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We initiate our coverage on Systems Limited (SYS) with a DCF based Jun-20 TP of Rs.113 which provides an upside potential of 22%. A dividend yield of 5%, if incorporated gives a total return of 27%.

Despite challenging macroeconomic conditions the company still managed to grow its revenues and earnings at a 5-year CAGR of 18.27% and 24.02% respectively.

Going forward, we expect the company's revenues and earnings to propel at a 5-year CAGR of 18.06% and 20.89% respectively, owing to 6.73% depreciation of PKR since last reporting date as approximately 69% of the company's revenue is export based.

Company is immune to interest rate risk as at the moment it has no long term borrowing arrangements.

Industry Overview

According to PSEB's website, Pakistan's IT & ITeS-BPO industry comprises of more than 2,500 companies, and this number is growing each year. The industry employs over 300,000 English-speaking professionals with many world-class experts. IT is one of the sectors which has a lot of potential. It can not only increase the much-needed export receipts of the country, but it can also provide jobs to millions of Pakistanis if they are provided the opportunities and training. Pakistan is ranked as the 4th most popular country for freelancing in the Online Labor Index published in 2017 by Oxford Internet Institute (OII). It is also listed as the 4th most financially attractive country in the world for outsourcing services as per A.T. Kearney's Global Services Location Index 2016.

According to the findings of Research Consultancy IDC, global Information Technology is expected to reach \$5 trillion in 2019. The United States of America is the leading and largest technical market in the world that is representing approximately 31% of the total. Roundabout \$1.6 trillion will be generated from the industry by the USA in 2019.

Pakistani Information Sector occupies only 1% of the total global IT industry. According to official data, Pakistan's IT industry has exhibited positive growth trends for the last four years with 100pc growth in export earnings.

During 2016-17, Pakistan's IT exports were \$3.3 billion, which have jumped to \$5 billion and are expected to grow to \$6 billion next year. Pakistan's IT industry is growing at a fast pace across different categories.

Enterprise software has grown by 17pc, marketing tech 15pc, financial services 13pc, consumer goods 9pc, retail/e-commerce 8pc, professional services 8pc, internet of things/hardware 7pc, health care 4pc, media 4pc and non-profit 3pc. Facebook, Amazon and other giants of the IT sector are anticipating something huge in the start-up world of Pakistan as evidenced by the huge number of sponsors.

The previous government also promoted start-ups, for example, they gave three-year exemption from taxes to the start-ups and set up national incubation centers in Lahore, Islamabad, Peshawar, Karachi, and Quetta.

The targets set for IT exports are ambitious but can be achieved if opportunities are availed timely by national companies in fields such as Cloud Computing, Mobile Apps, Artificial Intelligence, blockchain and etc.

(DuniyaNews) (BusinessRecorder) (ProPakistani)

Key Statistics

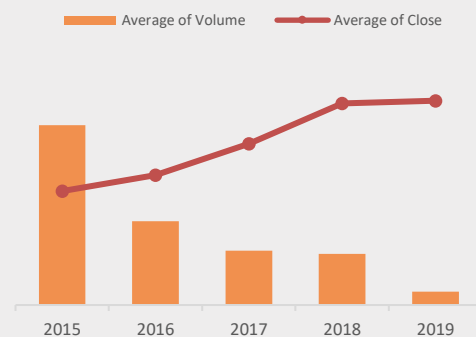
TP - Jun 20	113
LDCP	92.22
Upside (%)	22
Current Mkt. Cap ('mn)	11,383,167
KSE Symbol	SYS
Free Float ('mn)	61.7
Beta	1.00
Sector P/E	10.38

Source: ACPL Research, Company Financials

KSE 100 index vs SYS



Stock Price Yearly Closing Summary



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Company Overview

Systems Limited, Pakistan's first software house, was founded in 1977. Through its commitment to innovation and technical excellence, it has now become a globally recognized leader in next-generation IT and BPO services with a track record of successfully delivering large-scale projects. Over the past 10 years, Systems Limited has developed a strong presence in the Mortgage, Apparel, and Retail sectors in the US.

