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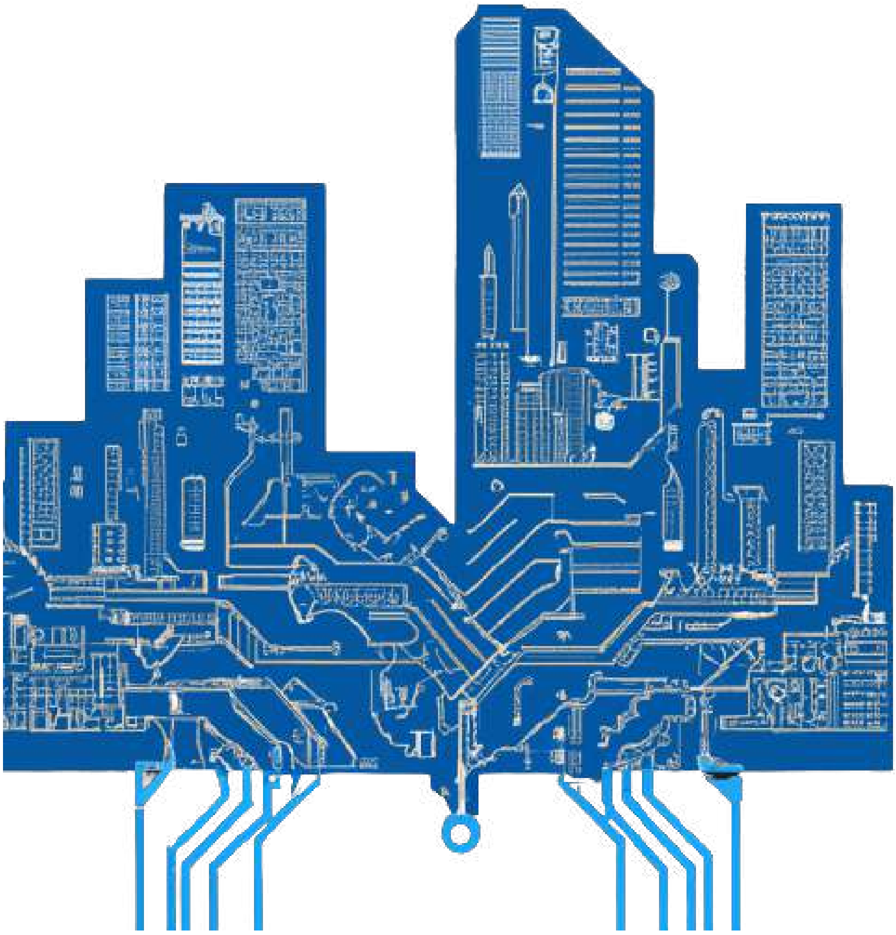

KSA Software & Services Sector

KSA's Economic Transformation to be Digitally Lead by the Largest Providers at the Frontline

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Table of Contents

Executive Summary: Long streak of growth ahead for the sector's fundamentals

The Software & Services sector sits at the heart of the Saudi Arabian economic transformation as the initiatives in place are largely technologically led. IT spending in the Kingdom is expected to grow at a CAGR of 5.2% from FY19-26 while the IT sector size is expected to grow at a CAGR of 8.3% from FY22-25. All while the FY24 preliminary budget describes various initiatives in which the sector will be able to service as the addressable market for the sector continues to expand. The sizes, brand recognition, technical abilities, and key engagements with public and private sectors for our covered companies sets us to expect these firms to be on the front line of the digital transformations and initiatives in the Saudi Arabia. As they have been in the past few years. Going forward our covered providers are expected to post an average 18.24% FY22-25 top line CAGR and a 24.55% bottom line CAGR for the same period. Expected 12% growth in the IT services sector in the next two years (as per IDC report), supportive demand, optimized cost controls, and lean human capital requirements for our covered firms will further support margins in the MT, even in light of the ongoing expansions. All firms under our coverage are currently undergoing organic and inorganic expansions- Elm is eyeing to acquire e-government provider THIQA, while Solutions has completed two acquisitions in the past year with one more announced in their M&A pipeline, as well as Perfect Presentation's expansion into three new business lines to be in effect by Q4-23 to Q1-24. We initiate our coverages on Elm at a "Neutral" recommendation with a target price of SAR 566.5 per share, and Solutions at SAR 363.5 per share at an "Overweight" recommendation. We have also upwardly revised our target price on 2P at SAR 26.0 per share, in light of its recent and upcoming expansions at an "Overweight" rating.

Economic diversification initiatives under the Vision 2030 are the underlying driver for the sector: IT market of Saudi Arabia has grown by 37.2% over FY19-22 to contribute towards the USD 42bn ICT market size (as per MCIT), driven by government's economic transformation plan, that is promoting growth of digital economy. Government tech spending has grown by 13.5% over 2019-21. The Ministry of Communications & IT (MCIT) has targeted growing the ICT market by 50% as well as having the sector contribute USD 13.4bn towards the Kingdom's GDP. We expect momentum in the ICT sector to continue as government services (passport, traffic affairs, expatriate services, civil affairs) and wide ranging businesses/sectors across the economy such as financial services (digital payments, savings, crowd funding, micro lending), health care (telemedicine, health apps, electronic health records), retail (online stores, IoT devices, real time consumer data, optimization of inventory management) and logistics/supply chain (automated fulfilment, inventory tracking, ware housing) adopt new technologies. In the medium to long-term, mega and giga projects such as NEOM, the Red Sea Project, the Smart City and Quality of Life programs are only some of the initiatives which will underpin the growth in the Software and Services sector.

Our covered tech players' profits have soared a collective average of almost 2.9x over the last 3 years, boosted by large government client ship: Our coverage witnessed a 3 year (2019-22) revenue/net income CAGR of 23%/45.0% and a 127.1% surge in market cap from H1-22 to date. The aforementioned digitalization/technology initiatives undertaken by the government soared profitability of tech companies, as government client ship for the companies under our coverage constitute 83%, 49% and 43% of their H1-23 revenues (for 2P, Solutions, and Elm respectively). 2P led the growth amongst companies under our coverage, with FY19-22 top line CAGR of 46.0% and a bottom line CAGR of 73.9%. ELM and solutions followed 2P with a revenue/net income CAGR of 29.9%/18.4% and 44.9%/38.4% respectively. Looking ahead, we expect our coverage's aggregate sales and profits to grow by 17.78% and 25% over 2022-25; we forecast ELM to lead the listed tech space with a 2022-25E revenue/earnings CAGR of 20.4/30.3%. 2P is expected to post revenue/earnings CAGR of 18.0/21.8% over 2022-25, while Solutions is forecasted to post 21.55% bottom line CAGR over FY22-25.

Large players to experience rapid growth through acquisitions and expansions: Strong balance sheets of large tech players (Elm/ Solutions Net debt-to -equity of -0.68/-0.67x respectively) have enabled them to grow rapidly through acquisitions. Note that Elm has announced that it is eyeing to acquire THIQA, a PIF owned company with a similar business model to Elm. Solutions' recently acquired Giza group for SAR 466mn (at a 6.6x EV/EBITDA) to leverage Giza Group's expertise to service more asset intensive sectors such as Energy and Telecoms. Solution's pending Devoteam acquisition could funnel more engagements towards Solutions' other segments. Perfect Presentation (2P) is a firm in a stage of organic expansion as it adds IoT, Networking, and Cybersecurity to its portfolio of services. The firm is awaiting regulatory approvals on the IoT business, the segment is already witnessed interest from two government/semi-government entities and one private entity. Other new segments are expected to be reflected by Q1-24 at the latest.

Recommendation: We initiate our coverage on **Elm** with target price of **SAR 566.5** per share and a "**Neutral**" recommendation. Note that, the announcement on Elm's acquisition of PIF owned THIQA surged the stock price by nearly 70% from announcement to peak, we believe the stock price is well ahead of current growth prospects at 2024E PE of 34.9x. While we have not reflected THIQA's prospects onto Elm's valuation, we believe a significant upside could be found in the acquisition should it go through. We begin coverage on **Solutions** at target prices of **SAR 363.5** per share and "**Overweight**" recommendation, due to efficient acquisition integrations and current market valuations. We have also revised our target price on **2P** at **SAR 26.0** per share, in light of its recent and upcoming expansions at an "**Overweight**" rating.

Company	Recommendation	TP (SAR per share)	Upside/Downside	Net Profit FY23E (SAR mn)	Net Profit FY24E (SAR mn)	DY% (FY24)
Elm	**Neutral**	**566.5**	-23.7%	1,334.6	1,706.1	1.4%
Solutions	**Overweight**	**363.5**	15.8%	1,380.4	1,662.2	2.6%
Perfect Presentation	**Overweight**	**26.0**	15.1%	135.6	183.7	1.9%

Source: AlJazira Capital, closing price as of 30th November 2023.

Sector Overview: Favourable drivers across all facets of the economy

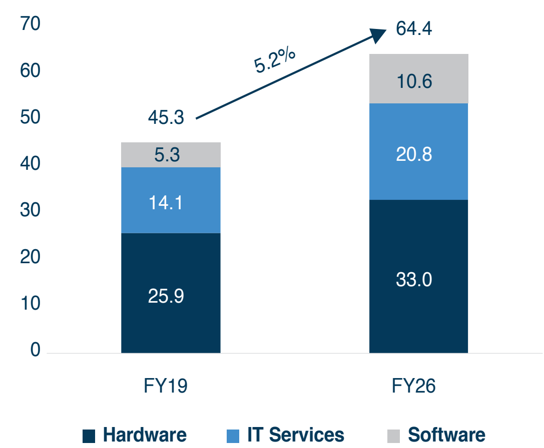
Entity creation from SME's, new cities, and influx of international companies to expand the addressable market for the Software & Services sector:

The Kingdom's economic transformation lead to the sector's size growth of nearly 37.2% from FY19 to FY22: The transformation in the Kingdom touches upon all sectors, and aspects of social day to day life with the Software and Services sector at the front line of those transformations. Government expenditure on IT services was reportedly the largest purchaser of IT services in FY21, after growing 13.5% from FY19. Expenditures on digitalizing government services (which now 97% of government services are done online), developing city experiences, and other areas of the economy directly translated to the sector's growth. COVID related projects such as virtual schooling, and healthcare platforms further proved a case of resilience for the sector at a time of economic headwinds. Going forward, the sector in the ST is still supported by initiatives such as those summarized from the budget report. Furthermore, transformations across the healthcare sector, real estate, government administrations, and PPP programs, and social aspects will all require digital spending from private and public sectors which will punctuate IT spending past USD 34.5bn in FY23 alone.

In the LT, Vision 2030 programs are in place supporting the sector in the long run: On the 'large-scale' end of the developments in progress are the Smart Cities initiatives in Riyadh and Giga projects such as NEOM, as well as the Quality of Life program which is already integrating AI technologies, IoT and cloud computing to improve the city experience for residence, driven by technological integration among other programs. All providers in our coverage have secured engagements for Mega and Giga projects. Besides the technological infrastructure needs for these projects and new cities from MEGA and GIGA project, the entities they will create and attract are expected to increase the addressable market for the providers under our coverage in the long-run. NEOM's high technological integration in the city's infrastructure, and targeted 9mn population and other large scale projects such as The Red Sea project (set to employ 70,000 people by 2030) and Qiddiya Project will boost the demand for ICT infrastructures and IT & managed services as well.

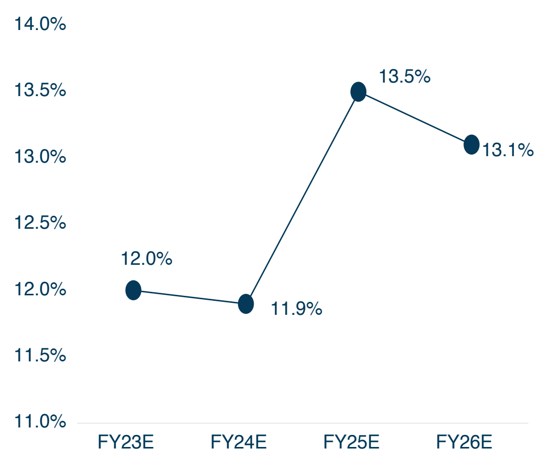
The creation of entities, resulting from Vision 2030 initiatives, are expected to expand the market opportunities for software sector in the LT as well: The Kingdom is targeting FY24 as the year to take into effect a regulatory requirement to only permit entities with headquarters in Saudi Arabia to be able to conduct business with the government. Blue-chip firms have already begun to relocate their regional headquarters to the Kingdom with a growing number of firms setting plans to become based in the kingdom; a program that will result in direct demand for ICT services and infrastructures. Already, PepsiCo, PwC, Unilever, SAP, Baker Huges are among some of the large corporations that have migrated their regional headquarters to KSA. Financial Times reports that about 80 international firms have already migrated to Riyadh (2023).

Fig 2: IT spending by KSA technology market (SAR bn)



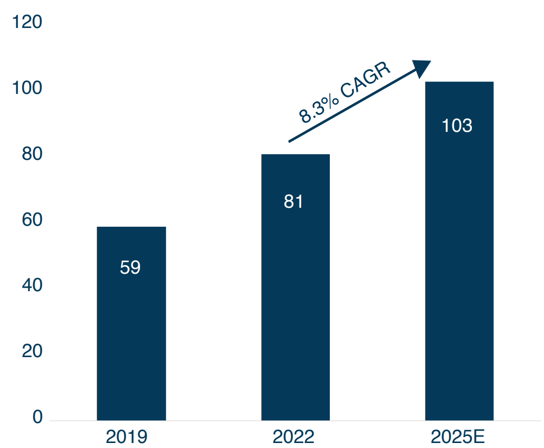
Sources: 2P Company Prospectus, AlJazira Capital.

Fig 3: KSA IT Sector Growth (%)



Sources: IDC (Solutions presentation), AlJazira Capital.

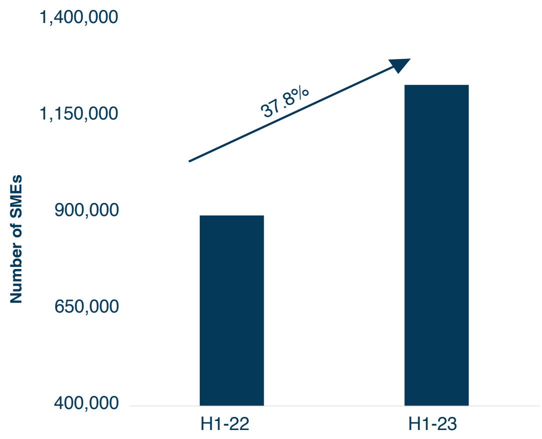
Fig 4: KSA IT Sector Size (SAR bn)



Sources: IDC (Digital Tech Forum), AlJazira Capital.

Emergence of SMEs will also play a role in the long term demand expansion from a larger addressable market. SMEs constitute 99.7% of the businesses in the Kingdom (Monsha'at, 2023), and while their IT expenditure is lesser than their larger company counterparts their volume and technological agility deems the client segment a target that tech providers cannot neglect. The rise in SMEs in just over a year came as a result of a rise in entrepreneurialism among the Kingdom, and more initiatives are underway to slingshot this growth further. MCIT's FY23 report reported that SME's contribution to GDP has increased 9%, towards a goal of 20% to 35% contribution to GDP by 2023. One initiative in line with the digital SME initiatives is the SAR 2.8bn government owned Saudi Venture Capital Company, focusing on seeding SME's in the Kingdom. The PIF's role in the series initiatives supporting the sector also includes the launch of Jada Investments, to also support seeding the Kingdom's SMEs, and is expected to generate 58,000 jobs to the economy by FY27 (2P prospectus, 2022). The creation of a new tech-heavy FinTech sector is also displaying developments, in support of the Software & Services sector. The number of SAMA licensed FinTechs nearly doubled by 2022, and are targeted to increase from 30 (in 2022) to 525 firms by 2030 (SAMA Annual Fintech Report 2022); spurring more demand for the sector's services. The digital empowerment of national youth is likely to spur entrepreneurially driven SME start-ups in the future. Attesting to those initiatives are the increase in 340,000 jobs Y/Y in the ICT sector by FY22. The Kingdom has several digital empowerment initiatives in place to expand the technical abilities in the domestic workforce such as the SAR 2.5bn budget on the National Technology Development Program for training in areas such as AI and IS.

Fig 5: KSA SME Segment Growth



Sources: Monshaat.gov, AlJazira Capital.

Going forward, Saudi Arabia's target of having the ICT economy contribute $13.4bn towards of Saudi Arabia's GDP will be achieved through the various fronts mentioned. The initiatives underway already have lead the sector's market cap to surge past a 250% three year CAGR from FY20, and saw the growth in listed companies increase by 9x from FY20. PPP partnerships have contributed to the sector's growth as well, as providers are contracted for managing public services such as airports and tourism by leveraging their technical abilities. Firms in the sector are expanding organically and inorganically to satisfy the expected IT spending of over USD 34.5bn in the Kingdom for FY23, and the predicted CAGRs for Software services (11.4%) and IT services (8.7%) through FY22-26 (as per IDC, 2023). Empowering the domestic workforce with technological skillsets grew the Saudianization rate from 37% in FY17 to 62% in FY22 to rank the Kingdom as the ninth in growth in digital skills, and we expect that further continue as a result of ongoing initiatives to further support in-housing operations in favor of the expected 24.55% FY22-25 bottom line CAGR for our covered firms. Smart city initiatives, PPP initiatives, new mega and giga projects all present significant upsides for the sector as the government spending aims towards technological services.

KSA Sector-Budget Allocation Priorities Tilted to the Software & Services sector:

Much of the transformation in the kingdom will be digitally led. Below are only some of key initiatives which the Software & Services sector is able to service towards KSA's 2023 goals. While some may seem unrelated to Software & Services, on the contrary, the sector is involved with much of these operations as they service Operations and Maintenance of processes as a part of their services. Such as Elm's involvement in the initiative to plan and manage for crowd control during Umra and Hajj (SAR 69.9mn contract). Firms have begun positioning themselves to be able to service the needs for the digital transformation, with them being Solutions as it acquires Giza Group to further expand its services for asset heavy industries such as energy and industrials.

Fig 6: Addressable KSA 2023 Budget Allocation Sample

Justice: Launching virtual legislation platform	Justice: Launching "Real Estate Market" platform	Foreign Affairs: Platform for employment of Saudi's abroad	MoI: Crowd control initiative for Hajj and Umra (Elm secured contract)	Industry: Establishing 105 factories in industrial areas	SME's: Launching platform to support e-commerce	Social Development: Launching Social Responsibility Platform
ICT: Increasing fiber coverage to 64% and 4G to 99%.	ICT: Increase data center capacity to 150 megawatts	SDAIA: E-gates for e-passports and travel	SDAIA: Implementing open data strategy	Education: Launch of 'Study in Saudi' platform	E-gov: Platform for ICT contractors and government projects	Energy: Enhance electronic interconnection with nations
Energy: Developing 10 renewable energy projects	Health: E-archiving of cardiac images	Health: Expanding medical coverage to 88%	Health: 3 new hospitals at 900 beds	Commerce: Automation of stock and price monitoring	Military: Monitoring military procurement	Cybersecurity: Establish or support more than 60 emerging firms
		Transportation: Launching 12 platforms to enhance service	Tourism: Achieving 5.2% of GDP	Environment: Regional center for early warnings		

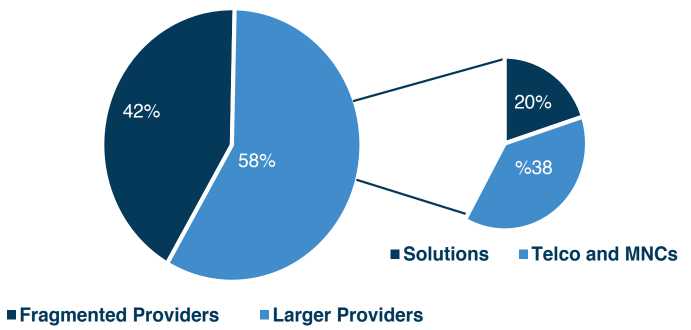
Sources: MoF Budget Report, AlJazira Capital

KSA Tech Providers Expanding to Meet a Growing Market:

The local market is earmarked by a fragmented structure as almost 52% of the market consists of SME providers servicing the public and private market: Of the other 48%, Solutions leads by market share, constituting a share almost as sizable as the international providers in the kingdom hold. Competitiveness however, is reserved for the larger players as they are able to secure projects, leverage government relationships and brand image, as well as their technical capabilities that are sought after for larger projects with more sensitive applications such as data management. SME services can overlap, however, with standard ICT services also offered by the larger providers.

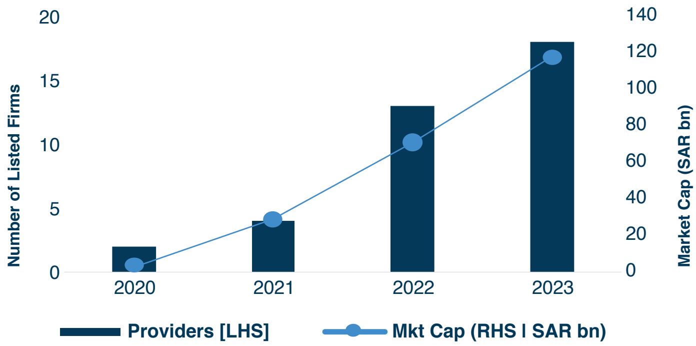
The technology sector is an emerging market as the capital market witnessed a 252.2% three year CAGR in listed market cap from since 2020. Growth in the provider firms as a result of increased demand, and maturity to list publically are catalysts for the expansion of the public IT market. As a result, the number of firms publically listed grew from 2 to 18 providers through 2022-2023.

Fig 7: Current Expected B2B ICT Market Share (Solutions Share as Per IDC)



Sources: Solutions Company Reports, AJC Research

Fig 8: KSA IT Sector Growth

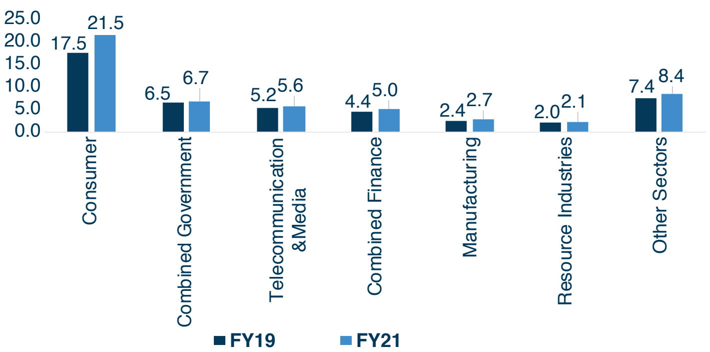


Sources: IDC (Digital Tech Forum presentation), AlJazira Capital.

