

Recommendation	Buy
Current Market Price (SAR)	314.80
52wk High / Low (SAR)	392.20/216.80
Mkt. Cap. (USD/SAR Mn)	10,067/37,776
Shares Outstanding (mn)	120.0
Free Float (%)	20%
3m Average Vol. (000)	167.8
3m Avg Daily Turnover (SAR'000)	57,707.2
Dividend Yield '23e (%)	2.7%
P/E'23e (x)	22.4
EV/EBITDA'23e (x)	15.0

Source: Bloomberg

We initiate coverage on Arabian Internet and Communications Services Co. (Solutions) and assign a 'BUY' rating with a target price of SAR 357.9/sh., offering an upside of 13.7%. The stock currently trades at FY23e P/E of 22.4x.

The rapid upward trend in the top line is expected to continue, driven by a strong industry growth outlook and favorable macroeconomic conditions

The Information and Communications Technology (ICT) market in the KSA is projected to experience robust growth, with a CAGR of 8-10% expected during FY22-27, driven by increasing demand for technology solutions aimed at enhancing business efficiency. This is particularly beneficial for major IT companies like Solutions, which currently holds a solid market share of ~21% as of FY22. Additionally, Solutions boasts a portfolio of over 150 prominent global IT suppliers, catering to various sectors including healthcare, education, tourism, mega-projects, and smart cities. The company is well-aligned with the Kingdom's long-term digital transformation objectives. Furthermore, Solutions' ongoing acquisition of new projects, with more than 200 signed during 1H23, is poised to support its organic business growth. Coupled with inorganic growth resulting from acquisitions and a substantial revenue contribution from its strategic partner, the Saudi Telecom Company (STC), this sets the stage for Solutions to achieve a revenue CAGR of ~15% during FY22-27e.

Margins continue to improve in the coming years

Solutions has witnessed substantial growth in its profit margins since FY19, and we expect this favorable trajectory to extend into the future. This positive momentum can be primarily attributed to the company's effective implementation of its LEAP strategy, which has resulted in enhanced internal efficiencies. Accordingly, we expect the company's operating margins to improve from ~13% in FY22 to ~16% in FY27e while net margin from ~12% in FY22 to ~15% in FY27e.

Robust cash flow generation, and low debt obligations to enable the company to actively pursue its inorganic growth strategy

Solutions has adopted an asset-light business model, maintaining consistently low capital expenditure requirements, which have remained at ~1-2% of revenue over the past two years. Looking ahead, the company is expected to maintain similar capex levels, in line with the guidance provided by the management for FY23e. This, combined with sustainable profitability growth, is anticipated to result in strong free cash flow generation throughout the forecast period. Furthermore, Solutions' low leverage, indicated by a debt-to-equity ratio of just 0.3x, places it in an advantageous position for expanding its business operations in the MENA region.

Healthy dividend payouts

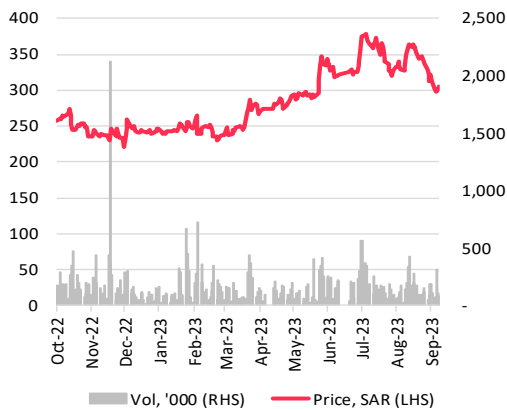
The company has a track record of consistently providing healthy dividend payouts to its shareholders. In FY22, shareholders received a dividend of SAR 5.0 per share (57% payout ratio). Looking ahead in the medium term, the company is projected to continue this trend, aided by its strong cash flow visibility. This consistent dividend policy is likely to be appealing to income-seeking investors.