In the early 2000s, Systems Limited launched BPO services in the Pakistani domestic market and expanded into North America in 2006. In 2012, Systems Limited established offices in the Middle East. Systems maintain operations in the UAE, Qatar, and Oman, serving a vast list of government and corporate entities, including several Fortune 500 companies, and is considered to be the most valuable company for IT and BPO services in Pakistan. The company is principally engaged in the business of software development, trading of software and business process outsourcing services.

Systems Limited won the 2018 Microsoft Country Partner of the Year Award for Pakistan. The company was honored among a global field of top Microsoft partners for demonstrating excellence in innovation and implementation of customer solutions based on Microsoft technology.

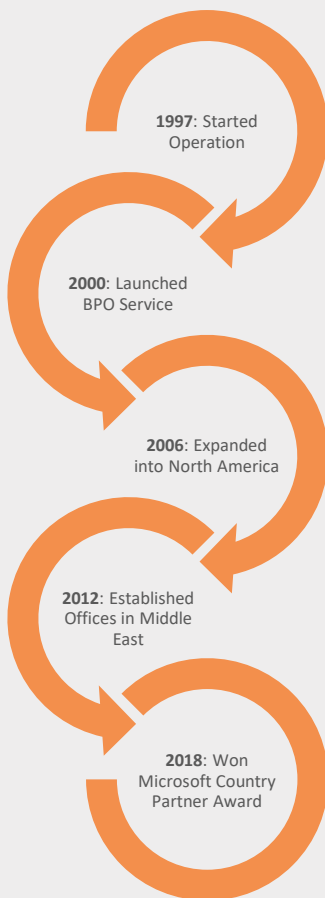
Being a leading Microsoft and IBM partner with deep experience in public and private sectors, Systems Limited is uniquely positioned to deliver complete solutions to medium and large organizations. Its areas of expertise are ERP, CRM, BI, portals & collaboration, e-commerce, mobility, and managed services. With the recent launch of the OneLoad digital payment aggregation platform and the mobile payment gateway, Systems Limited has also begun to reach out directly to a large number.

On the Domestic front, the Company has started producing a profit. The company signed significant projects this year in terms of Baluchistan Board of Revenue (BBOR) LRMIS project and other public and private sector contracts which are expected to add significantly to the Company's topline and bottom-line. The Company is expecting the new financial budget to bring positive changes to the IT sector. Government has a high focus on digitization at both the Federal and Provincial level. A number of new opportunities are expected to arise, and the Company is looking forward to high revenue growth in this sector.

The Company through their associate Visionet Systems (VSI) has started exploring opportunities in Europe last year. VSI has opened an office in Germany to cater for business opportunities in DACH (Germany (D), Austria (A) and Switzerland (CH)) region. The European company has appointed a local CEO and a few key resources have been moved to this sector from Systems Limited for sales activity. The European company is seeing growth and Systems Limited is hopeful to get more offshore business in 2019.

2018 has been a year of structural changes and internal alignment with cutting-edge technologies and expanding our global footprint. We have been investing heavily in the development of resources. Key focus had been on Artificial Intelligence, Machine Learning, Robotics Process Automation, Digital Commerce, Digital Transformation, Data, and Cloud. These technologies are key enablers for the current and future market. There is a scarcity of resources in these technologies, but high demand and we are working on building a good resource pool so that we can leverage this in global and domestic markets.

(Company Financials)



Sources: ACPL Research, Company Financials

Group Structure

The Group comprises of Systems Limited (Holding Company) and its subsidiaries – TechVista Systems FZ LLC and E-Processing Systems (Private) Limited. TechVista Systems FZ LLC (TVS), a limited liability Company incorporated in Dubai Technology and Media Free Zone Authority, is 100% owned subsidiary of Systems Limited. TVS is engaged in the business of developing software and providing ancillary services. TVS has also invested in TechVista Systems LLC and currently owns 49%. This company is also registered as a software house, but it does not have any independent operations and was created to support the projects of TechVista Systems FZ LLC. E-Processing Systems (Private) Limited (EPS), a private limited Company registered under Companies Ordinance 1984, incorporated on 06 February 2013, is a 53% owned subsidiary of Systems Limited. EPS is currently engaged in the business of purchase and sale of teleco's airtime and related services. The product of the Company is called OneLoad. The financial statements of the Company and the Group truly reflect the state of the Company's affairs and fair review of their business.

