

Paycom

Good close to a tough year but 2024 adjusted EBITDA outlook light

Reiterate Rating: NEUTRAL | PO: 205.00 USD | Price: 199.03 USD

2024 revenue outlook for +11% y/y unsurprising

Paycom reported decent Q4 results to cap off the year, with revenue (\$434.6mn (+17% y/y)) and adjusted EBITDA (\$176.6mn; 40.6% adjusted EBITDA margin) both ahead of our \$422.9mn and \$172.2mn, respectively. Outperformance in the quarter was driven by new business wins, though somewhat offset by more limited cross-selling within the client base. While the Q4 results were ahead of our estimates, the in line C24E revenue outlook for \$1.873bn (+11% y/y), paired with a lower adjusted EBITDA guide for \$725mn (39.5% margin), is likely what drove shares down after market close.

Beti impact quantified; customer count grows +1% y/y

We appreciate the disclosure on the call today that approximately 5% of total 2023 revenue was coming from after-the-fact corrections. This should provide investors with additional visibility into the business model. That said, we think the deceleration in top line is also impacted by lower sales productivity per rep, stemming from 1) a structurally more difficult selling environment post-COVID (no stimulus), 2) tighter monetary policy prompting additional churn in Paycom's smaller customers and more limited expansion activity, and 3) an increasingly challenging competitive landscape with new entrants coming to market and a larger share of payroll vendors reaching basic feature parity.

Meaningful step up in investments for 2024

We view 2024 as a transition period for Paycom. The magnitude of the step up in investments this year suggests some serious changes are underway across both the sales & marketing and product development functions. The company also appointed Chris Thomas (prior COO) to co-CEO, allowing Chad Richison to work more closely on product development and strategy, which we view positively. The full year adjusted EBITDA margin is expected to compress to 38.7% in 2024 from 42.5% in 2023 and estimated total operating expense growth of +25% y/y is well ahead of the +11% y/y revenue guide for the year. We expect shares to be rangebound in the near term given the combination of sharp topline deceleration and margin compression.

Lower FCF estimate; reiterate Neutral

We reiterate our Neutral rating and lower our PO to \$205 (was \$210). We roll forward our valuation and the new \$205 PO is based on 30x C25E FCF (was 48x C24E) to reflect our lower FCF estimate.

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	6.14	7.75	6.82	7.94	9.10
GAAP EPS	4.84	5.90	5.45	6.83	7.93
EPS Change (YoY)	37.1%	26.2%	-12.0%	16.4%	14.6%
Consensus EPS (Bloomberg)			8.11	9.15	10.78
DPS	0	1.12	0	0	0
Valuation (Dec)					
P/E	32.4x	25.7x	29.2x	25.1x	21.9x
GAAP P/E	41.1x	33.7x	36.5x	29.1x	25.1x
Dividend Yield	0%	0.6%	0%	0%	0%
EV / EBITDA*	19.1x	15.4x	15.3x	13.2x	11.7x
Free Cash Flow Yield*	2.1%	2.6%	2.4%	3.4%	4.1%

* For full definitions of *IQmethod™* measures, see page 6.

07 February 2024

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	210.00	205.00
2024E Rev (m)	1,859.5	1,872.6
2025E Rev (m)	2,092.7	2,107.5
2026E Rev (m)	2,345.0	2,361.5
2024E EPS	8.27	6.82
2025E EPS	9.47	7.94
2026E EPS	10.81	9.10

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Stock Data

Price	199.03 USD
Price Objective	205.00 USD
Date Established	7-Feb-2024
Investment Opinion	C-2-7
52-Week Range	146.15 USD - 374.04 USD
Mkt Val (mn) / Shares Out (mn)	11,251 USD / 56.5
Free Float	84.1%
Average Daily Value (mn)	155.00 USD
BofA Ticker / Exchange	PAYC / NYS
Bloomberg / Reuters	PAYC US / PAYC.N
ROE (2024E)	25.3%
Net Dbt to Eqty (Dec-2023A)	-12.6%
ESGMeter™	Medium

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to "BofA ESGMeter Methodology".

