

Paychex, Inc.

US CORE HOLDING*

Recommended since 21.11.23

21.11.2023



Country US	Market capitalization (bn) USD 43.3	Perf. since reco. (%)
Sector Industrial Goods & Services	Free float 89.3%	Paychex, Inc. 0.0
Factset PAYX-US	Closing price USD 118.77	Sector 0.0
ISIN US7043261079	ESG Risk score* 16.7 Low risk	

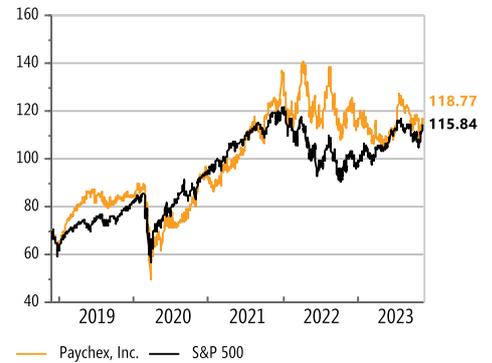
*From 2015, B&Cie separates its investment recommendations into Core Holdings (higher organic growth potential, high free cash flow, ROCE in excess of the cost of capital and balance sheet efficiency throughout the cycle) and Satellite Recommendations, which do not meet the above criteria but are likely to outperform in the short-to-medium term.

Profile

Paychex, Inc. provides small and medium-sized companies with integrated digital human capital management solutions: payroll, human resources, insurance, retirement, hiring, professional insurance, time and attendance management, employee benefits, etc. The company employs 16,600 people, was founded in 1971 and has been publicly traded since 1983. It is headquartered in Rochester, New York.

Market - competition - positions - barriers to entry

The US private sector has more than 130 million employees, for a human capital management market worth c.90 billion dollars, c.70 million of which are in companies with fewer than 1,000 employees. Paychex provides services to c.740,000 companies with 10 million employees, i.e. 14% of the total market. Its competitors are Automatic Data Processing, which covers all sizes of company, and smaller unlisted players (Gusto-Zen Payroll, OnPay), or listed companies such as Intuit (QuickBooks) and New Zealand's Xero



Source: Factset

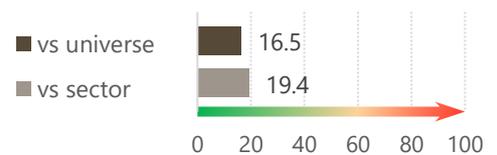
Investment case

- Paychex is one of the compounders, with average annual growth of 8% in revenues and 11% in earnings per share over the last 10 years. Underlying market growth is estimated at 5-7% p.a. The operating margin generated, which has grown slowly and steadily over the years, is notably high compared with the company's capital intensity, with investments focused on technology and digitisation, and enables a first-rate return on capital employed and free cash flow generation.
- Paychex's suite of integrated applications enables customers to automate and optimise their HR processes, beyond simple payroll services (56% of revenues), in an ever-changing regulatory environment. The introduction of AI several years ago has made it possible to automate customer interactions (chatbots) and to harness the vast amounts of employee data, in order to provide more services and advice to customers, whose loyalty is evidenced by a retention rate of c. 90%, which translates into high predictability of revenues.
- Overall, we expect continued strong growth in sales and earnings, and hence in dividends (payout ratio of 70-80%), over the next 10 years, with surplus cash flow being used for acquisitions as and when required.
- The stock has underperformed the US market over the past year, in the wake of rising interest rates and their expected impact on small and medium-sized businesses, Paychex's customers. We believe that this sequence is coming to an end, with a likely pause in rate rises by the Federal Reserve (the market is even starting to anticipate rate cuts in 2024), and that Paychex retains all its potential for development over the medium to long term. In the first quarter of the 2024 financial year, the Group, which remains in a positive net cash position, reported 7% growth in sales and 11% growth in adjusted EPS, and raised its full-year 2024 targets by the margin.
- This should lead to relative outperformance in the event of a market correction, assuming a US recession, and to a rise in the share price more in line with the market in the event of a soft landing for the US economy. We therefore recommend buying the stock on any

ESG - risks and key points

- Paychex has a low risk of financial impact from ESG factors, due to its low exposure to and solid management of these risks.
- The most significant risk relates to the security of the personal and sensitive data that Paychex receives, stores and processes, for which internal procedures are considered robust and regular assessments are carried out.

ESG risk vs. universe & sector (percentile)*



Source: Sustainalytics

Valuation** in USD

Current price	Value Bordier Scenario
119	123

Our scenario takes into account 10-year US interest rates at 3.5%, below-normal sales growth for 2024-25 (due to the expected slowdown in the US economy), then a return to the long-term trajectory, and an operating margin within the range targeted by management, consistent with historical performance.