(Company Financials)

Product Portfolio

EdgeAX is a highly collaborative and scalable software solution designed to address the global needs of enterprises in the Apparel and Retail Industries. EdgeAX suite of business solutions that helps businesses thrive and compete in a rapidly changing global environment.

Each component of the EdgeAX suite has been built upon the core strengths of MS Dynamics AX infrastructure to maintain an end-to-end delivery of complex solutions. The modules' workflows and functionality follow the Apparel and Retail industry standards that highlight our value-added business processes and guarantees greater ROI to our clients.

OneLoad is a unique product offering for the local market that provides aggregated prepaid airtime recharge and a host of other value-added services. Using a multi-channel approach, OneLoad facilitates the purchase and disbursement of mobile prepaid vouchers and using SMS, IVR, the web, and mobile apps. With an integrated and seamless service ecosystem, OneLoad offers an extremely simple, convenient and easy-to-use service.

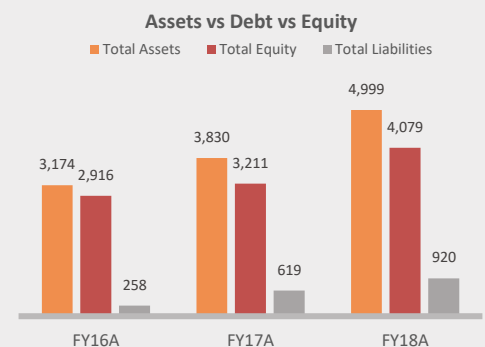
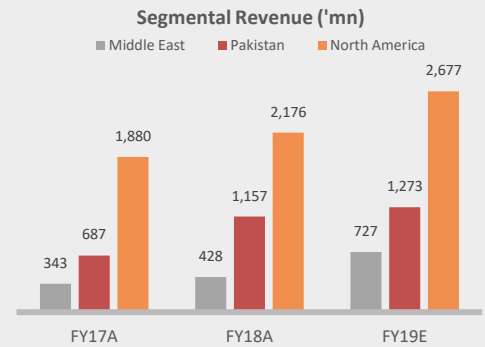
Users can easily create a OneLoad account online and easily credit it through a vast, extensive outreach of well over 25,000+ branded retail outlets around the country. Using their OneLoad account, consumers can avail services from multiple mobile operators and utility companies at the tip of their fingers using SMS or mobile app - there is no need to make multiple, physical trips to the shop anymore.

Globally, leading organizations consider their employees as an asset rather than overheads because of the business results they deliver. **SysHCM**, Human Capital Management solution of Systems Limited, offers organizations the tools to help manage, share and steer the vast capabilities of its staff, to focus on its critical talent and support strategic HR processes. It enables organizations to create a workforce that can become their most coveted competitive advantage. The modular architecture of SysHCM application makes it simple to add modules to the core application as the organization grows.

The application supports organizations to lower its human resource costs, streamline the entire recruit-to-retire spectrum, expand the talent pool, shorten the hiring process and make it easy for employees to manage their own HR information and benefits.

Talent Suite is a suite of products that cater to your complete human capital management needs. From recruitment to retirement, complete employee management cycle can be handled through company's AX Talent Suite. AX Talent Suite is a top Microsoft Dynamics AX add on for managing employees from profiles, to payrolls, and from performance to final settlements.

