Foundation Securities
A Fauji Foundation Group Company
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PAKISTAN **September 1, 2023**

Foundation Alert

SYS: Analyst Briefing Takeaways

Event

- Systems Limited (SYS PA) held its analyst briefing yesterday to discuss its financial performance for 1HCY23/2QCY23 along with future outlook of the company. Following are the key takeaways of the briefing.

Impact

- Systems Limited (SYS PA) profitability clocked in at Rs1.4bn (EPS Rs4.87, down 20/64% YoY/QoQ) in 2QCY23 against profit of Rs1.8bn (EPS Rs6.08) in 2QCY22. This takes 1HCY23 profitability to Rs5.3bn (EPS Rs18.23, up 79% YoY) as compared to profit of Rs2.3bn (EPS Rs10.21) in 1HCY22.
- Company revenue/cost of revenue increased by 102%/117% in 1HCY23. The increase in revenue has been led by Middle East. However gross margin declined by 4.9bps to 27.0% in 1HCY23.
- Management attributed decline in gross margin due to (1) investment in subsidiaries along with inflationary pressures, (2) increase in energy prices adversely impacting company overheads costs and (3) devaluation of Rs-$ impacting onsite resource costs and licenses & subscriptions which are paid in US$.
- In 1HCY23, Selling and Admin cost increased by 114% YoY in 1HCY23 due to higher admin and marketing cost given upfront investment in infrastructure and business development.
- Company Operating Margin declined by 2.3% given (1) WHT on payments from subsidiaries classified as admin, (2) one-off adjustment of investment in JOMO and (3) higher IFRS9 adjustment on receivables amid macro-economic conditions.
- In 1HCY23, all geographies posted robust growth, with the Middle East & Africa Region leading the trend. Export sales of the company are roughly 82% of services revenue in 1HCY23.
- Pakistan segment has about half of the contracts denominated in US$, hedging the company from devaluation.
- SYS management also discussed its headcount and disclosed that company has added 380 new IT professionals in 1HCY23 taking the total number of IT employees to 4,922 (vs 4,532/3,416 in CY22/CY21).
- Management also shared breakup up of revenue and disclosed that BFS/Telecommunication/Technology/Public Sector/Retail & CPG/Others are driving majority of company business with sales contribution of 31/20/15/12/11/11% in 1HCY23.
- Management shared that company has strong focus on building AI competency by building and developing a resource pool. The Company is also developing AI offerings for the BFS, Telco and Retail/CPG verticals.
- Company believes that the economic environment is expected to remain stable in MEA and other key geographies during 2023 and the company can capitalize on the opportunities available in these markets.
- Company is continuing to evaluate various M&A opportunities outside of Pakistan, which will further strengthen its future growth trajectory.

Outlook

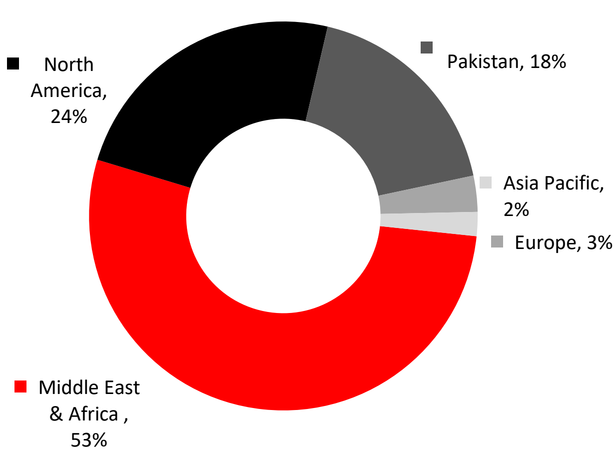
- We have an "Underperform" stance on the scrip with Dec'23 TP of Rs369 as stock is currently trading at significant premium to the market despite increase in business risk. Systems business risk has increased as it has changed its strategy to expand into new geographies through its associates (common directorship) instead of its 100% owned subsidiaries outside Pakistan.