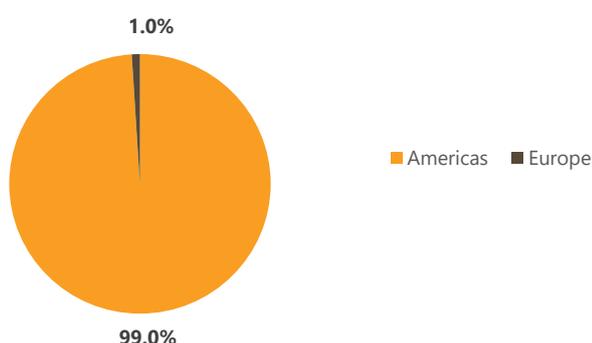
** The theoretical value reflects the company's business model, our baseline growth and profit scenario and market data, exogenous to the company (risk-free rate and equity risk premium). It does not in itself constitute a target price.

"Bordier Core Holding" indicators

In millions of USD	2022	2023	2024e	2025e	2026e
Sales revenue	4 612	5 021	5 347	5 668	6 065
Sales growth %	13.7%	8.9%	6.5%	6.0%	7.0%
a/w organic	13.7%	8.9%	6.5%	6.0%	7.0%
EBIT	1 840	2 033	2 219	2 369	2 547
% of sales	39.9%	40.6%	41.5%	41.8%	42.0%
Net income	1 368	1 548	1 700	1 813	1 946
Adjusted EPS	3.79	4.30	4.72	5.03	5.40
Adjusted EPS growth	23.8%	13.3%	9.8%	6.7%	7.4%
Capex/Sales	2.9%	2.5%	2.5%	2.5%	2.5%
Free cash-flow	1 373	1 573	1 501	1 656	1 743
FCF/Sales	29.8%	31.4%	28.1%	29.2%	28.7%
Dividend per share	2.77	3.26	3.64	3.88	4.17
Dividend yield	2.4%	2.8%	3.1%	3.3%	3.5%
ROCE - WACC	30.7%	28.4%	28.4%	27.6%	27.2%
ROE (%)	45.1%	44.6%	43.8%	42.2%	41.1%
Net debt/Ebitda	21.5%	-16.1%	-22.7%	-31.2%	-37.7%

Source: Factset, Bordier estimates

Sales breakdown - 05/2023



Governance and ownership structure

Since October 2022, John Gibson is Chairman and CEO.

Key shareholders (if any):

The company is majority owned by mutual funds and c. 11% by employees.

Any special characteristics of ownership (multiple voting rights, controlling holding company, shareholders' agreements)

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Ratios

	Paychex, Inc.	S&P 500 Sector	S&P 500 Market
PE (x)***			
2023	24.3	21.6	18.4
2024e	24.9	20.1	20.6
2025e	23.4	17.8	18.5
P/B (x)***			
2023	10.9	5.4	4.0
2024e	10.9	5.2	4.2
2025e	9.9	4.7	3.8
Beta (2Y, daily) vs market:			1.00

***) The valuation ratios set out are provided for information only. They do not constitute the criteria based upon which Core Holdings are selected, and may present significant premiums representing the quality of the company's business model.

Agenda

21.12.2023: Q2-2024 results

27.03.2024: Q3-2024 results

Glossary

ESG Risk Score

At B&Cie, we take particular care to ensure that the companies in which we recommend investing are sustainable. Accordingly, our selection process takes account of risks relating to environmental, social and governance (ESG) issues. This approach is underpinned by research from Sustainalytics, the global leader in ESG and corporate governance analysis, whose methodology aims to identify major controversies and risks and assess a company's ESG risks relative to both its sector and the investment universe as a whole. The corresponding score is expressed as a percentile: the lower the overall risk score, the lower the risk within the investment universe.

b-Digital, b-Transition & b-Well

Over and above the conventional geographical and sectoral approaches to asset management, at B&Cie we believe the world of tomorrow is being shaped by structural trends. We have identified three main megatrends: ongoing digital globalisation of the economy; economic transition, particularly in the energy sector; and the quest for wellness. We believe selecting and investing in companies that play an active role in these transformations should lead to more resilient portfolios that generate higher long-term returns. Our investment recommendations in the digital globalisation space are labelled "b-Digital", those in the economic transition space "b-Transition" and those in the wellness space "b-Well". A given recommendation may fall under more than one theme, in which case it will carry the relevant matching labels.

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