Demand over the Software & Services sector is underpinned by economic conditions:

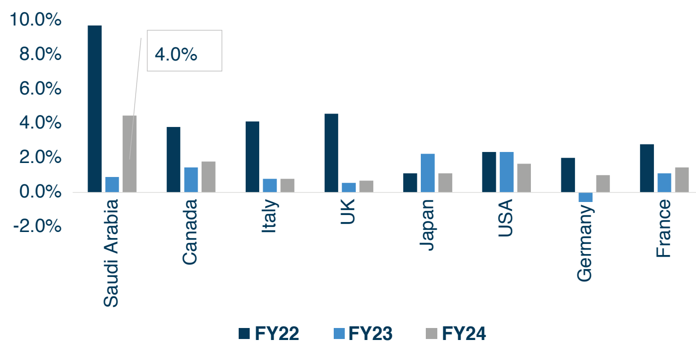
IT spending in the Kingdom is expected to reach past USD 34.5bn by FY23 (IDC, 2023) driven by foreign direct investments and government initiatives to transform the Kingdom's economy: Excluding consumers, the government makes up the majority of IT spending's in the Kingdom. As government client ship for the companies under our coverage constitute 83%, 49% and 43% of their revenues (for 2P, Solutions, and Elm respectively), government spending and initiatives are able to dictate the sector's performance. Government's CAPEX is supported by Saudi Arabia recording its ninth consecutive economic expansion, and with IMF forecasting an outperformance in the Kingdom's GDP as compared to G7 economies; in favor of spending in the sector. Much of the transformations detailed in the MoF budget report, across non-oil sectors, are digitally led as well, as the companies under our coverage are already engaging with transformations in healthcare and tourism amongst other sectors. Non-oil sectors are forecasted to grow 5.9% by FY23 as per FY24's budget report. Economic wellness will directly benefit the Software & Services sector, and especially the large providers in the domestic fragmented sector.

Fig 9: IT Spending by Sector (SAR bn) *



Sources: Company Reports, AlJazira Capital, IDC

Fig 10: KSA Real GDP Growth comparables (Y/Y)



Sources: GASTAT, AlJazira Capital, IMF

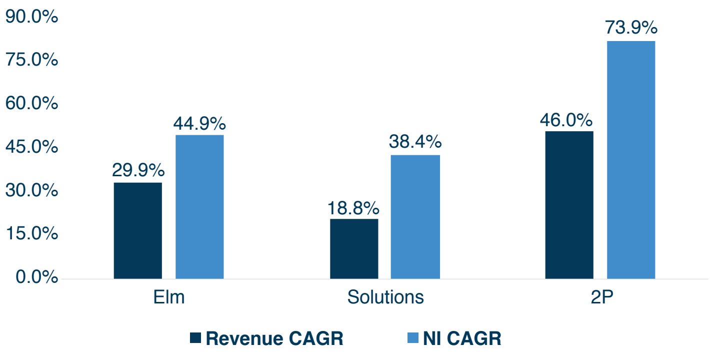
Sector Peer & Financial Analysis (TTM)

	P/E	Market Cap (SAR)	Revenue CAGR (FY19-22)	Net profit CAGR (FY19-22)	ROAA	ROAE	Debt/Equity	GP Margin	Net Margin	Receivable Days (Net)	Receivable Days (Non-Net)	Quick Ratio
Elm	47.5	59.4	29.90%	44.90%	19.08%	38.35%	0%	41.11%	22.49%	118.7	147.7	1.96
Solutions	30.1	37.5	18.80%	38.40%	12.61%	41.93%	21.8%	24.95%	11.57%	152.7	154.9	1.39
2P	24.5	3.4	46.00%	73.90%	15.00%	48.60%	104.00%	20.40%	13.30%	123.2	125.8	1.35
Arab Sea	NEG	0.7	1.80%	-100%	-14.30%	-15.80%	0%	38.90%	-56.90%	84.9	271	1.15
MIS	24.8	3.7	-7.50%	8.10%	4.34%	23.80%	217.00%	19.33%	5.12%	143.2	153.5	1.15
Median	27.5**	NM	NM	NM	12.61%	38.35%	21.8%	24.95%	11.57%	123.2	153.5	1.35

Source: Company Reports, AlJazira Capital *As price closing of 30th November 2023 I Excluding negative values

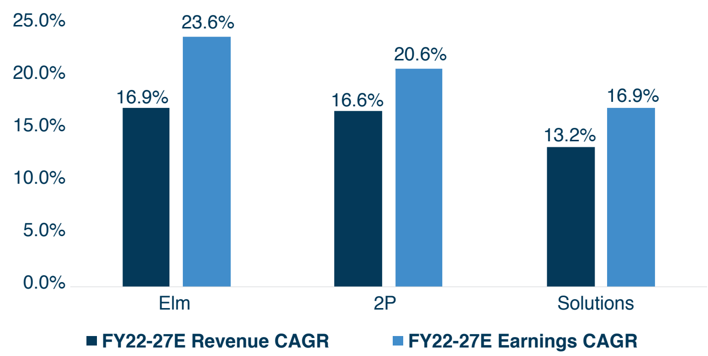
Revenue and Earnings growth: Within our coverage, 2P has the best revenue and earnings growth at 46.0% and 73.9% respectively, over FY19-22. However, over FY22-27E, we expect Elm to outpace the peers, given an uptick in its digital business which is likely to be a key beneficiary of KSA's economic transformation initiatives across government services, tourism, entertainment shipping, financial and pilgrim activities.

Fig. 11: 2P outperformed peers in terms of revenue and earnings growth over FY19-22.



Source: Company Reports, AlJazira Capital

Fig. 12: Elm to outpace peers by being a key beneficiary of KSA's transformation over FY22-27E.

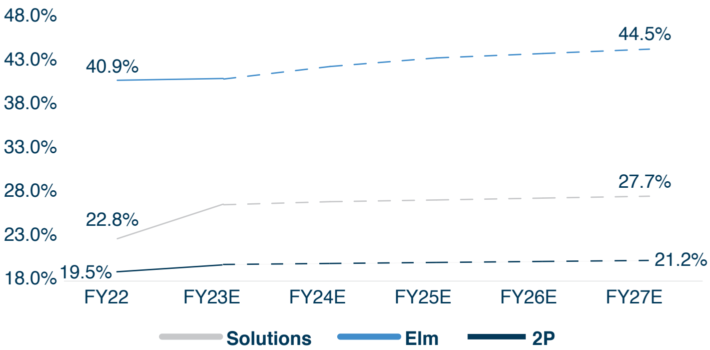


Source: Company Reports, AlJazira Capital

PE Valuations: Direct and indirect ownership of PIF in Elm and Solutions provides them access to larger client base and strategic safety. Hence these companies demand premium PE multiple within our coverage. Elm's PE is the highest amongst the peers, as apart from being directly owned by PIF, it also offers a concentrated exposure to software services in KSA.

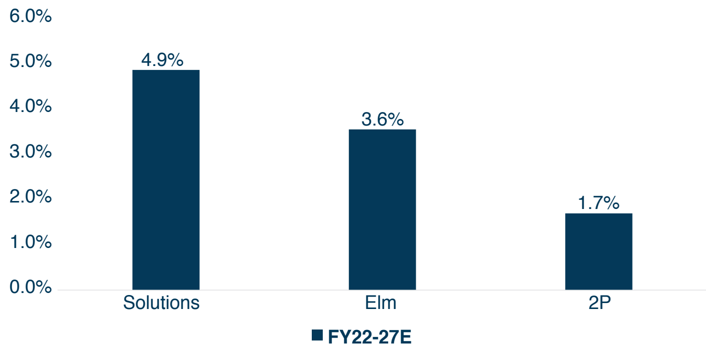
GP Margins: Within our coverage, Elm has the highest gross margins at 40.9% in FY22, mainly attributable to its business model and benefitting from economies of scale. However, over FY22-27E, we expect Solutions gross margins to expand by 490bps, the highest within our coverage.

Fig. 13.A: Elm has the highest gross margins within our coverage.



Source: Company Reports, AlJazira Capital

Fig. 13.B: Gross margins are likely to expand faster at Solutions over FY22-27E.

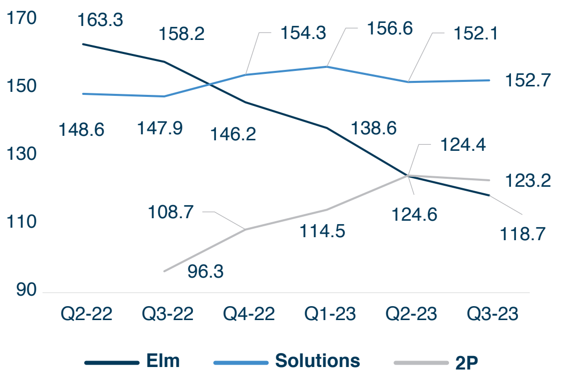


Source: Company Reports, AlJazira Capital

Working Capital Considerations

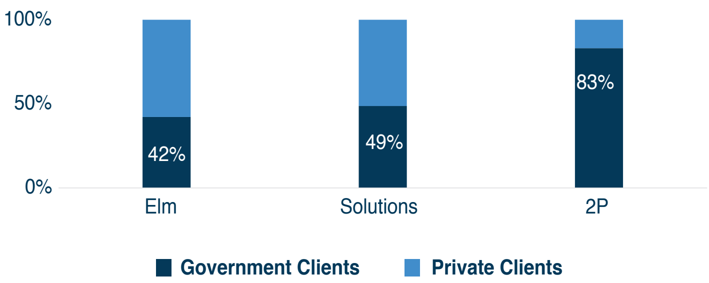
2P's receivable days rise towards the industry median, as per the firm's client mix and the firm's weighted average collection days from its government and business clients. 2P's cash conversion cycles are subject to rise as a result of increases in hardware procurement and thus payable days. Similarly, Solutions has underwent a cycle of hardware procurement to fulfill its current contract mix. While 59.5% of FY22 receivables are owed from its mother company, only an unsymmetrical 18.5% of bad debt provisions are dedicated to STC receivables as the firms are able to optimize their balances. Elm's collection periods are in line with 2P's albeit at a different working capital profile with the highest quick ratio among the sector. We expect increases in the Digital Business segment to further support their working capital profile. 2P holds the least provisions to receivables among the sector, as we also expect a possible reshaping of its working capital profile as a result of introducing a new B2C segment.

Fig. 14: Sequential Receivable Days (TTM) Trends



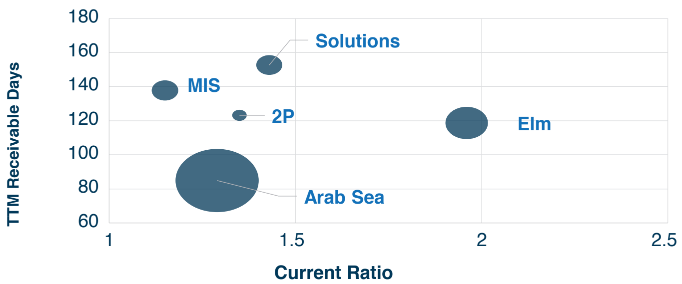
Source: Company Reports, AlJazira Capital

Fig. 15: Government Clients Exposure (% of 12M-to-1H23 Revenue)



Source: Company Reports, AlJazira Capital

Fig. 16: Current Liability Coverages and Provisions-to-Receivables Profiles (TTM)



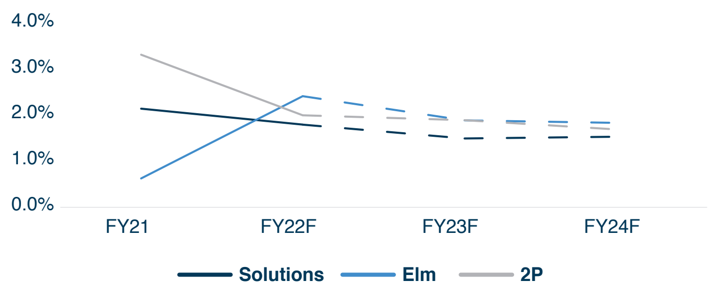
*Bubble size reflects % of provisions-to-receivables (TTM)
Source: Company Reports, AlJazira Capital

Elm services the most diverse client base, followed by Solutions. 2P's government client concentration was seen translated in its increased receivable days as its government engagements increased. However a more diverse client base can improve 2P's working capital management, as well as offer a more resilient revenue structure should government clients turn the other way from a firm, as seen in other cases in the Saudi Stock Market. It is notable that as the government is the largest purchaser of IT services, and as all firms have different focuses, a larger government concentration does not translate to a risk in the conventional sense for other sectors.

Low Capex intensity is another feature of the sector: Solutions and 2P are expected to significantly cut down on capex intensity, to 2% and 1% respectively, as they come off a period of organic and non-organic expansions. Elm's capex intensity could possibly be heightened if the THIQA acquisition goes through and requires operational costs to consolidate the businesses. Further expansions, and CAPEX needs could also limit future dividend distributions.

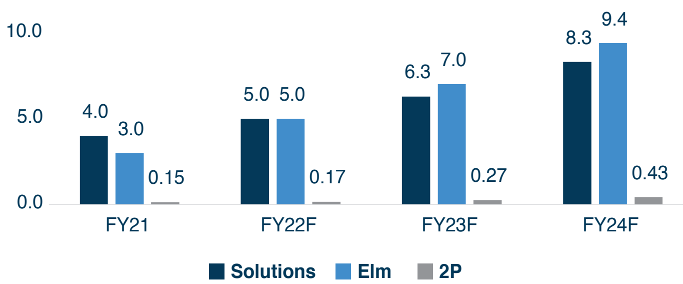
We expect payout ratios to remain at their current levels: Despite the expansion plans for the companies under our coverage, dividend payouts to remain at their current levels due to their strong cash flow position. Solutions and Elm's negative net D/Es of -0.6x and -0.7x further support the dividend growths even in the backdrop of an economic downturn. Solutions' management indicates no intentions of revising dividend policies in the Short to Medium term and we expect the same for the rest of our coverage amid their expansion phases.

Fig. 17: Capex Intensity to stabilize, despite their expansion plans



Source: Company Reports, AlJazira Capital

Fig. 18: Dividend payout to remain at their current levels, supported by strong cash flow position



Source: Company Reports, AlJazira Capital

Sector Investment Thesis: Mega providers to reap the benefits of growing sector

Investment Thesis: The IT sector sits at the heart of the Kingdom's economic transformation and growth and the companies under our coverage offers a direct hyperactive exposure to the Kingdom's initiatives across all sectors. Conventionally, the IT sector is earmarked with being digital services providers. However, on average, 44.5% of our coverage's revenue comes from managing operational processes as outsourced providers. Tech firms are able to leverage their technical expertise beyond digital and core IT services to succeed in being providers for outsourced services ranging from maintenance to project planning and management. In line to support the Kingdom's budget plans to build factories, or reshape planning processes (such as crowd management, and procurement planning).

With transformations in tourism, healthcare, real estate as well as government administrative sectors among others at full swing, the sector is able to service all of those facets of an expanding economic make-up. Furthermore, large scale projects such as NEOM, and Qiddiya projects are also sources of an increased target market for the providers under our coverage. At a shorter term, Quality of Life initiatives which aims to ease day to day living in the Kingdom across various social and living aspects are digitally lead as well. SMEs are reported to be an emerging target for the sector as their agility and receptiveness to technological adoption outweigh that of their mature company counterparts. Despite SMEs' limited IT spending budget, their large presence in the economy poses opportunities to the sector. Attesting to the condition of the sector is the exponentially shaped growth in public market cap of the listed companies in the Saudi stock market which saw a growth of 44x. To encapsulate our view on the sector- the economic transformation is digitally lead, and will underline the expected 8.3% FY22-25 CAGR in the market's size. Valuations across our coverages for Elm, Solutions and 2P are summarized at forward PEs (FY24) of 34.9x 22.7x and 18.4x respectively- capturing the prospects for the mega providers, yet with more headroom available for 2P's current market valuation.

Sector-wide Upsides:

- Increased government expenditure
- Emergence of more entities including SMEs and multinationals needing services
- Increased economic activity across all segments
- Digital disruptions and innovations spurring new demand

Sector-wide Downsides

- Large firms in-housing their IT operations
- Slowdowns in government expenditure and projects
- Increased regulation on data and tech handling
- Introduction of multinationals as providers is a long term risk

Arabian Internet and Communications Services Co. (Solutions)

A leading market share of 20% of the Kingdom's IT sector, and a 17.3% four-year bottom line CAGR earmarks Solutions by STC. The firm's successful integration of recent acquirees CCC, and Egypt based Giza Group (and possibly Devoteam) expands the firm's engagements in servicing asset heavy sectors such as telecoms, oil, and utilities, as well as Customer Experience and professional consulting. Negative current net D/E of -0.6x supports the firm further towards future acquisitions and dividend distributions. We are optimistic about Solutions' core business in the medium term, supported by a focus on SMEs, the introduction of Egyptian giant Giza Group into the Saudi Arabian market, as well as the support of CCC and the pending Devoteam onto Solutions' business model to support our expected growth for Solutions' earnings by a FY22-25 CAGR of 21.6%. SME focus and current H1-23 client breakdown is a signal of improving working capital conditions as well. We initiate our coverage at an "Overweight" rating with a target price of SAR 363.5 price per share due to efficient acquisition integrations and current market valuations.

Rapid growth at an FY19-22 top line CAGR of 18.8% is punctuated with a NI CAGR of 38.4% to maintain beat on the back of efficient M&A strategy: Solutions has seen double digit growths across its reported years since 2018 to date, with the exception of 2021. Growth in top line was mainly led by its core ICT Services segment which since 2018-to-date reaped the majority of Solutions' revenues annually. Expanded GP and EBITDA margins supported the bottom line growth further at an FY22-25 bottom line CAGR of 21.55%. Going forward, the success in its inorganic growth strategy is found in the cases of the quick integration of Giza Group and CCC. Giza group has already begun contributing double-digits towards Solutions' GP at 11.0% YTD. As Solutions streamlines its costs to share with Giza Group to reach a GP Margin average of 21.2% since consolidation. Which comes at a significant step-up from Giza's previous margins pre-acquisition average of 15.7% (FY19-21). CCC is Solutions' more recent acquisition, finalized in Q2-23 extends Solutions' scope of services into the Customer Experience segment. A SAR 2.8bn large market (FY21) and likely larger today as a result of Quality of Life programs. CCC contributed towards 5.7% of Q2-23's GP at a GP Margin of 23.4% for the segment. Dovoteam's integration could possibly pressure margins further in the ST. Furthermore, Solutions is one of a short handful of mega providers in the Kingdom with a track record granting it data-sensitive projects and engagements. Furthermore, H1-23 contribution to revenue from private sector customers (excluding STC) rose by 11.8% Y/Y, attesting to the firm's efforts on SME focus and expanding addressable market. We expect FY22-25 CAGR to reach 16.34% as a result of expansions and increased demand.

Solid balance sheet and managed debt levels to support shareholder returns via future acquisitions and supported dividend distribution: Negative current net D/E ratio of -0.6x (FY22: -0.91x) as a result of cash (and Murabaha) holding further supports expansion strategies and distributions, which we forecast to remain at current payout levels and improve thereafter should avulsions are on hold after Devoteam. Solutions' dividend payout ratio of nearly 55% is manageable with their ending cash (and Murabaha) balance alone, which covers expected FY23 dividend distributions by nearly 3.3x.

STC ownership is a strategic feature of Solutions which supports the firm's marketplace in the sector: STC ownership supports the firm's growth in connecting Solutions with clients. Solutions also sells to clients through STC supporting its sales channel further. In fact, 66.7% of YTD sales to STC were for services where STC was an agent of the sale, and not the final customer of that sale. Furthermore, as over half of FY22 receivables are recorded as revenue due from its mother company, we consider its receivables to be more easily managed and optimized as opposed to companies with third part debtors. STC's position in Solutions' business model is a supporting driver for future backlog growths and adds a competitive advantage towards Solutions' client reach and contracts towards STC themselves such as the most recent SAR 112mn three-year contract announced in October FY23.

Investment Thesis and Valuation: Attractive return profile at current TTM ROAA and ROAE of 12.61% and 41.9% respectively stands favorably above sector averages of 7.3% and 27.4%. We expect ROA to improve by 350bps in the next 3 years from FY22 levels as a result of business expansions and growing demand over IT services in the Kingdom. Low CAPEX intensity model, and a three year ROIIC of 32.5% also earmark efficient capital allocation as the firm decides to reinvest capital. On the other hand, dividend distributions are expected to remain consistent at current payouts while the firm eyes the possibility of more acquisition driven expansion. Focus on SME segments are expected to further improve receivable collections. Though cash conversion cycle could hold off at an improved FY23 level as a result of inventory requirements. Expected FCF growth of CAGR 13.13% (FY23-27) also supports our "**Overweight**" recommendation at a TP of **SAR 363.5** per share as we initiate our coverage on Solution

Recommendation	**Overweight**
Target Price (SAR)	**363.5**
Upside/(Downside)	**15.8%**

Source: Tadawul Prices as of 30th November 2023

Key Financials

(in SAR mn, unless specified)	FY21	FY22	FY23E	FY24E
Revenues	7,208.3	8,805.1	10,826.0	12,400.5
Growth %	4.6%	22.2%	23.0%	14.5%
Gross Profit	1,708	2,011	2,893	3,357
Net Income	830	1,054	1,380	1,662
Growth %	18.3%	27.0%	31.0%	20.4%
EPS	6.9	8.8	11.5	13.9
DPS	4.0	5.0	6.3	8.3

Source: Company Reports, AlJazira Capital

Key Ratios

	FY21	FY22	FY23E	FY24E
Gross Margin	23.7%	22.8%	26.7%	27.1%
Net Margin	11.5%	12.0%	12.8%	13.5%
ROE	36.6%	37.3%	40.2%	40.5%
ROA	11.6%	10.3%	11.7%	12.8%
P/E (x)	NA	27.6	27.4	22.7
P/B (x)	NA	10.3	11.0	9.2
EV/EBITDA (x)	NA	21.4	20.7	17.8
Dividend Yield	NA	2.1%	2.0%	2.6%

Source: Company reports, Aljazira Capital

Key Market Data

Market Cap(bn)	37.5
YTD%	+31.1%
52 week (High)/(Low)	377/220
Share Outstanding (mn)	120.0

Source: Company Reports, AlJazira Capital

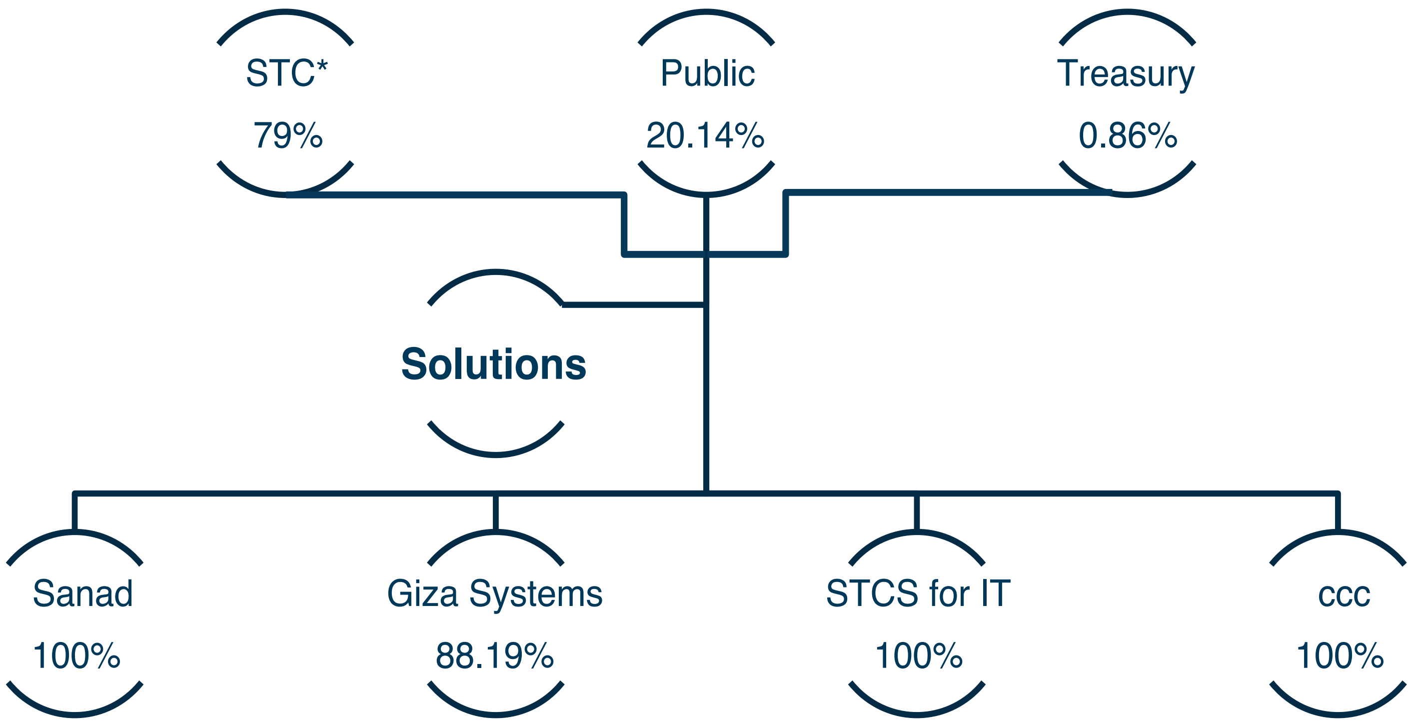
Fig. 21: Price-performance

Source: Bloomberg, AlJazira Capital

Company Overview: Solid Market Position Supported by STC

Solutions by STC, was formerly known as AwalNet when it was acquired by STC in 2007 before it was rebranded to its current name in 2014, and began trading on the Saudi Arabian main market on September 30th 2021 under the ticker code 7202. Solutions, under the ownership of Saudi telecom giant STC, offers a range of ICT services to classify under Tadawul's Software & Services sector as it services 10 sectors in the Middle Eastern, North West East and Central African regions as well as an anchor office in the USA through their recent Giza Group acquisition. Solutions has placed itself in the MSCI Emerging Markets index as it garnered at almost 20% market share in the fragmented Saudi Arabian IT sector. Currently, Solutions is in what it describes as its 'Horizon III' of its strategy spanning from 2020-2025, which focuses on stable revenue growth and profitability, after its 'rapid growth' strategy in 2014-2019's 'Horizon II' phase. The firm's key partnership with its mother company STC grants the IT provider synergies to extend its customer reach to fulfil its strategies. STC plays a significant role in introducing Solutions to B2B clients and government entities.