Key Indicators

Year	FY20	FY21	FY22	FY23e	FY24e	FY25e
Revenues (SAR mn)	6,891	7,208	8,805	10,715	12,471	14,094
Net income (SAR mn)	702	833	1,053	1,302	1,638	1,999
Gross margin	20.6%	23.7%	22.8%	24.0%	24.5%	25.0%
Net profit margin	10.2%	11.6%	12.0%	12.2%	13.1%	14.2%
RoE	44.1%	39.7%	41.6%	42.6%	44.8%	45.3%
DPS (SAR/share)	3.3	4.0	5.0	6.5	8.0	9.8
P/E (x)	11.6x	27.1x	27.7x	22.4x	17.8x	14.6x
EV/EBITDA (x)	8.3x	18.9x	19.5x	15.0x	11.8x	9.3x

Source: Company Reports, Yaqaen Capital

Price Volume Performance



Price to EPS



Major Shareholders (%)

Saudi Telcom Company	79.00%
Arabian Internet & Com	1.00%
Vangaurd Group	0.71%
Blackrock	0.57%
Canadian Imperial Bank	0.13%
Govt Pension Investment Fund	0.11%
FMR LLC	0.09%

Source: Bloomberg, Yaqaen Capital

Valuation Summary

We arrived at the target price on the stock using a blend of DCF and relative valuation. For DCF, we have used a 5-year explicit forecast period (2023-27), terminal growth rate of 2%, and weighted average cost of capital (WACC) of 10.2%. For relative valuation, we have used average 1 year forward P/E multiple and FY24e EPS to arrive at the fair value estimate. We assigned equal weightings to fair values derived using DCF and relative valuations, to arrive at a target price of SAR 357.9.

DCF Method		FY23e	FY24e	FY25e	FY26e	FY27e
	27-09-2023	31-12-2023	31-12-2024	31-12-2025	31-12-2026	31-12-2027
No. of days		95	461	826	1,191	1,556
Time Remaining (Years)		0.26	1.26	2.26	3.26	4.26
Operating profit Before Interest and Tax		1,468	1,811	2,172	2,480	2,806
growth(%)			23%	20%	14%	13%
Tax rate		10%	10%	10%	10%	10%
Post-tax operating profit (NOPAT)		1,321	1,630	1,955	2,232	2,525
Add: Depreciation & amortization		265	295	344	387	428
Less: Change in working capital		157	491	531	566	924
Less: Capex		-284	-330	-373	-322	-313
Free Cash Flow to Firm		1,459	2,086	2,457	2,864	3,564
Discount factor		0.97	0.88	0.80	0.73	0.66
PV of Free Cash Flows		1,423	1,845	1,971	2,084	2,353
Sum of present values of FCFs		9,676				

Free cash flow (t+1)	3,636
Terminal value	44,171
Present value of terminal value	29,161

		Inputs	
EV	38,836	Valuation Date	27-09-2023
Less:		Risk free rate (Rf)	4.3%
Debt	-744	Adjusted Beta	0.85
Minority Interest	-27	Market Risk Premium (Rm-Rf)	7.0%
Employee Retirement Benefits	-400	Cost of Equity (Ke)	10.2%
Add:		Terminal or perpetual growth rate (g)	2.0%
Cash and Bank Balances	2,635	Pre-tax Cost of Debt	12.0%
Equity Investment		Effective Tax rate	10.0%
Equity value	40,300	After-tax Cost of Debt	10.8%
Fair value per share (SAR)	336	D/D+E	0.0%
Upside/Downside	6.7%	WACC	10.2%
Current Price	315		

Relative Valuation

EPS 2023e (SAR)	10.85
Target P/E multiple (x)	35.0x
Target price per share (SAR) - P/E Multiple	379.87

Valuation Method	Fair Value per share (SAR)	Weightage	Weighted value per share (SAR)	Upside/downside
DCF Valuation	336	50%	168	7%
Relative Valuation - P/E	380	50%	190	21%
Fair Value (SAR)			357.9	
CMP (SAR)			315	
Upside/(Downside)			13.7%	

