

# ZAREA

## We Recommend Against Subscribing to the IPO

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Despite strong revenue growth, we have concerns about the company's business model and valuation. While it operates in e-commerce for construction products, it faces key risks, including low digital adoption, logistics challenges, payment constraints, market fragmentation, and price volatility.

Given its historically volatile financials and high valuation, we recommend against subscribing to the IPO.

### Company Overview

Zarea Limited ("ZL") is a digital technology company revolutionizing Pakistan's commodity trading market. Its proprietary platform enables buyers to access competitive pricing and monitor market trends seamlessly. Focused on digitalizing B2B marketplaces, ZL offers value-added services such as Logistics & Storage facilitation, Credit Sales, and Data Analytics, enhancing user experience and customer retention.

ZL operates an e-commerce marketplace for commodities like cement, steel, and agri-biomass, generating revenue through platform fees. With plans to expand into coal, chemicals, grains, and more, ZL aims to strengthen its market position. As Pakistan's digital economy grows, ZL presents a strong investment opportunity with a scalable platform and diversified portfolio, ensuring sustainable growth and profitability.

### Purpose of the Issue

The proceeds will be strategically allocated to support working capital requirements, expansion in logistics and technology, marketing initiatives, and office and vehicle infrastructure. A key objective of this capital utilization is to drive growth by expanding the customer base through increased user acquisition.

A significant portion of the funds will be directed towards broadening the range of commodities available on the platform, thereby enhancing its market presence. Additionally, ZL aims to streamline and optimize its digital infrastructure to improve efficiency and user experience. Furthermore, approximately 7.5% of the total issue size will be allocated to marketing efforts to strengthen brand awareness and drive platform adoption. These strategic investments position ZL for sustainable growth in Pakistan's evolving digital economy.

### Issue details

This issue consists of 62 million Ordinary Shares, equivalent to 23.81% of Zarea Limited's total post-IPO Paid-up Capital, with a face value of Rs1/ each.

The entire issue will be offered through the Book Building at a floor price of PKR 16/- per share (including a premium of PKR 15/- per share) with a maximum price band of up to 40% i.e., PKR 22.4 per share.

The book-building phase will start from Feb 10, 2025, to Feb 11, 2025.

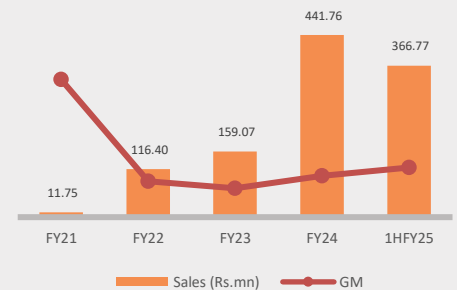
### Financial Performance

Zarea's financial performance shows strong growth, with revenue increasing by 36.65% in 2023 and 177.14% in 2024, reaching Rs 442mn. However, the cost of sales grew disproportionately, rising by 10% in 2023 and 290% in 2024, impacting margins.

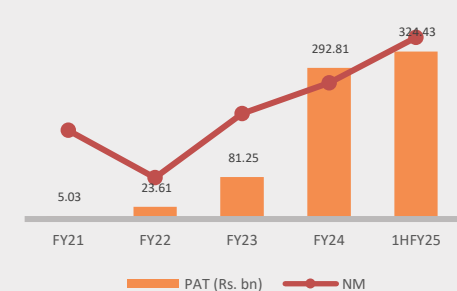
### Key Statistics

Company Name	Zarea Limited
Face Value (PKR)	1
Floor Price (PKR)	16
Upper Band (40%) (PKR)	22.4
Free Float (%)	23.81
Pre-IPO No. of Shares (mn)	200
Post-IPO No. of Shares (mn)	262
BVPS (Post Issue)	2.62
FY25E EPS	2.47
P/E (Forward)	6.48
Book Building Dates	10-11 Feb, 2025
IPO Dates	17-18 Feb, 2025

### Sales (Rs'mn) vs Gross Margin



### PAT (Rs'bn) vs Net Margin



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Gross Profit increased by 46.10% in 2023 and 147.65% in 2024, while operating expenses escalated significantly, particularly in 2024. Administrative and General Expenses rose by 373.76%, and Selling and Distribution Expenses increased by 223.76%, raising concerns about cost efficiency.

Investment performance showed volatility, with a loss in 2022, a smaller loss in 2023, and a gain in 2024. Finance costs remained minimal.

Profit before taxation grew by 220.81% in 2023 and 181.41% in 2024, while Net Profit after taxation surged by 244.15% and 260.12%, totaling 292,811,085 Rupees

## Valuation

Based on the floor price of PKR 16, the P/E multiple of ZL is around 6.48x (based on extrapolated 1HFY25 earnings and post-IPO number of shares). At the maximum price of 22.4 allowed in book building, the P/E of the IPO stands at 9.06x.

## Recommendation

Despite strong revenue growth over the past two years, we have concerns about the business model and valuation. While the company operates in the e-commerce sector for construction products, it is significantly influenced by construction industry dynamics. This is important because construction-related stocks typically trade at lower multiples compared to technology stocks.

Additionally, the concept of selling construction materials and other commodities like coal, chemicals, and grains online is relatively new in Pakistan. If successful, the company could benefit from a first-mover advantage. However, there are the following inherent risks to such platforms in Pakistan:

- **Low Digital Adoption in B2B Transactions:** Unlike traditional e-commerce, bulk buyers in the construction sector still prefer direct dealings and offline negotiations due to trust and pricing flexibility.
- **Logistics & Supply Chain Challenges:** Efficient nationwide delivery of heavy construction materials, coal, chemicals, and grains remains a logistical hurdle due to high transportation costs and infrastructure limitations.
- **Payment & Credit Constraints:** Large-scale buyers often rely on credit-based purchases, while online platforms typically require upfront payments, which could limit customer adoption.
- **Market Fragmentation & Supplier Reluctance:** The construction industry is highly fragmented, with suppliers and contractors accustomed to long-standing personal networks. Convincing them to shift to an online marketplace may be difficult.
- **Regulatory & Price Volatility Risks:** Construction materials and commodities are subject to frequent price fluctuations, taxation changes, and import restrictions, making online standardization challenging.

The company's historically volatile financial performance reflects these risks, making its valuation appear high. Therefore, we recommend against subscribing to the IPO.

## Key Risks

- **Potential First-Mover Advantage:** Early success could lead to market dominance.
- **Digital Adoption Growth:** The construction sector may gradually shift toward online platforms.
- **Strategic Partnerships:** Collaborations with major suppliers could drive adoption.
- **IPO Demand & Market Sentiment:** Strong investor interest could push stock prices higher despite concerns.

## Key Statistics

	FY22	FY23	FY24	1HFY25
Sales (Rs. Mn)	116	159	442	367
Sales Growth	-	37%	177%	-17%
GPM	74%	79%	70%	70%
NPM	20%	51%	66%	56%
Diluted EPS	0.09	0.31	1.12	1.24

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**DEFINITION OF TERMS**

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

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