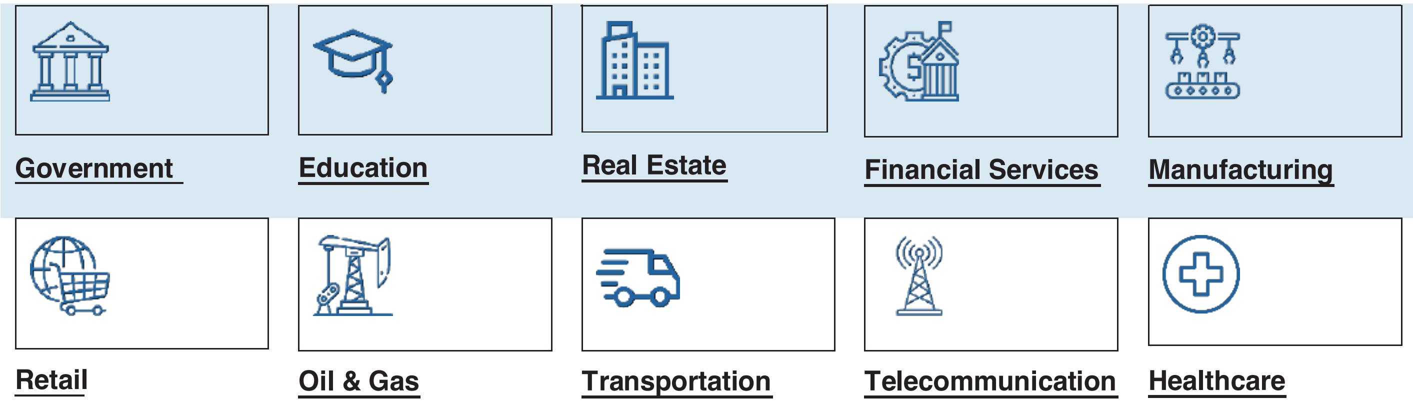
Ownership Structure



STC's ownership over Solutions plays a key role in Solutions' client attraction and client base growth: Historically, STC made up nearly half of Solutions' sales in 2017. As of TTM however, STC sales made up only 32.1% of Solutions' sales, partially as a result of efforts to capture opportunities for growth from servicing the SMEs segment. The remaining portion of revenue sources are from B2Bs and government entities,though a portion of non-STC sales are done through STC, where STC is not the final beneficiary of the service. Furthermore, STC's largest ownership and beneficiary is the PIF, at a 64.0% ownership of Solutions' mother company STC. Solutions still attributes much of its business relationships and introductions to clients due to synergies with its mother company.

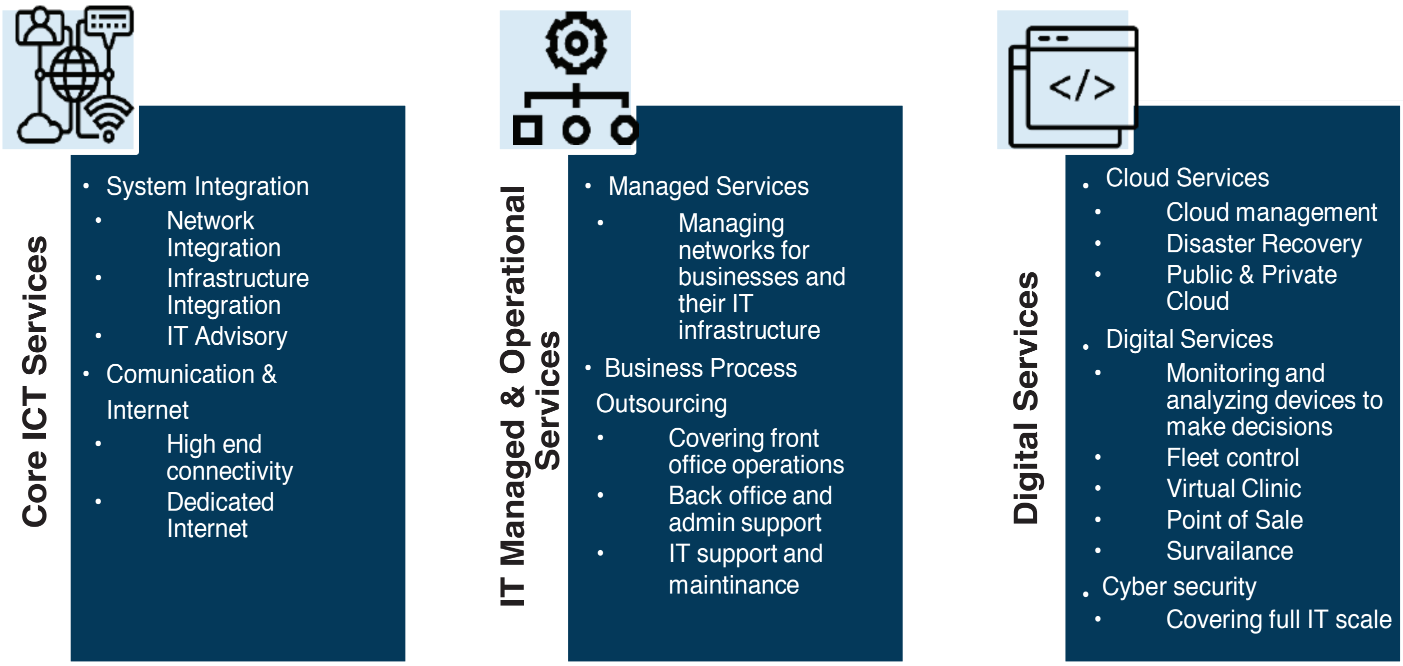
Diverse Basket of Sectors Served by Solutions

Fig. 22: Solutions' Key Sectors Served



Sources: Company Fillings, AlJazira Capital

Business Lines



Solutions' acquisitions strengthen the firm's engagements in asset heavy sectors and expands operations into Customer Experience segments: As the Kingdom's transformation initiatives span over asset heavy sectors such as oil and utilities, Solutions' recent Giza Group acquisition aims to strengthen its engagements in these sectors as it leverages Giza's asset heavy services expertise. The full acquisition of CCC from STC also adds onto Solutions' IT & Outsourcing segment through customer experience services, in light of the Kingdom's efforts in the Quality of Life initiatives and Smart City programs which focus on user experiences.

LEAP Strategy

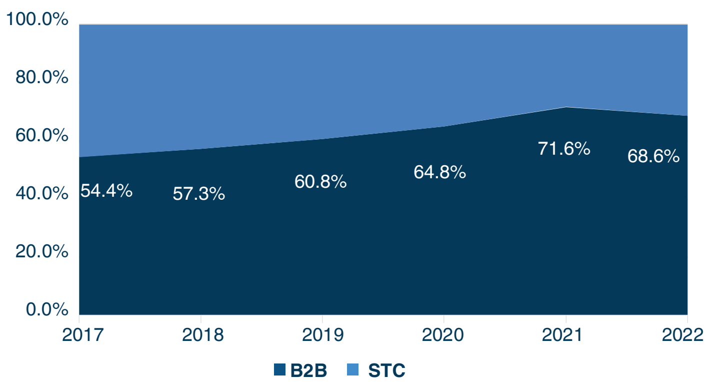
Solutions is in its Horizon III phase of its growth plan. Horizon I being 'Start right' from 2007-2014, and Horizon II being 'Rapid Growth' from 2014-2019. Horizon III is categorized as 'Sustainable Growth with Strong Profitability'. Solutions aims to accomplish this target using its LEAP strategy from 2020-2025.

Revenue structure supported by STC

Less STC reliance is expected to continue as the wider economy lags the telecom giant's digitalization needs, and as Solutions caters to SMEs: Business with STC holds a bulk of Solutions' revenue earned (31.4%), yet as of 2022, the current revenue contribution split between revenues from STC and revenues from other B2B sales sits at 31.4% and 68.6% as the growth contribution from other B2B's have been continuously outperforming that from STC. The split was reported a lot closer to 50%-50% in FY17 (see fig. 22), though that figure continuously redistributed towards B2B sales from since then. As the tech-heavy telecom provider is likely ahead of the curve on digitalization initiatives than the wider economy, it is expected that the revenue split will favor B2B businesses more as the wider economy catches up on digitalization initiatives in the coming years. The emergence of new entities, as well as Solutions' focus on servicing the SME segment drives is expected to support increase in private client business. Apart from sales to STC directly, management indicates that almost 32.1% of B2B sales are in fact still done through STC to fulfill a client. We do not consider the STC-Solutions relationship as a risk in the same conventional sense for cases which have a concentration on one client, however we do consider a more diversified client base as a signal of increased wider demand.

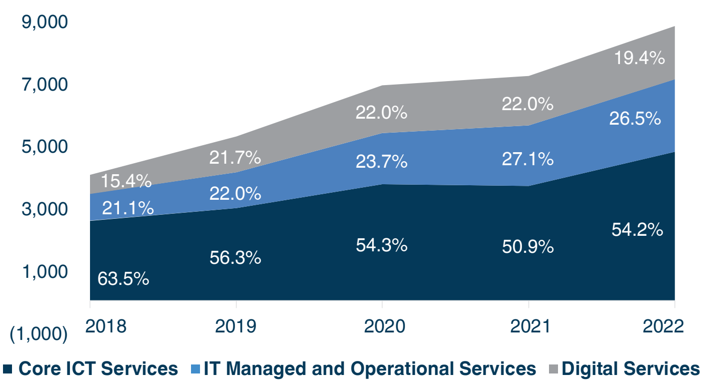
Revenue streams from 'Core ICT Services' to remain as the majority contributor towards revenues: From since 2018 (till 2022), Core ICT revenues (out of the three revenue streams) grew by a four-year CAGR of 16.8%; Both IT Managed & Operational Services, and Digital Services outpaced the staple business line as they grew a four-year CAGR of 28.5% and 28.7% respectively. IT & Managed Operational Services is expected to continue growing at a 10.3% four-year CAGR as completed contracts roll over to the management business line. We expect the IT Managed and Operational Services line to outpace all revenue streams at a four-year CAGR of 16.1% as the Kingdom continues to transform in its economy public and private fronts, and driven by Vision 2030 initiatives in place.

Fig. 23-A: Solutions' client mix diversifying towards less STC reliance



Source: Company Filings, AlJazira Capital

Fig. 23-B: Solutions' Revenue Streams



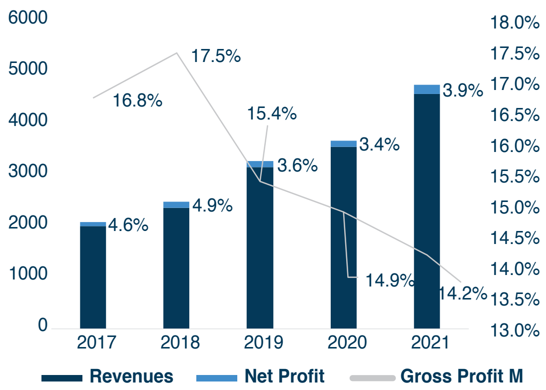
Source: Company Reports, AlJazira Capital

Healthy financials unshaken by acquisition integration and supportive of more

Revenue and net income growth (FY22-25 CAGR of 16.34% and 21.55%) expected to be led by government spending, increase in private sector audience, and Solutions' acquisitions to meet the growing demand: The expected growth in the sector driven by government spending and increased productivity from the private sector in the Kingdom is expected to directly translate to growth for a Solutions with a more diverse basket of offering post acquisitions. CCC and Giza have opened the firm up towards the 1) Customer Experience segment, a market that was estimated to be SAR 2.5bn large in 2021 by IDC and likely larger today, and 2) Heavy-asset focused (such as manufacturing, Oil and gas, and Utilities sectors) through Giza's integration services. As seen in the Kingdom's FY22 and FY23 budget reports, there is a focus on heavy-asset sectors as a part of the budget's mandate which Solutions will be able to service more post Giza acquisition. Furthermore, NI growth from FY22-25 is expected to be supported by an expansion in GP and EBITDA margins which Solutions has begun to display through initiatives on efficient acquisition integration. GP margins (9MTD Y/Y) have already expanded by nearly 260bps from 23.5% to 26.1%, over a base unburdened with acquisition integrations. We expect the steady margin expansions to enhance the bottom line summarized by a FY22-25 CAGR of 21.55%.

Financial profile and operational efficiency to absorb well the short term pressures from acquisition integration: We do forecast that the financial profile for Solutions will remain resiliant even in light of consolidating with its financials with firms with previously less eyewatering financial profiles. Namely with Giza Group and Devoteam ME, both historically recording single digit net margin figures far from the median domestic market's bottom line margin. Solutions' management recognises the effect and indicated that an optimization initiative is in place to normalise the effect of consolidating with lesser financially healthy firms, which we have begun to see, at a quick pace of change, on the GP margin for Giza Group as costs are streamlined. We expect the optimization innitatives to continue reflecting better onto Solutions' financials as summaried in the figures below.

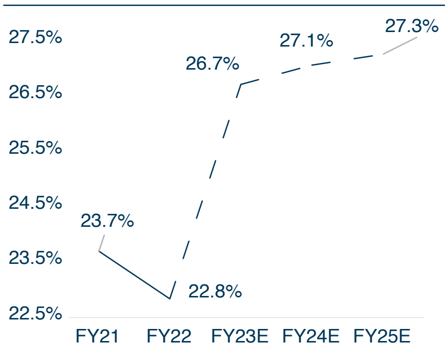
Fig. 24: Giza Systems' consistent revenue growth came with limited NI margins (EGP I Pre-Acquisition)



Source: Company Presentations, AlJazira Capital

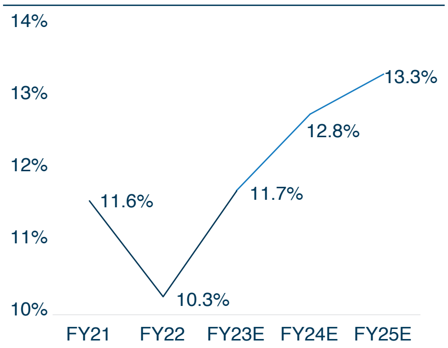
Fig. 25: Solutions' financials to pick up post consolidation of acquires

Gross Profit marigns



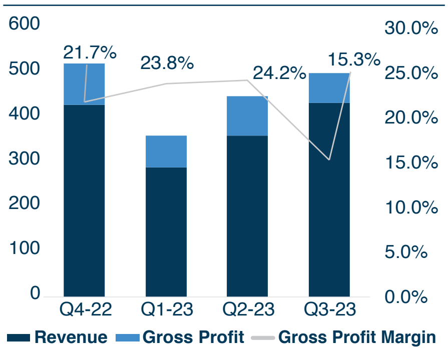
Source: Company Presentations, AlJazira Capital

Return on Assets



Source: Company Presentations, AlJazira Capital

Fig. 26: Giza post Acquisition (SAR)



Source: Company Presentations, AlJazira Capital

Solutions is in the midst of an active acquisition strategy

Company:	Contact Center Co. (CCC) by STC (H1-23)	Giza Systems, and Giza Arabia (Giza Group) (H2-22)	Devoteam Middle East (DME) (Pending)
Ownership:	100.0%	88.19%, and 92.21%	40.0%
Purchase Value:	SAR 450mn	SAR 466mn	Based on EV of SAR 741.7mn
Funding:	Cash	Bank Facilities	Cash
Description:	Solutions acquired 100% of Contact Center Company (CCC) from STC and ESM Holdings. CCC operates in the Business Process Outsourcing space to service clients with bulk messaging services.	Egyptian acquiree, Giza Systems, expands Solutions' reach to a presence in East and Central Africa as well as the Middle East and the USA. Giza Systems nearly doubles the amount of employees under Solutions' as the aquiree serves over 2,000 clients with a focus on digital transformation.	With a focus on digital transformation and consultancy, Solutions aims to expand its services and product portfolio in alignment with its LEAP strategy.

Source: Company Presentations, AlJazira Capital

Giza Systems & Giza Arabia acquisitions to expand Solutions' geographic reach, human capital, technical, and bottom line

Giza Systems to aid margins as it yields the highest average GP Margins since its consolidation: at Giza Systems boasts an impressive historical revenue growth at a CAGR of 23.1%, and now improved margins after optimizing cost structures with Solutions. Giza Group was acquired for nearly SAR 465.6mn, at an attractive EV/EBITDA valuation of almost 6.6x. The firm aligns itself with Solutions' LEAP goals as it rebranded its corporate image to reflect digital transformation offerings as it engages more with the Saudi Arabian market. As a result, EBITDA margins and NI margins contracted during H1-22 for Giza Systems by nearly 30bps and 160bps (Y/Y) respectively during the rebranding initiative. The firm's focus on heavy asset industries extends Solutions' capabilities into those segments such as oil, telecoms, and utilities at a time where transformation initiatives are in place across those sectors. The average GP margins for Giza, since consolidating with Solutions, have improved nearly 880 bps over the average levels Giza yielded during FY19-21 as Giza's operations are now channeled over Solutions' cost base.

Nearly 60% of Giza Group's exchange rate risk mitigated, with more to become favorable as contracts end: Part of Solutions' integration of Giza Systems was managing the exchange rate risks of the Egyptian services provider. With hedging products in Egypt not being ideal, the firm resorted to restructuring Giza's balance sheet to dollarize the firm and conducting transactions in dollars and Saudi Riyals instead of the volatile Egyptian Pound. Currently, 60% of Giza's revenues are mostly in SAR, and then dollars.

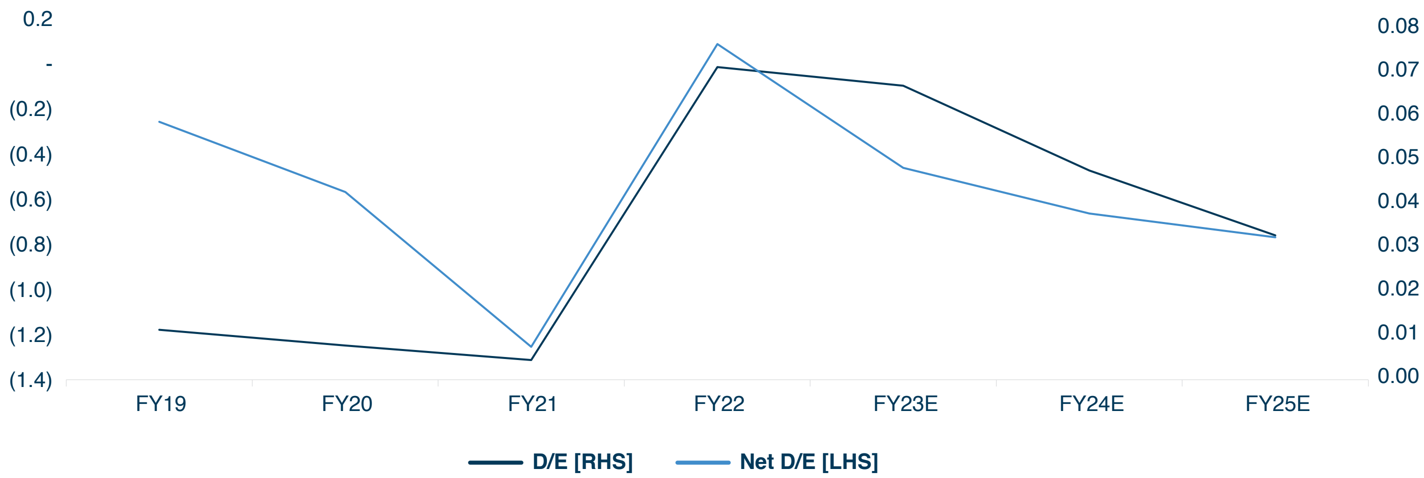
CCC is a part of Solutions' most recent portfolio of acquisitions which extends the firm's operations into providing customer experience services: From customer care and telesales, to other segments in line with Solutions' BPO segment such as recruitment and HR management, CCC is a channel in which the firm is able to service a wider requirement from the economic growth including Quality of Life initiatives. CCC has contributed towards nearly 5.7% of revenues at a GP Margin of 23.4% during H1-23. This market is expected to grow further beyond IDC's estimate of SAR 2.8bn in 2021E as a result of increased government initiatives on Quality of Life programs and digitalizing much of customer experience segments operations and monitoring.