Source: Company Reports, Bloomberg, Yaqeen Capital

Key Charts

Fig. 1: Saudi economy to grow moderately post strong FY22

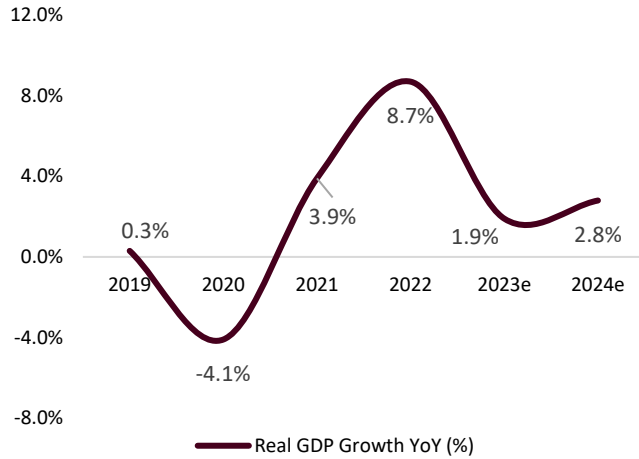


Fig. 2: IT Sector Expected to Sustain Strong Growth Trajectory

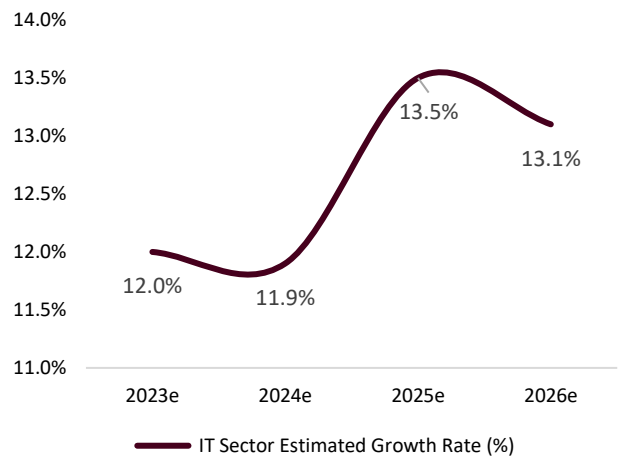


Fig. 3: IT Services are expected to push overall ICT sector growth

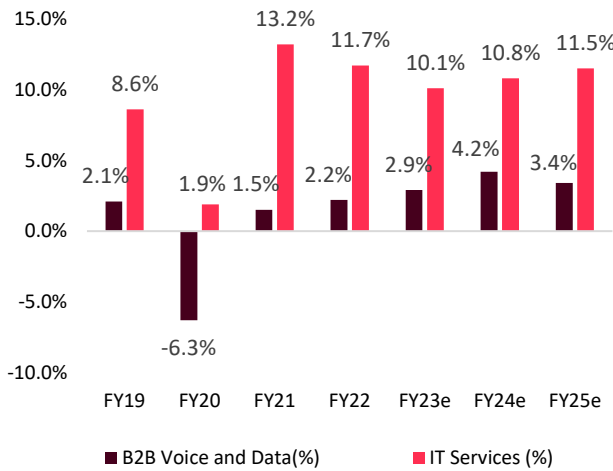


Fig. 4: KSA Lags Behind GCC Peers in Per Capita Data Storage Capacity