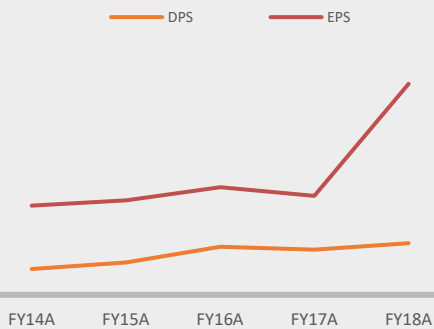
Key Statistics



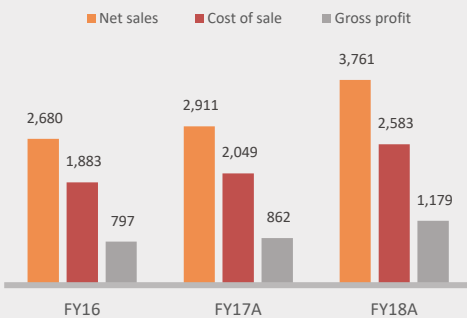
Sources: ACPL Research, Company Financials

Key Statistics

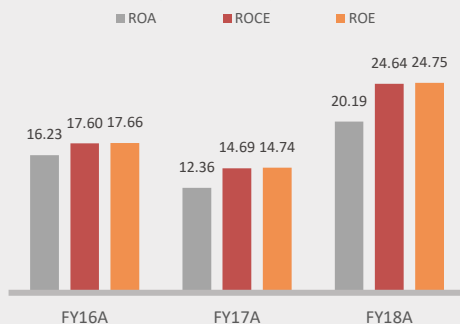
EPS vs DPS



Sales vs Gross Profit



Key Profitability Ratios



Sources: ACPL Research, Company Financials

Financial Performance

The company's revenue is primarily from software development and IT services work subcontracted by its subsidiary **TVS** operating in the **Middle East region** and its associated company **Visionet Systems** operating in the **North America region**. Over **69%** of its revenue is **export based**. In recent years, the Company has started taking projects and engagements in the domestic market. In CY18, the Company's revenues grew by 29% as compared to CY17. The Company was able to sign significant new projects with both new and existing customers this year. The US and Middle East businesses have also achieved sizable growth in terms of both top line and bottom line.

Gross margins recorded an increase of 1.72 bps to 31.33% in CY18 from 29.62% in CY17. However, the net margins showed significant growth of 10.58 bps to 26.84% in CY18 as compared to 16.26% in CY17. Profitability staggered on account of other income of PKR 376 million arising from currency devaluation where the average USD rate in CY18 had been 121.73 per dollar during the year as compared to the average rate of PKR 105.42 per dollar in CY17.

CY18 has been a good year for the subsidiary EP Systems. The OneLoad business has picked momentum in CY18 with average throughput of over PKR 20 million per day during the year which has already gone to PKR 23 million per day in March. The Company has achieved revenue growth of 153% from PKR 76.5 million in CY17 to PKR 193.8 million in CY18. Even higher revenue growth is expected in CY19.

In CY18, SYS net sales increased by 29% YoY owing to increased domestic operations due to revenue recognition from projects. Secondly, 72% YoY increase in domestic trading operations. Thirdly, increased business with Microsoft. Lastly, average 15.46% YoY rupee depreciation in CY18.

Among other major heads company's other income surged by 270% YoY to 437 million rupees in CY18 as compared to 118 million rupees in CY17, majority of which was incurred due to foreign currency translation gain as Rupee has depreciated 32.77% YoY between reporting dates.

Furthermore, the company's management remains optimistic about the North America market and entry in European markets due to lucrative margins as compared to the Middle East. The Company through their associate Visionet Systems (VSI) has started exploring opportunities in Europe last year. VSI has opened an office in Germany to cater for business opportunities in DACH (Germany (D), Austria (A) and Switzerland (CH)) region.

Moreover, management expects OneLoad to achieve financial breakeven in the nearby future and still awaits regulatory approval from SBP for the provision of enhanced financial services.

Interest Rate Risk

Company's debt to equity ratio in CY18 is at 11.81% which reflects that the company's reliance on debt is very minimal. In the last five years company has never engaged in any kind of long-term borrowing arrangement whatsoever. This makes it an optimal investment opportunity as the profitability of the company won't be affected by continuously rising interest rates. However, for the past 2 years the company has been borrowing short term loans for its day to day operations under the export refinance arrangement. These loans carry very modest interest rates (3% + spread) compared to commercial borrowing rates. On the flip side, the rise in the interest rate is expected to positively impact the company's profitability. As the company has significant long-term and short-term investments and long-term deposits.

