

**Neutral**

**Price Target (SAR): 175.0**

Current: 181.40  
Upside/Downside: 3.5% below current

Valuation Multiples	22	23E	24E
P/E (x)	51.3	54.6	41.8
P/B (x)	6.8	6.8	6.6

Major Shareholders	% Ownership
Public Investment Fund	60.00

Price Performance	1M	3M	YTD
Absolute	7.9%	-10.0%	0.2%
Relative to TASI	4.7%	-7.9%	-6.6%

**Earnings**

(SARmn)	2022	2023E	2024E
Revenue	1,071	1,002	1,138
Revenue growth	(8.1%)	(6.5%)	13.6%
Gross profit	684	557	655
Gross margin	63.8%	55.5%	57.6%
EBITDA	633	362	447
EBITDA margin	59.1%	36.1%	39.3%
Net profit	425	399	521
Net margin	39.6%	39.8%	45.8%
EPS	3.54	3.32	4.34
DPS	2.31	2.50	3.26
Payout ratio	65.3%	75.2%	75.0%
EV/EBITDA	24.6x	44.6x	35.7x
P/E	51.3x	54.6x	41.8x
RoE	13.5%	12.5%	16.0%

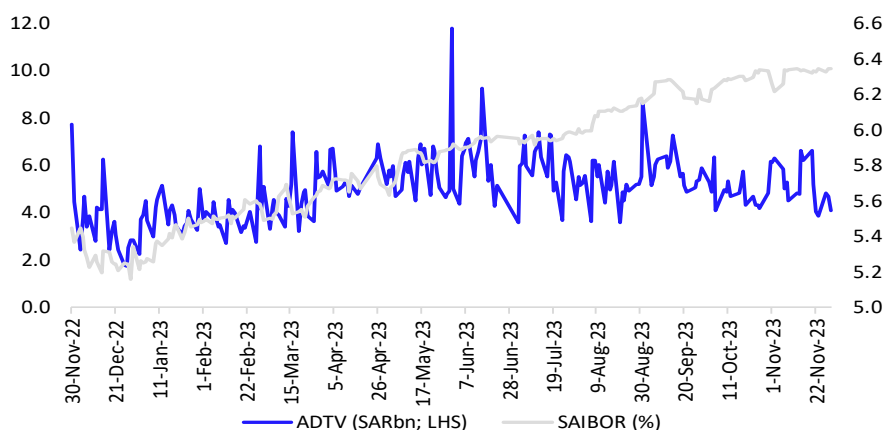
Source: Company data, Al Rajhi Capital estimates

# Saudi Tadawul Group Holding

## Initiating Coverage with a TP of SAR175.0/sh

We initiate coverage on Saudi Tadawul Group (STG) with a neutral rating and a target price of SAR175/sh, implying a downside of 3.5% to the last close. STG's financial performance in 9M2023 has taken a hit, with the top line and bottom line declining by 13 and 19% y-o-y, respectively. The YoY decline in profitability can primarily be attributed to reduced average daily traded value (ADTV) from SAR6.9bn in FY22 to SAR5.4bn in 9M2023. As global interest rates have risen to a historic high, money has flowed away from risky assets to safer havens, resulting in pressure on equity markets, in general. While this trend has led to an uptick in trading within the Saudi fixed-income market, the market's relatively smaller size has limited impact on STG's revenues. However, we believe that the interest rates have peaked and we expect interest rates to decline next year, resulting in better ADTV YoY for Saudi equities. Our projections indicate a steady rise in trading ADTV at a 5-year CAGR of 11%. The future looks promising for STG as the group explores new avenues for increasing ADTV and has recently launched derivatives and other financial instruments. The potential for derivatives can be huge; however, we have not included their potential impact in our valuations as we wait to see the response and acceptability of recently launched single-stock options by the masses. Hence, we initiate on STG with a "Neutral" rating.

Figure 1 SAIBOR and average daily traded value (ADTV) graph



Source: Bloomberg, Al Rajhi Capital

**STG to drive economic transformation under Vision 2030:** STG is the central pillar of Saudi Arabia's Vision 2030 and is crucial for achieving the goals outlined in its primary Vision Realization Programs (VRPs) like the Financial Sector Development Program (FSDP), PIF program and Privatization Program. These VRPs aim to boost 1) the stock market capitalization to GDP ratio from 66.5% in 2019 to 80.8% by 2025 (ex-Aramco; 88% by 2030), 2) privatize state-owned assets, 3) foster new sectors in the economy, and 4) establish an exemplary clearing house. As the only exchange in Saudi Arabia, STG stands at the forefront of the country's economic overhaul, a key component for achieving the Financial Sector Development Program. This positioning is geared towards meeting the 2025 targets, which include plans for increased annual listings; elevating foreign ownership; and expanding the debt instrument market, among other objectives.

**Vertically integrated exchange; a monopoly in KSA:** In 9M2023, the ADTV has declined to SAR5.4bn, down 29% YoY but is still comfortably above its peers. In terms of market cap, STG has a total market cap of SAR11.4bn as of 9M2023 and was 9<sup>th</sup> largest exchange globally. Besides being a dominant force regionally in terms of traded value, the group holds a monopoly within the Kingdom as the only entity for listing and trading on the Exchange and provides end-to-end services including securities clearing, settlement services, and overseeing technology & data operations. Main market and NOMU observed substantial Initial Public Offering (IPO) activity in 2022, with 18 IPOs on the main market and 19 on NOMU. The IPOs collectively contributed SAR147bn to the market capitalization of the main market by the end of 2022. Moreover, 8 IPOs have already been initiated in 2023YTD in the main market and 32 in the NOMU market.

**Expanding its product offerings:** STG is gearing up to expand its product offerings. The company first entered into the derivatives space by launching single stock futures in July 2022. The exchange has also launched single stock options (SSO) in Nov 2023 which allow call/put options namely on four stocks Aramco, Al Rajhi, SABIC, and STC for now. STG plans to increase the SSO in the near future. In markets like India the paper market represent 219x of the cash markets. We have forecasted ADTV and revenues to grow at a 5-year CAGR of 3% and 7%, respectively. In our investment case, we have not included the potential upside that SSO provides as we await and see the acceptance of the said product. SSOs are a potential growth avenue that STG is targeting in the near future and provides a potential upside to our investment case.