Dovteam acquisition to be a supporter for Solutions' core businesses, at the cost of low margins: 40% of Devoteam Middle East is set to be acquired by Solutions with the aim of expanding Solutions further into the consulting space but also as a channel to funnel projects and engagements to Solutions' other revenue streams. Traditionally, consulting firms globally witness lower net margins (9.0% TTM), including Devoteam ME's parent company Devoteam which from 2004 until it was delisted in 2021 saw its highest NI margin at 6.17%. While we are confident in Solutions' track record of optimizing aquirees, we believe the nature of the business will remain in the low margins as it converts engagements to grow Solutions' other, higher margin segments.

Business expansion plans to be facilitated internally with strong net debt position

With the recent reliance on bank loans to fund the acquisition strategy, the debt-to-equity ratio increased to 0.26x. However, after deducting the cash balance, the net-debt-to-equity ratio stood at -0.67x, enabling it to facilitate its acquisition plan. Should Solutions not engage in another acquisition, we expect repayments to normalize its debt profile.

Fig. 27: Company's debt-to-equity position remains healthy on net debt basis



Source: Company Presentations, AlJazira Capital

Control on the receivable days and lower capex intensity to keep cash conversion healthy

Cash conversion is an underappreciated metric in the KSA's software and service sector, as investors focus more on a company's ability to expand overall growth and margins for re-rating a stock. We believe the cash conversion also plays a key role in gauging the valuation of a company.

Expected credit loss as % of gross trade receivables rose from 2.4% in FY19 to 5.4% in FY22 due to increased exposure to government clients to 50.5% in FY22, thereby leading to a sharp rise in receivable days. However, since then, the company has better managed the receivable days, as the concentration of government clients is nearly 6% down, supporting our expectation of Solutions' receivable days normalizing to the industry mean.

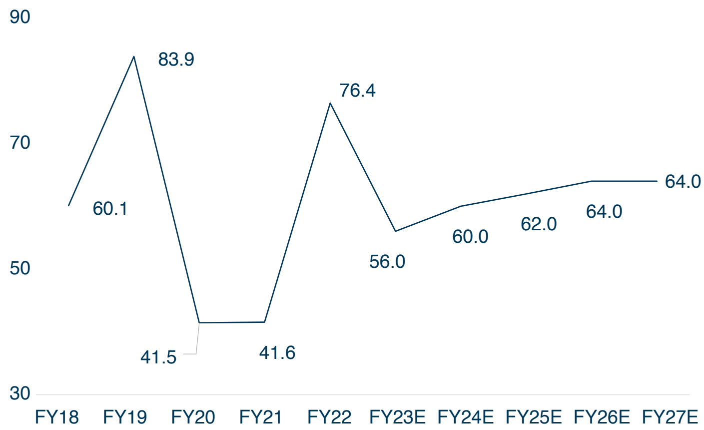
Fig. 28: Increased exposure to government clients impacted receivable days but likely to normalize to the industry mean

SARmn	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E
Gross trade receivable	2,635	2,804	3,021	4,345	4,506	5,003	5,420
Expected credit loss	65	75	211	233	240	263	279
As % of gross trade receivable	2.4%	2.7%	7.0%	5.4%	5.3%	5.3%	5.2%
Receivable days	183	148	153	180	160	155	150

Source: Company Presentations, AlJazira Capital

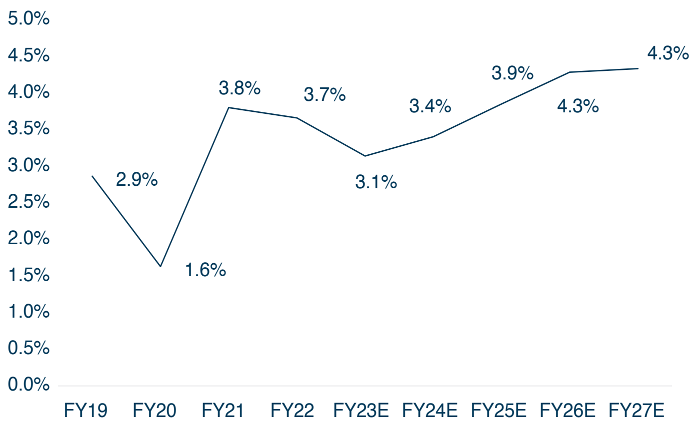
The cash conversion cycle spiked on account of an increase in receivable and inventory days. Nevertheless, going forward, we expect receivable days to improve on increased engagements with private sector enterprises (SMEs), while inventory days could remain elevated on its exposure to asset heavy industries.

Fig. 29: Cash conversion cycle to slightly increase on account of elevated inventory levels



Source: Company Presentations, AlJazira Capital

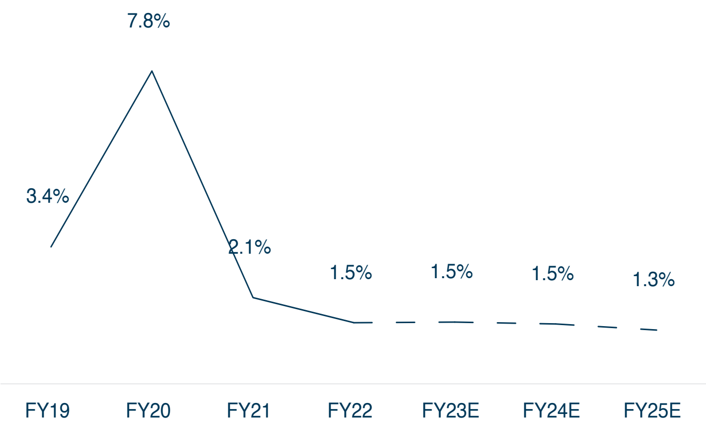
Fig. 30: Inventory levels could remain elevated on exposure to asset heavy enterprises



Source: Company Presentations, AlJazira Capital

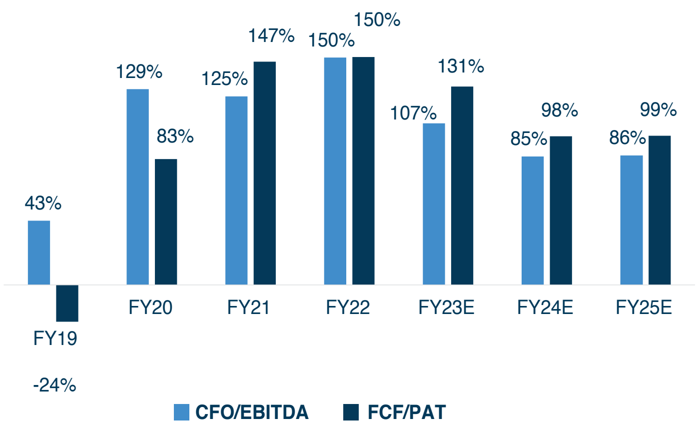
The company's CFO/EBITDA improved from 43% in FY19 to 150% in FY22. Over the said period, CFO posted 125% CAGR, outperformed EBITDA CAGR of 48%. Furthermore, the diminishing capex intensity from 3.4% as a percent of revenue in FY19 to 1.5% in FY22 aided the company in maintaining a healthy FCF/PAT conversion. We expect this momentum to continue despite the acquisition of Dovteam in the pipeline.

Fig. 31: Diminishing capex intensity to continue



Source: Company Presentations, AlJazira Capital

Fig. 32: Healthy momentum of cash conversion likely to continue

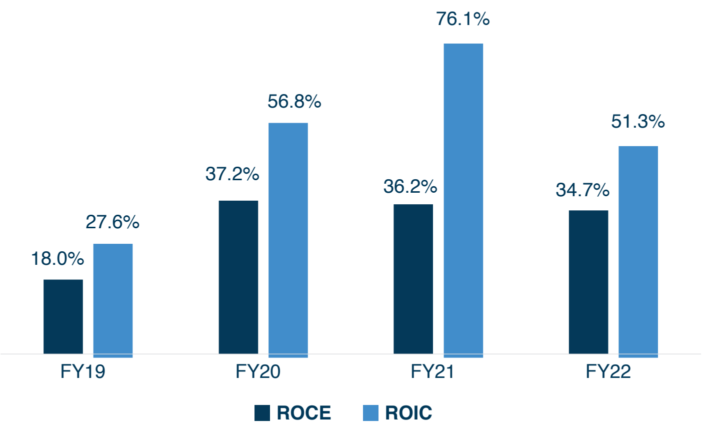


Source: Company Presentations, AlJazira Capital. Note: FCF post-acquisition considered

Attractive return profile coupled with healthy cash flow momentum to support historical dividend payouts

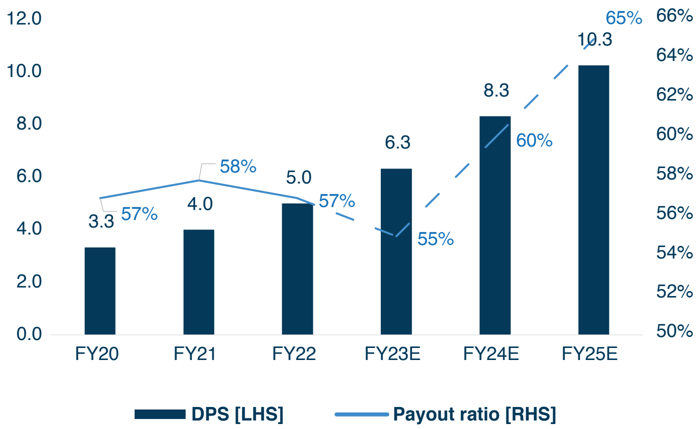
Over FY19-22, the company's efficiency in utilizing the capital employed improved as the ROCE's expanded from 18.0% to 34.7%, supported by ~670bps operating margin expansion to 13.2% in FY22 and reduction in working capital days from 84 to 76. Government spending, increase in private sector audience, and margin accretive acquisitions aided margin expansion over the said period. This attractive return profile, coupled with healthy cash flows, enables the company to maintain its historical dividend payout ratios going forward.

Fig. 33: Margins expansion driving improvement in return profile.



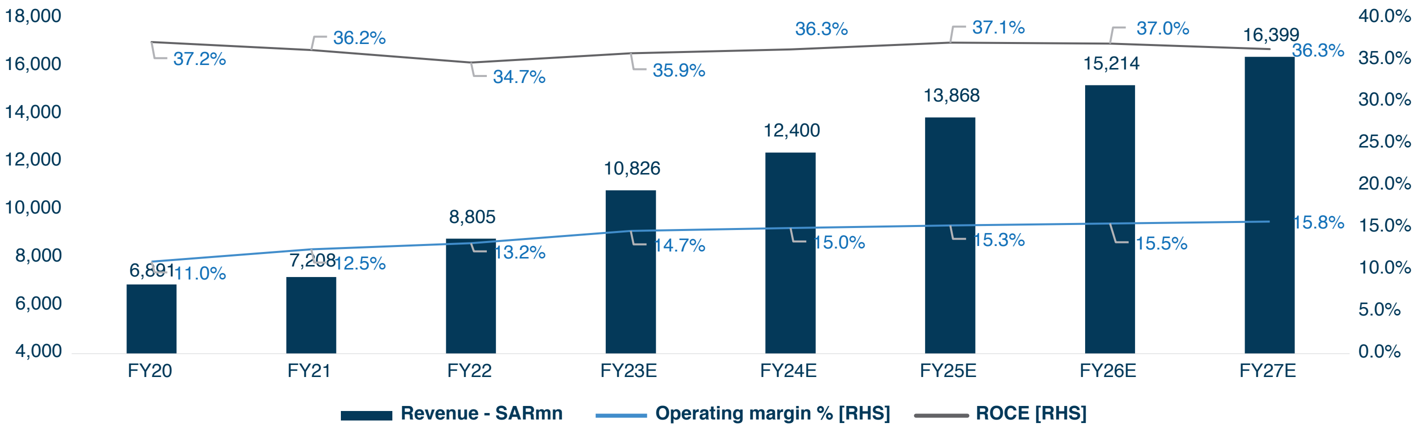
Source: Company Presentations, AlJazira Capital

Fig. 34: Margin is likely to enable the company to sustain its historical dividend payouts



Source: Company Presentations, AlJazira Capital

Fig. 35: Attractive business model and KSA's Vision 2030 benefits to enable 13.2% revenue CAGR over FY22-27E, while turnaround of acquired companies to drive margin and return expansion



Source: Company Presentations, AlJazira Capital

AJC view and Valuation: Solutions has established itself as a prominent entity in the industry, notably due to its association with STC and remarkable growth in both revenue and net income. Over FY17-22, Solutions reported revenue growth of 24.3% and net income CAGR of 13.9% over the said period. Its ROIC expansion from 27.6% in FY19 to 51.3% in FY22 is a testament of the management's efficient capital allocation decisions. We favor Solutions for its a) strong business model and consistent profitability b) long standing relationship with STC and c) strategic position towards Vision 2030 initiatives and SMEs. We expect it to report revenue CAGR of 13.2% over FY22-27E. We are confident in Solutions' abilities to optimally integrate its recent acquisitions (CCC and streamline) as a part of its inorganic growth strategy. We expect operating margins to expand 260bps to 15.8% over FY22-27E, resulting in 16.8% PAT CAGR, but await the ST effects of Dovoteam's integration. We value the stock at **SAR 363.5/share**, implying an upside of 15.8%. We initiate our coverage with an "**Overweight**" recommendation on Solutions as we favor its strong balance sheet in face of its inorganic growth strategy with a proven track record.

Valuation Methodologies

DCF Valuation

We performed DCF valuation based on our forecasts for the next five years. We assumed risk free rate of 3.5%, market risk premium of 5.4% and beta of 0.9 to arrive at WACC of 8.5%. Terminal growth rate is assumed at 3%. Our DCF valuation on Solutions yielded an enterprise value of SAR 43.2bn and fair value to equity shareholders of SAR 45.7bn, which translated into a TP of **SAR 380.7 per share.**

	FY23E	FY24E	FY25E	FY26E	FY27E
NOPAT	1,586.3	1,859.8	2,122.8	2,365.2	2,585.8
Depreciation & Amortization	277.7	295.3	293.0	309.5	323.3
Change in working capital	123.3	437.2	371.2	344.8	253.7
Capex	(174.2)	(190.9)	(190.6)	(192.3)	(193.1)
FCFF	1,813.1	2,401.4	2,596.3	2,827.2	2,969.7
Discounting factor	1.0	0.9	0.8	0.8	0.7
Present value of FCFF	**1,789.4**	**2,173.7**	**2,150.2**	**2,140.5**	**2,054.8**
Sum of the PV					10,308.6
Terminal Value					47,570.6
Enterprise Value					43,520.7
Equity Value to common shareholders					45,976.1
No outstanding shares (mn)					120
Fair value per share					**380.7**

Source: Aljazira Capital Research

Terminal growth rate	WACC 7.50%	8.0%	8.5%	9.0%	9.5%
2.6%	363.61	363.60	363.59	363.58	363.57
2.8%	371.89	371.88	371.87	371.86	371.85
3.0%	380.68	380.67	380.66	380.65	380.64
3.2%	390.04	390.03	390.01	390.00	389.99
3.4%	400.01	400.00	399.99	399.98	399.97

Source: Aljazira Capital Research

Above is an illustration of sensitivity of our DCF valuation to the change assumptions of terminal growth rate (range: 2.6%-3.0%) and WACC (7.5%-9.5%). The sensitivity analysis indicates valuation in the range between a minimum of SAR 363.6 (at terminal growth rate of 2.6% and WACC of 9.5%) and SAR 400 per share (at terminal growth rate of 3.4% and WACC of 7.5%).

Relative Valuation:

We valued Solutions using the relative valuation methodology based on P/E multiple applied to our FY24 estimates.

PE Valuation (E2024):

P/E Valuation (SAR)	
P/E multiple	25
Premium/discount over peers	0%
Implied Market value	41,555.7
Shares (mn)	120.0
Relative value (SAR/share)	**346.3**

Source: Aljazira Capital Research

Valuation Summary	Fair Value	Weight	Weighted Average
DCF	380.4	50.0%	190.2
P/E	346.3	50.0%	173.1
Weighted Avg. 12-month TP			**363.3**
Current Market Price (SAR /share)			315.0
Expected Capital Gain/Loss			**15.8%**

Source: Aljazira Capital Research

We assigned 50% weightage to the DCF valuation, and 50% towards P/E multiples. Based on the combined valuation, we arrived at a TP of **SAR 363.5/share.** The TP indicates a 15.8% upside potential from the current market price.

Upside risks

- Influx of new entities to KSA from government initiatives
- Quicker integration and optimization of aquirees
- Technological disruptions spurring demand
- Quicker ramp up from Mega/Gega projects
- Stronger-than-anticipated demand from newly entered geographies

Downside risks

- Sluggish acquire integration and optimization pressuring costs
- Prolonged inflationary pressure on costs.
- Economic slowdown impacting government expenditure
- Fragmented market presenting competitive domestic or international providers
- Shifting data and technology regulations requiring compliance campaigns

Key Financial Data

Amount in SAR mn, unless otherwise specified	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E	FY26E	FY27E
Income statement											
Revenues	2,962	4,041	5,257	6,891	7,208	8,805	10,826	12,400	13,868	15,214	16,399
Y/Y		**36.4%**	**30.1%**	**31.1%**	**4.6%**	**22.2%**	**23.0%**	**14.5%**	**11.8%**	**9.7%**	**7.8%**
Cost of Sales	(2,048)	(3,076)	(4,410)	(5,469)	(5,500)	(6,794)	(7,933)	(9,043)	(10,086)	(11,032)	(11,857)
Gross profit	**915**	**965**	**847**	**1,422**	**1,708**	**2,011**	**2,893**	**3,357**	**3,782**	**4,182**	**4,543**
Selling, marketing and distribution expenses	(207)	(270)	(350)	(205)	(347)	(246)	(596)	(708)	(790)	(865)	(931)
Administrative expenses	(86)	(113)	(158)	(460)	(462)	(605)	(711)	(790)	(869)	(951)	(1,025)
Finance charges	(3)	-	(3)	(3)	-	(16)	(96)	(72)	(52)	(43)	(37)
Finance income	24	30	16	2	-	54	132	133	116	98	98
Other income	6	6	2	(2)	2	(27)	(40)	(16)	(17)	(19)	(21)
Operating profit	**597**	**608**	**435**	**754**	**901**	**1,172**	**1,584**	**1,907**	**2,171**	**2,403**	**2,629**
Zakat	(48)	(52)	(41)	(52)	(71)	(118)	(204)	(244)	(278)	(308)	(337)
Net income	**550**	**557**	**394**	**702**	**830**	**1,054**	**1,380**	**1,662**	**1,893**	**2,095**	**2,292**
Y/Y	**0.0%**	**1.2%**	**-29.2%**	**78.2%**	**18.3%**	**27.0%**	**31.0%**	**20.4%**	**13.9%**	**10.7%**	**9.4%**
EPS (SAR)	4.6	4.6	3.3	5.8	6.9	8.8	11.5	13.9	15.8	17.5	19.1
DPS (SAR)	-	-	-	3.3	4.0	5.0	6.3	8.3	10.3	11.3	13.4
Balance sheet											
Assets											
Cash & bank balance	596	892	414	993	1,608	544	1,683	1,935	2,357	3,005	3,677
Accounts receivable	977	1,829	2,635	2,804	3,021	4,345	4,506	5,003	5,420	5,751	5,995
Inventories	71	140	151	112	274	322	340	422	534	652	711
Other current assets	1,788	1,399	1,323	1,661	1,544	4,172	4,510	5,023	5,368	5,593	5,791
Property & Equipment	42	102	167	594	551	473	432	383	334	275	208
ROU assets	-	-	77	72	55	41	34	31	28	23	19
Other non-current assets	34	87	110	98	121	385	330	278	227	173	114
Total Assets	**3,508**	**4,450**	**4,877**	**6,335**	**7,173**	**10,282**	**11,835**	**13,074**	**14,268**	**15,473**	**16,515**
Liabilities & owners' equity											
Total current liabilities	2,018	2,659	3,377	4,068	4,634	6,656	7,535	8,184	8,745	9,216	9,562
Total non-current liabilities	92	126	243	343	268	803	848	764	724	714	709
Paid -up capital	100	100	100	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200
Statutory reserves	50	50	50	120	203	309	447	605	605	605	605
Other reserve	-	-	28	(7)	88	9	9	9	9	9	9
Retained earnings	-	-	-	-	(181)	(156)	(156)	(156)	(156)	(156)	(156)
Total owners' equity	1,398	1,665	1,257	1,924	2,271	2,823	3,451	4,125	4,798	5,543	6,243
Total equity & liabilities	**3,508**	**4,450**	**4,877**	**6,335**	**7,173**	**10,282**	**11,835**	**13,074**	**14,268**	**15,473**	**16,515**
Cashflow statement											
Operating activities	668	160	183	1,119	1,380	2,091	1,992	1,831	2,069	2,256	2,495
Investing activities	(555)	436	151	(536)	(155)	(3,190)	(174)	(435)	(285)	(189)	(191)
Financing activities	-	(300)	(813)	(4)	(610)	57	(679)	(1,039)	(1,297)	(1,382)	(1,600)
Change in cash	114	297	(478)	579	615	(1,042)	1,139	358	486	685	704
Ending cash balance	**596**	**892**	**414**	**993**	**1,608**	**546**	**1,683**	**1,935**	**2,357**	**3,005**	**3,677**
Key fundamental ratios											
Liquidity ratios											
Current ratio (x)	1.7	1.6	1.3	1.4	1.4	1.4	1.5	1.5	1.6	1.6	1.7
Quick ratio (x)	1.7	1.5	1.3	1.3	1.3	1.4	1.4	1.5	1.5	1.6	1.6
Profitability ratios											
GP Margin	30.9%	23.9%	16.1%	20.6%	23.7%	22.8%	26.7%	27.1%	27.3%	27.5%	27.7%
Operating Margins	21.0%	14.4%	6.5%	11.0%	12.5%	13.2%	14.7%	15.0%	15.3%	15.5%	15.8%
EBITDA Margin	21.6%	15.5%	8.2%	14.0%	15.4%	15.8%	17.2%	17.4%	17.4%	17.6%	17.7%
Net Margins	18.6%	13.8%	7.5%	10.2%	11.5%	12.0%	12.8%	13.5%	13.7%	13.8%	14.1%
Return on assets	15.7%	12.5%	8.1%	11.1%	11.6%	10.3%	11.7%	12.8%	13.3%	13.6%	14.0%
Return on equity	39.3%	33.4%	31.3%	36.5%	36.6%	37.3%	40.2%	40.5%	39.7%	38.0%	36.9%
Market/valuation ratios											
EV/sales (x)	NA	NA	NA	NA	NA	3.4	3.6	3.1	2.8	2.5	2.3
EV/EBITDA (x)	NA	NA	NA	NA	NA	21.4	20.7	17.8	15.8	14.3	13.1
EPS (SAR)	4.6	4.6	3.3	5.8	6.9	8.8	11.5	13.9	15.8	17.5	19.1
BVPS (SAR)	11.7	13.9	10.5	16.0	18.9	23.5	28.8	34.4	40.0	46.2	52.0
Market price (SAR)*	NA	NA	NA	NA	NA	242.8	315.0	315.0	315.0	315.0	315.0
Market-Cap (SAR mn)	NA	NA	NA	NA	NA	29,136	37,800	37,800	37,800	37,800	37,800
Dividend yield	NA	NA	NA	NA	NA	2.1%	2.0%	2.6%	3.3%	3.6%	4.2%
P/E ratio (x)	NA	NA	NA	NA	NA	27.6	27.4	22.7	20.0	18.0	16.5
P/BV ratio (x)	NA	NA	NA	NA	NA	10.3	11.0	9.2	7.9	6.8	6.1

Source: Company Reports, AJC Research

Elm Co.

