# Paychex, Inc (PAYX)

*Updated July 2nd, 2023 by Nathan Parsh*

## Key Metrics

| | | | | | |
|---|---|---|---|---|---|
| **Current Price:** | $112 | **5 Year CAGR Estimate:** | 11.4% | **Market Cap:** | $40 billion |
| **Fair Value Price:** | $117 | **5 Year Growth Estimate:** | 8.0% | **Ex-Dividend Date:** | 08/11/23[1] |
| **% Fair Value:** | 96% | **5 Year Valuation Multiple Estimate:** | 0.9% | **Dividend Payment Date:** | 08/25/23[2] |
| **Dividend Yield:** | 3.2% | **5 Year Price Target** | $172 | **Years Of Dividend Growth:** | 12 |
| **Dividend Risk Score:** | C | **Retirement Suitability Score:** | C | **Rating:** | Buy |

## Overview & Current Events

Paychex, Inc, which was incorporated in 1979, provides payroll accounting, benefits and human resource services to businesses that employ between 10 and 200 employees. Paychex provides services to more than 700,000 small and medium-sized businesses, primarily in the U.S. The company operates two segments: Management Solutions, which provides employers with payroll and retirement resources, and PEO & Insurance, which offers outsourced human resource services and insurance.

On April 28th, 2023, Paychex increased its quarterly dividend 12.7% to $0.89 per share, extending the company's dividend growth streak to 12 years.

On June 29th, 2023, Paychex announced earnings results for the fourth quarter and full fiscal year (the company's fiscal year ends May 31st). For the quarter, revenue grew 7.9% to $1.23 billion, beating estimates by $10 million. Adjusted earnings-per-share of $0.97 compared to $0.81 and was in-line with expectations. For the year, revenue of $5 billion compared to $4.6 billion in the prior year while adjusted earnings-per-share of $4.27 was a 13.3% improvement year-over-year.

For the quarter, Management Solutions increased 7% to $905 million due to higher number of clients and client employees receiving services. Demand remains robust for HR Solutions while revenue per client increased due to better realized prices and product demand. PEO & Insurance Solutions grew 5% to $299.5 million due to higher average worksite employees and increases in average wages per employee. Interest on funds held for clients improved 69% to $24.9 million.

Paychex provided guidance for fiscal year 2024 as well. Revenue is projected to grow 6% to 7% while adjusted earnings-per-share is expected to increase 9% to 10%. We have initiated our earnings-per-share target for the fiscal year accordingly.

## Growth on a Per-Share Basis

| Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2029 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| EPS | $1.71 | $1.85 | $2.09 | $2.25 | $2.45 | $2.84 | $3.00 | $3.04 | $3.77 | $4.27 | ***$4.68*** | ***$6.88*** |
| DPS | $1.40 | $1.52 | $1.68 | $1.84 | $2.18 | $2.24 | $2.48 | $2.52 | $2.77 | $3.26 | ***$3.56*** | ***$4.54*** |
| Shares[3] | 363 | 361 | 360 | 359 | 359 | 359 | 359 | 360 | 361 | 362 | ***362*** | ***359*** |

Paychex saw a slight decline in earnings during the last recession. Considering that the company's revenue largely depends on the number of people on payrolls, Paychex did an admirable job suffering just a slight decline in earnings-per-share as unemployment reached high levels. As long as unemployment is low, Paychex should see earnings continue to grow. If unemployment remains elevated, it is possible that the company could experience a slight reduction in earnings based on how well the company navigated the last recession. Paychex grew earnings at a rate of 10.7% per

[1] Estimated ex-dividend date
[2] Estimated dividend payment date
[3] Share count in millions

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year over the past decade. We reaffirm our expected EPS growth rate of 8% to better reflect the company's historical performance and recent business results.