**Diversified investor base:** The key advantage of the Saudi market is the diversified investor base it boasts. As of FY22 and continuing through the end of the third quarter in 2023, foreign ownership within the Saudi market has stabilized around 3.5%. However, despite this seemingly modest ownership percentage, foreign investors have significantly contributed, representing 18.6% of the total trading value in 2022. Moreover, this proportion has surged to exceed 20% in the 9M23. This heightened involvement of foreign investors in trading activities suggests the potential for a substantial uptick in trading volumes over time, aligning with an anticipated increase in foreign investments.

**Attractive margins driven by high operating leverage:** STG has maintained robust margins over the past five years, boasting an average gross margin c.60%, alongside average operating and net margins at 33% and 38% respectively. The company managed to record a 70% gross level margin in 2021, owing to a peak ADTV of SAR8.9bn. Since then, ADTV has plummeted gradually and is expected at SAR5.3bn by FY23 end. Hence, the recent decline in the gross margin in 9M23, dropping to 56%, below the historical average, can be associated with diminished equity market trading volumes. Despite this short-term setback, a positive long-term margin trajectory is anticipated, and we foresee gross margins to improve to 63.9% by FY27.

**Valuations:** We utilize relative valuation techniques to assess the company's worth and have established a target price of SAR175/sh. This valuation is based on employing the 2024e P/E, EV/EBITDA, and Price-to-Book (P/B) consensus multiples from a global peer set of STG. Using the above-mentioned approach, we arrive at a weighted average target price of SAR175/sh. The stock provides a downside of 3.5% from its last closing. Hence, we initiate coverage on STG with a "Neutral" rating.

**Key risks:** 1) lower than expected ADTV; 2) investors unwillingness to adopt derivatives; 3) higher volatility due to retail investors, 4) unfavorable regulatory changes like reduction in fees structure, 5) slowdown in IPOs, 6) failure to lure foreign investors, and 7) decline in oil prices leading to macro weakness.

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## Company Overview

The company, initially named “Saudi Stock Exchange” upon its establishment in 2007, transitioned to Saudi Tadawul Group (STG) in March 2021. Since its inception, it has undergone significant development and innovation, cementing its position as a leading force in the regional capital market. In 2009, the Fixed Income market was introduced, followed by the launch of ETFs in 2010. Between 2016 and 2017, the company established Edaa and Nomu, along with listing REITs for the first time. A pivotal moment occurred in 2019 with the listing of Saudi Aramco and the market's inclusion in major indices such as MSCI, FTSE, and S&P. Most recently STG introduced single stock options which includes 11 futures and 4 options. STG acts as the holding company for four subsidiaries: the Saudi Exchange Company, Edaa, Muqassa, and WAMID.

Saudi Tadawul stands as the largest financial exchange in the Middle East and ranks as the 9<sup>th</sup> largest globally. It assumes a pivotal role in the advancement of Saudi Arabia's capital markets, aligning with the economic transformation objectives outlined in the Saudi Vision 2030. Benefiting from a vertically integrated structure, Tadawul oversees centralized trading, clearing, settlement, and depository services.

Currently, equities represent the primary source of its trading revenues. However, the company has identified the diversification of revenue streams as a key long-term priority. This diversification encompasses fixed income, derivatives, data and technology, as well as post-trade and other services. Operating across three distinct business segments, the company aims to solidify its position and expand its offerings.

### STG Structure

**Saudi Exchange Company:** The Saudi Exchange, established on March 30, 2021, as a closed joint-stock company with a single shareholder, specializes in the listing, trading, and dissemination of market information regarding securities. Its core functions encompass managing the Exchange, providing a robust platform for trading listed securities, granting companies access to financial resources, and enabling investor participation in listed securities. Structured around five primary divisions—Listings, Cash Markets, Derivatives, Market Information, and Client Relations Development—the Saudi Exchange orchestrates its operations, effectively facilitating trading activities, disseminating market data, and nurturing client relationships.

**EDAA:** Edaa, formally known as the Securities Depository Center Company, was established on August 30, 2016, as a wholly owned subsidiary. Its primary focus lies in offering comprehensive securities settlement for all market-traded securities, encompassing depository services such as custody, registration, and maintaining registries for clients. At the core of its operations is the management and upkeep of the Depository and Settlement System (DSS), an advanced electronic book-entry system crucial for recording and managing securities, as well as authenticating ownership. Beyond its operational functions, Edaa is dedicated to advancing the efficiency of securities deposit and registration services, aligning with the goals of Saudi Vision 2030. Its overarching aim is to cultivate a more dynamic environment conducive to excellence across all sectors within the capital market.

**Muqassa:** Muqassa, established on February 18th, 2018, operates as a single shareholder closed joint stock company. Its primary function revolves around providing clearing services for derivative products. By doing so, Muqassa effectively mitigates post-trade risks, delivers centralized counterparty risk management services, and cultivates clearing solutions aligned with global best practices. Functioning as an intermediary between parties involved in securities trading, Muqassa assumes the role of the buyer to every seller and the seller to every buyer. Consequently, it assumes responsibility for ensuring the settlement of transactions, alleviating concerns related to counterparty risks for the trading entities. Muqassa is poised to expand its clearing services to encompass all other securities in the near future.