Elm's as an investment vehicle offering a hyperactive exposure to the developments in the Saudi economy, is expected to benefit from virtually all developments in the Saudi Arabian economy. We forecast Elm's bottom line to continue growing at a FY22-FY25 CAGR of 30.3% as the Kingdom's initiatives across all facets of economic diversification will directly benefit Elm's organic growth- from increased financial activity, immigration, shipping, among others. Involvement in Healthcare Suite apps and Real Estate are potentials of upside growth for the stock. The announcement on Elm's acquisition of PIF owned THIQA surged the stock price to nearly 70% from announcement to peak, ahead of any disclosed details on THIQA itself. Solid financial position and a cash rich balance sheet is a characteristic of Elm which can further support the firm for any future acquisitions or dividend distribution. We believe the stock price is well ahead of Elm's current growth prospects. We initiate our coverage of Elm with a "Neutral" rating at a TP of SAR 566.5 per share. We highlight THIQA as a possible major upside risk for Elm.

Elm's Digital Business segment expected to pick up momentum to support Elm in the MT. Possibility of turning Smart City projects and other projects into products an upside driver as well: Increased activity in government services, tourism, entertainment, shipping, financial activity, pilgrim activities and immigration amongst others are areas where Elm is directly involved in, through its Digital Business products and services. We expect Elm's other revenue streams to support upselling its DB business, where its most favorable margins are created. We forecast solid fundamentals in the MT for Elm, summarized by FY22-25 revenue CAGR at 20.4% (bottom line CAGR of 30.3% for the same period) driven by favorable economic initiatives within Elm's economic exposure, namely financial activities, tourism (including religious), and e-government services. As well as a backlog of nearly SAR 2.9bn and an average recognition rate of two years. Expected increase in DB supports an anticipated GP margin expansion of 160bps from FY22 to FY24. Government projects across the sectors mentioned as well as privatizations, are expected to support the BPO segment as well, at a 4 year FY22-25 CAGR of 11.4%.

Potential upsides are seeded in various areas across Elm's business. Namely Smart City projects, healthcare, tourism and real estate: Management indicates there is a potential area in visitor experience management as an area to service. Such an engagement could likely be a project initially before possibly becoming a staple wide-use app. Elm also has smart city initiative projects which are also potential breeding grounds to become a product (i.e. a long standing platform). The healthcare sector's privatization is another fertile ground for possible upsides where Elm is involved in managing various projects, as Elm also develops a remote-healthcare service to be offered to hospitals. Elm's healthcare suite platforms such as Wahed (among others), are also in line with the Kingdom's Quality of Life target to have 50% of healthcare consultations to be done via AI technology to add SAR 12bn to the Saudi Arabian GDP. Elm also launched three new Real Estate products in FY22 in line with Quality of life initiatives as well as involvement in the sector through its associate investments.

Solid financial position outshines its peers which expect Elm to continue doing so (in absence of the possible in-the-dark THIQA acquisition): Above average ROAA and ROAE is achieved at an unleveraged balance sheet with a current debt-to-equity ratio of -0.7x. Cash and Murabaha contracts made up nearly 43% (FY22) of total assets held, in a sign of a cash-rich balance sheet which grants Elm the ammunition to facilitate any future expansions or acquisitions internally. We expect that in the event of a large acquisition, Elm could possibly consider for a cash-and-debt method to facilitate the purchase. On the other hand Elm's efficient working capital management if favored for its no-inventory business model and quicker receivable days then payables which leaves Elm at a negative cash conversion of 137 days (FY22). We expect receivable days to further improve however as a result of a less concentration on government clients which is already down 13% Y/Y as of H1-23.

A possible full acquisition of PIF owned THIQA is up in the air with little disclosed on the stock exchange: THIQA offers business services and transformational services for government and private entities through its three business lines A) Digital Solutions services such as market place platforms, and platforms for commercial use. B) Operations Solutions covering financial and logistics management among others, and C) Professional Solutions such as customer experience and project management. The firm's operations are tantamount to Elm's which we believe could be an easy integration into Elm's business model. However, with very little around the possible acquisition, and as it stands in its early stages, we await for further details to assess whether the 70% price increase from announcement to peak is justifiable.

Investment Thesis and Valuation: Elm aligns itself to be the digital enabler of the economy's transformation initiative while boasting an impressive four-year revenue CAGR of 24.36%, led mainly by its Digital Business (DB) segment. With the Vision 2030 initiatives being technologically led, and Elm's technical leadership in the sector and direct involvements in several economic activities, we recognize that the upside risks for Elm's financial performance is possibly significant. Elm's diversified portfolio of activities is likely to make up for losses in other areas- as seen during their involvement in Covid related projects during the economic slowdown led by the pandemic. We forecast ROA and ROE to expand 330bps and 290bps respectively from FY22-25 amid Elm's expected involvement in the Saudi Arabian economic transformation. THIQA is a possible upside to the stock and we await further detail on the possible acquisition. Until then, we initiate our coverage on Elm with a "**Neutral**" recommendation at a target price of **SAR 566.5** per share while a forward PE (FY24) currently sits at 34.9x, summarizing the heightened market valuation seen by Elm.

Recommendation	**Neutral**
Target Price (SAR)	**566.5**
Upside/(Downside)	**-23.7%**

Source: Tadawul Prices as of 30th November 2023

Fig. 36: Key Financials:

(in SAR mn, unless specified)	FY21	FY22	FY23E	FY24E
Revenues	3,827.65	4,606.10	5,802.13	6,949.52
Growth %	55.2%	20.3%	26.0%	19.8%
Gross Profit	1,322.9	1,885.9	2,383.8	2,954.8
Net Income	566.9	930.2	1,334.6	1,706.1
Growth %	91%	64%	43.5%	27.8%
EPS	7.09	11.63	16.7	21.3
DPS	3.0	5.0	7.0	9.4

Source: Company Reports, AlJazira Capital

Fig. 37: Key Ratios

	FY21	FY22	FY23E	FY24E
Gross Margin	34.6%	40.9%	41.1%	42.5%
Net Margin	14.8%	20.2%	23.0%	24.5%
ROE	20.2%	30.5%	34.1%	34.4%
ROA	10.9%	15.4%	17.6%	18.5%
P/E (x)	NA	NA	44.6	34.9
P/B (x)	NA	NA	15.2	12.0
EV/EBITDA (x)	NA	NA	40.2	31.0
Dividend Yield	NA	NA	0.9%	1.3%

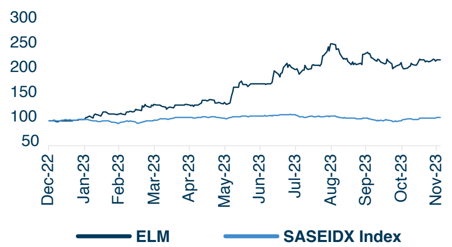
Source: Company reports, Aljazira Capital

Key Market Data

Market Cap(bn)	59.4
YTD%	+124.3%
52 week (High)/(Low)	850/321
Share Outstanding (mn)	80.0

Source: Company Reports, AlJazira Capital

Fig. 38: Price-performance

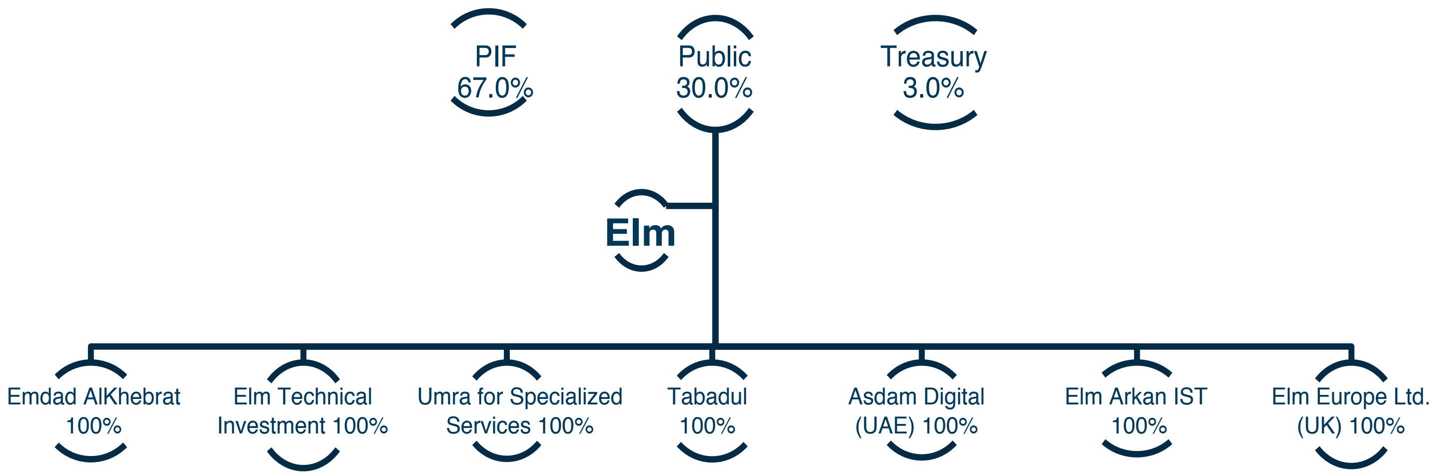


Source: Bloomberg, AlJazira Capital

Company Overview: Elm Operates at the Front Line of All Major Facets of the Economy

Elm IPO'd on the Saudi Main market under the Software & Services sector in February 2022 to offer a hyperactive exposure to Saudi Arabia's economic activity, and is the second largest IT provider in the Kingdom. Previously 100% owned by the PIF, Elm is at the front line of all major economic activities through its 'Digital Business' applications and platforms, as it aims to be the digital enabler for the Kingdom. The frequent-use and wide operations of these platforms make it so that nearly 59.3% of Elm's revenues come from the platforms; Absher, Fasah, Tamm, Muqeem, Yakeen and Nusuk. Which service e-government operations (38mn operations in FY22), shipping, virtual authentication for the financial sector and other public entities, car rental processing, expatriate processes, and Hajj and Umra processes. The PIF owned firm is also active in its Business Process Outsourcing segment, where it offers a multi-dynamic portfolio of services ranging from crowd management to customer experience and financial management to service tourism, Smart City initiatives, Hajj and Umra, and Healthcare among others. Access to data from PIF synergies differentiate Elm from its competition as well, which enables Elm to service sectors such as travel, trade, and pilgrimage.

Ownership Structure



Previously 100% PIF owned, Elm firm was listed with a 30% public offering for 24mn shares and was oversubscribed by 1311%. The firm's strategic relationship with its mother company grants Elm synergies to place it in the front line of the economy, such as its project involvement in Smart City initiatives, wide use Real Estate products commissioned by PIF owned Real Estate Registration Services, and managing AlUla's airport are examples of how Elm is able to etch itself in the deep ridges of the Saudi Arabian economy. This key specification is a differentiator for the firms under our coverage. Notably, Elm acquired Tabadul in 2020 to encapsulate itself further in the logistics and shipping sector which became a top contributor to its revenues. Additionally, Elm has a portfolio of 10 associate firms which it is invested in- all of which are possible upside contributors to Elm, should the services offered by its associate companies, such as a wide-service used car market place, should become staple frequent use platforms.

Business Segments:

Digital Business

- Digital Projects
  - Serviced based revenue with a project timeline
- Digital Products
  - High margin, stand-alone products
  - Revenue based on subscriptions, fees, or partnerships
  - Ability to raise service charges

Business Process Outsourcing

- Inspection and Monitoring
  - Field inspections: fleet management, financical asset monitoring, building managemen
  - Monitoring: crowd contol management, survey data based planning
  - Meqyas: Customer experience managem
- Business Centers
  - Customer and crowd managemnet
- Operational Outsourcing

Proffessional Services

- Consulting
- Advanced Analytics
- Strategic Management
  - Business Transformation
- Digital Consulting

Top Six Platforms:

Top six platforms contribute the most to Elm's revenues. Virtually wholly internally developed, this segment yields a GP Margin of 47.0% (TTM). Should this segment continue to outperform others, Elm's GP Margins will remain buoyant. From top left to right: **Absher** is an e-government platform which is a part of the MoF's budget targets to expand its operations and services even further. **Fasah** is a part of the Tabadul subsidiary to service import and export management, verification and tracking and serviced 28mn operations during 2022. **Tamm** is a car rental insurance and validation program, an unrivalled platform, which serviced nearly 13mn transactions in 2022. **Muqeem** is an expat management platform which serviced the issuance of 1 million iqamas in 2022 and 5mn renewals among other operations. Yaqeen is a validation platform targeting financial services (such as instances when verifying an investor's subscription in an IPO and account creations), the app has an almost monopoly on this service with the exception of the Telecom sector. Yaqeen serviced 2mn operations in 2022. **Nusuk** plans pilgrims Hajj and Umra visits and issues permits for visitors from outside KSA. This app joined the top six contributor list in H1-23 as Hajj and Umra visits nearly doubled Y/Y in FY23.

Strategy:

Pillar 1:	Pillar 2:	Pillar 3:	Pillar 4:	Pillar 5:
Being customer cenric while providing a quality service	Developing digital platforms and solutions for public and private and public entities	Acheiving strategic partnerships based growth or aquisitions	Encouraging innovation and addopting new methods through reseach	Expanding internationally by exporting digital solutions and products

Lean Business Model with Digital Business Focus

Revenue Structure:

Fig 39: TTM Segment Contribution

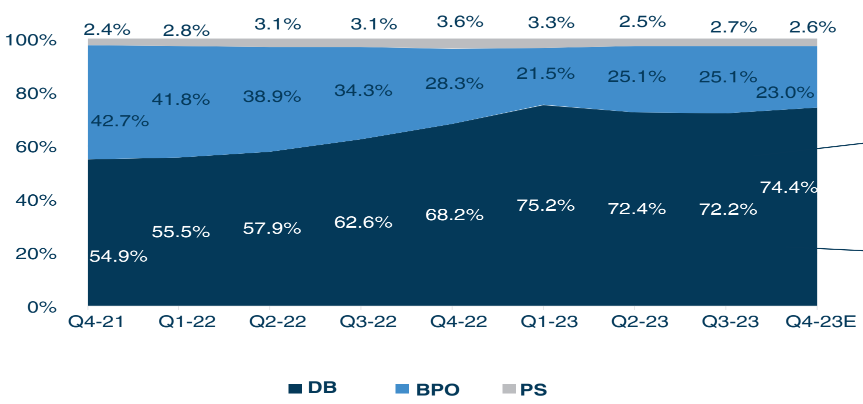
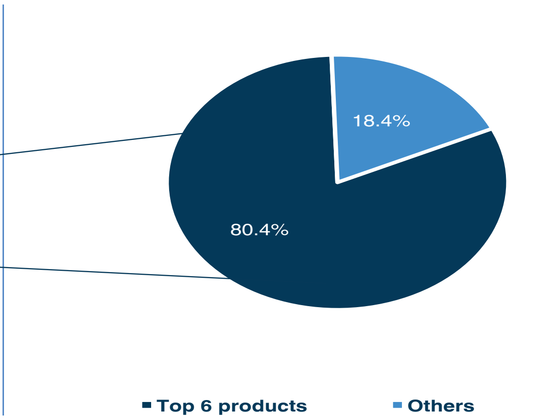


Fig 40: YTD DB Segment Contribution



Source: Company Presentations, AlJazira Capital

Elm's high margin DB segment contributes 72.2% of revenues in Q3-23, led by six products. Expected to remain buoyant as a result of diversified product portfolio to lead the forecasted FY22-25 NI CAGR of 30.27%: DB develops platforms as a project solution for clients, or wide scale use platforms as products charging service fees. Business Processing Outsource (BPO), another major contributor at almost a quarter of revenues, is a channel which with Professional Services (PS) supports the main DB line with upselling solutions from that segment. BPO covers services where Elm manages a client's operations such as monitoring and maintenance or operations and assets, whereas PS is more akin to a consulting line of business. Platforms under DB are also subject to repricing of the service charges. Revenue grew a 24.36% CAGR from FY19-FY22 and we expect revenue growth to remain strong, led by growths in top DB platforms as a result of momentum in entertainment activities, tourism, government, and financial activity from change in base rates and upcoming Saudi Arabian IPO backlog, which Elm also services through the Yaqeen platform. BPO revenues were minor set back by 1% Y/Y (9M-23) as Covid related projects diminish. We believe the segment will close the year at a modest growth driven by high growth momentum in other projects filling the gap Covid related projects left. At a backlog of SAR 2.3bn, we forecast a FY22-25 revenue CAGR of 20.4% with NI at a CAGR of 30.27% supported by favorable margins.

Cost Structure:

Fig. 41: Cost of Revenue Distribution I Revenue (SAR MNs) per Employee

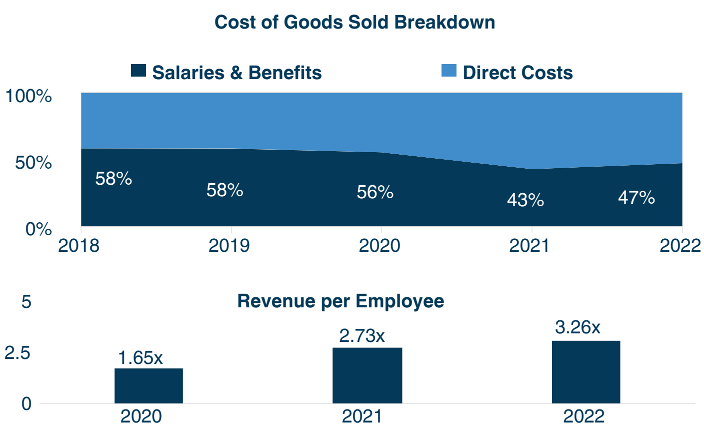
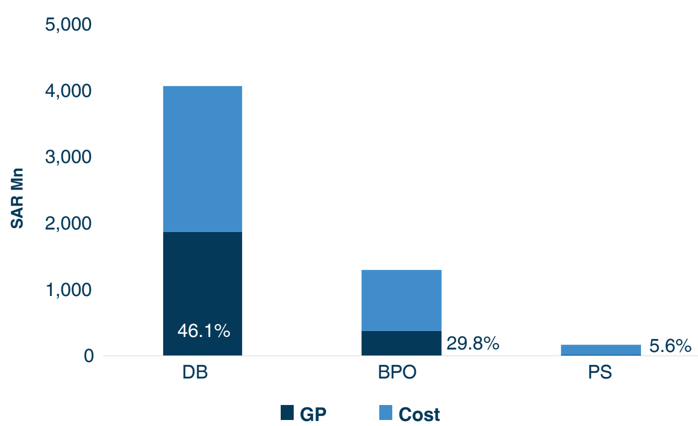


Fig. 42: GP Margin Per Segment (TTM)



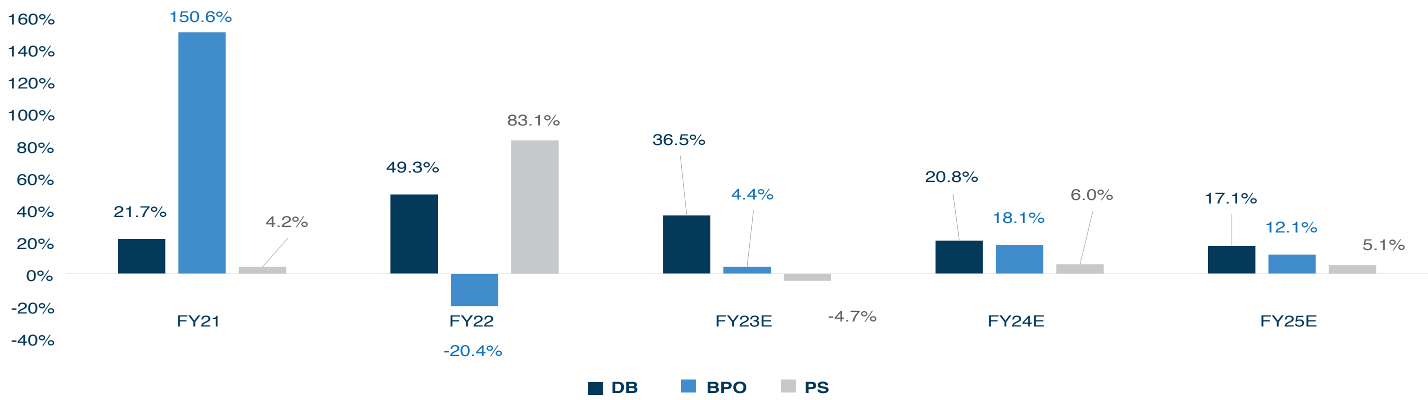
Source: Company Presentations, AlJazira Capital

Acquisition strategy underway with THIQA in the crosshairs

DB and BPO segments are key growth drivers for its overall growth

Elm's DB business contributes 72% of its revenues and exhibited a robust growth with a 27.0% CAGR in revenue from FY19 to FY22. We expect this growth outperformance to continue over FY22-25E with DB segment reporting 24.6% revenue CAGR. This projection is underpinned by the segment's pivotal role as a key beneficiary of increased activities in government services, tourism, entertainment, shipping financial, and pilgrim activities. Moreover, with an impressive gross margin of 49%, this high-margin business is expected to facilitate a 160 basis points gross margin expansion from FY22 to FY24E. Elm's Business Process Outsourcing (BPO) segment is poised for growth, bolstered by substantial projects arising from healthcare initiatives and other potential management contracts aligned with KSA's long-term objectives.