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Refer to important disclosures on page 7 to 9. Analyst Certification on page 5. Price Objective Basis/Risk on page 5.

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Timestamp: 07 February 2024 11:35PM EST

iQprofileSM Paycom

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	25.0%	26.8%	19.4%	17.6%	16.0%
Return on Equity	34.4%	36.1%	25.3%	21.9%	19.3%
Operating Margin	34.4%	34.3%	26.7%	28.2%	28.9%
Free Cash Flow	232	292	265	381	460

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	1.0x	1.1x	1.2x	1.3x	1.3x
Asset Replacement Ratio	1.4x	1.7x	1.6x	1.3x	1.2x
Tax Rate	26.3%	25.6%	25.0%	26.0%	26.0%
Net Debt-to-Equity Ratio	-21.5%	-12.6%	-23.4%	-33.1%	-40.6%
Interest Cover	NM	NM	NM	NM	NM

Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	1,375	1,694	1,873	2,107	2,361
% Change	30.3%	23.2%	10.6%	12.5%	12.1%
Gross Profit	1,167	1,428	1,559	1,754	1,965
% Change	29.9%	22.3%	9.1%	12.5%	12.1%
EBITDA	580	719	725	840	950
% Change	38.3%	24.1%	0.8%	15.8%	13.2%
Net Interest & Other Income	11	21	21	21	21
Net Income (Adjusted)	357	448	390	455	521
% Change	37.2%	25.5%	-13.0%	16.5%	14.5%

Free Cash Flow Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	357	448	390	455	521
Depreciation & Amortization	93	114	126	142	159
Change in Working Capital	(101)	(106)	(128)	(134)	(132)
Deferred Taxation Charge	(3)	3	0	0	0
Other Adjustments, Net	19	26	82	106	111
Capital Expenditure	(133)	(193)	(204)	(188)	(199)
Free Cash Flow	232	292	265	381	460
% Change	17.0%	25.8%	-9.2%	43.6%	20.7%
Share / Issue Repurchase	(100)	(365)	0	0	0
Cost of Dividends Paid	0	(65)	0	0	0
Change in Debt	361	120	131	139	147

Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	401	294	559	940	1,400
Trade Receivables	23	16	18	21	23
Other Current Assets	2,341	2,503	2,653	2,815	2,985
Property, Plant & Equipment	402	498	594	690	785
Other Non-Current Assets	736	886	1,025	1,169	1,310
Total Assets	3,903	4,198	4,849	5,634	6,504
Short-Term Debt	20	23	25	27	29
Other Current Liabilities	2,357	2,512	2,665	2,830	3,005
Long-Term Debt	127	108	119	129	139
Other Non-Current Liabilities	216	252	265	281	298
Total Liabilities	2,720	2,895	3,073	3,268	3,470
Total Equity	1,183	1,303	1,776	2,366	3,034
Total Equity & Liabilities	3,903	4,198	4,849	5,634	6,504

* For full definitions of iQmethodSM measures, see page 6.

Company Sector

Server & Enterprise Software

Company Description

Paycom (NYSE: PAYC) is a provider of a comprehensive, cloud-based HCM solution delivered as SaaS. Paycom solutions requires no customization and are based on a core system of record maintained in a single database for all HCM functions, including payroll, talent acquisition, time and labor management, talent management and human resources management applications. Paycom was founded in 1998 and became a publicly traded company through its initial public offering in 2014.

Investment Rationale

Paycom is a pioneer in payroll and human resources cloud software primarily to US-based companies. The company has consolidated decent market share (we estimate 10%) in what historically has been a fragmented market of application providers, regional providers, and in-house (DIY) payroll solutions. We think Paycom is well positioned to continue gaining share of the \$35.2bn global TAM, though we are Neutral as the company undergoes changes impacting both the top and bottom line trajectories.

