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Solutions by STC | Europe

3Q23 flash results: Double-digit profit beat

Reaction to earnings

Unchanged

Impact to our investment thesis



Meaningful upside

Financial results versus consensus



Meaningful revision higher

Impact to next 12-month consensus EPS

Source: Company data, Morgan Stanley Research

Key Takeaways

- 3Q revenue of SAR 2,795m was 1% below MS, 2% above consensus
- EBITDA of SAR 517m was 17/12% above MS/consensus
- Net income of SAR 387m was 16/13% above MS consensus

Solutions posted robust 3Q results. Top-line performance was broadly in-line with MS/consensus, with the core Solutions business +7% y/y, a modest acceleration on the 1H performance. Within the mix, Digital Services performance was weak at -4%, but was broadly compensated by stronger growth in Core ICT and IT Managed & Operational Services. Gross margins were once again very strong at 28.5%, with Solutions calling out "improvement in the product mix and cost optimisation initiatives", helping drive a meaningful beat vs. estimates on EBITDA and net income. FCF at SAR 141m was also above MS at SAR 118m. As usual, we look forward to the full results in due course to understand underlying performance in the quarter (i.e. excluding movements in provisions, impairments etc). We also look for any updates to guidance. We will update our forecasts at that point. On our current forecasts and at SAR 314, Solutions trades on c. 25x FY24 adj. P/E. We see the current valuation as continuing to bake in earnings beats (particularly given the premium valuations vs. European IT Services), so we would not expect more than a low-single-digit % positive price reaction.

Exhibit 1: 3Q23 results versus MS estimates and consensus

SAR m	Actual	3Q23 MSe	Consensus	% Δ vs	
				MSe	Cons
Core ICT Services	1,474	1,382			
y/y growth (%)	45%	34%			
IT Managed and Operational Services	897	926			
y/y growth (%)	53%	58%			
Digital Services	424	510			
y/y growth (%)	-4%	22%			
Total revenue	2,795	2,819	2,734	-0.8%	2.2%
y/y growth (%)	37%	38%	34%		
Gross profit	796	634	705	25.5%	12.9%
% margin	28.5%	22.7%	25.2%		
Stated EBITDA	517	441	460	17.2%	12.4%
% margin	18.5%	15.8%	16.5%		
Stated net income	387	332	344	16.5%	12.5%
Free cash flow	141	118			

Source: Company data, Company compiled consensus, Morgan Stanley Research estimates (e)

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Solutions by STC (7202.SE, SOLUTION AB)

EEMEA - Technology | Saudi Arabia

Stock Rating

Industry View

Price target

Shr price, close (Oct 29, 2023)

52-Week Range

Mkt cap, curr (mn)

Net debt (12/23e) (mn)*

EV, curr (mn)*

Equal-weight

No Rating

SAR 305.00

SAR 315.00

SAR 385.00- 216.80

SAR 37,800

SAR (2,748)

SAR 35,281

* = GAAP or approximated based on GAAP

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Valuation Methodology and Risks

Solutions by STC (7202.SE)

We value Solutions by STC with a 10-year DCF, using a WACC of 8.5%, and a 2.5% terminal growth rate.

Risks to Upside

- New contract wins particularly with the KSA government
- International expansion into other GCC countries in the mid-term
- Bolt-on M&A

Risks to Downside

- Slowdown in contract wins or contract losses once they reach the end of their term
- Weaker than expected delivery on existing large contracts leading to margin compression
- Impairments/provisions on contracts/inventory
- Longer working capital cycles than expected

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(as of September 30, 2023)

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	Count	% of Total	Count	% of Total IBC	% of Rating Category	Count	% of Total Other MISC
Overweight/Buy	1350	37%	281	43%	21%	608	39%
Equal-weight/Hold	1673	46%	303	46%	18%	709	46%
Not-Rated/Hold	3	0%	0	0%	0%	1	0%
Underweight/Sell	608	17%	68	10%	11%	225	15%
Total	3,634		652			1543	

Data include common stock and ADRs currently assigned ratings. Investment Banking Clients are companies from whom Morgan Stanley received investment banking compensation in the last 12 months. Due to rounding off of decimals, the percentages provided in the "% of total" column may not add up to exactly 100 percent.

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Stock Price, Price Target and Rating History (See Rating Definitions)

Solutions by STC (7202.SE) - As of 10/29/23 in SAR
Industry : EEMEA - Technology



Stock Rating History: 11/1/21 : E/NR; 1/11/22 : E/NR; 5/12/22 : E/NR

Price Target History: 11/1/21 : 205; 5/12/22 : 250; 8/10/22 : 262.5; 11/2/22 : 270; 12/12/22 : 277.5; 2/28/23 : 268; 5/16/23 : 287; 7/5/23 : 295; 8/10/23 : 303; 10/13/23 : 305

Source: Morgan Stanley Research Date Format: MM/DD/YY Price Target --- No Price Target Assigned (NA)

Stock Price (Not Covered by Current Analyst) — Stock Price (Covered by Current Analyst) ■

Stock and Industry Ratings (abbreviations below) appear as ♦ Stock Rating/Industry View

Stock Ratings: Overweight (O) Equal-weight (E) Underweight (U) Not-Rated (NR) No Rating Available (NA)

Industry View: Attractive (A) In-line (I) Cautious (C) No Rating (NR)

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George W Webb Solutions by STC (7202.SE)	E (05/12/2022)	SAR 315.00

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