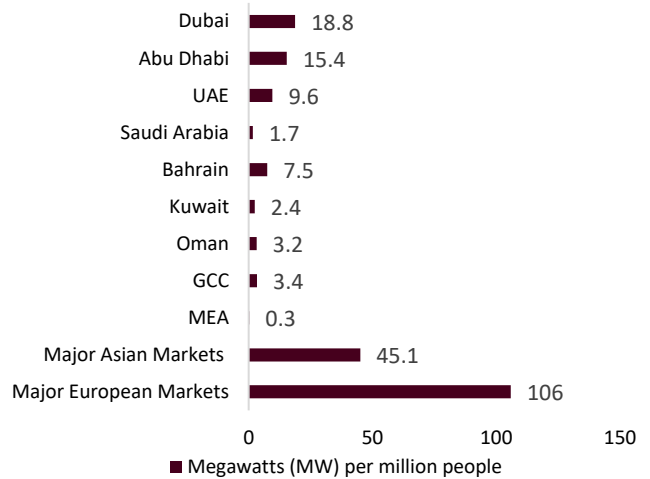


Fig. 5: IoT is expected to rise the most in its segment

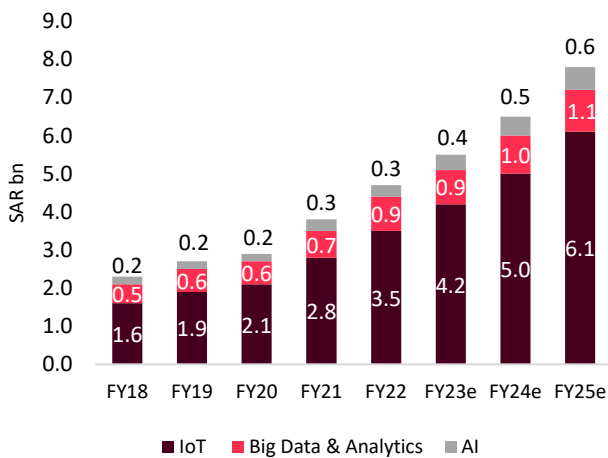
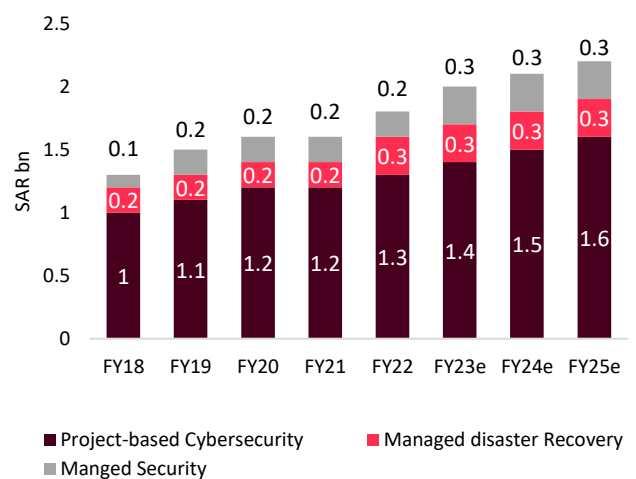


Fig. 6: As Technology Advances, Cyber Threats rise



Source: Company Reports, GASTAT, Yaqeen Capital

Fig. 7: Double-Digit Growth Projected to Continue in Revenue

Fig. 8: Segment Wise Revenue

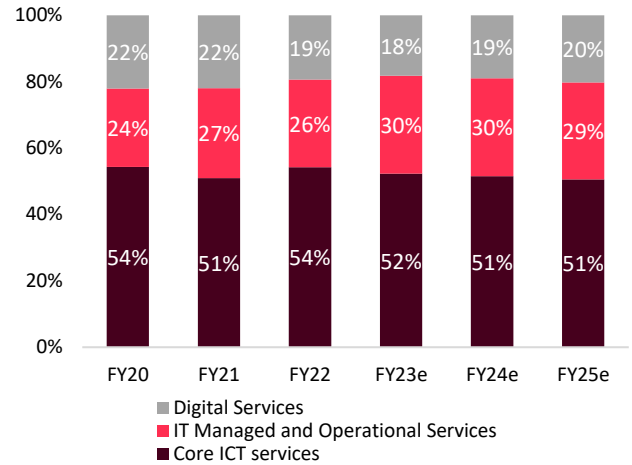
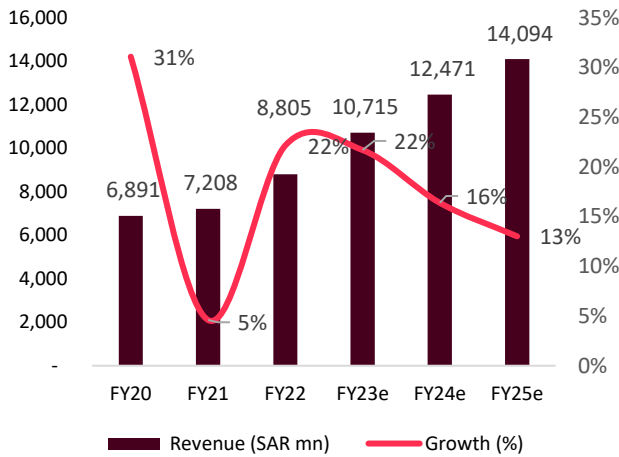


