

Paylocity

Slower client employee growth & sales productivity ramp prompts lower rev guide

Reiterate Rating: NEUTRAL | PO: 175.00 USD | Price: 171.91 USD

Beats on total revenue but driven by interest income

We reiterate our Neutral rating and lower our PO to \$175 to reflect the slower top line growth trajectory of the business and increasing macro headwinds. Total revenue of \$326.4mn (+20% y/y) in the quarter landed ahead of our \$324.3mn, however, this was primarily driven by higher interest income (+\$1.8mn to our estimate). Recurring revenue of \$298.4mn (+16% y/y) was just shy of our \$298.7mn, prompted roughly equally by further moderation in client employee growth again in Q2 and lower than expected sales productivity.

Cuts FY24 top line guide to +18% y/y (from +20% y/y)

H2 assumptions for revenue acceleration proved to be too aggressive, as we cautioned in [our prior note](#), prompting a guide down for revenue for the full year. The earnings print today backs our recent view that the payroll software industry is undergoing somewhat of a reset, stemming from 1) a structurally more difficult selling environment as post-COVID stimulus funds run dry, 2) tighter monetary policy prompting incremental churn/moderated expansions, 3) a tighter labor market, and 4) an increasingly challenging competitive landscape with new entrants coming to market and a larger share of payroll vendors reaching basic feature parity.

FY25 top line likely to fall below the 20% LT outlook

The Q3 and full year guide implies a Q4 exit growth rate of +12-13% y/y. As a result, we lower our FY25E recurring revenue growth estimate materially to +12% y/y (from +17% y/y), 8pts below the longer-term 20%+ growth outlook. Incremental efforts to sell back into the base should help offset some of the macro headwinds, which prompted roughly half of the revenue shortfall in the revised top line guide. We think the sharp deceleration (+38% y/y in FY23 to +18% y/y FY24E) could temporarily shake some growth investors out or keep incremental buyers sidelined in the near term. On the other side of the ledger, however, Paylocity's ability to maintain its Adj EBITDA outlook (34.3% margin) despite the lowered top line should help provide valuation support in the NT.

Lower PO to \$175 to reflect slower growth trajectory

Our \$175 PO (was \$180) is based on 32x EV/C25E FCF (was 34x C24E), roughly in line with payroll and HCM peers trading at 31x C25E FCF.

Estimates (Jun) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	3.25	5.15	6.40	6.81	7.48
GAAP EPS	1.61	2.49	2.67	2.65	3.19
EPS Change (YoY)	54.0%	58.5%	24.3%	6.4%	9.8%
Consensus EPS (Bloomberg)			6.14	6.99	8.14
DPS	0	0	0	0	0
Valuation (Jun)					
P/E	52.9x	33.4x	26.9x	25.2x	23.0x
GAAP P/E	106.8x	69.0x	64.4x	64.9x	53.9x
EV / EBITDA*	38.6x	24.5x	19.3x	17.6x	15.4x
Free Cash Flow Yield*	1.4%	2.7%	3.5%	3.8%	4.0%

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

09 February 2024

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	180.00	175.00
2024E Rev (m)	1,405.6	1,387.4
2025E Rev (m)	1,626.4	1,548.1
2026E Rev (m)	1,865.4	1,732.6
2024E EPS	6.45	6.40
2025E EPS	7.28	6.81
2026E EPS	8.19	7.48

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Stock Data

Price	171.91 USD
Price Objective	175.00 USD
Date Established	9-Feb-2024
Investment Opinion	C-2-9
52-Week Range	139.40 USD - 232.47 USD
Mrkt Val (mn) / Shares Out (mn)	9,657 USD / 56.2
Free Float	76.2%
Average Daily Value (mn)	83.50 USD
BofA Ticker / Exchange	PCTY / NAS
Bloomberg / Reuters	PCTY US / PCTY.OQ
ROE (2024E)	28.6%
Net Dbt to Eqty (Jun-2023A)	-34.3%
ESGMeter TM	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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iQprofileSM Paylocity

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	28.6%	36.3%	27.1%	18.8%	15.9%
Return on Equity	33.7%	40.1%	28.6%	19.4%	16.3%
Operating Margin	23.1%	27.3%	28.2%	28.8%	29.5%
Free Cash Flow	137	261	338	371	384

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	0.8x	1.0x	1.0x	1.0x	1.0x
Asset Replacement Ratio	0.2x	0.1x	0.1x	0.2x	0.2x
Tax Rate	6.2%	10.1%	12.4%	15.5%	18.5%
Net Debt-to-Equity Ratio	-22.8%	-34.3%	-31.8%	-35.7%	-37.9%
Interest Cover	NM	NA	NA	NA	NA

