

OCTOPUS

We recommend to subscribe the IPO with DCF based Jun-22 TP of Rs.100

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We recommend to subscribe the IPO with a DCF based Jun-22 TP of Rs.100 which provides an upside potential of 245% relative to its floor price of Rs.29

The registration process of eligible investors has already been commenced from 6th Sep 2021 and will close at 3:00 pm on 10th Sep 2021

Bidding dates are from 9th Sep 2021 to 10th Sep 2021 (From 9:00 am to 5:00 pm)

Dates of public subscription are from 16th Sep 2021 to 17th Sep 2021 from 9:00 am to 5:00 pm

Company Overview

Octopus Digital Limited is a wholly-owned subsidiary of Avanceon Limited. It was incorporated on 29th December 2017 as a private limited company in Lahore, Pakistan. The company is a technology service-oriented company that provides After Market Support (AMS) services to a wide range of clients, both locally and internationally. The AMS services include the provision of parts, repair, maintenance, and digital services for the equipment which is installed in their customers' plants.

The prime business of the Company is to carry out Information Technology enabled services which includes but are not limited to online data/information storage, online monitoring, and review of employees efficiency, online monitoring of cost and production efficiency, online monitoring and maintenance of plant and machinery, sale and trade of related software and equipment, etc.

Purpose of the Issue

The company wants to raise Rs 793mn by issuing 27.35mn shares at the floor price of Rs29 per share. The purpose of the new issuance is to fund the development of various Digital Dashboard platforms to upgrade its services suite to industry 4.0, which is an industrial revolution that includes automation of traditional manufacturing and industrial practices.

Industry 4.0 refers to a new phase in the industrial revolution that focuses heavily on interconnectivity, automation, machine learning, and real-time data. The target markets for these services will be Pakistan, the Middle East, and the United States. It is pertinent to mention here that the entire requirement of funds shall be funded through IPO Proceeds. Details of the utilization of IPO proceeds are given below:

Particulars	PKR (mn)	Usage	%
IPO Proceeds	793	Intellectual Property	88
		HR Cost of Marketing	5
		HR Cost of Sales	7
Total	793	Total	100

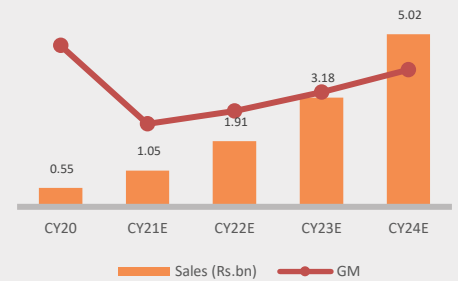
Industry Overview

The 4th Industrial Revolution is currently taking place and it is digital. The actual size of the 2016 digital economy was \$11.5 trillion globally, which was 15.5% of the global GDP. Digital growth in Pakistan is going through a rapid evolution. IT/ITeS Sector is one of the fastest-growing sectors of Pakistan contributing about 1% of the GDP of Pakistan at about \$3.5 billion. It doubled in the past four years and experts expect it to grow a further 100% in the next two to four years to \$7 billion.

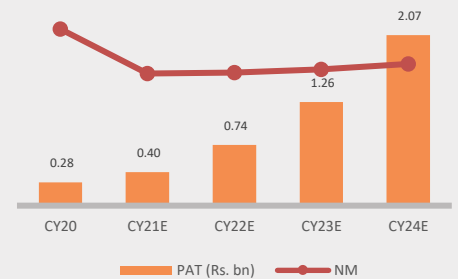
Key Statistics

Symbol	OCTOPUS
TP - Jun 22	100.00
Floor Price	29.00
Upside	245%
Free Float (mn)	27
Market Cap. (Rs.mn)	3,966

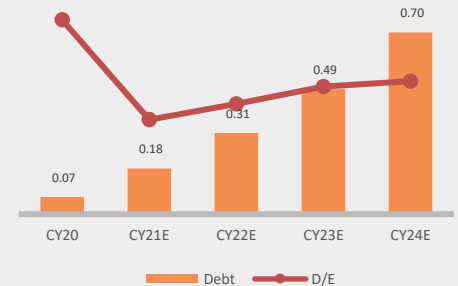
Sales (Rs'bn) vs Gross Margin



PAT (Rs'bn) vs Net Margin



Debt (Rs'bn) vs D/E



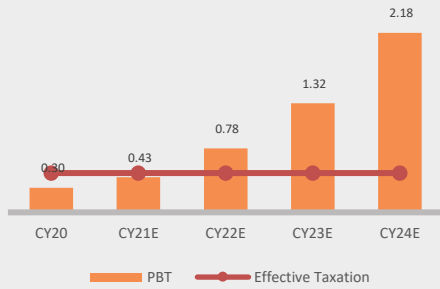
Sources: ACPL Research, Company Financials, PSX.