Fig. 9: Margins seen largely in an uptrend

Fig. 10: ROA, ROE, Asset Turnover

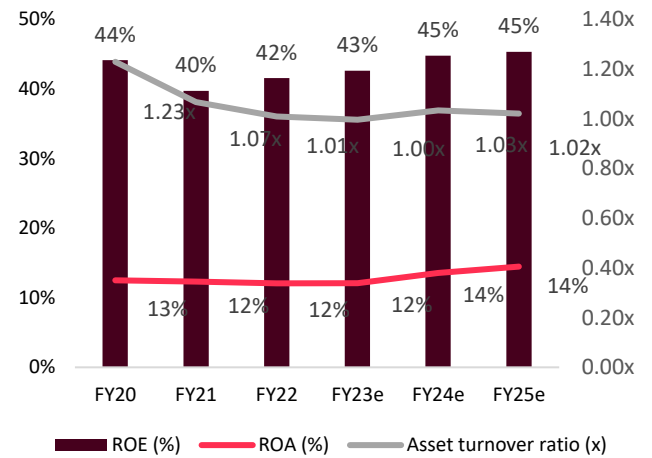
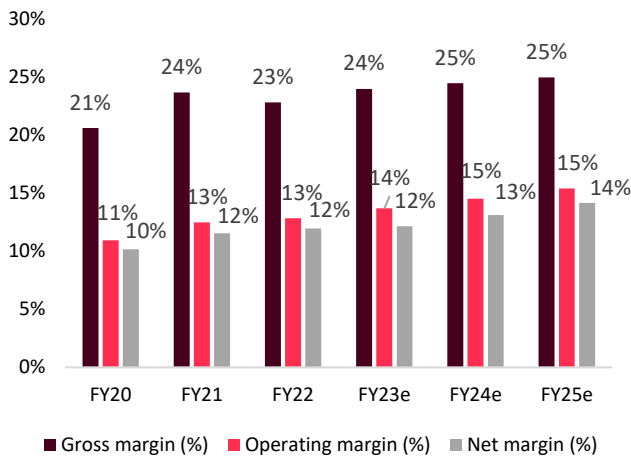


Fig. 11: Dividend and Dividend Yield (%)