Income Statement Data (Jun)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	853	1,175	1,387	1,548	1,733
% Change	34.1%	37.8%	18.1%	11.6%	11.9%
Gross Profit	606	865	1,030	1,153	1,295
% Change	35.2%	42.8%	19.1%	12.0%	12.3%
EBITDA	238	375	476	523	598
% Change	39.9%	57.8%	26.9%	9.8%	14.4%
Net Interest & Other Income	(1)	4	15	15	15
Net Income (Adjusted)	184	292	364	389	429
% Change	54.6%	58.9%	24.8%	6.8%	10.2%

Free Cash Flow Data (Jun)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	183	292	364	389	429
Depreciation & Amortization	96	147	186	204	224
Change in Working Capital	(76)	(77)	(59)	(16)	(38)
Deferred Taxation Charge	(7)	14	15	0	0
Other Adjustments, Net	(41)	(93)	(147)	(176)	(197)
Capital Expenditure	(18)	(22)	(21)	(31)	(35)
Free Cash Flow	137	261	338	371	384
% Change	18.7%	90.4%	29.7%	9.6%	3.5%
Share / Issue Repurchase	0	0	0	0	0
Cost of Dividends Paid	0	0	0	0	0
Change in Debt	0	(1)	13	0	0

Balance Sheet Data (Jun)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	140	289	540	823	1,119
Trade Receivables	16	25	26	30	34
Other Current Assets	4,076	2,735	3,477	3,893	4,508
Property, Plant & Equipment	63	64	68	71	75
Other Non-Current Assets	514	583	673	698	763
Total Assets	4,809	3,696	4,784	5,515	6,498
Short-Term Debt	0	0	0	0	0
Other Current Liabilities	4,121	2,775	3,019	3,146	3,484
Long-Term Debt	0	0	0	0	0
Other Non-Current Liabilities	75	78	64	64	64
Total Liabilities	4,196	2,853	3,083	3,210	3,548
Total Equity	613	843	1,702	2,305	2,950
Total Equity & Liabilities	4,809	3,696	4,784	5,515	6,498

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

Company Sector

Server & Enterprise Software

Company Description

Paylocity (NASDAQ: PCTY) is a cloud-based provider of human capital management and payroll software solutions. Paylocity offers an intuitive product suite that helps businesses attract and retain talent, build culture and connection with their employees, and streamline and automate HR and payroll processes. The company was founded in 1997 (as Ameripay Corporation, renamed in 2005) and became a publicly traded company through its initial public offering in 2014.

Investment Rationale

The US payroll and HR market is a \$19.4bn opportunity and we view Paylocity as a continued share gainer. The payroll outsourcing industry has been in a land grab phase for 10+ years and share takers will likely benefit from customer expansions as payroll and HR systems increasingly converge. That said, the US economy is already at near-peak employment levels and thus what was a 4pt+ tailwind to revenue growth is now a headwind, which may constrain revenue growth for Paylocity in the near term.

Stock Data

Average Daily Volume 485,712

Quarterly Earnings Estimates

	2023	2024
Q1	0.98A	1.40A
Q2	1.12A	1.49A
Q3	1.74A	2.13E
Q4	1.32A	1.39E

Earnings summary and estimate changes

Exhibit 1: BofA estimates versus reported results

Revenue landed 0.6% above our estimate, however, this was primarily driven by higher interest income

\$ in thousands (except per share data)	BofA Estimates	2Q24A Actuals	Variance
Income Statement			
Recurring	\$298,746	\$298,416	-0.1%
Interest income on funds held for clients	\$25,556	\$27,945	9.3%
Total Revenue	\$324,302	\$326,361	0.6%
Cost of revenue	\$85,452	\$89,231	4.4%
Gross Profit	\$238,850	\$237,130	-0.7%
Operating expenses			
Sales and marketing	\$72,138	\$69,621	-3.5%
Research and development	\$48,178	\$49,726	3.2%
General and administrative	\$33,292	\$29,632	-11.0%
Income (Loss) from Operations	\$85,243	\$92,765	8.8%
Other Income (Expenses), net	\$3,225	\$3,800	17.8%
Pretax income (loss)	\$88,468	\$96,565	9.2%
Income tax provision	\$10,531	\$12,096	14.9%
Net income (pro forma)	\$77,936	\$84,469	8.4%
EPS (pro forma)	\$1.37	\$1.49	8.5%
Net Income (GAAP)	\$29,879	\$38,116	27.6%
EPS (GAAP)	\$0.53	\$0.67	27.7%

