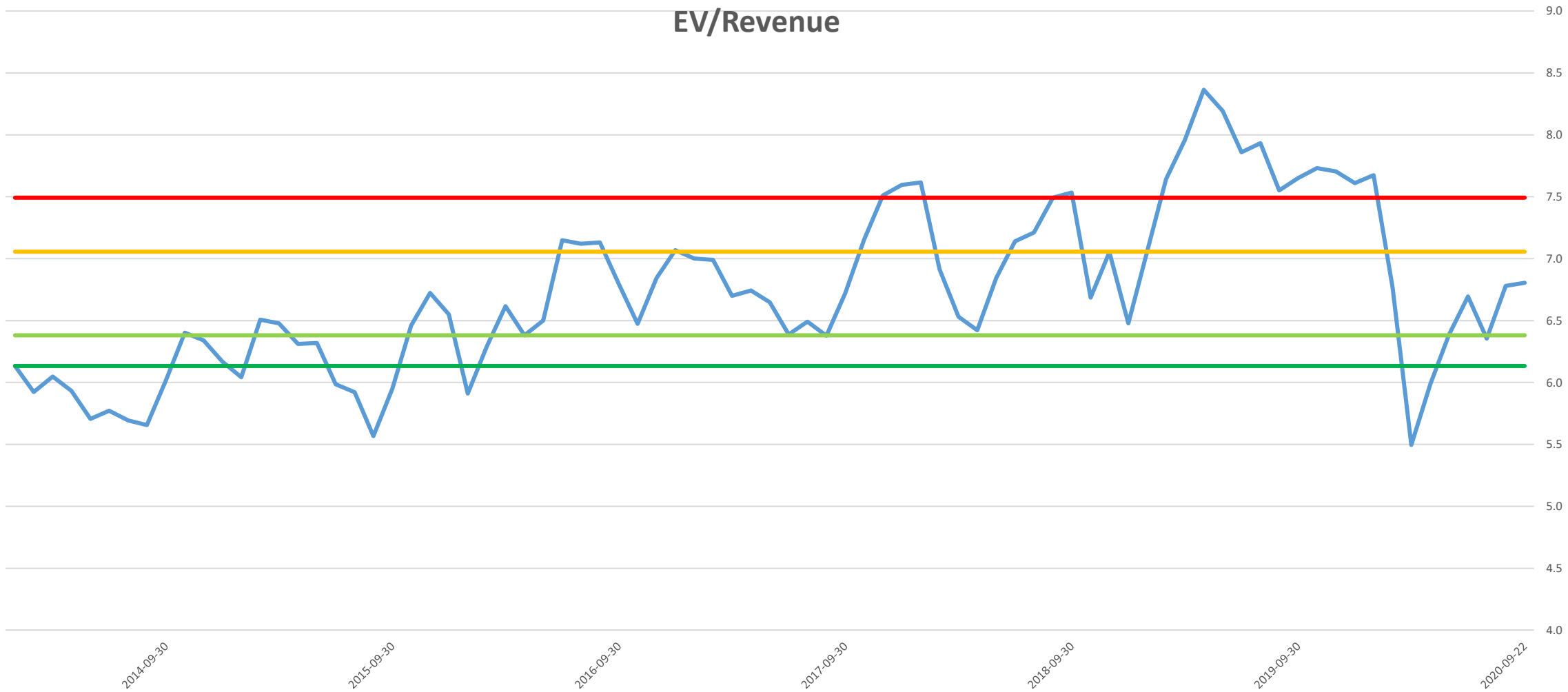
Price/Earnings less Cash



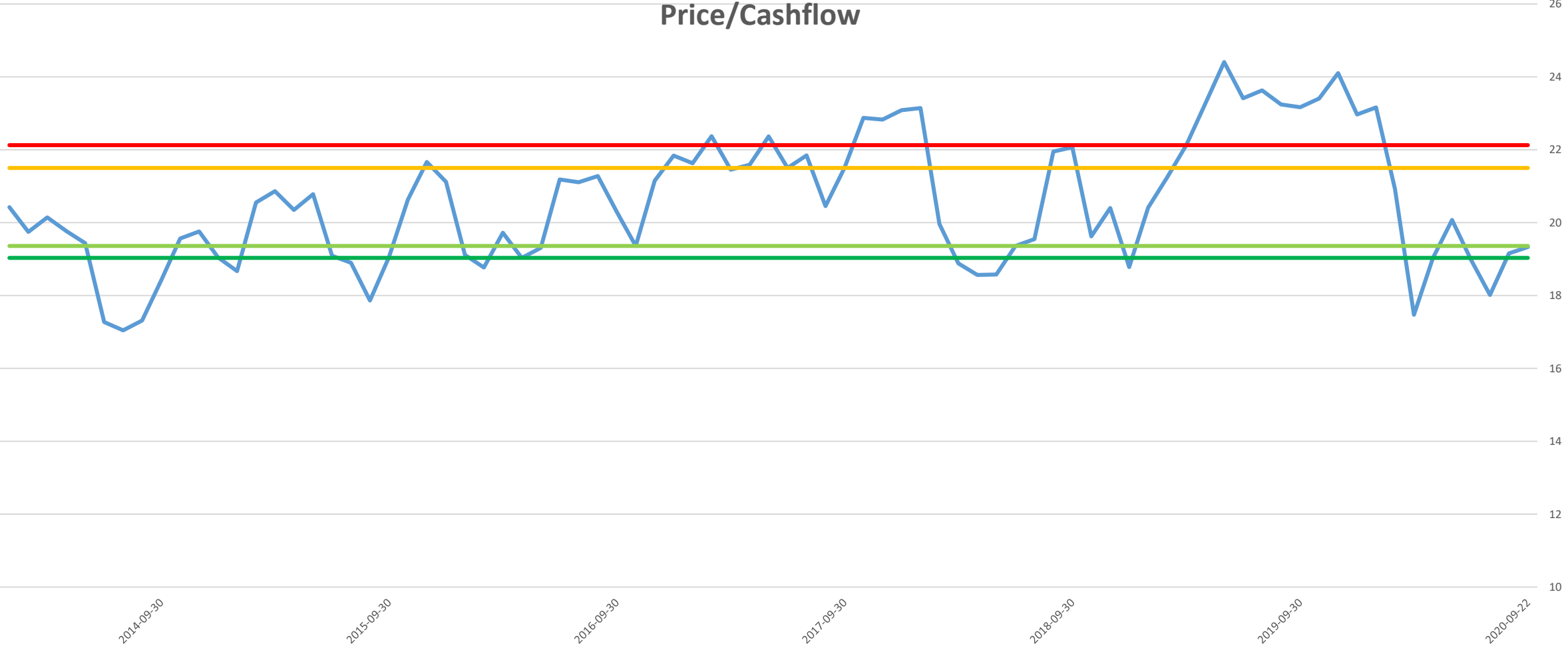
Price/Free Cashflow



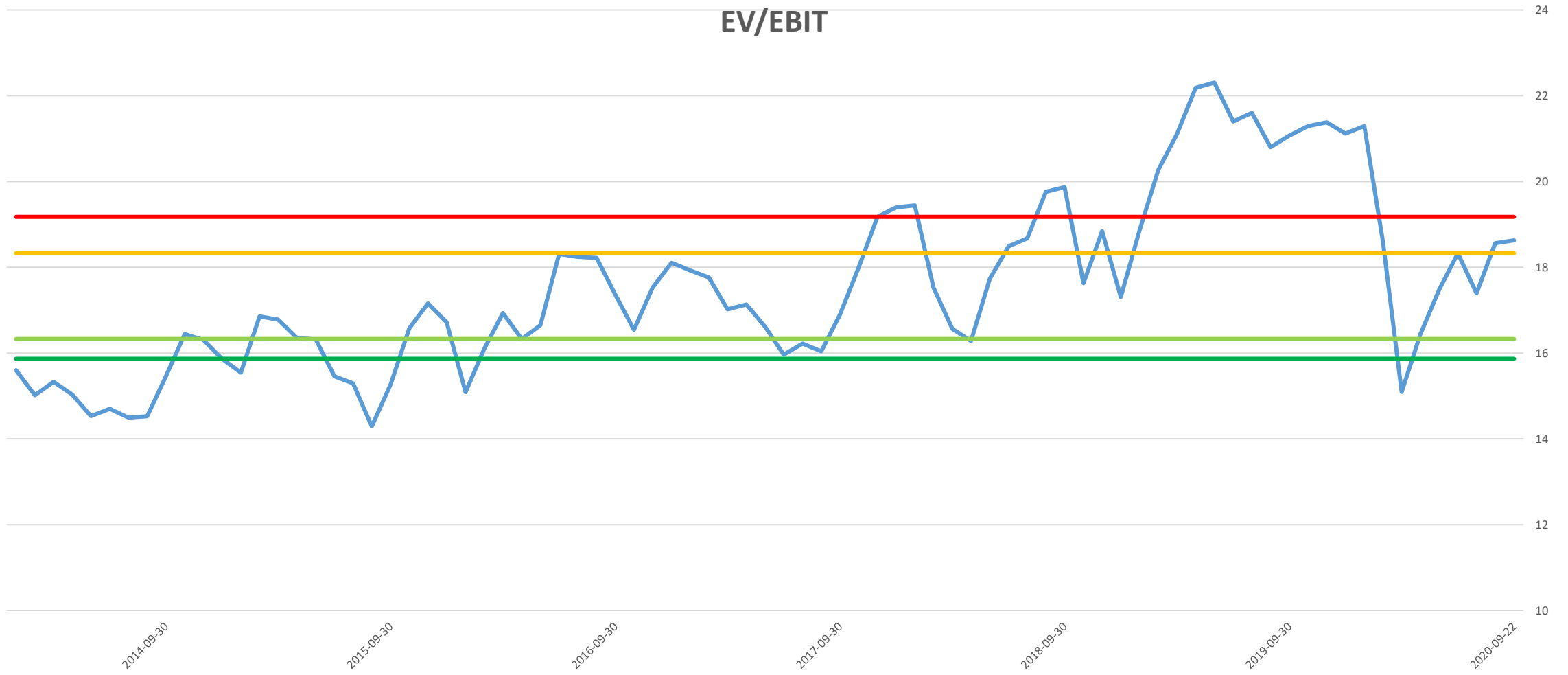
EV/Revenue



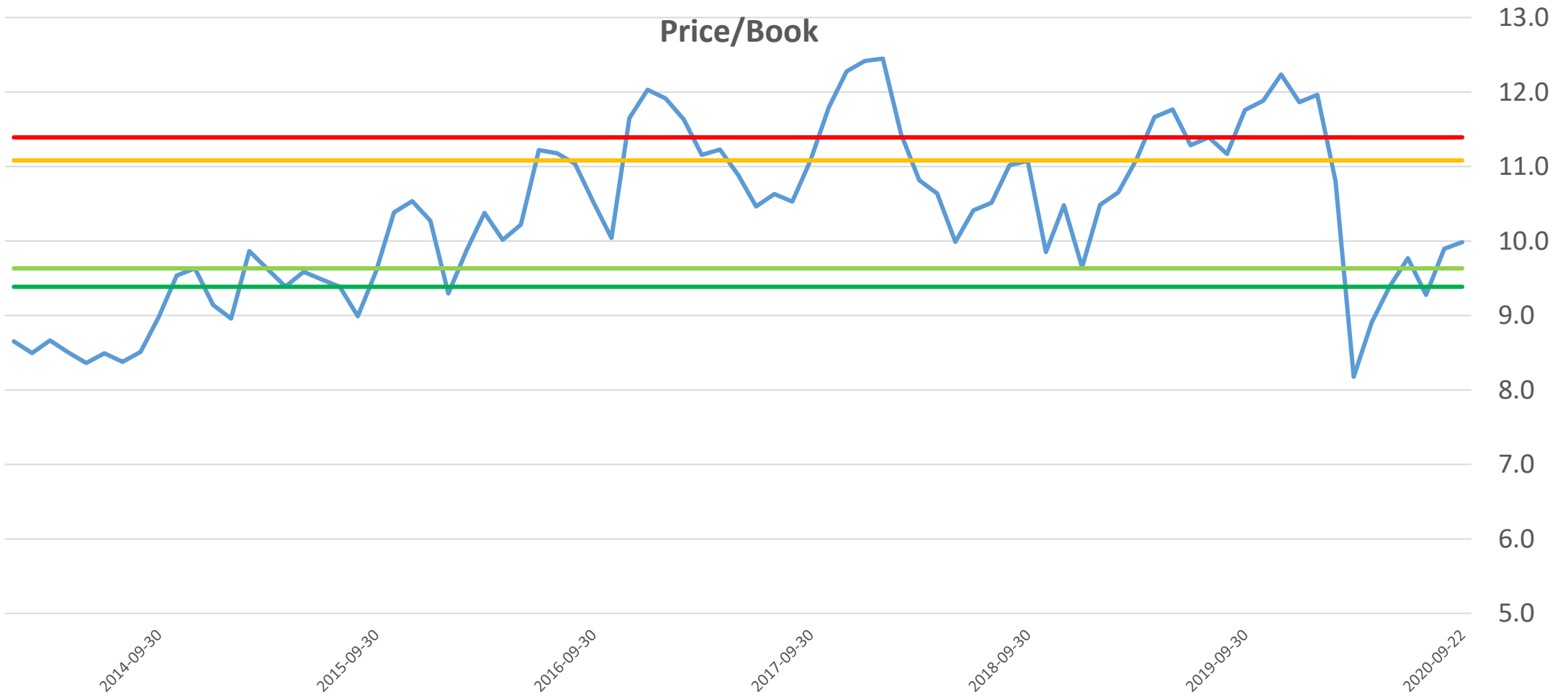
Price/Cashflow



EV/EBIT



Price/Book



Joseph's Magical DCF @ Target Stock Price \$70

5 year EPS projection							Discount rate:					Price to meet 5 year IRR of 15%
							P/E	Projected price	PV	5 year Upside	annual return	
