Paychex, Inc (PAYX)

Updated October 1st, 2024 by Nathan Parsh

Key Metrics

Current Price:	$140	**5 Year CAGR Estimate:**	8.1%	**Market Cap:**	$50 Billion
Fair Value Price:	$125	**5 Year Growth Estimate:**	8.0%	**Ex-Dividend Date:**	11/13/24[1]
% Fair Value:	112%	**5 Year Valuation Multiple Estimate:**	-2.2%	**Dividend Payment Date:**	11/29/24[2]
Dividend Yield:	2.8%	**5 Year Price Target**	$184	**Years Of Dividend Growth:**	13
Dividend Risk Score:	C	**Retirement Suitability Score:**	C	**Rating:**	Hold

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 May 1st, 2024, Paychex increased its quarterly dividend 10.1% to $0.98 per share, extending the company's dividend growth streak to 13 years.

On October 1st, 2024, Paychex announced earnings results for the first quarter of fiscal year 2025 (the company's fiscal year ends May 31st). For the quarter, revenue improved 2.5% to $1.32 billion, which was $10 million more than expected. Adjusted earnings-per-share of $1.16 compared to $1.14 in the prior year and was $0.02 above estimates.

For the quarter, revenue for Management Solutions improved 1% to $961.7 million due to gains in the number of clients served across its human capital management platform. This segment continues to see higher numbers of client worksite employees and increased product penetration. PEO & Insurance Solutions grew 7% to $319.3 million. As with prior quarters, this segment saw growth in number of average employees per worksite and gains in insurance revenue. The company noted demand from its small- and medium-sized businesses remains strong. Interest on funds held for clients increased 15% to $37.5 million. As of the end of the quarter, Paychex held $1.6 billion in cash and equivalents against short-term and long-term borrowings, net of debt issuance costs, of $817.6 million.

Paychex reaffirmed prior guidance for fiscal year 2025 as well. Revenue is projected to grow 4% to 5.5% year-over-year while adjusted earnings-per-share are expected to be up 5% to 7% for the new fiscal year.

Growth on a Per-Share Basis

Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2030
EPS	$1.85	$2.09	$2.25	$2.45	$2.84	$3.00	$3.04	$3.77	$4.27	$4.72	***$5.00***	***$7.35***
DPS	$1.52	$1.68	$1.84	$2.18	$2.24	$2.48	$2.52	$2.77	$3.26	$3.65	***$3.92***	***$5.00***
Shares[3]	361	360	359	359	359	359	360	361	362	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 remains low, Paychex should see earnings continue to grow. If unemployment becomes 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 11% per 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.

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[1] Estimated ex-dividend date

[2] Estimated dividend payment date

[3] Share count in millions

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.

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Valuation Analysis

Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	Now	2030
Avg. P/E	24.8	24.0	26.2	25.1	29.6	24.1	33.3	32.8	24.6	25.5	***28.0***	***25.0***
Avg. Yld.	3.3%	3.4%	3.1%	3.3%	2.7%	3.4%	2.5%	2.2%	3.1%	3.0%	***2.8%***	***2.7%***

Shares of Paychex have gained $21, or 17.6%, since our June 30th, 2024 report. Based off estimates for earnings-per-share for the current fiscal year, the stock has a P/E ratio of 28.0. For context, shares of Paychex have an average P/E of 27.0 over the last ten years. We reaffirm our target P/E of 25.0. If shares were to revert to this target by fiscal 2030, then valuation would reduce annual returns by 2.2% over this period.