(Company Financials)

Impact of PKR devaluation

In CY18, company's other income surged by 270% YoY to 437 million rupees as compared to 118 million rupees in CY17, majority of which was incurred due to foreign currency translation gain as Rupee had depreciated 32.77% YoY between reporting dates. Secondly, the company's net sales in CY18 increased by 29% YoY and the major reason behind such a significant increase was again massive currency devaluation. Furthermore, PKR in CYTD has further depreciated by 6.73% which according to our calculation will result in a further increase of around 24% in revenue for CY19 to 4,677 million rupees. However, appreciation of PKR could adversely affect revenue growth and the company's profitability.

Future Outlook

The company appears to be very lucrative owing to exponential growth from MEA operations. Secondly, an entry in European markets. Thirdly, the commencement of financial contributions from OneLoad. Furthermore, extended fiscal/financial incentives and lastly, enhanced product portfolio. Moreover, SYS has remained an optimal beneficiary of Rupee depreciation given 69% export driven revenue and will continue to benefit from it in CY19 owing to 6.73% depreciation of PKR since Dec last year.

We expect this steadfast performance to continue and sales to grow at a 5-year CAGR of 18.06%. Whereas earnings will grow at a 5-year CAGR of 20.89%. This can be backed by the fact that the government is eagerly wanting to increase the country's exports. New policies and framework are being finalized for the next four years. All of which will be unveiled with the upcoming FY19-20 budget and will indeed boost the country's exports and IT sector will be amongst the greatest beneficiaries.

Valuation

SYS is currently trading at CY20E PE of 7.04x respectively. Furthermore, the script is trading at a CY20E P/BV of 1.94x which offers a significant discount of 52% relative to its historical 5-year average of 4.02x. We have a **BUY** stance on the script with a DCF based Jun-20 TP of Rs.113 which provides an upside potential of 27%. Furthermore, it also offers a dividend yield of 5% which makes the total return of 27%.

Key Risks to Valuation

- Appreciation of PKR
- Less than expected growth in demand

Key Ratios

Profitability Ratios		FY14A	FY15A	FY16A	FY17A	FY18A	FY19E	FY20E	FY21E	FY22E
GP Margin	%	35.36	33.44	29.75	29.62	31.33	33.09	33.16	33.30	33.65
NP Margin	%	22.19	19.99	19.22	16.26	26.84	32.94	29.20	29.29	29.50
OP Margin	%	22.62	20.66	19.00	16.91	28.55	33.57	29.75	29.83	30.03
ROE	%	19.87	18.13	17.66	14.74	24.75	31.68	27.57	26.46	25.37
ROCE	%	19.81	18.08	17.60	14.69	24.64	29.10	25.60	24.80	23.98
ROA	%	17.53	15.85	16.23	12.36	20.19	26.40	23.26	22.62	21.96
Liquidity Ratios		FY14A	FY15A	FY16A	FY17A	FY18A	FY19E	FY20E	FY21E	FY22E
Current	x	7.81	6.80	10.04	4.59	4.21	8.35	8.71	9.31	9.99
Acid-test	x	6.65	5.27	7.41	3.22	3.08	6.06	6.41	6.99	7.66
Cash to current Liab.	x	3.52	0.41	0.74	0.73	0.44	0.80	1.23	1.88	2.57
Activity Ratios		FY14A	FY15A	FY16A	FY17A	FY18A	FY19E	FY20E	FY21E	FY22E
Average Inventory		196,853	220,533	282,554	354,456	376,678	404,011	483,011	563,906	645,214
Receivables Days		155	191	192	149	210	206	202	200	198
Payables Days		4	10	3	29	10	10	10	10	10
Operating Cycle		151	181	188	120	200	196	192	189	188
Investment Ratios		FY14A	FY15A	FY16A	FY17A	FY18A	FY19E	FY20E	FY21E	FY22E
EPS		3.46	3.67	4.17	3.84	8.18	12.48	13.09	15.20	17.47
DPS		1.00	1.25	1.86	1.75	2.00	4.99	5.24	6.08	6.99
Div. Yield	%	1.08	1.36	2.02	1.90	2.17	5.41	5.68	6.59	7.58
Dividend Cover		3.46	2.93	2.24	2.19	4.09	2.50	2.50	2.50	2.50
BVPS		17.40	20.22	23.63	26.02	33.04	39.39	47.49	57.46	68.84
Payout	%	28.93	34.10	44.57	45.63	24.46	40.00	40.00	40.00	40.00
Retention	%	71.07	65.90	55.43	54.37	75.54	60.00	60.00	60.00	60.00
No. of Shares	'mn	123.43	123.43	123.43	123.43	123.43	123.43	123.43	123.43	123.43
P/E		26.68	25.16	22.10	24.05	11.28	7.39	7.04	6.07	5.28
Sales per share		15.58	18.34	21.71	23.58	30.47	37.89	44.84	51.90	59.21
P/BV		5.30	4.56	3.90	3.54	2.79	2.34	1.94	1.61	1.34
Price to Sales		5.92	5.03	4.25	3.91	3.03	2.43	2.06	1.78	1.56
Gearing Ratios		FY14A	FY15A	FY16A	FY17A	FY18A	FY19E	FY20E	FY21E	FY22E
Debt to Equity	%	0.47	0.51	0.58	6.85	11.81	0.66	0.54	0.45	0.38
Interest Cover		109.11	220.47	158.46	45.96	57.02	270.00	283.26	328.70	377.45