Bear	Current	2021	2022	2023	2024	2025	20.0x	\$ 85.28	\$ 55.42	21.8%	4.0%	\$ 43
	3.04	3.2528	3.480496	3.724131	3.98482	4.2637573	25.0x	\$ 106.59	\$ 69.28	52.3%	8.8%	\$ 53
	5yr growth estimate	7%	7%	7%	7%	7%	30.0x	\$ 127.91	\$ 83.13	82.7%	12.8%	\$ 64
Base	Current	2021	2022	2023	2024	2025	20.0x	\$ 97.92	\$ 63.64	Upside 39.9%	6.9%	\$ 49
	\$3.04	3.344	3.6784	4.04624	4.450864	4.8959504	25.0x	\$ 122.40	\$ 79.55	74.9%	11.8%	\$ 61
	5yr growth estimate	10%	10%	10%	10%	10%	30.0x	\$ 146.88	\$ 95.46	109.8%	16.0%	\$ 73
Bull	Current	2021	2022	2023	2024	2025	20.0x	\$ 112.02	\$ 72.81	Upside 60.0%	9.9%	\$ 56
	3.04	3.4352	3.881776	4.386407	4.95664	5.6010029	25.0x	\$ 140.03	\$ 91.01	100.0%	14.9%	\$ 70
	5yr growth estimate	13%	13%	13%	13%	13%	30.0x	\$ 168.03	\$ 109.21	140.0%	19.1%	\$ 84

Conclusion

- Wide Moat Company
- Great business economics
- High quality financials
- Predictable and consistent
- Fairly valued



