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## SYS: 2QCY24 EPS to clock in at PKR 6.5, up 34% YoY

### Systems Limited

PSX: SYS | Bloomberg: SYS PA | Reuters: SYSE.PSX

- **Dec-24 PT of PKR 501/share, with a potential upside of 18.4%:** We maintain a 'BUY' rating on Systems Limited, with a blended price target (PT) of PKR 501. The stock offers an upside potential of 18.4% with a dividend yield of 1.2%, translating into a total return of 19.6%. SYS is expected to benefit from strategic partnerships and the growing demand in the Middle East and APAC regions, partly due to the demand spurt from UAE's 2031 and KSA's 2030 Vision. In addition, initiation of the rate cut cycle by Fed in Sep-2024, will also serve as a trigger for stimulating topline growth in North America.
- **2QCY24 EPS expected at PKR 6.53:** We expect SYS to post in 2Q24 EPS of PKR 6.53, up 34.2% YoY, driven by a stable increase in North America (5% YoY) and continued growth in the Middle East and APAC (15% and 45% YoY, respectively). Local revenues are expected to experience muted growth as the company is undergoing a transitional period due to a shift in focus from government and small private clients towards private sector enterprise clients.
- **Margins to gradually recover from next year:** Reduction of PKR cost exposure from 80% in CY21 to 60% in CY23 to attract foreign talent and achieve scale in the overseas markets combined with a sharp increase in wage inflation has translated into a decline in gross margins from the 2018-23 average of 30% to 23% in 1QCY24. The high base induced downward adjustment to the inflation trajectory would provide support to the gross margins post 2024.

Summary	CY21A	CY22A	CY23A	CY24F	CY25F	CY26F
EPS	16.21	23.6	29.9	28.5	39.5	54.3
EPS YoY	-8.9%	45.7%	26.4%	-4.6%	38.7%	37.5%
DPS	3.5	5.0	5.0	5.7	7.9	10.9
BVPS	12.5	16.3	22.2	23.5	21.0	19.2
PER	36.1	22.8	15.8	17.6	12.7	9.2
Div. Yield	0.4%	0.5%	1.1%	1.2%	1.6%	2.2%
P/B	30.0	28.6	19.8	21.3	23.9	26.0
ROE	43.7%	37.9%	31.4%	23.3%	26.4%	29.0%

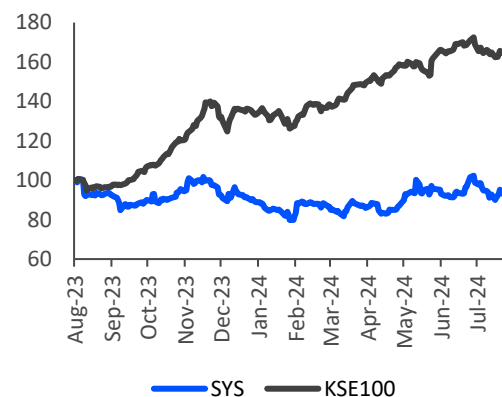
Source: Company Accounts, Akseer Research

### Key Data

PSX Ticker	PSX
Target Price (PKR)	501
Current Price (PKR)	423
Upside/(Downside) (%)	+18.4%
Dividend Yield (%)	1.2%
Total Return (%)	19.6%
12-month High (PKR)	468
12-month Low (PKR)	371
Outstanding Shares (mn)	291
Market Cap (PKR mn)	123,129

Source: PSX, Akseer Research

### Price Performance



Source: PSX, Akseer Research

### Dec-24 PT of PKR 501/share, with a potential upside of 18.4%

Our Dec-24 PT of PKR 501/share for SYS offers a 18.4% upside from the current price and a total return of 19.6%, including a 1.2% dividend yield. We have valued SYS using a blended valuation approach, incorporating equal weightage of 50% to both the FCFE-DCF valuation and the P/E multiple-based valuation. Our DCF valuation yields a PT of PKR 498.9/share, based on a risk-free rate of 15.0%, a market risk premium of 6.0%, and a beta of 1.1, resulting in a cost of equity of 20.6%.

For relative valuation, we determined a PT of PKR 502.2/share by applying a premium of 3.5x over the KSE-100's P/E. This premium was calculated by assigning equal weightages to the average IT sector premium of 8 regional countries relative to their market indices and SYS's premium over the market.

### 2QCY24 EPS expected at PKR 6.53

We expect SYS to report a 2QCY24 EPS of PKR 6.53, reflecting a 34.2% YoY increase, bringing the 1HCY24 EPS to PKR 11.9 and representing a 41.3% YoY decline primarily due to the absence of exchange gain. To note the company recorded a hefty exchange gain of PKR 2.4bn in 1QCY23. Revenue from the Middle East is expected to increase by 15.0% YoY, driven by the persistent demand for digital banking in the region, as exhibited by the recent agreements with Oman Housing Bank and to operate CMD (Temenos) within APAC (banking software - product of subsidiary NDC Tech). We project revenue from North America to grow modestly by 5.0% YoY, consistent with the growth recorded in 1QCY24.