Y/Y Growth			
Total Revenues	18.8%	19.5%	0.8%
Operating profit (loss)	30.9%	42.5%	11.6%
Non-GAAP net income	23.7%	34.1%	10.4%
Margins			
Gross Margin	73.7%	72.7%	(1.0%)
Operating expenses % of revenue			
Sales and Marketing	22.2%	21.3%	(0.9%)
Research and Development	14.9%	15.2%	0.4%
General and Administrative	10.3%	9.1%	(1.2%)
Operating Margin	26.3%	28.4%	2.1%
Net Income Margin	24.0%	25.9%	1.9%
Balance Sheet & Cash Flow			
Cash and cash equivalents	\$383,192	\$366,904	(4.3%)
OCF	\$94,298	\$75,070	(20.4%)
FCF	\$73,319	\$57,092	(22.1%)

Source: BofA Global Research estimates, company report

BofA GLOBAL RESEARCH

Exhibit 2: Estimate change summary table

We adjust estimates to reflect the updated outlook and Q2 earnings results

	3Q24E				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
Recurring revenue	\$369,150	17.5%	\$364,437	16.0%	\$1,293,781	17.8%	\$1,271,817	15.8%	\$1,508,090	16.6%	\$1,427,608	12.2%
Interest income	\$31,172	21.4%	\$32,625	27.0%	\$111,779	46.0%	\$115,621	51.0%	\$118,300	5.8%	\$120,531	4.2%
Total revenue	\$400,322	17.8%	\$397,062	16.8%	\$1,405,560	19.7%	\$1,387,438	18.1%	\$1,626,390	15.7%	\$1,548,140	11.6%
Operating margin	34.0%	...	34.0%	...	28.7%	...	28.9%	...	29.2%	...	28.8%	...
Net income	\$122,598	24.5%	\$121,267	23.1%	\$366,790	25.7%	\$364,207	24.8%	\$415,774	13.4%	\$388,936	6.8%
EPS	\$2.15	23.7%	\$2.13	22.4%	\$6.45	25.0%	\$6.40	24.2%	\$7.28	12.9%	\$6.81	6.4%
OCF	\$146,263	14.9%	\$144,972	13.8%	\$362,948	28.4%	\$359,241	27.1%	\$445,942	22.9%	\$401,750	11.8%
FCF	\$120,366	5.3%	\$118,429	3.7%	\$274,920	27.4%	\$273,914	26.9%	\$344,796	25.4%	\$302,892	10.6%

Source: BofA Global Research estimates, company report

BofA GLOBAL RESEARCH

Price objective basis & risk

Paylocity (PCTY)

Our \$175 PO is based on 31x EV/C25E FCF is largely in line with the payroll and HCM the peer group.

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
	Datadog Inc	DDOG	DDOG US	Koji Ikeda, CFA
	DocuSign	DOCU	DOCU US	Brad Sills



US - Enterprise Software Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	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

Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

EV / EBITDA

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

Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash & Equivalents

EBIT

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

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill Amortization

Shareholders' Equity

Sales

N/A

N/A

Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

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

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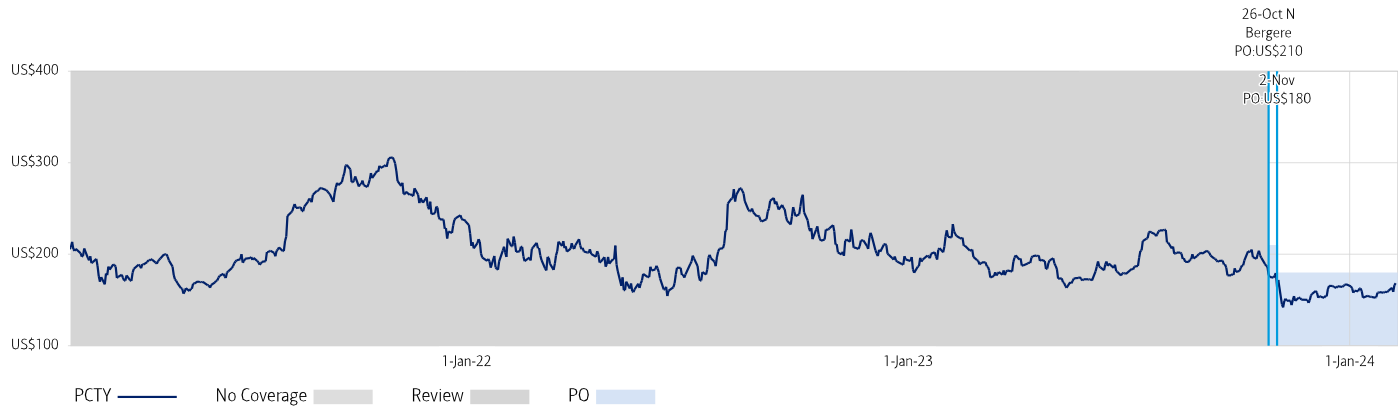
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Disclosures

Important Disclosures

Paylocity (PCTY) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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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