Stock Data

Average Daily Volume 778,775

Quarterly Earnings Estimates

	2023	2024
Q1	2.46A	2.23E
Q2	1.62A	1.45E
Q3	1.75A	1.43E
Q4	1.93A	1.71E

Earnings results & estimate changes

Exhibit 1: BofA estimate versus reported resorts

Revenue landed 3% above our estimates

\$ in thousands (except per share data)	BofA Estimates	4Q23A Actuals	Variance
Income Statement			
Total Revenue	422,889	434,595	2.8%
Cost of revenue	68,089	72,682	6.7%
Gross Profit	354,800	361,913	2.0%
Operating expenses			
Sales and marketing	106,963	100,943	(5.6%)
Research and development	48,130	50,541	5.0%
General and administrative	56,982	53,586	(6.0%)
Income (Loss) from Operations	127,450	140,146	10.0%
Other Income (Expenses), net	5,362	5,455	1.7%
Pretax income (loss)	132,590	145,335	9.6%
Income tax provision	37,125	35,139	(5.3%)
Net income (pro forma)	95,465	110,196	15.4%
EPS (pro forma)	\$1.65	\$1.93	16.9%
Net Income (GAAP)	78,595	81,757	4.0%
EPS (GAAP)	\$1.36	\$1.43	5.4%
Y/Y Growth			
Total Revenues	14.1%	17.3%	22.4%
Operating profit (loss)	(1.9%)	7.9%	(514.6%)
Non-GAAP net income	(4.7%)	10.0%	(313.7%)
Margins			
Gross Margin	83.9%	83.3%	(0.7%)
Operating expenses % of revenue			
Sales and Marketing	25.3%	23.2%	(8.2%)
Research and Development	11.4%	11.6%	2.2%
General and Administrative	13.5%	12.3%	(8.5%)
Operating Margin	30.1%	32.2%	7.0%
Net Income Margin	22.6%	25.4%	12.3%
Balance Sheet & Cash Flow			
Cash and cash equivalents	565,813	294,025	(48.0%)
Billings (calculated)	426,975	436,746	2.3%
Net cash provided by operating activities	130,452	134,468	3.1%
FCF	84,082	77,590	(7.7%)

Source: BofA Global Research estimates, company report

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Exhibit 2: BofA estimate change summary

We lower our revenue estimates meaningfully to reflect the revised revenue outlook

	1Q24E				FY2024E				FY2025E			
	Previous Estimate	Previous Y/Y Growth	New Estimate	New Y/Y Growth	Previous Estimate	Previous Y/Y Growth	New Estimate	New Y/Y Growth	Previous Estimate	Previous Y/Y Growth	New Estimate	New Y/Y Growth
Total revenue	492,717	9.1%	495,672	9.7%	1,859,472	10.6%	1,872,636	10.6%	2,092,694	12.5%	2,107,496	12.5%
Operating margin	40.4%	...	33.2%	...	33.7%	...	26.7%	...	34.5%	...	28.2%	...
Net income	151,172	6.0%	127,470	-10.6%	479,430	10.6%	390,146	-13.0%	549,120	14.5%	454,539	16.5%
EPS	\$2.61	6.0%	\$2.23	-9.5%	\$8.27	10.6%	\$6.82	-12.1%	\$9.47	14.5%	\$7.94	16.5%
FCF	131,432	24.6%	114,061	8.1%	348,880	16.7%	265,484	-9.2%	412,882	18.3%	381,134	43.6%

Source: BofA Global Research estimates, company report

BofA GLOBAL RESEARCH

Price objective basis & risk

Paycom (PAYC)

Our \$205 PO is based on 30x EV/C25E FCF. The 30x EV/C25E FCF multiple is a premium discount to payroll and HR peers which include Workday and Paylocity at 31x EV/C25E FCF to account for recent execution issues and uncertainty surrounding what a sustainable long term growth trajectory looks like.