## Valuation Analysis

| Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | Now | 2029 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Avg. P/E | 24.1 | 24.8 | 24.0 | 26.2 | 25.1 | 29.6 | 24.1 | 33.3 | 32.8 | 24.6 | ***23.9*** | ***25.0*** |
| Avg. Yld. | 3.4% | 3.3% | 3.4% | 3.1% | 3.3% | 2.7% | 3.4% | 2.5% | 2.2% | 3.1% | ***3.2%*** | ***2.6%*** |

Shares of Paychex have increased $3, or 2.8%, since our April 10th, 2023 report. Based off estimates for earnings-per-share for the current fiscal year, the stock has a P/E ratio of 23.9. For context, shares of Paychex have an average P/E of 26.9 over the last ten years. We reaffirm our target P/E of 25 as this is more in-line with the stock's long-term average valuation. If shares were to revert to this target by fiscal 2029, then valuation would add 0.9% to annual returns over this period.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

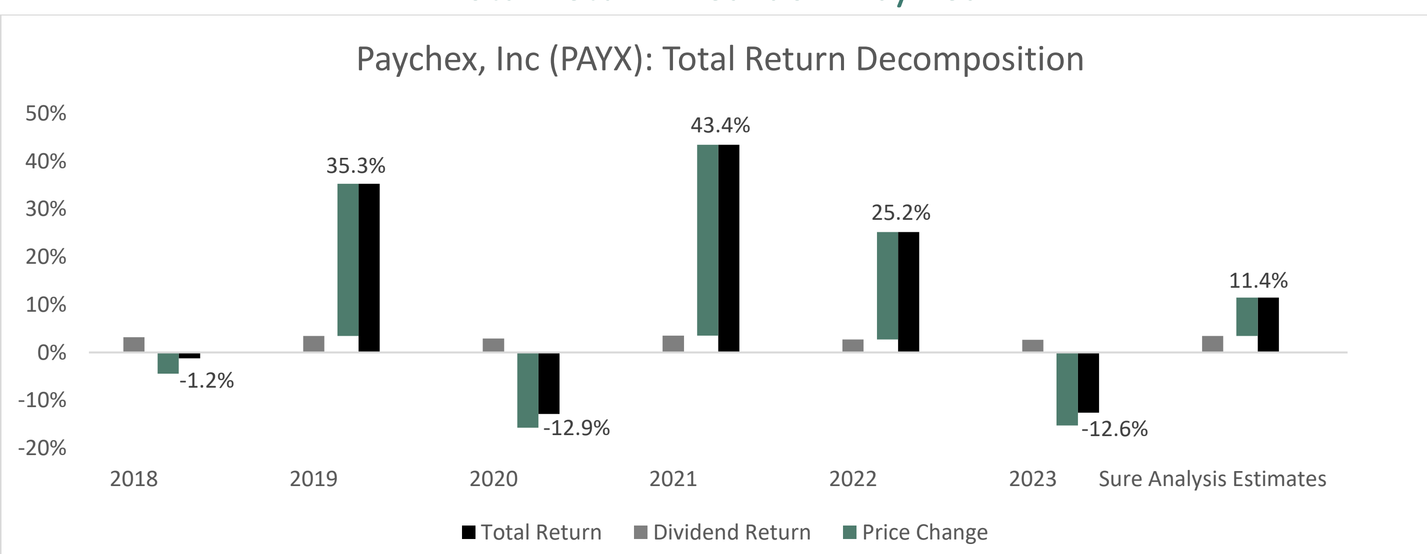
| Year | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2029 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Payout | 82% | 82% | 80% | 82% | 82% | 79% | 83% | 82% | 73% | 76% | ***76%*** | ***66%*** |

Shares of Paychex were not immune to lower earnings numbers during the last recession. With that said, the company held up well given the circumstances. Paychex's primary competitive advantage is that it is a leading provider of payroll, account, benefits, and human resource services for small and medium sized companies. Another advantage is that Paychex has very little long-term debt on its balance sheet. This allows the company to access debt markets to fund acquisitions.

## Final Thoughts & Recommendation

After fourth quarter results, Paychex is now projected to offer a total annual return of 11.4% through fiscal 2029, up slightly from our previous estimate of 10.0%. We expect that an 8% earnings growth rate, a starting yield of 3.2%, and a small tailwind from multiple expansion over the next five years. Paychex continues to post solid growth rates in both of its businesses. The company also provided strong guidance for the new fiscal year. We have raised our five-year price target $15 to $172 to reflect guidance. Shares of Paychex continues to receive a buy rating due to projected returns.