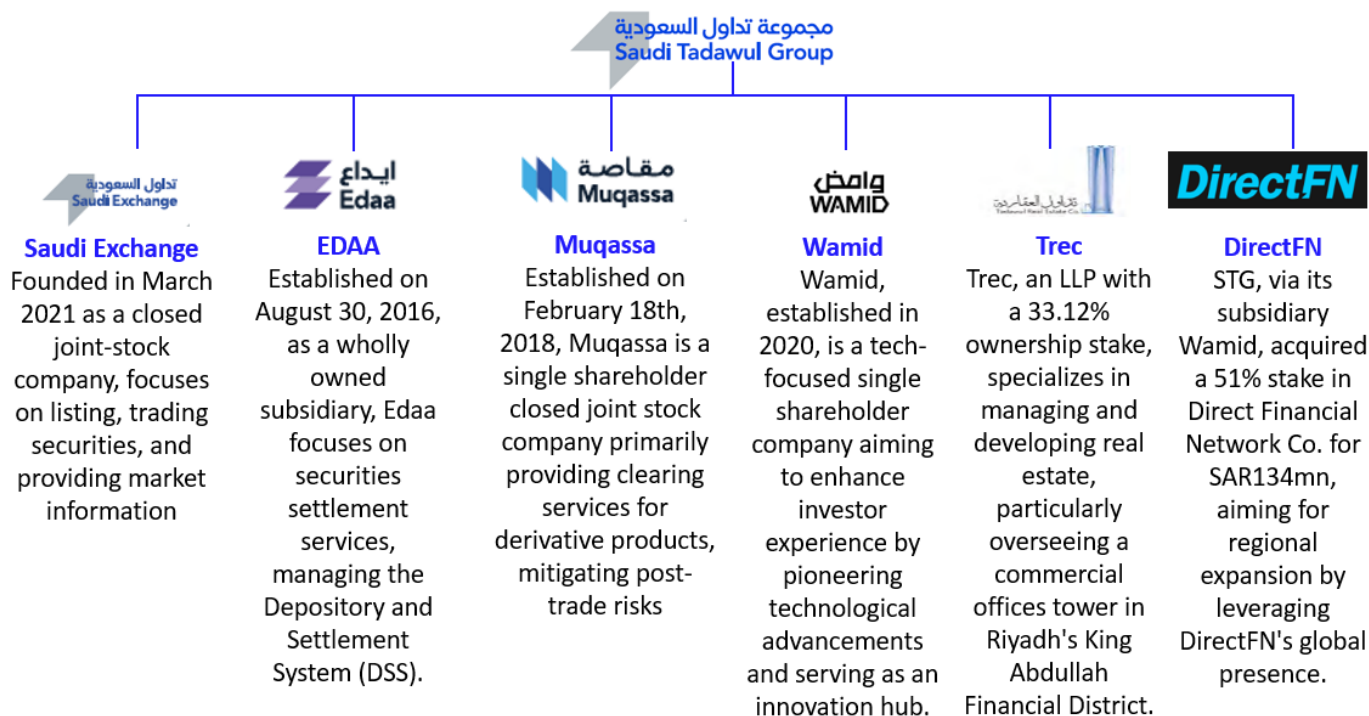
**Wamid:** Wamid, known formally as Tadawul Advanced Solutions Company, was established on September 28th, 2020, functioning as a single shareholder closed joint stock company. Its diverse

range of activities encompasses financial technology solutions, extensive research and development in engineering and technology, as well as conducting market research and opinion polls. The core objective of Wamid revolves around enriching the investor experience within the market by spearheading technological advancements and facilitating access to crucial data. Acting as a central hub for innovation across the company, Wamid aims to drive progress and innovation within the industry.

**Trec:** Trec, an LLP in which there is a 33.12% ownership stake, stands for Tadawul Real Estate Company. Specializing in real estate management and development, Trec is presently engaged in overseeing the commercial offices tower located within the King Abdullah Financial District in Riyadh city.

**DirectFN:** STG completed the acquisition of a 51% stake in the Direct Financial Network Co. (DirectFN) group in May 2023 via the former's subsidiary, Tadawul Advanced Solutions Co. (Wamid). DirectFn is headquartered in Riyadh, with offices in the UAE, Sri Lanka, and Pakistan. STG acquired DirectFN for SAR134mn using its internal resources. The transaction is expected to facilitate STG's regional and global expansion by utilizing DirectFN's presence in 20 countries. This collaboration will grant STG access to two development centers and 500 employees, including 300 software developers, through DirectFN. Leveraging DirectFN's technical expertise in emerging technologies, STG aims to introduce innovative tech solutions to the Saudi capital market, aligning with Vision 2030's Financial Sector Development Program

Figure 2 Organisation Structure



Source: Company IPO prospectus, News articles, Al Rajhi Capital

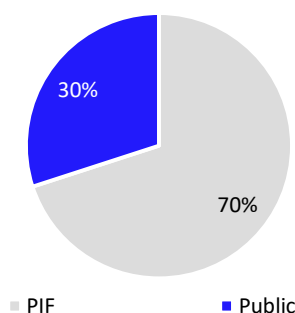
**The group identifies revenues from three major segments:**

**Capital Markets:** This segment's activities encompass various revenue streams, such as trading commissions for securities and derivatives, admission fees for initial listings and subsequent capital raises, annual fees for securities traded within the group's markets, and earnings from secondary market services. Approximately 77% of the total revenues from the capital markets segment are derived from equities, followed by 22% from listing fees, with the remainder sourced from membership fees. The Saudi Exchange used to impose a fee of 0.9 basis points (bps) per trade on both buyers and sellers, resulting in a cumulative revenue of 1.8 bps based on the traded value. However, the group has recently revised its fee structure to 0.9bps for trading, 0.5bps each for deposit and clearing, and 0.1bps for safekeeping, resulting in 2.0bps fees (vs. 1.8bps earlier). Listing fees comprise charges for new listings and an ongoing annual fee structure. For the main market, the initial listing fee amounts to SAR 50,000, accompanied by an annual fee equivalent to 1 basis point of the paid-up capital, in addition to 0.5 basis points of the market capitalization, capped at SAR1.0mn. Membership fees are levied on brokerage firms engaged in trading activities at Tadawul, encompassing both an initial and an annual membership payment.

**Post-Trade Services:** These encompass critical functions such as clearing (Muqassa), settlement (Edaa), custody, and safekeeping (both handled by Edaa). Tadawul stands out as a vertically integrated exchange, offering all these services under a single roof—a rarity on a global scale. As an example, Euroclear in Europe operates as an independent clearing house. The operations within this segment involve the registration of investment portfolios within the filing and settlement system, recording ownership details, facilitating ownership transfers, managing settlement and clearing processes, and ensuring secure safekeeping of ownership records. Additionally, this segment handles the registration of any ownership restrictions pertaining to filed securities and collaborates with market members and settlement agents within the filing and settlement system. The bulk of its revenues, approximately 58% of the total post-trade revenues, are directly tied to trading volumes. The remainder is associated with depository and safekeeping services.