Table 1: SYS 2QCY23 Key Financial Highlights (Rs mn)

Rs mn	2QCY23	2QCY22	YoY	QoQ	1HCY23	1HCY22	YoY
Revenue-net	12,490	6,130	104%	17%	23,189	11,463	102%
Cost of revenue	9,022	4,075	121%	14%	16,931	7,809	117%
Gross Profit	**3,468**	**2,056**	**69%**	**24%**	**6,259**	**3,654**	**71%**
S&A expenses	1,547	689	125%	37%	2,679	1,251	114%
Other op. exp	270	(16)	na	na	221	20	979%
Operating Profit	**1,651**	**1,383**	**19%**	**-3%**	**3,359**	**2,383**	**41%**
Share of loss	113	75	52%	2%	223	149	50%
Other income	286	647	-56%	-89%	2,838	982	189%
EBIT	**1,824**	**1,956**	**-7%**	**-56%**	**5,974**	**3,216**	**86%**
Finance costs	251	52	388%	60%	408	84	384%
Profit before taxation	**1,573**	**1,904**	**-17%**	**-61%**	**5,566**	**3,132**	**78%**
Taxation	159	139	14%	41%	272	166	64%
Profit after taxation	**1,414**	**1,765**	**-20%**	**-64%**	**5,294**	**2,966**	**79%**
Profit attributable to parent	1,414	1,765	-20%	-64%	5,294	2,966	79%
EPS Diluted(@ 290.4mn sh)	**4.87**	**6.08**			**18.23**	**10.21**	
Gross Margin	27.8%	33.5%			27.0%	31.9%	
EBIT Margin	14.6%	31.9%			25.8%	28.1%	
Net Margin	11.3%	28.8%			22.8%	25.9%	

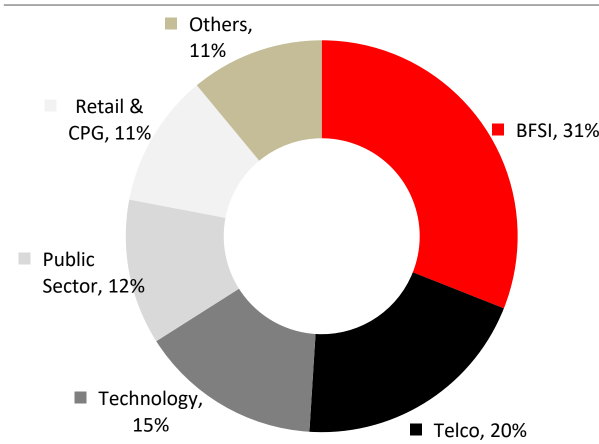
Source: Company Accounts, Foundation Research, September 2023

Fig 1: Middle East contributed the most in revenue



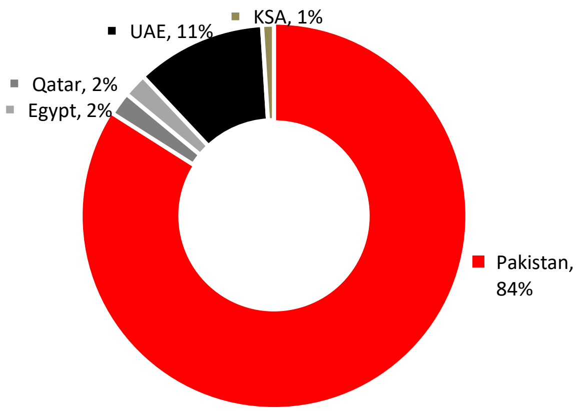
Source: PSX, Foundation Research, Sep 2023

Fig 2: BFSI leading in revenue mix



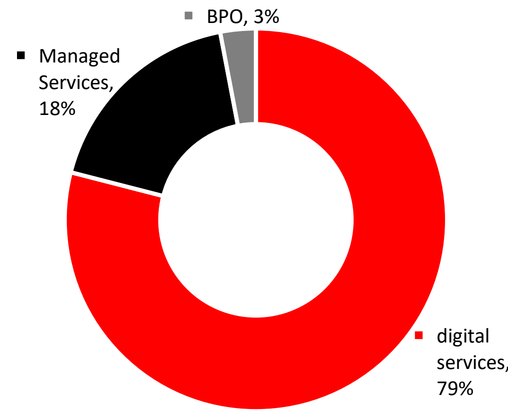
Source: PSX, Foundation Research, Sep 2023

Fig 3: Total headcount geographic dispersion



Source: PSX, Foundation Research, Sep 2023

Fig 4: Digital is the central driver of business



Source: PSX, Foundation Research, Sep 2023

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Recommendations definitions

If

Expected return >+10%	Outperform.
Expected return from -10% to +10%	Neutral.
Expected return <-10%	Underperform.