Financial Estimates (PKR 'Mn)	2QFY23	2QFY24	YoY	1HFY23	1HFY24	YoY
Sales	12,490	15,979	28%	23,189	31,173	34%
Cost of Sales	9,022	12,183	35%	16,931	23,874	41%
<b>Gross Profit</b>	<b>3,468</b>	<b>3,795</b>	<b>9%</b>	<b>6,259</b>	<b>7,299</b>	<b>17%</b>
Admin expenses	1,059	1,165	10%	1,844	2,273	23%
Distribution expenses	489	455	-7%	835	888	6%
Impairment losses	270	87	-68%	221	66	-70%
Other expenses	-	-	-	-	-	-
<b>EBIT</b>	<b>1,651</b>	<b>2,089</b>	<b>26%</b>	<b>3,359</b>	<b>4,073</b>	<b>21%</b>
Other income	286	115	-60%	2,838	59	-98%
Finance cost	251	142	-44%	408	290	-29%
Share from associate	-113	-8	93%	-223	-28	87%
<b>Profit before tax</b>	<b>1,573</b>	<b>2,054</b>	<b>31%</b>	<b>5,566</b>	<b>3,814</b>	<b>-31%</b>
EPS	4.9	6.5	34%	18.2	11.9	-35%

Source: Company Accounts, Akseer Research

### **Middle East growth plan pinned to KSA's V-2030 and UAE's V-2031**

Middle East emerged as the largest contributor to revenue from a geographic standpoint in CY23. The region contributed 55% to the company's revenues and reflected a considerable 3Y CAGR of 123%. The current positioning allows SYS to align itself with the upcoming growth spurt under KSA's Vision 2030 and UAE's Vision 2031. In particular, the introduction of 'Financial Infrastructure Transformation (FIT)' program to enhance the financial services sector and promotion of digital transactions in the UAE and 'Financial Sector Development Program' in Saudi Arabia aiming to achieve a similar objective will provide the company an opportunity to closely align itself in realizing the set objectives under the respective sovereign transformation plans. We expect, the strategic alliance with Temenos to act as a fulcrum in this regard and supplement the growth from Middle East. BFSI represented 29% of the topline and is expected to help Middle East maintain leadership position in terms of topline contributor for SYS.

### **Margins to gradually recover from next year**

SYS reduced its proportion of Pakistan-based workforce to 86% in CY23, down from 93% in CY21, resulting in lower PKR-denominated costs. Pakistan based cost has decreased from 80% in CY21 to 60% in CY23. This shift, combined with the considerable increase in domestic inflation drove up the salary expenses, pressuring margins to 23% in 1QCY24 from the historical 5Y average of ~30%. We expect margins to remain under pressure for the remainder of the year, projecting an average gross margin of 24.2% for the rest of 2024. However, with local inflation easing from a peak of 38.0% in May 2023 to 11.1% recently, we expect margins to gradually improve beyond CY24 as inflation levels adjust downwards. Our estimates are based on PKR devaluation of 6.5% (annual) post 2024 which should support SYS's gross margins as 95% of its revenue are dollar-denominated.

### **Company Description**

Systems Limited is a public limited company incorporated in Pakistan under the Companies Act, 2017. The company is principally engaged in the business of software development, trading of software and business process outsourcing services. SYS operates in 5 regions, including North America, the Middle East & Africa, Europe, APAC, and Pakistan.

Income Statement (PKR mn)	FY22	FY23	FY24E	FY25F	FY26F	FY27F
Net sales	31,760	53,435	66,908	80,528	97,269	117,841
Cost of sales	23,124	-39,779	-50,894	-60,356	-71,721	-85,872
<b>Gross profit</b>	<b>8,636</b>	<b>13,657</b>	<b>16,014</b>	<b>20,172</b>	<b>25,548</b>	<b>31,970</b>
Opex	-3,273	-5,924	-7,072	-8,616	-9,755	-11,814
<b>Operating profit</b>	<b>5,363</b>	<b>7,733</b>	<b>8,942</b>	<b>11,556</b>	<b>15,793</b>	<b>20,156</b>
Other income	2,230	3,194	702	1,267	1,463	1,452
Other charges	-324	-778	-44	-8	7	22
Finance cost	-288	-869	-583	-441	-300	-273
<b>Profit before tax</b>	<b>6,981</b>	<b>9,280</b>	<b>9,016</b>	<b>12,374</b>	<b>16,963</b>	<b>21,357</b>
Taxation	-352	-591	-717	-865	-1132	-1392
<b>Profit after tax</b>	<b>6,630</b>	<b>8,689</b>	<b>8,299</b>	<b>11,509</b>	<b>15,830</b>	<b>19,965</b>

Source: Company Accounts, Akseer Research

Balance sheet (PKR mn)	FY22	FY23	FY24E	FY25F	FY26F	FY27F
Fixed Assets	11,486	14,904	14,837	14,682	14,795	14,721
Other LT assets	2,564	2,246	2,209	2,216	2,206	2,237
<b>Non-current assets</b>	<b>14,051</b>	<b>17,151</b>	<b>17,046</b>	<b>16,898</b>	<b>17,001</b>	<b>16,958</b>
Current assets	24,275	33,515	39,047	49,106	66,453	85,844
<b>Total assets</b>	<b>38,326</b>	<b>50,666</b>	<b>56,093</b>	<b>66,004</b>	<b>83,454</b>	<b>102,803</b>
Non-current liabilities	1,995	2,966	2,170	1,987	1,840	1,766
Current liabilities	13,403	15,369	14,865	15,751	20,684	24,134
<b>Total liabilities</b>	<b>15,397</b>	<b>18,335</b>	<b>17,035</b>	<b>17,739</b>	<b>22,525</b>	<b>25,900</b>
<b>Equity</b>	<b>22,928</b>	<b>32,332</b>	<b>39,058</b>	<b>48,265</b>	<b>60,930</b>	<b>76,902</b>
<b>Total equity &amp; liabilities</b>	<b>38,326</b>	<b>50,666</b>	<b>56,093</b>	<b>66,004</b>	<b>83,454</b>	<b>102,803</b>

Source: Company Accounts, Akseer Research

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