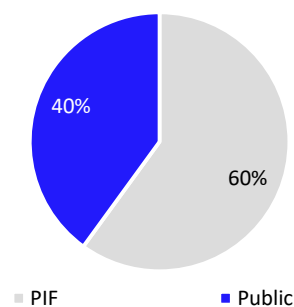
**Data & Technology:** The primary focus of this segment is to expand the scope of technology services, offering top-tier real-time trading data, reference data, market indices, and financial information to the financial community. Additionally, it involves providing financial technology solutions, conducting research and development in engineering and technology, and delivering innovative capital market solutions to stakeholders. The Data and Technology Services segment generates revenue by offering information and data products, such as benchmarks, tailored indices, real-time market data, reference data, and analytical services, to clients and stakeholders. This segment has witnessed significant growth in the last two quarters due to STG's acquisition of DirectFN. The group completed DirectFN acquisition on 7 May 2023, hence, the impact on revenues in 2Q23 is on pro-rata basis.

Figure 3 Post-IPO shareholding



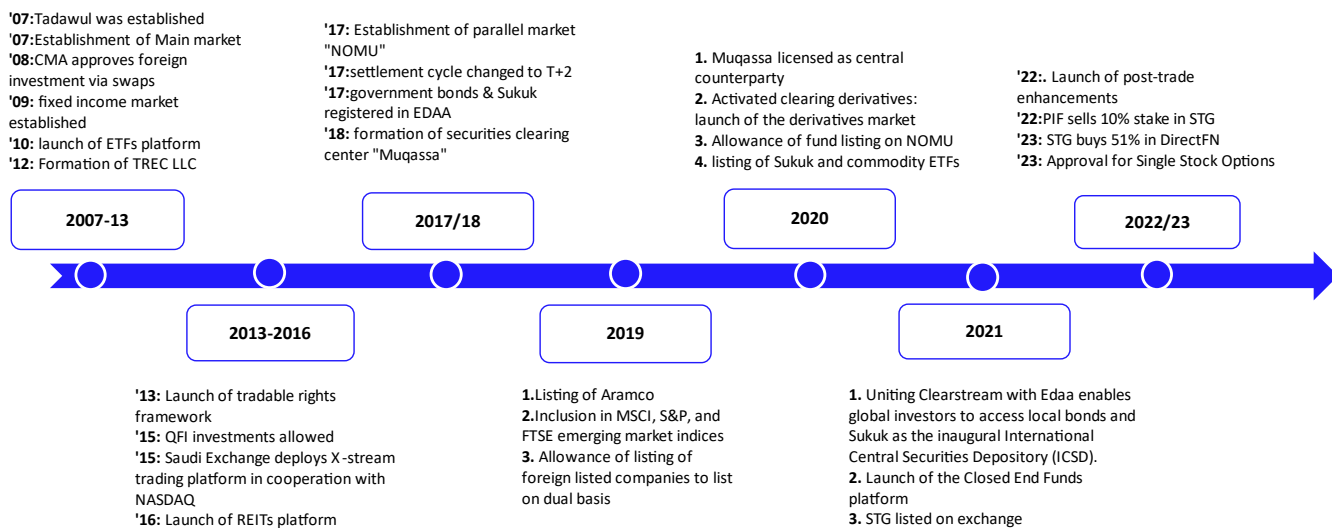
Source: IPO Prospectus, Al Rajhi Capital

Figure 4 Post-secondary offering shareholding



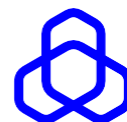
Source: Tadawul, Al Rajhi Capital

Figure 5 **STG Timeline**



Source: Company IPO Prospectus, News releases, Al Rajhi Capital





## Business Model

**Trading Revenues:** The primary revenue stream for the group originates from the fees applied to the executed transaction value. This fee structure involves 0.9 basis points for trading, equally levied on both buyer and seller, alongside 0.5 basis points each for clearing and safekeeping, and 0.1 basis points for EDAA, totaling 2.0 basis points. It's important to note that this represents a new fee structure, as the group previously charged a 1.8 basis points trading fee. The new fee structure implies no increase in charges for market participants as we believe that CMA's portion from gross commission has been reduced. Any adjustments to the fee structure will require approval from the Capital Markets Authority (CMA) and is likely to involve further reduction from CMA's portion. Derivatives carry a distinct fee structure. For Index futures, STG charges SAR25 per contract, whereas single stock futures incur a transaction cost of 2.5 basis points of the transaction value, and single stock options carry a SAR2 per contract transaction cost. Below we outline the fee structure of trading options and futures:

Figure 6 Transaction fee structure

Instrument	Transaction fee
Equity	2.0bps of trading value
Index Futures	SAR25/contract
Single Stock Future	2.5bps/transaction value
Single Stock Options	SAR2/contract

Source: Company reports, Tadawul Website, Al Rajhi Capital

Figure 7 Stock/Index options and futures offered

	Futures	Options
MT30 (MSCI Tadawul 30)	✓	✗
Aramco	✓	✓
AlRajhi	✓	✓
Alinma Bank	✓	✗
SABIC	✓	✓
STC	✓	✓
Saudi Kayan	✓	✗
Saudi Electricity	✓	✗
Almarai	✓	✗
Maaden	✓	✗
SNB	✓	✗

Source: Tadawul Website, Al Rajhi Capital

**Non-Trading Revenues:** This segment accounted for 38% of group's revenues in 2022. In 9M2023 non-trading revenues accounted for 47% of the total largely driven by Data & Technology segment and amplified by lower trading revenues. The company anticipates enduring demand for market data among market participants, emphasizing its significance. Management is strategically focusing on this segment and expresses confidence in its future performance. Examples like the ESG Index and specialized data highlight instances where institutional investors pay for access to specific data sets. The recent acquisition of DirectFN is in line with management's vision to increase non-trading revenues. Additionally, the company plans to introduce new services soon, including an E-register for unlisted companies, a crowdfunding platform, and fund administration services.