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Key Statistics

PBT (Rs'bn) vs Effective Taxation



Symbol	FY21 PE
AVN	30.75
TRG	9.06
SYS	35.90
Average	25.24
OCTOPUS (CY22 PE)	5.38
Discount	79%

In accordance with Pakistan Vision 2025 and the Digital policy of Pakistan 2018, the ICT industry size is targeted to reach \$20 billion by 2025. Most importantly, the security situation of Pakistan has improved. Startups like Careem, Daraz, Zameen.com, Rozee.pk and their success is bringing investment into Pakistan as evident from the recent acquisition of Daraz and Easypaisa by AliBaba. Traditional investors from other Pakistani sectors like textile, fertilizers are also taking a special interest in the startup ecosystem.

Investment Rationale

Octopus’s business model is based on recurring earnings based on term-based multi-year monthly subscription service instead of fixed cost or time & material-based projects thereby reducing the risk of volatile earnings as this is prevalent in other conventional businesses in Pakistan. Furthermore, 24/7 support and guaranteed response time allowing the company to stay ahead of its competitors.

In Pakistan, companies in the manufacturing sector have many processes that are outdated or conducted manually. Octopus is taking vital steps towards the implementation of automation processes and is focused on process efficiencies in the manufacturing sector, which will allow it to succeed in the near future.

The major portion of revenues of Octopus is coming from clients based in the Middle East. There are some international players operating in this segment in the Middle East, that is, Honeywell Automation, ABB, CISCO, and Rockwell automation. Octopus has procured cloud services from Microsoft and delivers AMS services using Microsoft’s cloud. This gives an edge to Octopus over these international players which do not possess Microsoft’s cloud.

Considering the competencies of the company and huge growth potential in local and international markets, the management of Octopus Digital Limited expects the revenues and earnings of the company to grow at a 6-year CAGR of 65% and 60% respectively going forward.

Valuation

The CY22E PE of the company stands at 5.38x at a floor price of Rs.29 which is highly discounted as compared to the industry average. Therefore, we recommend to **SUBSCRIBE** the IPO with a DCF based Jun-22 TP of Rs.100 which provides an upside potential of 245% relative to its floor price of Rs.29.

Key Risks to Valuation

- Appreciation of PKR
- Failing in the renewal of contracts
- Failing in developing proper technology as envisaged in their plan

Financial Projections

Rupees' millions	CY20	CY21E	CY22E	CY23E	CY24E	CY25E	CY26E
Net sales	549	1,054	1,908	3,176	5,020	7,586	10,867
Cost of sale	189	442	777	1,235	1,843	2,643	3,635
Gross profit	360	612	1,131	1,941	3,177	4,943	7,232
SG&A expenses	59	177	307	485	732	1,062	1,464
Operating Profit	302	434	824	1,456	2,445	3,881	5,768
US Taxation	-	-	33	108	230	445	769
Finance cost	5	8	15	25	39	58	83
Profit before taxation	297	426	776	1,323	2,176	3,379	4,917
Pakistan Taxation	15	21	39	66	109	169	246
Profit after taxation	282	405	738	1,257	2,067	3,210	4,671
EPS	2.06	2.96	5.39	9.19	15.11	23.47	34.16

Source: ACPL Research, Company Financials

Horizontal Analysis

	CY20	CY21E	CY22E	CY23E	CY24E	CY25E	CY26E
Net sales		91.9%	81.0%	66.5%	58.1%	51.1%	43.3%
Cost of sale		134.4%	75.6%	59.0%	49.3%	43.4%	37.5%
Gross profit		69.7%	84.9%	71.6%	63.6%	55.6%	46.3%
SG&A expenses		203.0%	73.0%	58.2%	50.8%	45.1%	37.9%
Operating Profit		43.9%	89.8%	76.7%	67.9%	58.7%	48.6%
US Taxation				226.0%	113.7%	93.1%	73.1%
Finance cost		60.9%	83.9%	68.9%	55.2%	47.0%	43.0%
Profit before taxation		43.6%	82.1%	70.4%	64.4%	55.3%	45.5%
Pakistan Taxation		43.6%	82.1%	70.4%	64.4%	55.3%	45.5%
Profit after taxation		43.6%	82.1%	70.4%	64.4%	55.3%	45.5%
EPS		43.6%	82.1%	70.4%	64.4%	55.3%	45.5%

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

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