Safety, Quality, Competitive Advantage, & Recession Resiliency

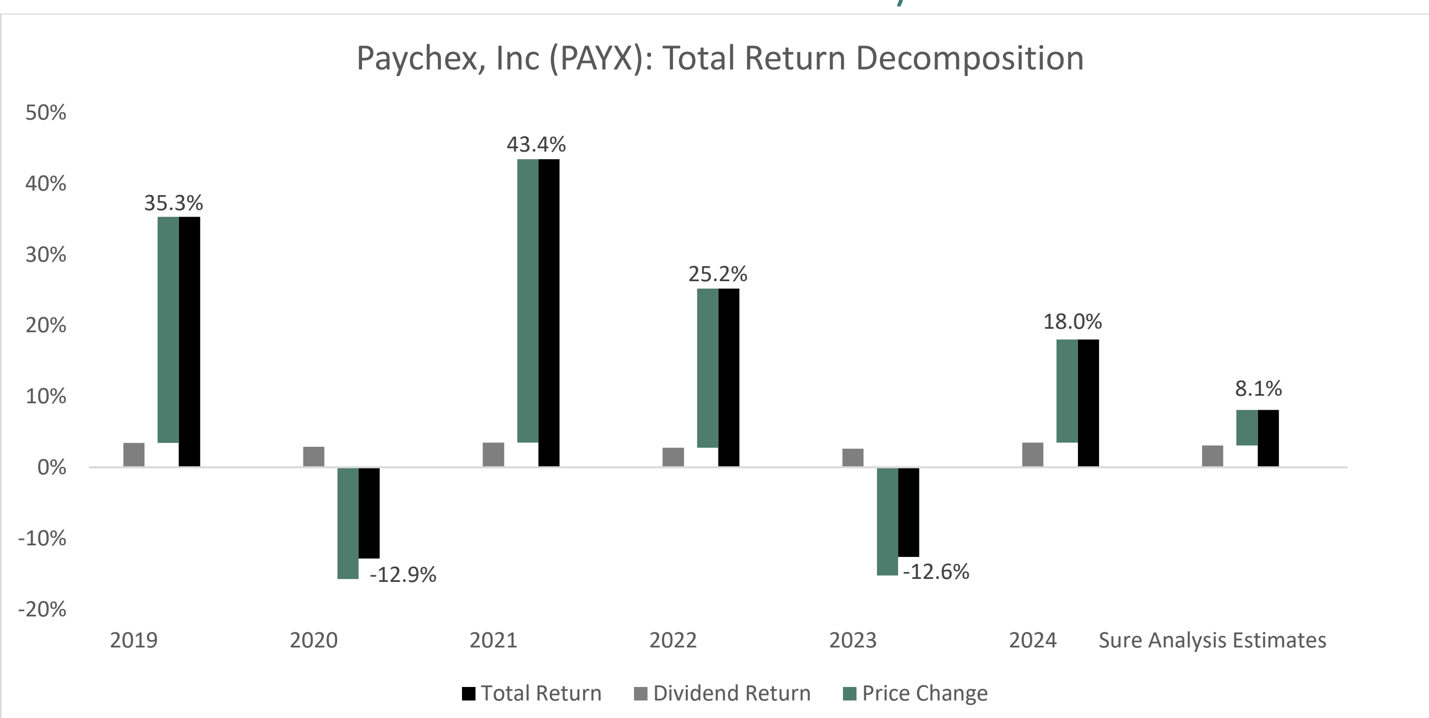
Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025	2030
Payout	82%	80%	82%	82%	79%	83%	82%	73%	76%	77%	***78%***	***68%***

Paychex was not immune to lower earnings numbers during the last recession. With that said, the company held up well given the circumstances. The company also posted growth during the Covid-19 pandemic. 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

Following first quarter results, Paychex is projected to offer a total annual return of 8.1% through fiscal 2030, down from 11.6% previously. Our projected return stems from an earnings growth rate of 8% and a starting yield of 2.8%, offset by a small headwind from multiple compression. Paychex continues to see growth in both of its businesses, with the company noting that small and medium-sized businesses remain resilient. We maintain our five-year price target of $184 due to guidance, but now rate shares of Paychex as a hold due to projected returns.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Revenue	2,740	2,952	3,153	3,378	3,773	4,041	4,057	4,612	5,007	5,278
Gross Profit	1,932	2,095	2,234	2,360	2,595	2,760	2,786	3,255	3,554	3,799
Gross Margin	70.5%	71.0%	70.8%	69.9%	68.8%	68.3%	68.7%	70.6%	71.0%	72.0%
SG&A Exp.	878	948	980	1,068	1,223	1,299	1,325	1,415	1,521	1,625
D&A Exp.	107	115	127	138	182	210	192	192	177	177
Operating Profit	1,054	1,147	1,254	1,292	1,371	1,461	1,461	1,840	2,033	2,174
Operating Margin	38.5%	38.8%	39.8%	38.2%	36.3%	36.1%	36.0%	39.9%	40.6%	41.2%
Net Profit	675	757	826	994	1,034	1,098	1,098	1,393	1,557	1,690
Net Margin	24.6%	25.6%	26.2%	29.4%	27.4%	27.2%	27.1%	30.2%	31.1%	32.0%
Free Cash Flow	792	921	866	1,122	1,148	1,314	1,142	1,372	1,556	1,736
Income Tax	385	394	433	306	334	339	337	432	491	528

Balance Sheet Metrics

Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Total Assets	6,468	6,441	6,834	7,915	8,676	8,551	9,227	9,635	10,546	10,383
Cash & Equivalents	170	132	185	358	674	905	995	370	1,222	1,469
Accounts Receivable	177	409	508	375	421	384	578	724	873	1,060
Goodwill & Int. Ass.	594	727	715	955	2,182	2,122	2,097	2,056	2,021	2,077
Total Liabilities	4,682	4,529	4,878	5,559	6,057	5,769	6,279	6,550	7,053	6,582
Accounts Payable	52	57	57	74	76	79	89	106	85	104
Long-Term Debt	-	-	-	-	796	802	805	806	808	817
Shareholder's Equity	1,786	1,912	1,955	2,357	2,620	2,781	2,948	3,085	3,493	3,801
LTD/E Ratio	-	-	-	-	0.30	0.29	0.27	0.26	0.23	0.22

Profitability & Per Share Metrics

Year	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Return on Assets	10.5%	11.7%	12.4%	13.5%	12.5%	12.7%	12.3%	14.8%	15.4%	16.2%
Return on Equity	37.9%	40.9%	42.7%	46.1%	41.6%	40.7%	38.3%	46.2%	47.3%	46.3%
ROIC	37.9%	40.9%	42.7%	46.1%	35.8%	31.4%	29.9%	36.4%	38.0%	37.9%
Shares Out.	361	360	359	359	359	359	360	361	362	362
Revenue/Share	7.51	8.14	8.70	9.34	10.43	11.19	11.20	12.70	13.82	14.58
FCF/Share	2.17	2.54	2.39	3.10	3.17	3.64	3.16	3.78	4.30	4.80

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