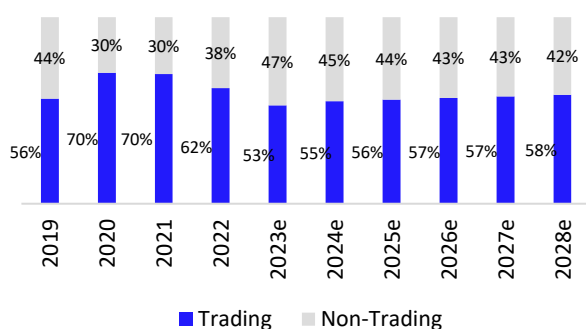
The group reports three main segments:

- Capital markets:** This is the segment largest segment and largely consists of trading revenues from equities, derivatives, fixed income etc. The non-trading income for this segment comes from listing services. This segment accounted for 38% of the total revenues in 2022 and 33% in 9M2023.
- Data & Technology Services:** This segment focuses on expanding STG's Technology Services division, offering premium real-time trading data, reference data, market indices, financial information, financial technology solutions, as well as conducting research and development in engineering and technology fields, and market research including opinion polls. The revenue generated by this business unit encompasses income derived from Data and Technology Services. This segment contributes completely to the non-trading revenues. Moreover, the revenues from DirectFN will also be accounted under this segment.



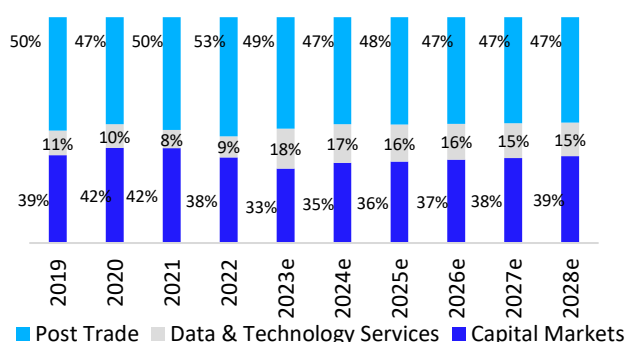
- Post-Trade:** This segment oversees various post-trade services, encompassing the registration of investment portfolios within filing and settlement systems, managing ownership records, facilitating transfers, settlements, and safekeeping of ownership, recording ownership restrictions on filed securities, collaborating with market members and settlement agents for filing and settlement systems. Additionally, it involves the coordination and management of securities issuers' records, organizing issuer general assemblies (including remote voting services), issuing reports, notifications, and related information, adhering to financial market regulations. The revenue generated by this business unit stems from post-trade services. More than 50% of this segment's revenues are classified as trading revenues.

**Figure 8 Activity-wise revenue split 2019-28e**



Source: Company data, Al Rajhi Capital

**Figure 9 Segment-wise revenue split 2019-28e**

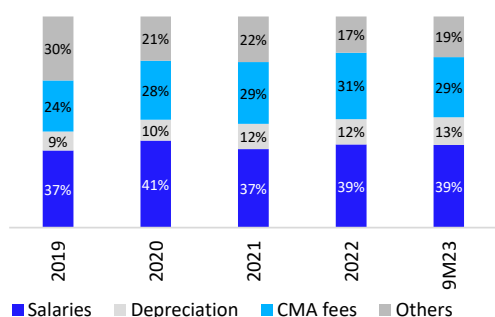


Source: Company data, Al Rajhi Capital

**Cost Model:** Approximately 45% of the cost of sales in 2022 comprised of depreciation and CMA fees. These cost components are predominantly fixed and are not contingent on revenues. Additionally, the most substantial cost factor is the employee expense which represents 39% of the total COGS in 2022 and 39% in 9M2023. The management intends to expand the workforce to explore new revenue streams, although this expenditure could be streamlined as the group aims for operational optimization.

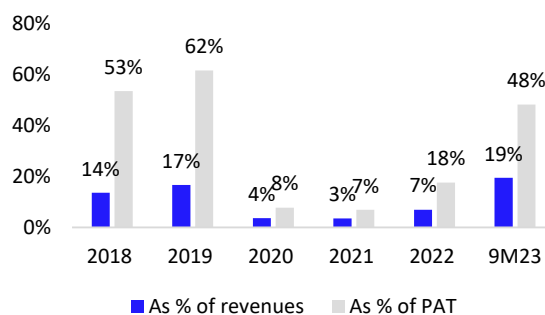
**Investment Income:** Besides its usual revenue sources, the group derives a substantial portion of income from various investments such as time deposits, SAMA bills, FVPTL, and amortized costs. In 2022, investment income accounted for nearly 7% of the total revenue and a whopping 18% of the bottom-line. This serves as a hedging mechanism for the group. For instance, the income from time deposits has notably risen in 9M23 due to higher interest rates, mitigating some of the effects of decreased trading activity.

**Figure 10 Cost contribution**



Source: Company data, Al Rajhi Capital

**Figure 11 Investment income as % of revenues and PAT**



Source: Company data, Al Rajhi Capital

## Investment Thesis

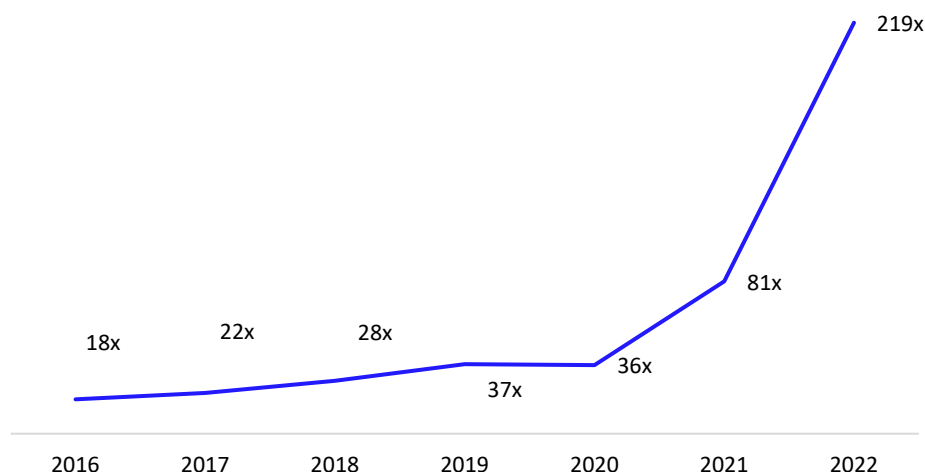
**STG to drive economic transformation under Vision 2030:** STG is the central pillar of Saudi Arabia's Vision 2030 and is crucial for achieving the goals outlined in its primary Vision Realization Programs (VRPs) like the Financial Sector Development Program (FSDP), PIF program and Privatization Program. These VRPs aim to boost 1) the stock market capitalization to GDP ratio from 66.5% in 2019 to 80.8% by 2025 (ex-Aramco; 88% by 2030), 2) privatize state-owned assets, 3) foster new sectors in the economy, and 4) establish an exemplary clearing house. As the only exchange in Saudi Arabia, STG stands at the forefront of the country's economic overhaul, a key component of the Financial Sector Development Program. This positioning is geared towards meeting the 2025 targets, which include plans for increased annual listings, elevating foreign ownership; and expanding the debt instrument market, among other objectives.