Fig. 43: Business segments' growths

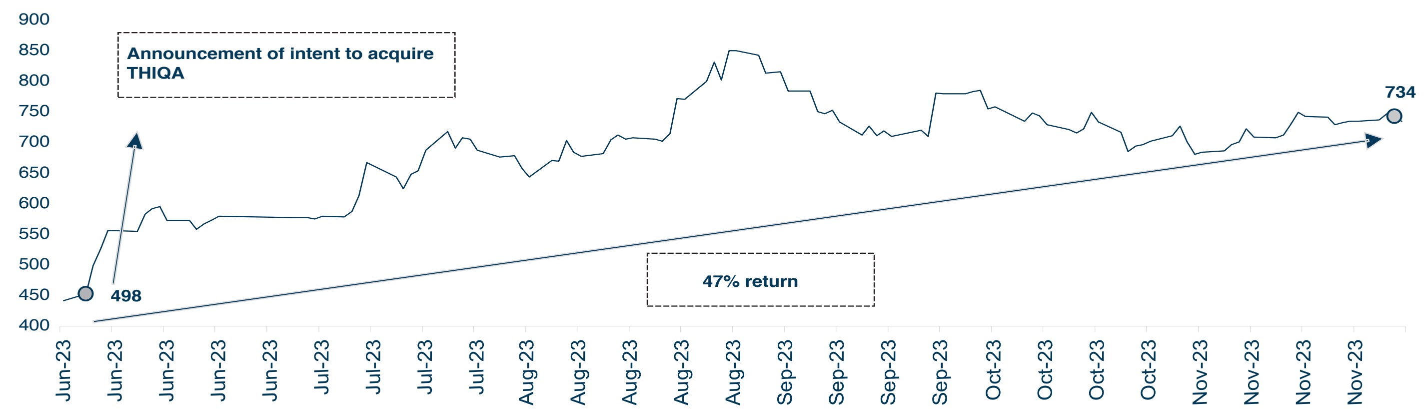


Source: Company Reports, AlJazira Capital

Unlocking THIQA's potential to supplement growth

PIF owned 'THIQA' is under the scope for a possible full-acquisition by Elm, yet very little information is available on the details of the acquisition, yet is a possible upside to the stock. The acquisition will be part of Elm's growth strategy of inorganic growth, to add onto its network of services through THIQA, an e-government services provider. The target company is a leading digital provider in the Kingdom with a focus on government digital transformations. Its operations are synonymous with Elm's- raising a larger possibility of a quick integration with streamlined processes. Elm reports THIQA's talented workforce, complementing products, and prospective revenue shared model. THIQA offers business services and transformational services for government and private entities through its three business lines A) Digital Solutions services such as market place platforms, and platforms for commercial use. B) Operations Solutions covering financial and logistics management among others, and C) Professional Solutions such as customer experience and project management. THIQA also witnessed success cases in its digital business segment through a real estate platform which is reported to have serviced over 25,000 bidders in the Kingdom, as well as a small-business authentication platform which service over 40,000 small businesses. The announcement resulted in a surge of nearly 46.5% from announcement-to-date. Little is disclosed on the acquisition, while the possible transaction's status is currently at an MoU.

Fig. 44: The stock rallied 47% just on acquisition intent announcement; Re-rating potential huge upon unlocking THIQA's potentials



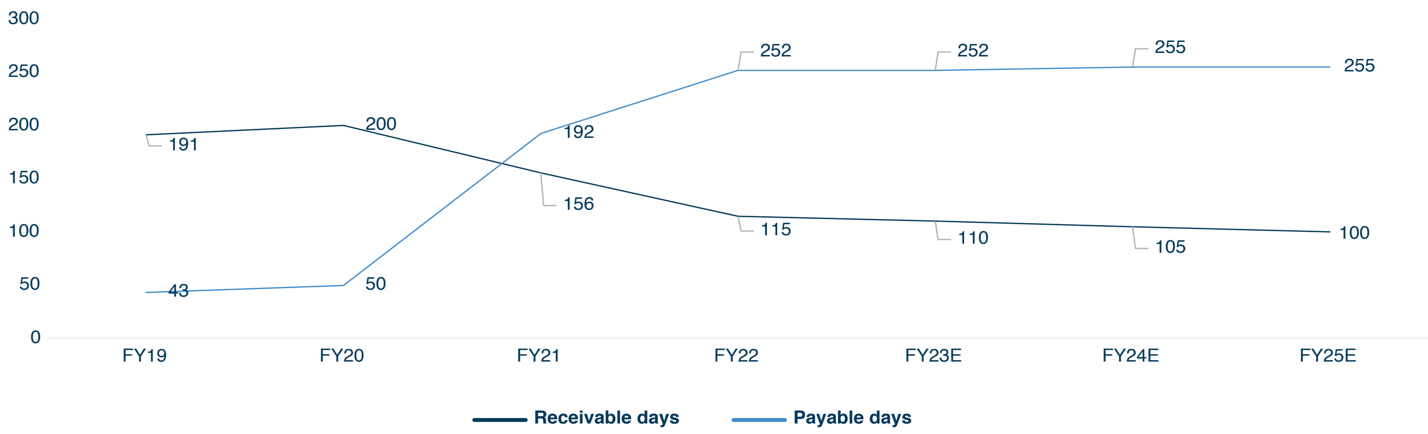
Source: Tadawul, AlJazira Capital

Attractive return profile, healthy cash position to boost existing dividend payout

Increased contribution from DB business segment and reducing government receivables exposure to reduce elevated receivable days

Elevated receivable days is a concern for Elm given the higher skew toward government clients in terms of trade receivables. However, the company has been working toward this and reduced this exposure by 13% in 1H-23. Going forward, we expect these efforts to reduce the exposure to government clients to continue and shall moderate receivable days from 115 in FY22 to 100 in FY25E.

Fig. 45: Moderation in receivable days given company's efforts to reduce exposure to government client receivables



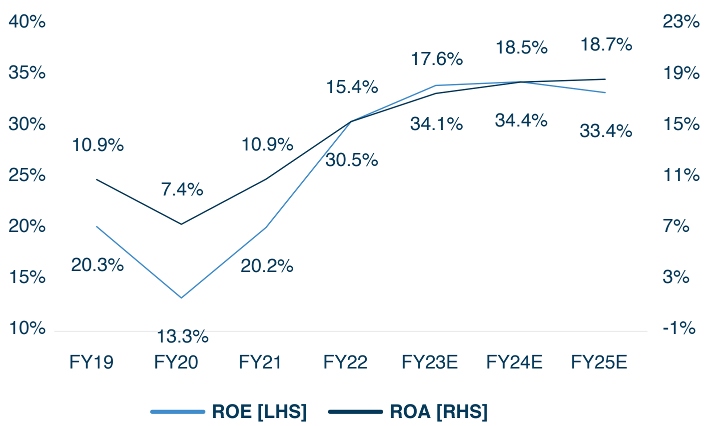
Source: Company reports, AlJazira Capital

Negative cash conversion cycle implies payments advanced quicker and before processing sales costs, as Elm never recorded carrying inventory. DB's business model on subscription or payment-for-services is a catalyst for the speedy collection period seen by Elm. We expect the trend to continue albeit at a slow rate due to the expected growth in the DB segment.

Return and leverage profile for Elm remains attractive: Elm's TTM ROAA at 19.1% is the best among our coverage and outperforms the market average of 7.4%. ROIC expansion from 35% in FY19 to 97% in FY22 is a testament to the company's efficient capital allocation.

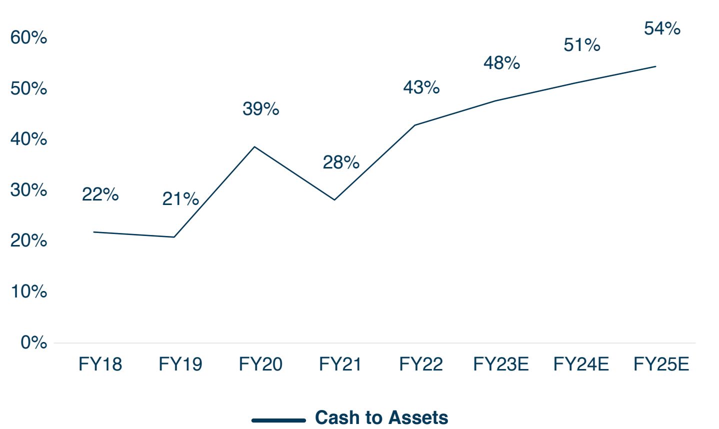
Cash rich financial position enables further expansions: Elm's cash holding (including Murabaha deposits) constitutes 43% of the total assets in FY22, enabling the company to invest in business operations. Operationally, we anticipate the company to leverage debt for significant acquisition plans. In our valuation approach, we consider the inclusion of debt in Elm's corporate structure, given its robust profitability, which is sufficient to cover debt costs.

Fig. 46: Improving return profile indicates efficient capital allocation; momentum likely to continue



Source: Company Reports, AlJazira Capital

Fig. 47: Increasing cash as a % of total asset enables company to depend on internal accruals for business expansion initiatives



Source: Company Reports, AlJazira Capital

Strong cash flow and return profile supports historical dividend payout levels: Elm's cash-rich position, improving return profile, and low capex intensity helps the company maintain the current 43% dividend payout. Furthermore, as the company expands its low-cost digital business segment, we anticipate the possibility of a further increase in the dividend payout ratio.

Fig. 48: Low capex intensity and increasing skew toward low-cost digital business segment to improve the dividend payout ratio

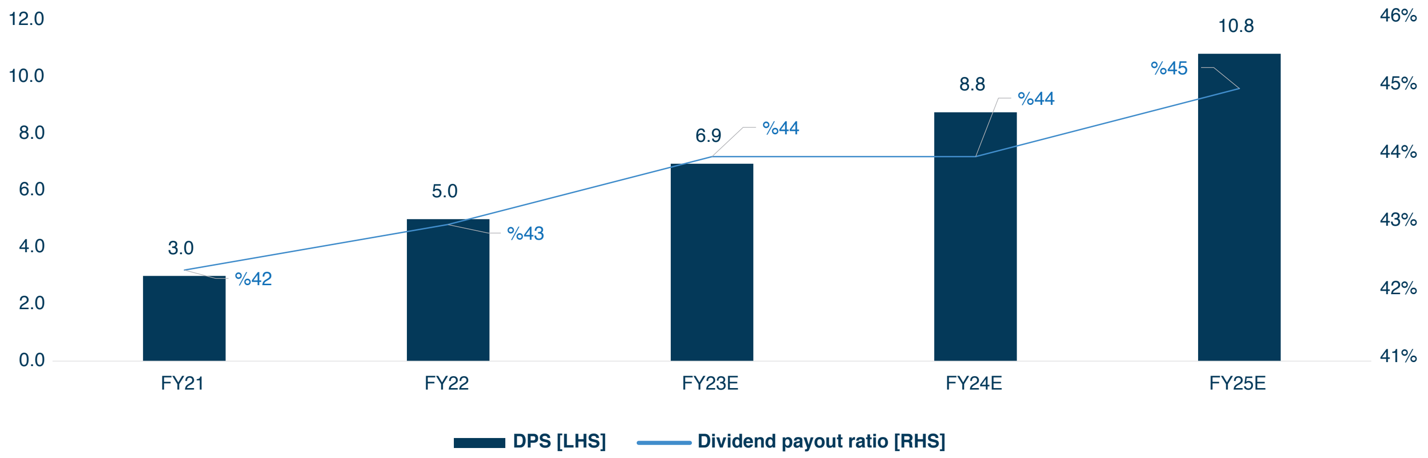
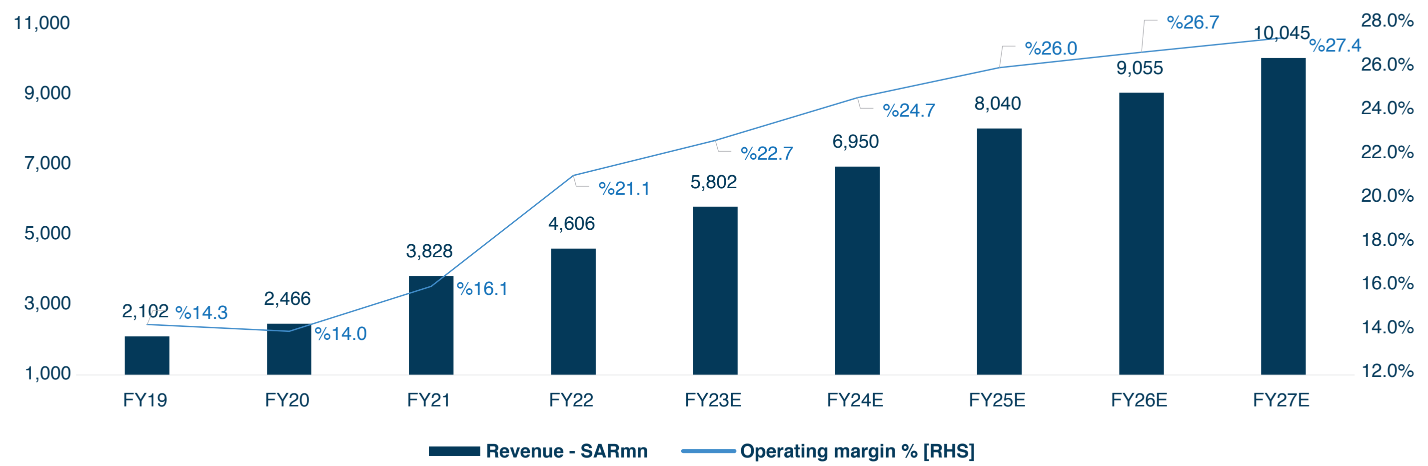


Fig. 49: The digital business and the BPO segment to drive overall revenue CAGR of 16.9% over FY22-27E, while the play of operating leverage and increased revenue contribution from digital business to support margin expansion of 630 basis points to 27.4%, over the said period.



Source: Company reports, AlJazira Capital

AJC view and Valuation: Although the stock has rallied since the company's announcement of its intent to acquire THIQA, we feel the future remains favorable for Elm. We expect the digital business segment, the highest revenue contributor (72%), to outperform other segments with a revenue CAGR of 24.6% over FY22-25E. This segment is likely to be a key beneficiary of the KSA's economic transformation initiatives across government services, tourism, entertainment, shipping financial, and pilgrim activities. We also expect the BPO business to report a revenue CAGR of 11.4% over FY22-25E, benefiting from large-scale projects across healthcare and other long-term initiatives planned for the KSA. Operating leverage play and increased revenue mix to the digital business segment should translate in operating margins expanding by ~490bps to 22.7% over FY22-25E. Further negative working capital requirement and strong cash balance are likely to support business expansion plans. We initiate our coverage with a "**Neutral**" recommendation on Elm at a target price of **SAR 566.5** per share while we await details on the THIQA expansion, as implied PEs stand at 44.6x and 34.9x for FY23 and FY24, respectively.

Valuation Methodologies

DCF Valuation

We performed DCF valuation based on our forecasts for the next five years. We assumed risk free rate of 3.5%, market risk premium of 5.4% and beta of 0.9 to arrive at WACC of 8.7%. Terminal growth rate is assumed at 3%. Our DCF valuation on Elm yielded an enterprise value of SAR 45.6bn and fair value to equity shareholders of SAR 47.96bn, which translated into a TP of **SAR 599.9 per share.**

	FY23E	FY24E	FY25E	FY26E	FY27E
NOPAT	1,318	1,715	2,094	2,421	2,753
Depreciation & Amortization	127	133	143	152	162
Change in working capital	204	61	66	114	132
Capex	(115)	(131)	(139)	(129)	(146)
FCFF	1,534	1,778	2,164	2,558	2,900
Discounting factor	0.98	0.90	0.82	0.75	0.69
Present value of FCFF	**1,514**	**1,614**	**1,806**	**1,963**	**2,047**
Sum of the PV					9,001
Terminal Value					51,898
Enterprise Value					45,859
Equity Value to common shareholders					48,282
No outstanding shares (mn)					80.0
Fair value per share					**599.85**

Source: Aljazira Capital Research

Terminal growth rate	WACC				
	9.90%	**9.60%**	**9.30%**	**9%**	**8.70%**
2.60%	483.7	503.2	524.5	547.8	573.4
2.80%	494.1	514.7	537.1	561.8	588.9
3.00%	505.1	526.8	550.5	576.6	605.5
3.20%	516.7	539.6	564.7	592.5	623.3
3.40%	529.1	553.3	580.0	609.5	642.4

Source: Aljazira Capital Research

Above is an illustration of sensitivity of our DCF valuation to the change assumptions of terminal growth rate (range: 2.6%-3.4%) and WACC (8.7%-9.9%). The sensitivity analysis indicates valuation in the range between a minimum of SAR 483.7 (at terminal growth rate of 2.6% and WACC of 9.9%) and SAR 642.4 per share (at terminal growth rate of 3.4% and WACC of 8.7%).

Relative Valuation:

We valued Elm using the relative valuation methodology based on P/E multiples for global and domestic peers applied to our FY24 estimates.

PE Valuation (E2024):

P/E Valuation (SAR)	
P/E multiple	25
Premium/discount over peers	0%
Implied Market value	42,651.7
Shares (mn)	80.0
Relative value (SAR/share)	**533.1**

Source: Aljazira Capital Research

Valuation Summary	Fair Value	Weight	Weighted Average
DCF	599.8	50.0%	299.9
P/E	533.1	50.0%	266.6
Weighted Avg. 12-month TP			**566.5**
Current Market Price (SAR /share)			744.6
Expected Capital Gain/Loss			**-23.7%**

Source: Aljazira Capital Research

We assigned 50% weightage to the DCF valuation, and 50% each towards P/E multiples. Based on the combined valuation, we arrived at a TP of **SAR 566.5/share.** The TP indicates a -23.7% downside potential from the current market price.

Upside risks

- Influx of new entities to KSA from government initiatives
- Increased activity in government services, tourism, financial activity, shipping, and entertainment activities
- Real Estate Suite, and Healthcare to grow with sector
- Technological disruptions spurring demand
- Successful THIQA acquisition and integration
- Larger government expenditure or speed up in initiatives

Downside risks

- Less government expenditure, or pause on initiatives
- Recessionary environment’s effects on Elm’s services and products
- Revenue mix on margins
- Less travel activity from economic conditions
- Shifting data and technology regulations requiring compliance campaigns

Key Financial Data

Amount in SAR mn, unless otherwise specified	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E	FY26E	FY27E
Income statement										
Revenues	1,926	2,102	2,466	3,828	4,606	5,802.13	6,949.52	8,040	9,055	10,045
Y/Y		**9.2%**	**17.3%**	**55.2%**	**20.3%**	**26.0%**	**19.8%**	**15.7%**	**12.6%**	**10.9%**
Cost of Sales	(1,206)	(1,421)	(1,639)	(2,505)	(2,720)	(3,418)	(3,995)	(4,543)	(5,071)	(5,575)
Gross profit	**719**	**681**	**827**	**1,323**	**1,886**	**2,383.8**	**2,954.8**	**3,497**	**3,984**	**4,470**
Selling and distribution expenses	(70)	(84)	(87)	(197)	(235)	(320)	(384)	(441)	(492)	(541)
Expected credit losses	(5)	-	(35)	(90)	(149)	(141)	(170)	(197)	(222)	(246)
Depreciation and amortization	(68)	(87)	(112)	(116)	(120)	(127)	(133)	(143)	(152)	(162)
General and administrative expenses	(217)	(210)	(247)	(306)	(373)	(477)	(553)	(623)	(697)	(769)
Operating profit	**360**	**301**	**345**	**615**	**972**	**1,318**	**1,715**	**2,094**	**2,421**	**2,753**
Zakat	-	(1)	(66)	(82)	(93)	(118)	(134)	(161)	(185)	(210)
Net income	**365**	**306**	**296**	**567**	**930**	**1,334.6**	**1,706.1**	**2,056**	**2,369**	**2,685**
Y/Y		**-16.1%**	**-3.2%**	**91.4%**	**64.1%**	**43.5%**	**27.8%**	**20.5%**	**15.2%**	**13.4%**
EPS (SAR)	4.6	3.8	3.7	7.1	11.6	16.7	21.3	25.7	29.6	33.6
DPS (SAR)	0.0	0.0	0.0	3.0	5.0	7.0	9.4	11.6	13.3	15.1
Balance sheet										
Assets										
Cash and cash equivalent	194	105	1,013	1,362	589	1,518	2,413	3,628	4,805	6,365
Accounts receivable	1,092	1,116	1,370	1,655	1,465	1,773	2,027	2,233	2,390	2,511
Other current assets	748	999	898	1,375	3,101	3,408	3,878	4,195	4,746	5,091
Property & Equipment	376	355	374	347	353	345	343	348	361	384
Intangible assets	34	19	83	165	180	182	184	173	131	87
Total Assets	**2,455**	**2,812**	**4,013**	**5,194**	**6,026**	**7,576**	**9,213**	**10,970**	**12,857**	**14,896**
Liabilities & owners' equity										
Total current liabilities	978	901	1,375	1,984	2,575	3,208	3,748	4,235	4,704	5,152
Total non-current liabilities	265	401	404	401	404	451	509	576	654	744
Paid -up capital	50	50	50	800	800	800	800	800	800	800
Statutory reserves	25	25	25	(27)	175	308	401	401	401	401
Other reserve	-	-	-	-	(24)	(24)	(24)	(24)	(24)	(24)
Retained earnings	1,137	1,435	1,709	1,955	2,404	3,140	4,086	5,289	6,630	8,131
Total owners' equity	1,212	1,510	2,234	2,810	3,047	3,916	4,955	6,158	7,499	9,000
Total equity & liabilities	**2,455**	**2,812**	**4,013**	**5,194**	**6,026**	**7,576**	**9,213**	**10,970**	**12,857**	**14,896**
Cashflow statement										
Operating activities	479	220	724	598	1,706	1,716	1,961	2,334	2,714	3,071
Investing activities	(369)	(219)	283	(175)	(1,731)	(319)	(396)	(265)	(506)	(325)
Financing activities	(402)	(91)	(98)	(75)	(748)	(468)	(670)	(855)	(1,030)	(1,186)
Change in cash	(292)	(90)	908	349	(774)	929	896	1,214	1,178	1,559
Ending cash balance	**195**	**105**	**1,013**	**1,362**	**589**	**1,518**	**2,413**	**3,628**	**4,805**	**6,365**
Key fundamental ratios										
Liquidity ratios										
Current ratio (x)	2.1	2.5	2.4	2.2	2.0	2.1	2.2	2.4	2.5	2.7
Profitability ratios										
GP Margin	37.4%	32.4%	33.5%	34.6%	40.9%	41.1%	42.5%	43.5%	44.0%	44.5%
Operating Margins	18.7%	14.3%	14.0%	16.1%	21.1%	22.7%	24.7%	26.0%	26.7%	27.4%
EBITDA Margin	22.2%	18.4%	18.5%	19.1%	23.7%	24.9%	26.6%	27.8%	28.4%	29.0%
Net Margins	18.9%	14.5%	12.0%	14.8%	20.2%	23.0%	24.5%	25.6%	26.2%	26.7%
Return on assets	14.9%	10.9%	7.4%	10.9%	15.4%	17.6%	18.5%	18.7%	18.4%	18.0%
Return on equity	30.1%	20.3%	13.3%	20.2%	30.5%	34.1%	34.4%	33.4%	31.6%	29.8%
Market/valuation ratios										
EV/sales (x)	NA	NA	NA	NA	NA	10.1	8.3	7.0	6.1	5.3
EV/EBITDA (x)	NA	NA	NA	NA	NA	40.4	31.1	25.1	21.4	18.3
EPS (SAR)	4.6	3.8	3.7	7.1	11.6	16.7	21.3	25.7	29.6	33.6
BVPS (SAR)	15.2	18.9	27.9	35.1	38.1	49.0	61.9	77.0	93.7	112.5
Market price (SAR)*	NA	NA	NA	NA	NA	747.0	747.0	747.0	747.0	747.0
Market-Cap (SAR mn)	NA	NA	NA	NA	NA	59,760	59,760	59,760	59,760	59,760
Dividend yield	NA	NA	NA	NA	NA	0.9%	1.3%	1.5%	1.8%	2.0%
P/E ratio (x)	NA	NA	NA	NA	NA	44.8	35.0	29.1	25.2	22.3
P/BV ratio (x)	NA	NA	NA	NA	NA	15.3	12.1	9.7	8.0	6.6

Source: Company Reports, AJC Research

Perfect Presentation (2P)

2P reported a notable FY19-22 revenue CAGR of 46.0%, and a 2.9x backlog expansion. The firm has recently added the Managed Services (MS) business line in H1-23 to support its revenue streams as well. We are optimistic about the additions of the new 'Networking' and 'Cybersecurity' segments which are likely to come into effect by Q4-23 to Q1-24. The 'IoT' segment is another source of organic growth that is currently witnessing interest from two major government bodies and one private entity. All segments are expected to kick off by FY24, though earlier inclusions are an upside risk for the stock. Furthermore, the fixed costs for these expansions are largely already incurred, and further salary costs are transferable among segments to support our margins outlook. We revise our target price for 2P in light of the expansions, product diversification, and expected NI CAGR (FY22-25) of 21.82% to SAR 26.0 per share at an "Overweight" recommendation. We consider the stock attractive at current market valuations considering its solid fundamentals.