Downside risks to our PO are: 1) multiple compression in the event of disappointing quarterly results, 2) meaningful SMB exposure, which is a market segment more prone to churn given it has a higher rate of business closures and/or failures, and 3) interest rate sensitivity.

Analyst Certification

I, Adam Bergere, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

US - Enterprise Software Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	8x8	EGHT	EGHT US	Michael J. Funk
	Adobe	ADBE	ADBE US	Brad Sills
	Alarm.com	ALRM	ALRM US	Michael J. Funk
	Amplitude, Inc.	AMPL	AMPL US	Koji Ikeda, CFA
	BILL	BILL	BILL US	Brad Sills
	CCC Intelligent Solutions	CCCS	CCCS US	Michael J. Funk
	Dropbox	DBX	DBX US	Michael J. Funk
	Dynatrace	DT	DT US	Koji Ikeda, CFA
	Elastic NV	ESTC	ESTC US	Koji Ikeda, CFA
	GitLab Inc.	GTLB	GTLB US	Koji Ikeda, CFA
	Global-e Online Ltd.	GLBE	GLBE US	Koji Ikeda, CFA
	HubSpot	HUBS	HUBS US	Brad Sills
	Informatica Inc.	INFA	INFA US	Koji Ikeda, CFA
	Intapp Inc.	INTA	INTA US	Koji Ikeda, CFA
	Intuit	INTU	INTU US	Brad Sills
	JFrog Ltd	FROG	FROG US	Koji Ikeda, CFA
	MeridianLink, Inc.	MLNK	MLNK US	Koji Ikeda, CFA
	Microsoft Corporation	MSFT	MSFT US	Brad Sills
	MongoDB Inc	MDB	MDB US	Brad Sills
	nCino, Inc.	NCNO	NCNO US	Adam Bergere
	NICE Ltd.	NICE	NICE US	Michael J. Funk
	NICE Ltd.	NCSYF	NICE IT	Michael J. Funk
	PagerDuty	PD	PD US	Koji Ikeda, CFA
	PowerSchool Holdings, Inc.	PWSC	PWSC US	Koji Ikeda, CFA
	RingCentral	RNG	RNG US	Michael J. Funk
	Salesforce.com	CRM	CRM US	Brad Sills
	ServiceNow	NOW	NOW US	Brad Sills
	UiPath	PATH	PATH US	Brad Sills
	Unity	U	U US	Michael J. Funk
	Weave	WEAV	WEAV US	Michael J. Funk
	Workday Inc.	WDAY	WDAY US	Brad Sills
	Zeta Global	ZETA	ZETA US	Koji Ikeda, CFA
	ZoomInfo	ZI	ZI US	Koji Ikeda, CFA
NEUTRAL				
	Autodesk	ADSK	ADSK US	Michael J. Funk
	Bentley Systems	BSY	BSY US	Michael J. Funk
	BigCommerce Holdings, Inc.	BIGC	BIGC US	Koji Ikeda, CFA
	Coveo	YCVO	CVO CN	Koji Ikeda, CFA



US - Enterprise Software Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Datadog Inc	DDOG	DDOG US	Koji Ikeda, CFA
	DocuSign	DOCU	DOCU US	Brad Sills
	Freshworks, Inc.	FRSH	FRSH US	Adam Bergere
	HashiCorp	HCP	HCP US	Brad Sills
	Jamf	JAMF	JAMF US	Koji Ikeda, CFA
	Lightspeed Commerce Inc.	LSPD	LSPD US	Koji Ikeda, CFA
	Lightspeed Commerce Inc.	YLSPD	LSPD CN	Koji Ikeda, CFA
	Oracle Corporation	ORCL	ORCL US	Brad Sills
	Paycom	PAYC	PAYC US	Adam Bergere
	Paylocity	PCTY	PCTY US	Adam Bergere
	Shopify, Inc.	SHOP	SHOP US	Brad Sills
	Snowflake	SNOW	SNOW US	Brad Sills
	Veeva Systems, Inc.	VEEV	VEEV US	Brad Sills
	Zoom Video Communications	ZM	ZM US	Michael J. Funk