**Vertically integrated exchange; a monopoly in KSA:** In 2022, the exchange experienced an Average Daily Trading Value (ADTV) of US\$1.8bn (approximately SAR6.8bn), significantly surpassing its closest regional competitor, ADX (UAE), which recorded a mere US\$0.5bn. So far in 9M2023, ADTV has declined to SAR5.4bn, down 29% YoY but is still comfortably above its peers. In terms of market cap, STG has a total market cap of SAR11.4bn as of 9M2023 and is 9<sup>th</sup> largest exchange globally as of Sep 2023. Besides being a dominant force regionally in terms of traded value, the group holds a monopoly within the Kingdom as the exclusive entity for listing and trading on the Exchange and provides end-to-end services including securities clearing, settlement services, and overseeing technology & data operations.

Additionally, the group operates in two distinct markets: the Tadawul Exchange (main market) and NOMU (alternate market). Both markets observed substantial Initial Public Offering (IPO) activity in 2022, with 18 IPOs on the main market and 19 on NOMU. The IPOs collectively contributed SAR147bn to the market capitalization of the main market by the end of 2022. Moreover, 8 IPOs have already been initiated in 2023YTD in the main market and 33 in the NOMU market. Lastly, the bond market has witnessed a significant boom with interest rates at a decade high. The total bond value traded increased to SAR14.3bn in 9M2023 as compared with SAR 11.4bn in 2022. Moreover, in 9M23 the number of transactions increased to 28mn from 6mn in 2022.

**Expanding its product offerings:** STG has lagged in terms of products when compared with global peers. But in line with Vision 2023, STG is gearing up to expand its product offerings. The company first entered into the derivatives space by launching single stock futures in July 2022. Since then, 10 SSF (ex-index future) have been listed with a meager ADTV of SAR0.8mn. The primary reason for the poor reception of SSF could be that these products were targeted toward institutions while STG is dominantly a retail market. Keeping this in mind, the exchange has launched single stock options (SSO) in Nov 2023 which allow call/put options namely on four stocks Aramco, Al Rajhi, SABIC, and STG for now. STG plans to increase the SSO in the near future. We believe that SSOs will take time to gain acceptability among the retail investors but once done have a tremendous potential to increase the ADTV. In markets like India, the annual traded value of the paper market represents 219x of the cash markets. We have forecasted ADTV and revenues to grow at a 5-year CAGR of 3% and 7%, respectively. In our investment case, we have not included the potential upside that SSO provides as we await and see the acceptance of the said product. SSOs are a potential growth avenue that STG is targeting in the near future and provide a potential upside to our investment case.

Figure 12 India – Derivatives vs Cash annual traded value



Source: National Stock Exchange (India), Al Rajhi Capital

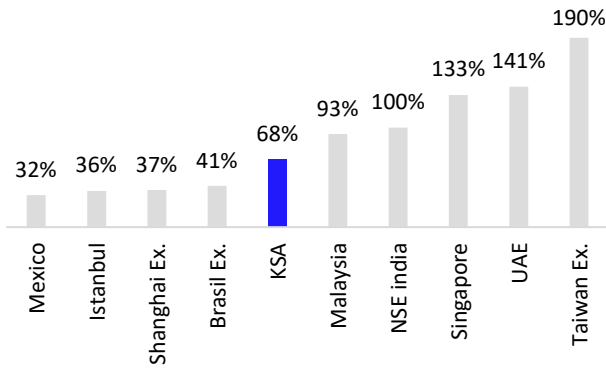
Moreover, the recent allowance of market makers by CMA will also help improve liquidity in the market while STG is also eyeing dual listing opportunities given the strong demand and successful dual listing of Americana. The company has also launched 4 new equity indices which will provide investors with a broad range of benchmarks encouraging them to offer new products based on innovative investing strategies. The four equity indices include the Tadawul Large/Medium, Small Cap, and Tadawul IPO indices.

**Diversified investor base:** The key advantage of the Saudi market is the diversified investor base it boasts. As of FY22 and continuing through the end of the third quarter in 2023, foreign ownership within the Saudi market has stabilized around 3.5%. However, despite this seemingly modest ownership percentage, foreign investors have significantly contributed, representing 18.6% of the total trading value in 2022. Moreover, this proportion surged to exceed 20% in the 9M23. This heightened involvement of foreign investors in trading activities suggests the potential for a substantial uptick in trading volumes over time, aligning with an anticipated increase in foreign investments. While Saudi Institutions' market share is on the rise (12.6% in 9M23 vs 6.3% in FY22), Saudi Individuals (retail investors) still constitute the major chunk of trading accounting for 64.9% of all trading activity in 9M23, which is a decline of 19.5 percentage points from 84.4% in FY21.

**Attractive margins driven by high operating leverage:** STG has maintained robust margins over the past five years, boasting an average gross margin c.60%, alongside average operating and net margins at 33% and 38% respectively. The company managed to record a 70% gross level margin in 2021, owing to a peak ADTV of SAR8.9bn. Since then, ADTV has plummeted gradually and is expected at SAR5.3bn by FY23 end. Hence, the recent decline in the gross margin in 9M23, dropping to 56%, below the historical average, can be associated with diminished equity market trading volumes. Despite this short-term setback, a positive long-term margin trajectory is anticipated due to a considerable portion of fixed expenses within the cost of sales, hinting at stability and potential margin improvement in the future. We foresee gross margins to improve to 63.9% by FY27. However, we cannot rule out a better-than-expected jump in gross margins given STG's constant efforts to increase ADTV by introducing new products specifically derivatives.