2P outperformed our covered companies' revenue and NI growth. We expect further growth across all segments going forward: 2P's past three years are categorized by a top line FY19-22 CAGR of 46.0% and a bottom line CAGR of 73.9% for the same period. The Customer Experience segment previously held a slightly larger contribution than the firm's other two segments, yet it was overtaken by the Operations and Maintenance and Software Development segments as they grew 67% and 62.4% Y/Y, respectively, during FY22. We anticipate more growth ahead for all the segments, in addition to the new Managed Services segment, with OPM leading at a 30% growth for FY23. Revenue and NI in the MT are forecasted at FY22-25 CAGR 17.98% and 21.82%

Backlog to expand organically by delayed revenue recognition and new business line expansions: Through the CX segment, and others, 2P expanded its backlog by 2.9x from 2019 to date. Its GP margins expanded at nearly 200bps during the same period, as we also expect the firm to continue expanding its margins by 30 basis points from FY22 until FY25 as much of the firm's fixed costs for its expansions including hirings and developments are incurred, and with more headroom over its current employee base. Our outlook is subject to change once the profitability of the new business lines 'Networking', 'Cyber Security' and 'IoT' become visible, yet we have accounted for it considering the addressable market sizes and management strategy. Support our GP margin forecast is the interchangeableness of talent among the segments, besides each segment's respective specialists.

Expansions to drive growth at an efficient cost: There are around 3 potential engagements in place for the 'Networking' and 'Cyber Security' segments each. IDC expects the current Cybersecurity market size at SAR 1.9bn; management indicates that they will only target 5% of the addressable market from that SAR 1.9bn for the first year. Thus ramp up is likely to be more significant by FY24's end for both Cybersecurity and Networking. Management indicates that the IoT segment and its infrastructures are ready and pending regulatory approvals as the business line requires approvals from several bodies regarding cloud computing and data handling. The segment has however already garnered significant interest from a private entity and two government bodies, which could ramp up the segment quicker than initial expectations, and past the initial addressable market targeted by management.

Solid fundamental's not reflected at current valuations: 2P leads the sector's TTM ROAE at a 48.6% return, as it also sits above the sector median ROAA and posts the most favorable non-net receivable days collections across our coverage. Revenue and NI growths outperformed the sector as well. All despite sitting as the lowest P/E among our coverage.

Investment Thesis and Valuation: 2P boasts an impressive FY22 RoE of 63.6%, above all its peers covered by AJC, and we expect that over performance to continue over the next two years albeit at a normalized rate of 45.1% by FY24. We look forward to the new business lines to contribute more to the firm, as we await the client mix and thus working capital shape-up to further improve as a result of the B2C and B2B "IoT" segment which focuses on integrating smart home products and infrastructures. The business lines are reportedly already witnessing interest, which we consider a promising signal during the pre-kick-off. We revise our target price to **SAR 26.0** per share, at an "**Overweight**" recommendation, mainly in light of the new expansions to come at a fuller swing by FY24, as we take the interest on these segments as a positive signal.

Recommendation	**Overweight**
Target Price (SAR)	**26.0**
Upside/(Downside)	**15.1%**

Source: Tadawul Prices as of 30th November 2023

Fig. 50: Key Financials:

(in SAR mn, unless specified)	FY21	FY22	FY23E	FY24E
Revenues	655	927	1,044	1,279
Growth %	35.9%	41.4%	12.6%	22.5%
Gross Profit	116	180	215	265
Net Income	81	131	136	184
Growth %	25.2%	62.8%	3.2%	35.4%
EPS	0.5	0.9	0.9	1.2
DPS	0.1	0.2	0.3	0.4

Source: Company Reports, AlJazira Capital

Fig. 51: Key Ratios

	FY21	FY22	FY23E	FY24E
Gross Margin	17.7%	19.5%	20.6%	20.7%
Net Margin	12.3%	14.2%	13.0%	14.4%
ROE	59.6%	63.6%	45.1%	45.1%
ROA	19.7%	20.1%	14.2%	15.6%
P/E (x)	NA	20.0x	25.0x	18.4x
P/B (x)	NA	10.4x	9.7x	7.2x
EV/EBITDA (x)	NA	19.1x	20.7x	15.5x
Dividend Yield	NM	1%	1.2%	1.9%

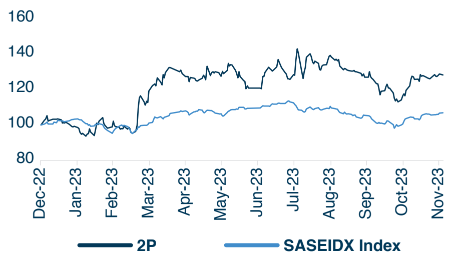
Source: Company reports, Aljazira Capital

Key Market Data

Market Cap(bn)	3.39
YTD%	+28.9%
52 week (High)/(Low)	25.8/13.88
Share Outstanding (mn)	150.0

Source: Company Reports, AlJazira Capital

Fig. 52: Price-performance (Since IPO)



Source: Bloomberg, AlJazira Capital

Business Model and Financial Structure Undergoing Reshaping Amidst a Growing Backlog

Revenue Structure:

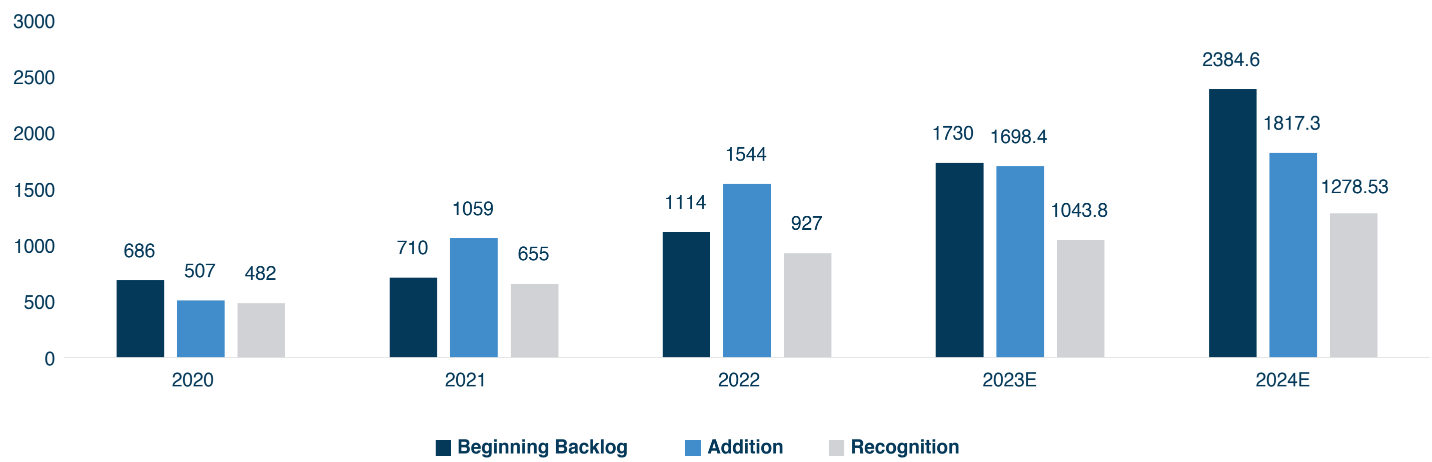
Customer Experience (CX)	Operations & Maintenance (O&M)	Software and Development	Managed Services
• CX systems • AI Chatbots • Technical solutions and feedback management • 'Build, Operate, and Maintain' service for customer support centers	• Curative Maintenance • Preventative maintenance • Managed IT services • Operating IT systems	• Custom program development • Decision Supporting Systems • Products such as: Tarasul, Yamamah & Wesal, among others	• Day-to-day perations management • Consulting • Application management • Help Desk Support • Desktop management

Source: Company Reports, AlJazira Capital

Managed Services to extend the lifeline of contracts under O&M, CX is expected to grow at a slower rate: The MS line is a service leveled agreement contract as opposed to a project based contract, which aims to convert contracts into a longer engagement. As for CX, 2P at one point during 2020 owned 8.1% market share in the customer experience market in KSA- yet 2P is likely to face competition in that segment from new entrants, as well as private entities adopting their own in-house technological solutions for bulk communications and customer experience. O&M, reaping an average of SAR 0.9mn in revenue per contract; and SWD, reaping in an average of SAR 0.94mn per contract are both expected to remain top contributors (in that order) after the CX segment. O&M contracts are in works to be migrated to the MS segment.

Preparations for the Networking and Cybersecurity lines have been incurred during H1-23, and are set to kick off modestly during FY24: Both segments have already engaged in negotiations for 3 contracts, indicating interest on the service offered. The business lines are set to contribute to revenue by Q4-23 to beginning of FY24. While the IoT integration business is expected to kick off by Q1-24 post regulatory approvals. We are optimistic on business lines given the reported interest seen on these segments pre-kick off.

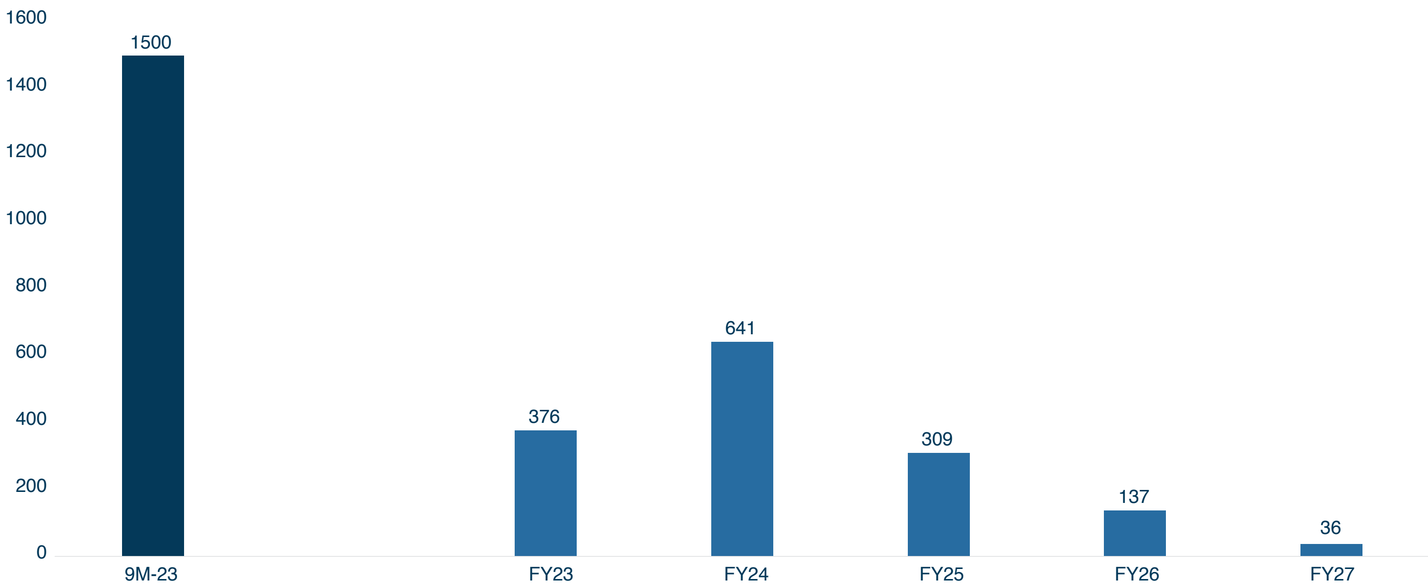
Fig. 53: 2P Backlog Outlook (SAR mn)*



Sources: Company Reports, AlJazira Capital I *Recognition is made after the close of the year.

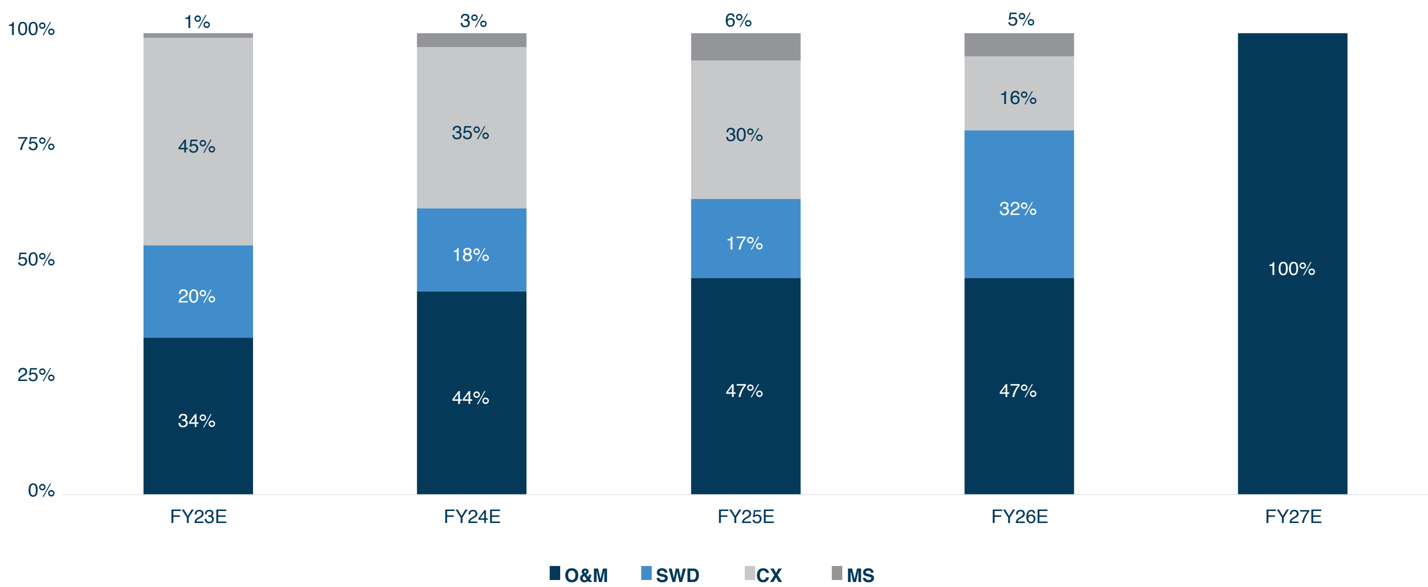
Historically high project bid win rate to bolster 24.4% backlog addition over FY22-25E: From FY19 to date, 2P's backlog orders expanded 2.9x, led by its historically high project bid win rate of 70%. We expect this win rate to continue and enable a 24.4% CAGR in backlog additions over FY22-25E. However, the revenue recognition of these backlogs can vary depending on the contract tenure.

Fig. 54: Current backlog recognition schedule suggests for 24.4% backlog addition growth over the next 3 years



Sources: Company Reports, AlJazira Capital *As per management expectations

Fig. 55: O&M business segment to have highest share of backlog recognition as per the management expectations



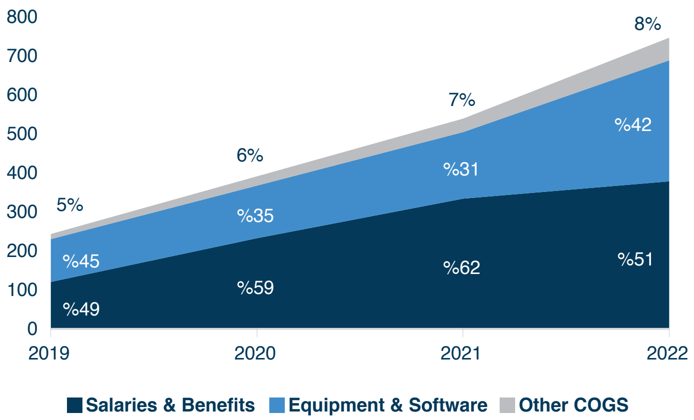
Sources: Company Reports, AlJazira Capital *As per management expectations

Operating leverage to support increase in margin despite expansion into new business lines

Employee benefit expenses account for almost 50% of the cost of goods sold, and the management expects this cost to remain elevated until FY26/27E on additional employee hiring. Costs incurred toward equipment, licenses, and software are the next largest cost item, which we believe will increase faster than employee benefits, given that the new business expansion plans are margin-dilutive in the short term.

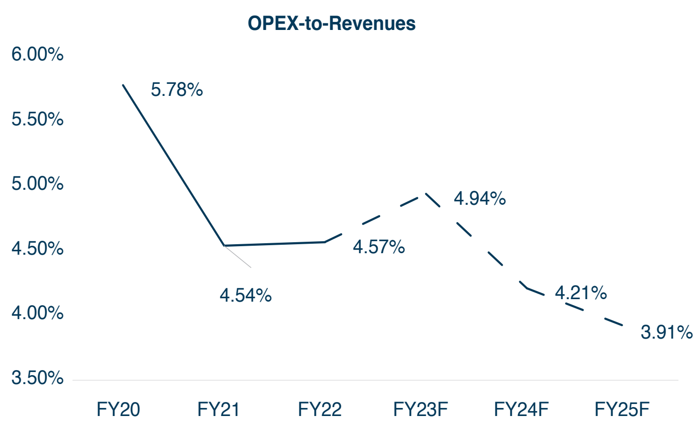
As the company promotes new business lines, especially B2C, we expect the selling and distribution expenses to be largely similar, as expansion into new project lines could require additional marketing efforts.

Fig. 56: Employee benefit and equipment, software cost account for larger chunk of cost of goods sold



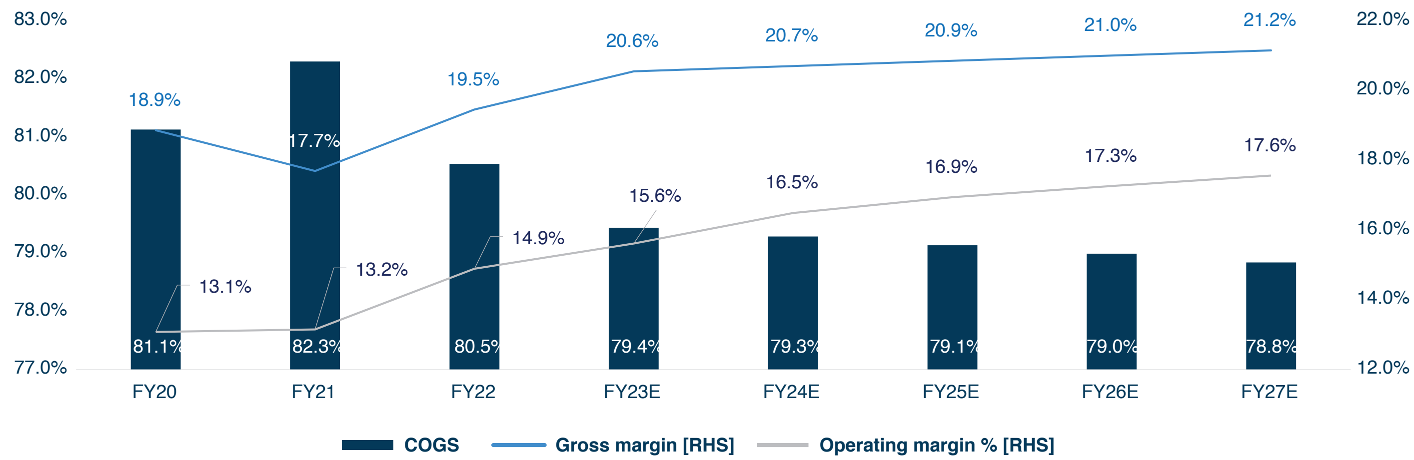
Source: Company Reports, AlJazira Capital

Fig. 57: Expansion into new business lines to increase operating costs in near term, but operating leverage play can lead to a decline



Source: Company Reports, AlJazira Capital

Fig. 58: Gross margins and operating margins to expand 170 and 270 basis points, respectively, over FY22-27E, driven by operating leverage play



Source: Company reports, AlJazira Capital

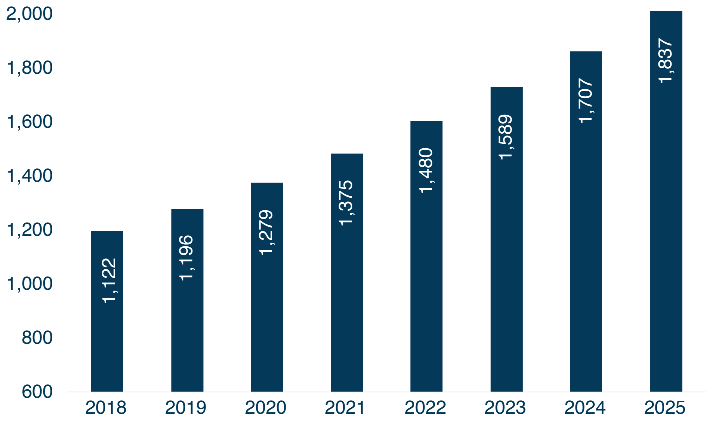
Expansion into cyber security, networking, and IoT to support overall growth story

Foray into new business lines from Q1-24

To expand its service offerings, 2P is expected to foray into three new business lines over Q4-23 to Q1-24. Of these, cybersecurity and networking are expected to be operative right from inception and thus support the overall growth story of 2P.

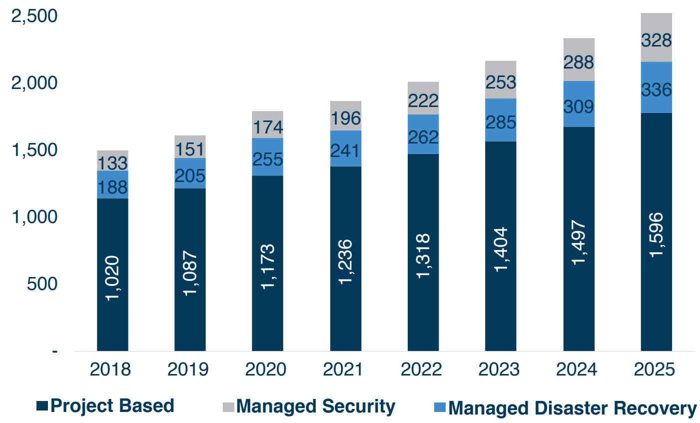
Both these segments will operate on a B2B model and currently have three contracts each in the pipeline. With these segments, the management targets only 5% of the total addressable market during the first year and gradually addresses the remaining market through large contracts. We believe networking and cyber security business lines could possibly add SAR10mn and SAR12mn, respectively, to the backlog in FY23. We arrive at this analysis by assuming 5% of the addressable market and a win rate of 50% with revenue recognition of 3/4th in the first year.