Source: ACPL Research, Company Financials

Financial Projections

Rupees' millions	FY14	FY15	FY16	FY17A	FY18A	FY19E	FY20E	FY21E	FY22E
Net sales	1,923	2,263	2,680	2,911	3,761	4,677	5,535	6,406	7,308
Cost of sale	1,243	1,507	1,883	2,049	2,583	3,129	3,700	4,273	4,849
Gross profit	680	757	797	862	1,179	1,547	1,835	2,133	2,459
Distribution expenses	60	70	37	114	47	100	116	132	151
Administrative expenses	199	262	251	287	377	398	475	555	642
Research and development expenses	2	29	2	-	-	-	-	-	-
Other expenses	23	20	31	88	118	23	28	32	37
Other income	39	92	33	118	438	544	431	497	564
Operating Profit	435	468	509	492	1,074	1,570	1,647	1,911	2,195
Finance cost	4	2	3	11	19	6	6	6	6
Profit before taxation	431	466	506	481	1,055	1,564	1,641	1,905	2,189
Taxation	4	13	-	9	46	24	25	29	33
Profit after taxation	427	453	515	473	1,009	1,540	1,616	1,877	2,156
EPS	3.46	3.67	4.17	3.84	8.18	12.48	13.09	15.20	17.47

Source: ACPL Research, Company Financials

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DEFINITION OF TERMS

TP	Target Price	CAGR	Compound Annual Growth Rate	FCF	Free Cash Flows
FCFE	Free Cash Flows to Equity	FCFF	Free Cash Flows to Firm	DCF	Discounted Cash Flows
PE	Price to Earnings Ratio	PB	Price to Book Ratio	BVPS	Book Value Per Share
EPS	Earnings Per Share	DPS	Dividend Per Share	ROE	Return of Equity
ROA	Return on Assets	SOTP	Sum of the Parts	LDCP	Last Day Closing Price

VALUATION METHODOLOGY

To arrive at our Target Price, Abbasi & Company (Private) Limited uses different valuation methods which include:

- I. Discounted Cash Flow Model
- II. Dividend Discount Model
- III. Relative Valuation Model
- IV. Sum of Parts Valuation

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Stock Rating	Expected Total Return
BUY	Greater than 15%
HOLD	Between -5% to 15%
SELL	Less than and equal to -5%

Sector Rating	Sector Outlook
Overweight	Positive
Market Weight	Neutral
Underweight	Negative

Ratings are updated to account for any development impacting the economy/sector/company, changes in analysts' assumptions or a combination of these factors.

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