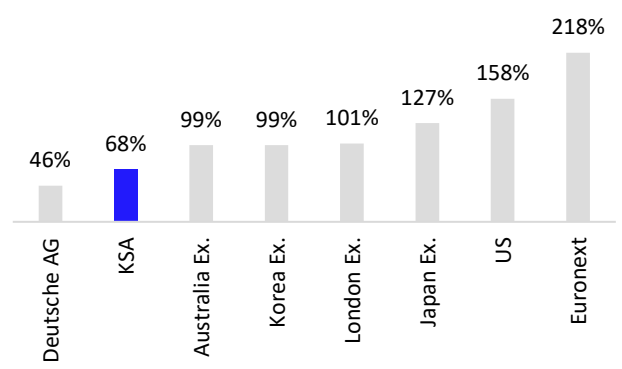
**STG vs Global Peers**

Figure 13 Mcap/GDP (%) – emerging markets\*



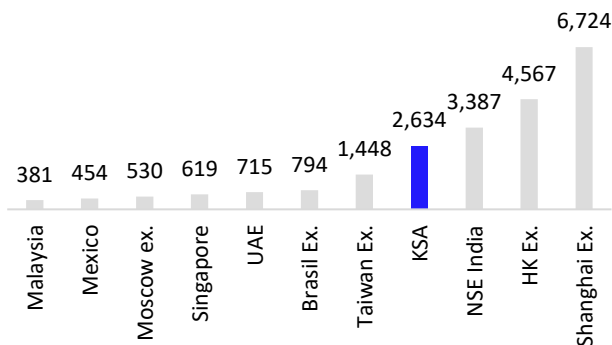
Source: World Federation of Exchanges, Tadawul Website, Al Rajhi Capital; \*2022 data

Figure 14 Mcap/GDP (%) – developed markets\*



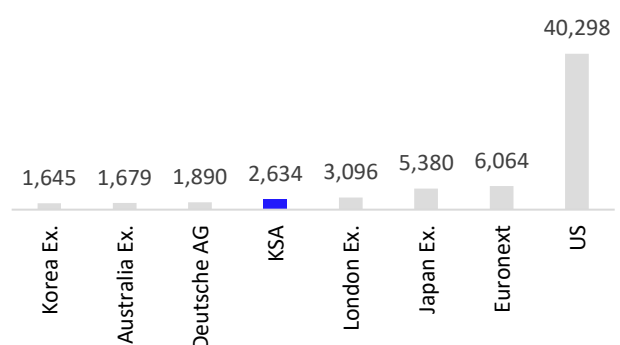
Source: World Federation of Exchanges, Tadawul Website, Al Rajhi Capital; \*2022 data; US data includes NASDAQ and NYSE

Figure 15 STG Mcap vs emerging markets (US\$bn)\*



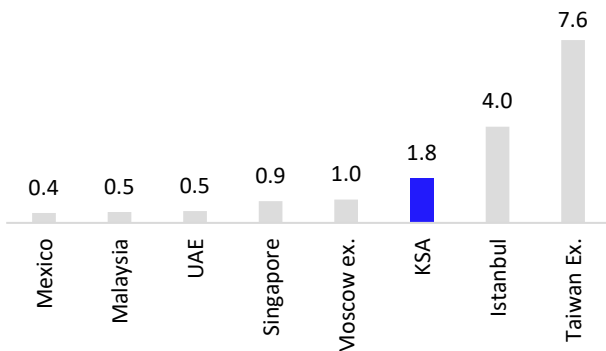
Source: World Federation of Exchanges, Tadawul Website, Al Rajhi Capital; \*2022 data

Figure 16 STG Mcap vs developed markets (US\$bn)\*



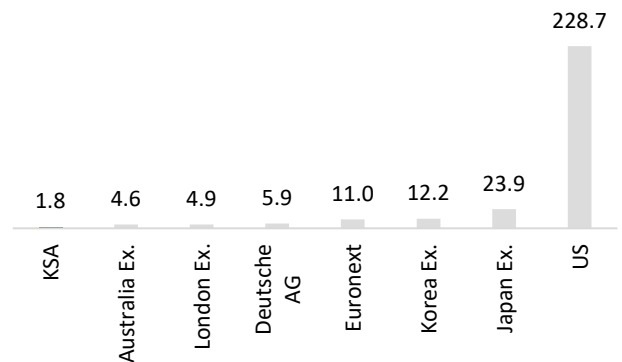
Source: World Federation of Exchanges, Tadawul Website, Al Rajhi Capital; \*2022 data; US data includes NASDAQ and NYSE

Figure 17 ADTV – Emerging Markets (US\$bn)\*



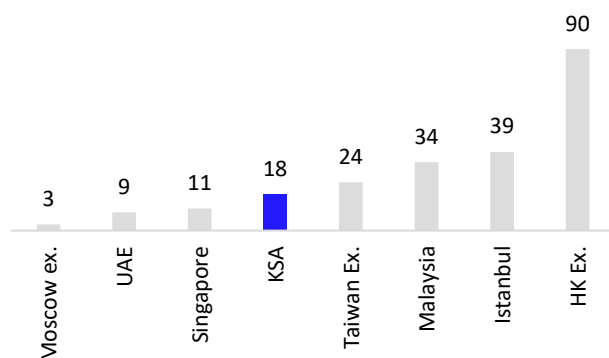
Source: World Federation of Exchanges, Tadawul Website, Al Rajhi Capital; \*2022 data

Figure 18 ADTV – Developed Markets (US\$bn)\*



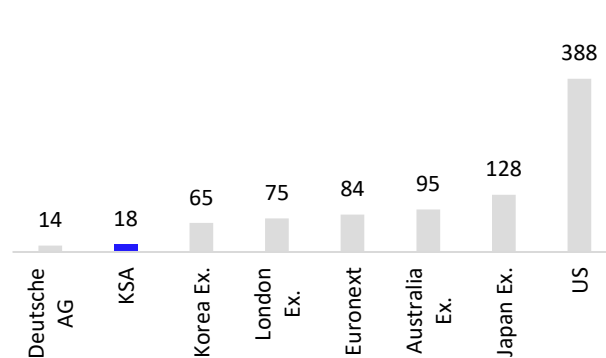
Source: World Federation of Exchanges, Tadawul Website, Al Rajhi Capital; \*2022 data; US data includes NASDAQ and NYSE