UNDERPERFORM

	AvidXchange, Inc.	AVDX	AVDX US	Brad Sills
	Blackbaud, Inc.	BLKB	BLKB US	Koji Ikeda, CFA
	BlackLine, Inc.	BL	BL US	Koji Ikeda, CFA
	C3.ai	AI	AI US	Brad Sills
	Confluent	CFLT	CFLT US	Brad Sills
	CS Disco, Inc.	LAW	LAW US	Koji Ikeda, CFA
	Enfusion, Inc.	ENFN	ENFN US	Koji Ikeda, CFA
	Five9	FIVN	FIVN US	Michael J. Funk
	Guidewire Software, Inc.	GWRE	GWRE US	Michael J. Funk
	Twilio	TWLO	TWLO US	Michael J. Funk
	Vertex, Inc.	VERX	VERX US	Brad Sills

RSTR

	Splunk	SPLK	SPLK US	Brad Sills
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iQmethodSM Measures Definitions

Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

iQmethodSM is the set of BofA Global Research standard measures that serve to maintain global consistency under three broad headings: Business Performance, Quality of Earnings, and valuations. The key features of iQmethod are: A consistently structured, detailed, and transparent methodology. Guidelines to maximize the effectiveness of the comparative valuation process, and to identify some common pitfalls.

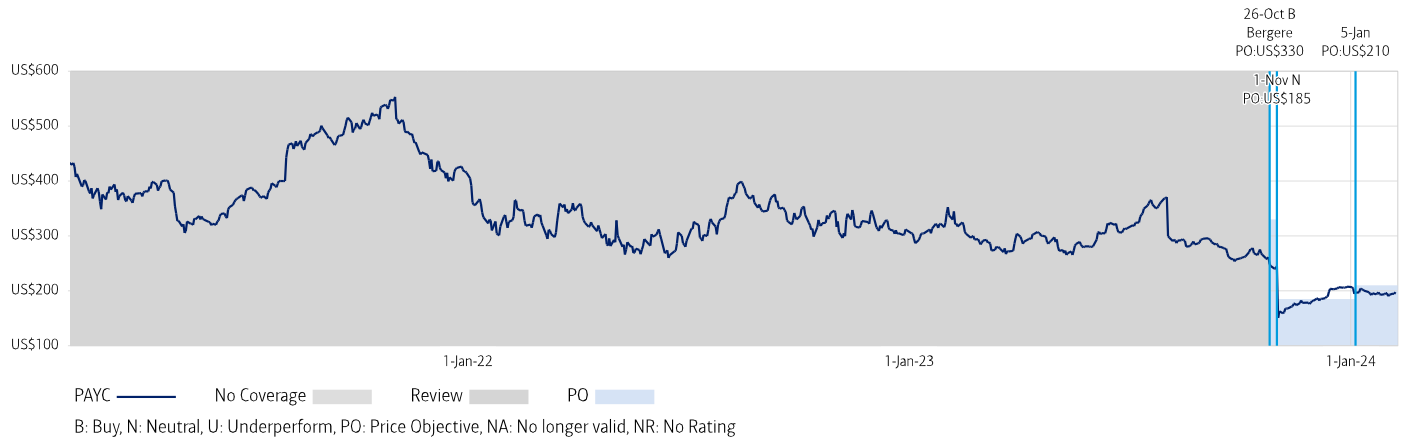
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Disclosures

Important Disclosures

Paycom (PAYC) Price Chart



The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

Equity Investment Rating Distribution: Technology Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	215	53.09%	Buy	111	51.63%
Hold	97	23.95%	Hold	45	46.39%
Sell	93	22.96%	Sell	24	25.81%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

^{R1} Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster ^{R2}
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

^{R2} Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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