Fig. 12: Capex as % of revenue

Source: Company Reports, Bloomberg, Knight Frank, Yaqeen Capital

Summary Financials

In SAR mn, except stated otherwise									
Income Statement	FY19	FY20	FY21	FY22	FY23e	FY24e	FY25e	FY26e	FY27e
Net sales/Revenues	5,257	6,891	7,208	8,805	10,715	12,471	14,094	15,684	17,397
Cost of sales	-4,410	-5,469	-5,500	-6,794	-8,144	-9,415	-10,571	-11,763	-13,048
Gross profit	847	1,422	1,708	2,011	2,572	3,055	3,524	3,921	4,349
General and administrative expenses	(350)	(460)	(462)	(605)	(701)	(792)	(876)	(951)	(1,026)
Operating profit	422	755	901	1,132	1,468	1,811	2,172	2,480	2,806
Other revenues	13	-1	3	38	65	78	97	121	150
Finance cost	-	-	-	-	-85	-69	-47	-31	-11
Profit before zakat and income tax	435	754	904	1,171	1,448	1,821	2,223	2,571	2,944
Zakat	-41	-52	-71	-118	-145	-182	-222	-257	-294
Profit for the period	394	702	833	1,053	1,302	1,638	1,999	2,312	2,648
EPS	3.9	5.8	6.9	8.8	10.9	13.6	16.7	19.3	22.1
DPS	8.0	3.3	4.0	5.0	6.5	8.0	9.8	11.0	13.0
Balance Sheet	FY19	FY20	FY21	FY22	FY23e	FY24e	FY25e	FY26e	FY27e
Cash and cash equivalents	414	993	1,608	544	2,503	3,468	4,672	6,092	8,031
Trade receivables, net	2,635	2,804	3,021	4,345	4,550	5,125	5,599	6,016	6,196
Inventories	151	2,804	3,021	4,345	4,550	5,125	5,599	6,016	6,196
Right of use leased assets	77	72	55	41	38	37	38	39	39
Property, plant and equipment, net	167	594	551	473	488	512	527	460	342
Total assets	4,877	6,335	7,173	10,282	11,232	12,910	14,714	16,599	18,690
Long term loans	0	1,705	2,277	3,266	3,429	4,053	4,651	5,254	5,915
Lease Liabilities	54	48	31	16	15	14	15	15	15
Trade payables	1,458	1,974	1,931	2,573	2,789	3,246	3,668	4,082	4,528
Total liabilities	3,621	4,411	4,902	7,459	7,885	8,885	9,858	10,749	11,751
Share capital	100	1,200	1,200	1,200	1,200	1,200	1,200	1,200	1,200
Retained earnings	1,079	610	960	1,432	1,824	2,338	2,967	3,728	4,551
Equity Attributable to Shareholders	1,257	1,924	2,271	2,794	3,317	3,994	4,823	5,815	6,902
Cash Flow Statement	FY19	FY20	FY21	FY22	FY23e	FY24e	FY25e	FY26e	FY27e
Net cash generated from operating activities	216	1,127	1,402	1,992	1,725	2,430	2,878	3,257	4,008
Net cash generated from investing activities	151	-536	-171	-3,191	1,015	-330	-373	-322	-313
Net cash (used in) provided by financing activities	-813	-4	-610	57	-781	-1,134	-1,300	-1,516	-1,756
Cash and cash equivalents at the end of the period	749	1,336	1,957	795	2,754	3,719	4,923	6,343	8,282
Ratios	FY19	FY20	FY21	FY22	FY23e	FY24e	FY25e	FY26e	FY27e
Gross margin (%)	16.1%	20.6%	23.7%	22.8%	24.0%	24.5%	25.0%	25.0%	25.0%
EBITDA margin (%)	9.8%	12.5%	15.4%	15.5%	16.2%	16.9%	17.9%	18.3%	18.6%
Operating margin (%)	8.0%	11.0%	12.5%	12.9%	13.7%	14.5%	15.4%	15.8%	16.1%
Net margin (%)	7.5%	10.2%	11.6%	12.0%	12.2%	13.1%	14.2%	14.7%	15.2%
ROA	8.4%	12.5%	12.3%	12.1%	12.1%	13.6%	14.5%	14.8%	15.0%
ROE	27.0%	44.1%	39.7%	41.6%	42.6%	44.8%	45.3%	43.5%	41.6%
Current Ratio (x)	1.3	1.4	1.4	1.4	1.5	1.5	1.5	1.5	1.6
Capex/Sales	3.4%	7.8%	2.1%	1.5%	2.5%	2.5%	2.5%	1.9%	1.7%
Debt-Equity Ratio	0.0	0.0	0.0	0.3	0.2	0.1	0.1	0.0	0.0
BVPS	2.0	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6
Dividend Payout Ratio	203%	57%	58%	57%	60%	59%	59%	57%	59%
Dividend Yield (%)	16.4%	4.9%	2.1%	2.1%	2.7%	3.3%	4.0%	4.5%	5.4%
P/E (x)	12.4	11.6	27.1	27.7	22.4	17.8	14.6	12.6	11.0
P/BV (x)	3.9	4.2	9.9	10.4	8.8	7.3	6.0	5.0	4.2
EV/EBITDA (x)	8.8	8.3	18.9	19.5	15.0	11.8	9.3	7.6	6.1

Source: Company Reports, Bloomberg, Yaqeen Capital



Rating Methodology

Buy: The Target share price exceeds the current share price by $\geq 10\%$

Hold: The Target share price is either more or less than the current share price by 10%

Sell: The Target share price is less than the current share price by $\geq 10\%$

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