Recommendation

Weight 3% of portfolio

Option Contract at \$65 per share

Or

Limit Order \$70 per share

Appendix

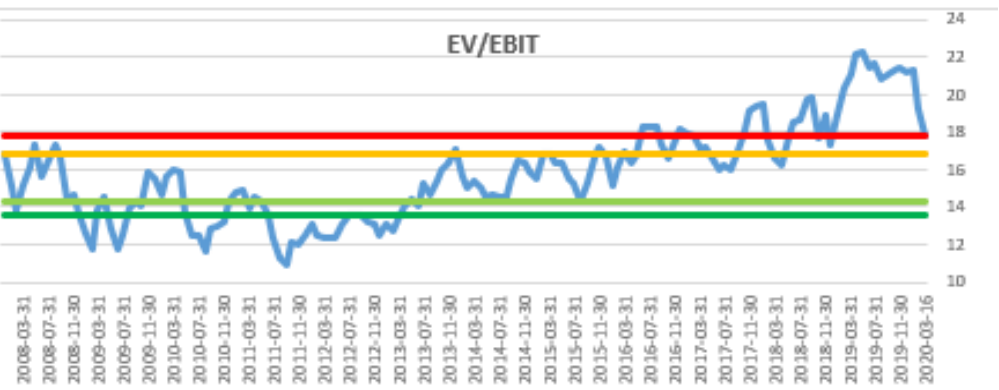
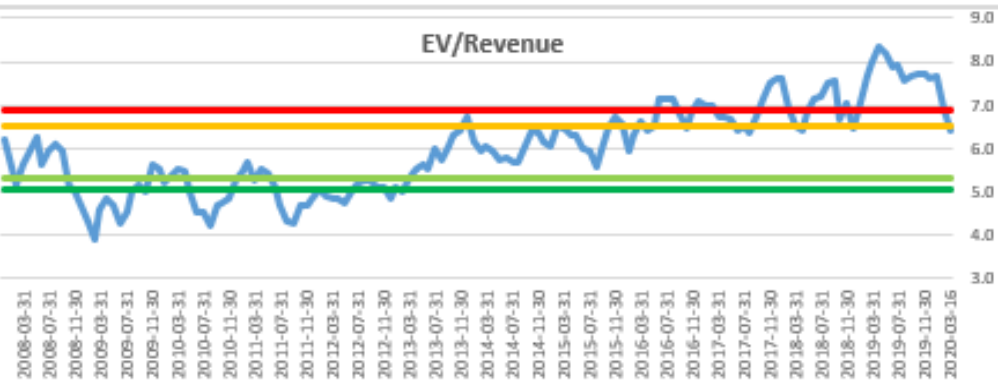
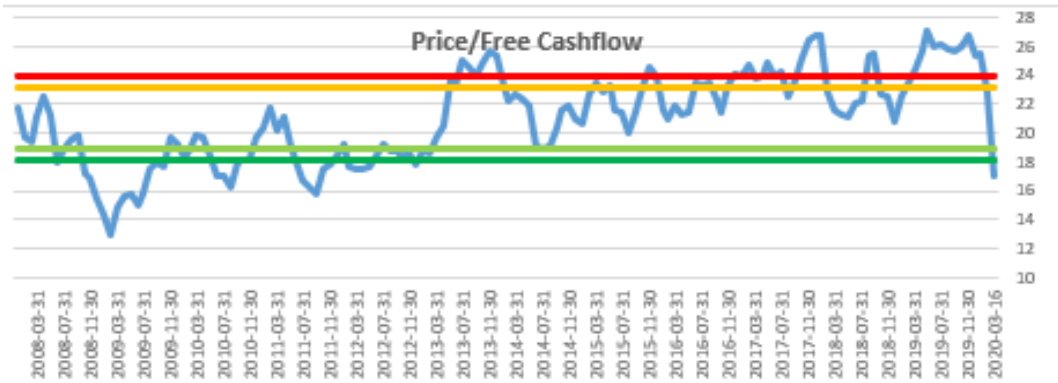
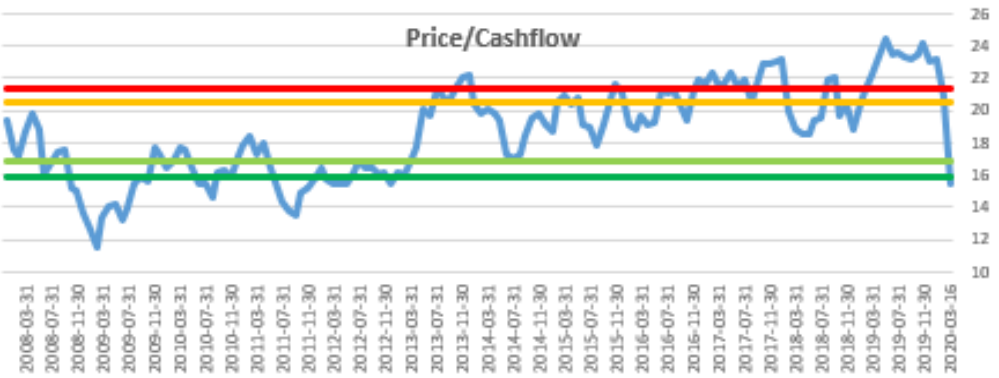


Back in March

Ticker:	PAYX	P/S	P/OE	P/E - \$	P/E	P/B	P/CFO	P/FCF	EV/Rev	EV/EBITDA	EV/EBIT
Name:	Paychex Inc	5.1	18.4	23.3	19.2	8.0	15.5	17.1	6.4	15.5	17.8
Price:	\$57.40	18%	21%	51%	9%	35%	14%	9%	65%	73%	81%
Full Value:	\$75	\$78	\$76	\$65	\$81	\$78	\$79	\$80	\$72	\$72	\$72
P/FV	76%	10Y PEG	5Y PEG	Est. PEG	Fwd. P/E	Shiller P/E	Industry P/E	Div Yield	Obligation	Share Count 5Y	10Y
Date:	3/16/2020	2.8	1.8	2.5	17.1	29.3		4.3%	0.8Y	-1%	-1%



Back in March



Back in May

Ticker:	PAYX		P/S	P/OE	P/E - \$	P/E	P/B	P/CFO	P/FCF	EV/Rev	EV/EBITDA	EV/EBIT
Name:	Paychex Inc		5.6	21.0	19.9	20.7	8.2	17.6	19.5	5.5	13.3	15.2
Price:	\$63.43		27%	39%	13%	12%	35%	31%	28%	33%	35%	40%
Full Value:	\$76		\$82	\$74	\$85	\$84	\$85	\$78	\$79	\$63	\$63	\$63
P/FV	84%		10Y PEG	5Y PEG	Est. PEG	Fwd. P/E	Shiller P/E	Industry P/E	Div Yield	Obligation	Share Count 5Y	10Y
Date:	5/17/2020		3.0	1.9	3.3	22.0	31.7		3.9%	0.8Y	-1%	-1%



Back in May