## Total Return Breakdown by Year

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## Income Statement Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|---|---|---|---|---|---|
| Revenue | 2,326 | 2,519 | 2,740 | 2,952 | 3,153 | 3,378 | 3,773 | 4,041 | 4,057 | 4,612 |
| Gross Profit | 1,655 | 1,786 | 1,932 | 2,095 | 2,234 | 2,360 | 2,595 | 2,760 | 2,786 | 3,255 |
| Gross Margin | 71.1% | 70.9% | 70.5% | 71.0% | 70.8% | 69.9% | 68.8% | 68.3% | 68.7% | 70.6% |
| SG&A Exp. | 750 | 804 | 878 | 948 | 980 | 1,068 | 1,223 | 1,299 | 1,325 | 1,415 |
| D&A Exp. | 98 | 105 | 107 | 115 | 127 | 138 | 182 | 210 | 192 | 192 |
| Operating Profit | 905 | 983 | 1,054 | 1,147 | 1,254 | 1,292 | 1,371 | 1,461 | 1,461 | 1,840 |
| Operating Margin | 38.9% | 39.0% | 38.5% | 38.8% | 39.8% | 38.2% | 36.3% | 36.1% | 36.0% | 39.9% |
| Net Profit | 569 | 628 | 675 | 757 | 826 | 994 | 1,034 | 1,098 | 1,098 | 1,393 |
| Net Margin | 24.5% | 24.9% | 24.6% | 25.6% | 26.2% | 29.4% | 27.4% | 27.2% | 27.1% | 30.2% |
| Free Cash Flow | 577 | 797 | 792 | 921 | 866 | 1,122 | 1,148 | 1,314 | 1,146 | 1,373 |
| Income Tax | 342 | 361 | 385 | 394 | 433 | 306 | 334 | 339 | 337 | 432 |

## Balance Sheet Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|---|---|---|---|---|---|
| Total Assets | 6,164 | 6,370 | 6,468 | 6,441 | 6,834 | 7,915 | 8,676 | 8,551 | 9,227 | 9,635 |
| Cash & Equivalents | 107 | 153 | 170 | 132 | 185 | 358 | 674 | 905 | 995 | 370 |
| Accounts Receivable | 133 | 149 | 177 | 409 | 508 | 375 | 421 | 384 | 578 | 724 |
| Goodwill & Int. Ass. | 579 | 581 | 594 | 727 | 715 | 955 | 2,182 | 2,122 | 2,097 | 2,056 |
| Total Liabilities | 4,390 | 4,593 | 4,682 | 4,529 | 4,878 | 5,559 | 6,057 | 5,769 | 6,279 | 6,550 |
| Accounts Payable | 43 | 49 | 52 | 57 | 57 | 74 | 76 | 79 | 89 | 106 |
| Long-Term Debt | - | - | - | - | - | - | 796 | 802 | 805 | 806 |
| Shareholder’s Equity | 1,774 | 1,777 | 1,786 | 1,912 | 1,955 | 2,357 | 2,620 | 2,781 | 2,948 | 3,085 |
| LTD/E Ratio | - | - | - | - | - | - | 0.30 | 0.29 | 0.27 | 0.26 |

## Profitability & Per Share Metrics

| Year | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|---|---|---|---|---|---|
| Return on Assets | 9.0% | 10.0% | 10.5% | 11.7% | 12.4% | 13.5% | 12.5% | 12.7% | 12.3% | 14.8% |
| Return on Equity | 33.7% | 35.3% | 37.9% | 40.9% | 42.7% | 46.1% | 41.6% | 40.7% | 38.3% | 46.2% |
| ROIC | 33.7% | 35.3% | 37.9% | 40.9% | 42.7% | 46.1% | 35.8% | 31.4% | 29.9% | 36.4% |
| Shares Out. | 365 | 363 | 361 | 360 | 359 | 359 | 359 | 359 | 360 | 361 |
| Revenue/Share | 6.38 | 6.88 | 7.51 | 8.14 | 8.70 | 9.34 | 10.43 | 11.19 | 11.20 | 12.70 |
| FCF/Share | 1.58 | 2.18 | 2.17 | 2.54 | 2.39 | 3.10 | 3.17 | 3.64 | 3.16 | 3.78 |

*Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.*