Fig. 59: KSA's B2B cyber security market is expected to post 7.5% CAGR over FY22-25E



Sources: Company Prospectus, AlJazira Capital

Fig. 60: Project-based service accounts for 89% of B2B cyber security and is expected to record 6.6% CAGR over FY22-25E



Sources: Company Prospectus, AlJazira Capital

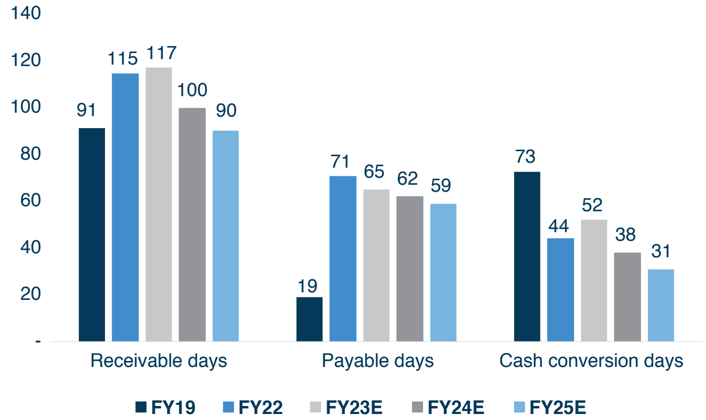
The B2C focused IoT business line could possibly pacify collection periods and diversify 2P's client base: We wish to see the effect of the B2C segment on marketing and selling costs, as we expect the segment to require more efforts on the selling front than its B2B segments, which upsell their services from one B2B segment to the next. The B2C segment will require brand and product awareness at the retail level, which is a different ballpark than selling B2B products through relationships and bidding processes. We expect this segment to modestly challenge costs in the medium term should marketing the segment require more sales efforts. The business, however, could potentially be of more interest to B2B clients, which would, in turn, significantly reduce B2C marketing costs. The segment will not require any inventory as it relates to the integration of IoT products. The line is currently awaiting final regulatory approvals before it is expected to kick off in Q1-24.

Gradual improvement in working capital requirement

2P's recent increased focus on the "build, operate, and maintain" business line will elevate inventory build-up and upfront payments for hardware purchases to keep payable days similar. However, the IoT segment and new business lines, once ramped up could improve the working capital requirement as they focus on private sector and consumer businesses.

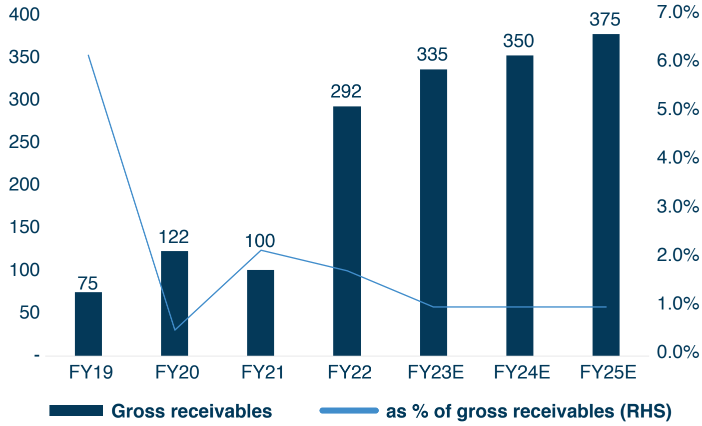
2P enjoys leaner receivable days versus peers with 123 days on TTM basis. Furthermore, its impairment allowance of 1.5% as a % of gross receivables on a three-year average is the lowest among peers.

Fig. 61: Build, operate and maintain business line to elevate the cash conversion days in the short term, but ramping up of new business lines to aid the working capital requirement



Sources: Company Reports, AlJazira Capital

Fig. 62: 2P benefits from lowest expected loss as % of gross receivables, implying management's efforts in improving its collection days

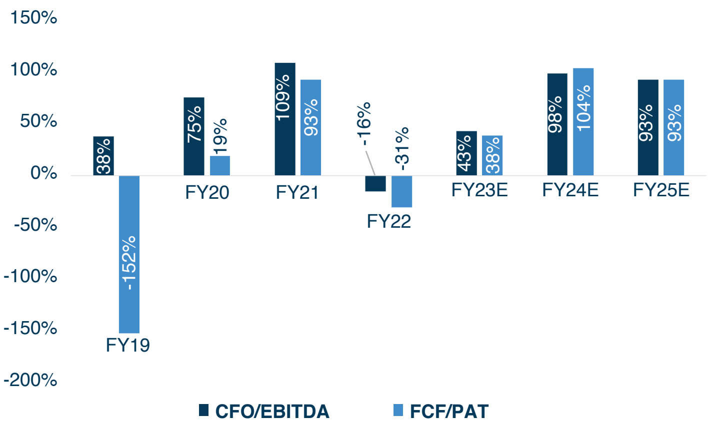


Sources: Company Reports, AlJazira Capital

Working capital efficiency to translate to healthy cash flow position

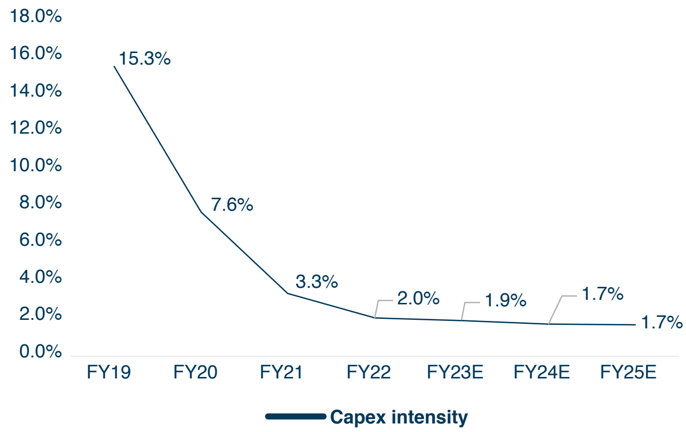
The company improved CFO/EBITDA from 38% in FY19 to 109% in FY21. Over the said period, CFO posted 207% CAGR, outperformed EBITDA CAGR of 82%. Furthermore, the diminishing capex intensity from 3.4% as a % of revenue in FY19 to 1.5% in FY22 aided the company in maintaining healthy FCF/PAT conversion. We expect this momentum to continue and enable 2P to internally facilitate its business expansion plans.

Fig. 63: Efficient management of working capital resulted in improvement in cash conversion metrics



Sources: Company Reports, AlJazira Capital

Fig. 64: While diminishing capex intensity benefiting FCF/PAT conversion

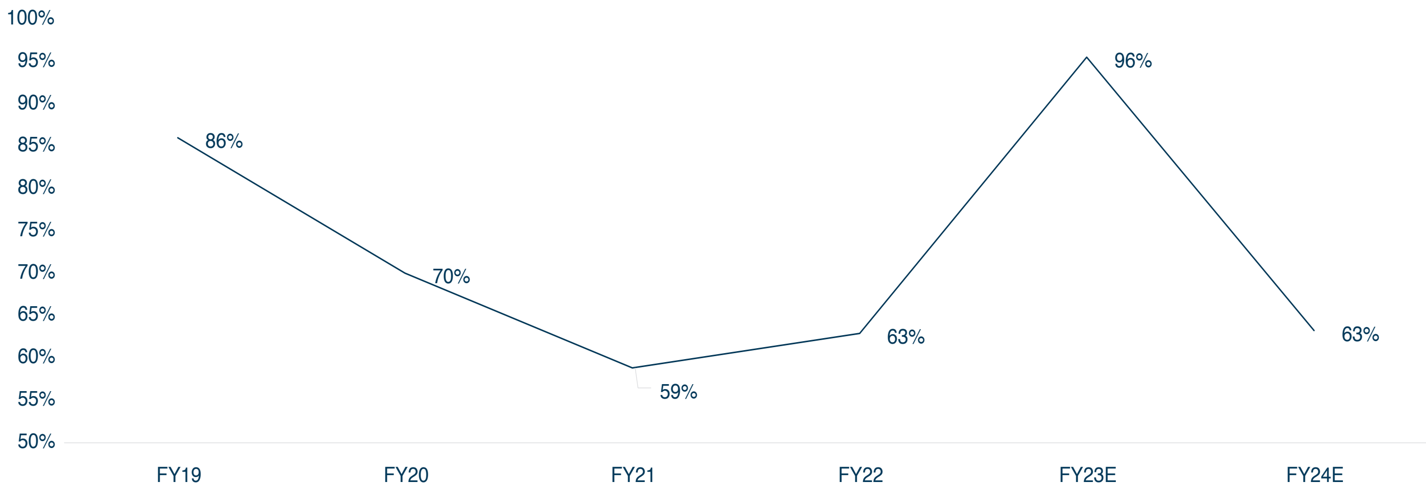


Sources: Company Reports, AlJazira Capital

Elevated debt profile on increased dependency on short-term loans

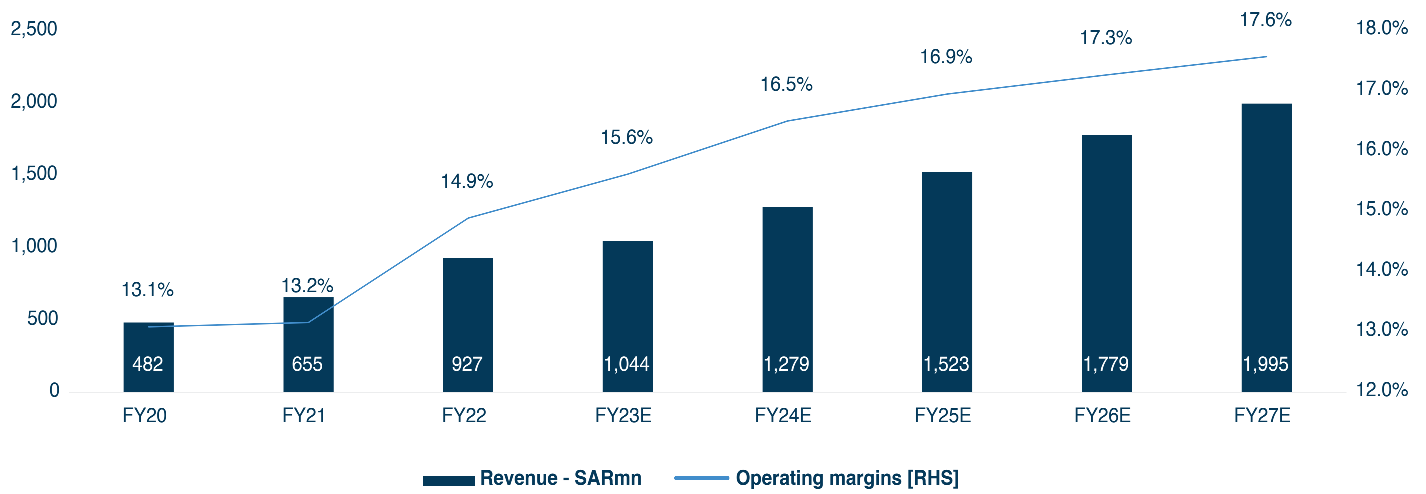
Since FY19, the company's debt-to-equity ratio reduced from 86% to 63% in FY22, but we expect a surge in the ratio in FY23, as the company is expected to foray into new business lines. The ratio is expected to normalize once these business lines ramp up and working capital requirement improves.

Fig. 65: Debt-to-equity to increase on foray into new business lines, before normalizing on business line ramp-ups



Sources: Company Reports, AlJazira Capital

Fig. 66: Revenue to post 16.6% CAGR over FY22-27E, driven by backlog expansions and immediate ramp-up of new business lines. Margins to expand 270bps to 17.6% by FY27E on operating leverage



Sources: Company Reports, AlJazira Capital

AJC view and Valuation: 2P's historical project win rates of 60-70%, 8% market share in customer experience business segment as of 2020, and government engagements in Mega and Giga projects planned establish its backlog addition. We expect the backlog addition to record 24.9% CAGR over the next three years. This, along with the immediate ramp-up of cybersecurity and networking business lines, should aid revenue to register 18% CAGR over FY22-25E. Although the foray into new business lines will pressurize margins over the short term, the operating leverage play should support operating margin expansion by 210bps to 16.9% in FY25E. Despite a TTM receivable days of 126, slightly above the industry average of 154, we consider it reasonable. The IoT segment, with a B2C focus, is anticipated to contribute to moderating receivable days and diversifying from government clients, potentially easing elevated receivable days. Accordingly, we raise our target price on 2P to **SAR 26.0** per share at an "**Overweight**" recommendation considering market valuations summarized by a forward PE of 18.4x (FY24E).

Valuation Methodologies

DCF Valuation

We performed DCF valuation based on our forecasts for the next five years. We assumed risk free rate of 3.5%, market risk premium of 5.4% and beta of 1 to arrive at WACC of 9.3%. Terminal growth rate is assumed at 3%. Our DCF valuation on 2P yielded an enterprise value of SAR 3.85bn and fair value to equity shareholders of SAR 3.9bn, which translated into a TP of **SAR 26.0 per share**.

	FY23E	FY24E	FY25E	FY26E	FY27E
NOPAT	168.8	218.5	267.3	318.1	363.1
Depreciation & Amortization	4.7	5.3	6.0	6.7	7.5
Change in working capital	-71.8	20.1	-1.2	-31.9	-19.2
Capex	-19.8	-21.5	-25.2	-26.3	-29.4
FCFF	81.9	222.3	246.9	266.5	321.9
Discounting factor	0.92	0.84	0.76	0.69	0.62
Present value of FCFF	**74.7**	**184.9**	**187.0**	**182.3**	**198.2**
Sum of the PV					827.1
Terminal Value					4,913.5
Enterprise Value					3,852.3
Equity Value to common shareholders					3,897.6
No outstanding shares (mn)					150.0
Fair value per share					**26.0**

Source: Aljazira Capital Research

Terminal growth rate \ Market Risk Premium	4.4%	4.9%	5.4%	5.9%	5.9%
2.5%	27.61	25.97	24.50	23.18	23.18
2.8%	28.53	26.78	25.22	23.82	23.82
3.0%	29.53	27.65	25.98	24.50	24.50
3.3%	30.62	28.60	26.81	25.22	25.22
3.5%	31.81	29.62	27.70	26.01	26.01

Source: Aljazira Capital Research

Above is an illustration of sensitivity of our DCF valuation to the change assumptions of terminal growth rate (range: 2.5%-3.5%) and market risk premiums (4.4%-5.9%). The sensitivity analysis indicates valuation in the range between a minimum of SAR 23.2 (at terminal growth rate of 2.5% and Risk Premium of %5.9%) and a maximum of SAR 31.8 per share (at terminal growth rate of 3.5% and Risk Premium of 4.4%).

Relative Valuation:

We valued 2P using the relative valuation methodology based on P/E multiple for our FY24 estimates.

PE Valuation (E2024):

P/E Valuation (SAR)	
Sector P/E	22x
Premium/discount over peers	0%
Implied Market value	4,040.6
Shares (mn)	150.0
Relative value (SAR/share)	**26.9**

Source: Aljazira Capital Research

Valuation Summary	Fair Value	Weight	Weighted Average
DCF	26.0	50.0%	13.0
P/E	26.9	50.0%	13.5
Weighted Avg. 12-month TP			**26.0**
Current Market Price (SAR /share)			22.58
Expected Capital Gain/Loss			**15.1%**

Source: Aljazira Capital Research

We assigned 50% weightage to the DCF valuation, and 50% towards P/E multiples. Based on the combined valuation, we arrived at a TP of **SAR 26.0/share.** The TP indicates a 15.1% upside potential from the current market price.

Upside risks

- Influx of new entities to KSA from government initiatives
- Consumer traction on IoT business
- New Managing Services line to channel sales to other segments
- Technological disruptions spurring demand
- Quicker ramp up from Mega/Gega projects
- Larger government expenditure or speed up in initiatives

Downside risks

- Less government expenditure, or pause on initiatives
- Increased competition in the CX market
- Revenue mix on margins (namely in a scenario where MS consulting does not upsell other segments)
- Fragmented market presenting competitive domestic or international providers
- Shifting data and technology regulations requiring compliance campaigns

Key Financial Data

Amount in SARmn, unless otherwise specified	FY19	FY20	FY21	FY22	FY23E	FY24E	FY25E	FY26E	FY27E
Income statement									
Revenues	298	482	655	927	1,044	1,279	1,523	1,779	1,995
Y/Y		**61.8%**	**35.9%**	**41.4%**	**12.6%**	**22.5%**	**19.1%**	**16.8%**	**12.2%**
Cost	(243)	(391)	(539)	(747)	(829)	(1,014)	(1,205)	(1,405)	(1,573)
Gross profit	**55**	**91**	**116**	**180**	**215**	**265**	**318**	**374**	**422**
Operating Expenses									
Selling and distribution expenses	(4)	(5)	(8)	(9)	(9)	(11)	(13)	(15)	(17)
General and administrative expenses	(16)	(20)	(20)	(29)	(32)	(38)	(44)	(49)	(53)
Impairment loss in trade receivables	(10)	(3)	(2)	(4)	(10)	(5)	(3)	(2)	(2)
Operating profit	**25**	**63**	**86**	**138**	**163**	**211**	**258**	**307**	**351**
Y/Y		**155.1%**	**36.6%**	**60.1%**	**18.1%**	**29.4%**	**22.4%**	**19.0%**	**14.1%**
Financing Expense (net)	(2)	(2)	(4)	(4)	(25)	(23)	(14)	(8)	(5)
Other income/expenses	2	5	2	2	2	2	2	2	2
Income before zakat	**24**	**66**	**84**	**136**	**141**	**190**	**246**	**301**	**348**
Zakat	(1)	(2)	(4)	(5)	(5)	(7)	(9)	(11)	(12)
Net income	**23**	**65**	**81**	**131**	**136**	**184**	**238**	**290**	**336**
Y/Y		**179.4%**	**25.2%**	**62.8%**	**3.2%**	**35.4%**	**29.4%**	**22.1%**	**15.6%**
EPS (SAR)	**0.15**	**0.43**	**0.54**	**0.88**	**0.90**	**1.22**	**1.58**	**1.94**	**2.24**
DPS	**0.05**	**0.15**	**0.15**	**0.17**	**0.27**	**0.43**	**0.55**	**0.77**	**0.89**
Balance sheet									
Assets									
Cash & equivalent	3	11	69	67.21	252	342	452	563	709
Other current assets	135	207	314	605.61	699	755	834	944	1,026
Total current assets	138	218	383	672.8	951	1,098	1,286	1,507	1,734
Property plant & equipment	64	98	117	131.12	146	163	182	201	223
Other non-current assets	-	1	2	2.05	2	2	2	2	2
Total assets	**202**	**317**	**501**	**806**	**1,099**	**1,262**	**1,470**	**1,710**	**1,960**
Liabilities & owners' equity									
Total current liabilities	124	182	313	522	718	758	809	873	921
Total non-current liabilities	7	24	28	32	34	37	39	41	41
Paid -up capital	20	20	20	150	150	150	150	150	150
Statutory reserves	3	6	6	13	27	45	69	98	131
Other reserves	7	7	7	-	-	-	-	-	-
Retained earnings	41	78	127	90	171	272	403	548	716
Total owners' equity	71	111	160	254	348	467	622	796	997
Total equity & liabilities	**202**	**317**	**501**	**807**	**1,099**	**1,262**	**1,470**	**1,710**	**1,960**
Cashflow statement									
Operating activities	10	49	97	(22)	72	213	246	268	325
Investing activities	(45)	(37)	(22)	(19)	(20)	(22)	(25)	(26)	(29)
Financing activities	32	(5)	(16)	40	132	(101)	(110)	(131)	(150)
Change in cash	(4)	7	59	(2)	184	90	110	110	146
Ending cash balance	**3**	**11**	**69**	**68**	**252**	**342**	**452**	**563**	**709**
Key fundamental ratios									
Liquidity ratios									
Current ratio (x)	1.1	1.2	1.2	1.3	1.3	1.4	1.6	1.7	1.9
Quick ratio (x)	1.1	1.2	1.2	1.3	1.3	1.4	1.6	1.7	1.9
Profitability ratios									
Gross profit margin	18.4%	18.9%	17.7%	19.5%	20.6%	20.7%	20.9%	21.0%	21.2%
Operating margin	8.3%	13.1%	13.2%	14.9%	15.6%	16.5%	16.9%	17.3%	17.6%
EBITDA margin	9.1%	13.6%	13.6%	15.3%	16.1%	16.9%	17.3%	17.6%	17.9%
Net profit margin	7.7%	13.4%	12.3%	14.2%	13.0%	14.4%	15.6%	16.3%	16.8%
Return on assets	11.4%	24.9%	19.7%	20.1%	14.2%	15.6%	17.4%	18.3%	18.3%
Return on equity	32.7%	71.0%	59.6%	63.6%	45.1%	45.1%	43.7%	41.0%	37.4%
Leverage ratio									
Debt / equity (x)	0.9	0.7	0.6	0.6	95.5%	0.6	0.4	0.3	0.2
Market/valuation ratios									
EV/sales (x)	NM	NM	NM	2.9	3.3	2.6	2.1	1.7	1.5
EV/EBITDA (x)	NM	NM	NM	19.1	20.7	15.5	12.1	9.8	8.1
EPS (SAR)	0.2	0.4	0.5	0.9	0.9	1.2	1.6	1.9	2.2
BVPS (SAR)	0.5	0.7	1.1	1.7	2.3	3.1	4.1	5.3	6.6
Market price (SAR)*	NM	NM	NM	17.52	22.58	22.58	22.58	22.58	22.58
Market-Cap (SAR mn)	NM	NM	NM	2,628	3,387	3,387	3,387	3,387	3,387
P/E ratio (x)	NM	NM	NM	20.0	25.0	18.4	14.3	11.7	10.1
P/BV ratio (x)	NM	NM	NM	10.4	9.7	7.2	5.4	4.3	3.4

Source: Company Reports, AJC Research

الجزيرة كابيتال
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RESEARCH DIVISION

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RATING TERMINOLOGY

1. Overweight: This rating implies that the stock is currently trading at a discount to its 12 months price target. Stocks rated "Overweight" will typically provide an upside potential of over 10% from the current price levels over next twelve months.
2. Underweight: This rating implies that the stock is currently trading at a premium to its 12 months price target. Stocks rated "Underweight" would typically decline by over 10% from the current price levels over next twelve months.
3. Neutral: The rating implies that the stock is trading in the proximate range of its 12 months price target. Stocks rated "Neutral" is expected to stagnate within +/- 10% range from the current price levels over next twelve months.
4. Suspension of rating or rating on hold (SR/RH): This basically implies suspension of a rating pending further analysis of a material change in the fundamentals of the company.

Disclaimer