Figure 19 New listings – Emerging Markets\*



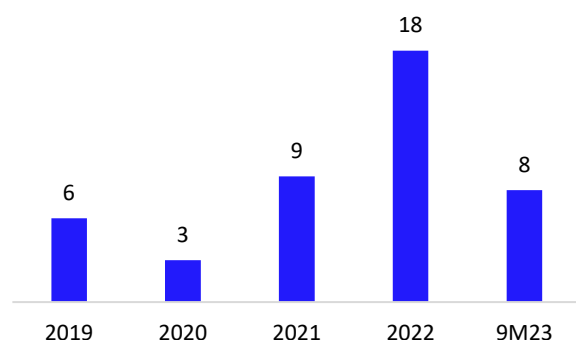
Source: World Federation of Exchanges, Tadawul Website, Al Rajhi Capital; \*2022 data

Figure 20 New listings – Developed Markets\*



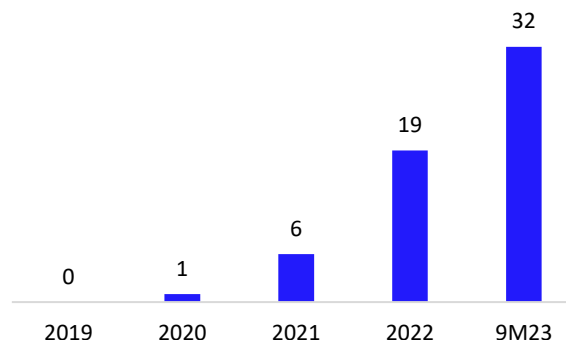
Source: World Federation of Exchanges, Tadawul Website, Al Rajhi Capital; \*2022 data; US data includes NASDAQ and NYSE

Figure 21 Number of IPOs – main market



Source: Tadawul Website, Al Rajhi Capital

Figure 22 Number of IPOs – NOMU



Source: Tadawul Website, Al Rajhi Capital

Figure 23 Tadawul FY22 listings

	Shares offered (mn)	Offer Price (SAR)	Close Price (SAR)	Mcap (SARbn)
East Pipes	6.3	80	37	0.8
Equipment House	6.0	52	61	1.2
Elm	24.0	128	332	26.6
Aldawaa	25.5	73	72	6.1
Nahdi Medical	39.0	131	167	21.7
Amak	19.8	63	72	4.7
Saudi Home Loans	30.0	20	20	2.0
Retal	12.0	120	124	4.9
Alamar	10.6	115	139	3.5
Naqi Water	6.0	69	66	1.3
Arabian Drilling	26.7	100	113	10.0
Marafiq	73.1	46	47	11.7
Alinma Hospitality REIT	51.1	10	-	-
2P	4.5	185	175	2.6
Americana	2,527.1	3	3	25.7
Riyadh Cables	33.0	43	36	5.4
AlSaif Stores	10.5	115	91	3.2
Luberef	50.0	99	93	15.7
<b>Total</b>	<b>2,955.3</b>			<b>147.4</b>

Source: Tadawul Website, Al Rajhi Capital

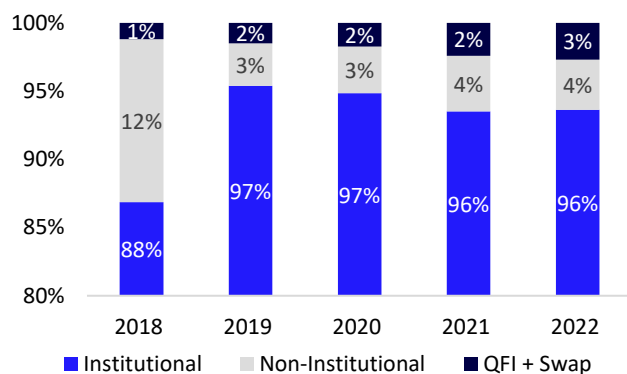
Figure 24 NOMU FY22 listings

	Shares offered (mn)	Offer Price (SAR)	Close Price (SAR)	Mcap (SARbn)
Gas Arabian	0.8	90	59	0.9
Raoom	1.0	80	113	0.6
Aljouf Mineral Water	0.6	35	39	0.1
Arabian International	5.0	82	37	0.7
Arabian Food	0.3	71	91	0.1
Ladun Investment	5.0	18	16	0.8
Amwaj International	0.6	72	108	0.6
Saudi Networkers Services	1.5	71	50	0.3
International Human Resources	0.5	34	56	0.1
Naba Alsaha Medical	1.4	57	43	0.3
Arabian Plastic Industrial	1.0	27	28	0.1
Albabtin Food	0.5	77	50	0.2
Alwaha REIT Fund	3.2	10	11	0
Knowledge Tower	0.4	40	60	0.1
Rayan Advanced	2.0			
Molan Steel	0.5	24	32	0.1
Saudi Top	0.9	133	113	0.5
Leen Alkhair	1.0	65		
Nofoth Food	0.3	150		
<b>Total</b>	<b>26.5</b>			<b>5.8</b>

Source: Tadawul Website, Al Rajhi Capital

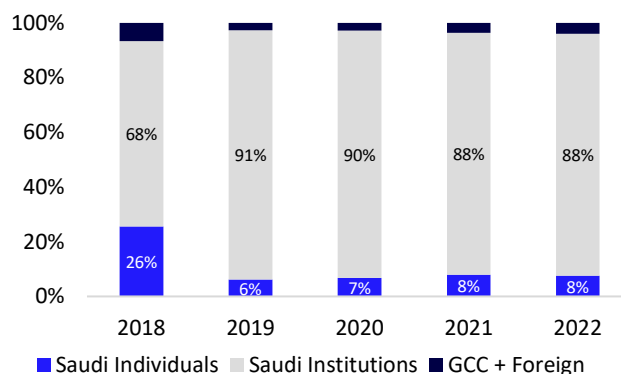
## Ownership and Trading Graphs

Figure 25 Ownership by type of investor (%)



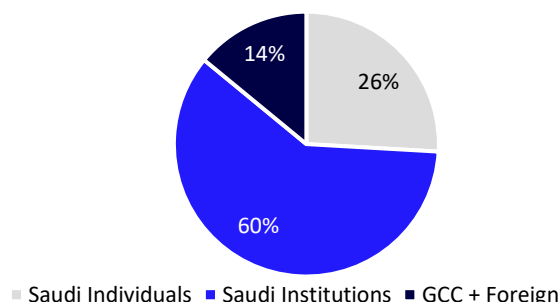
Source: Tadawul Website, Al Rajhi Capital

Figure 26 Domestic vs foreign ownership (%)



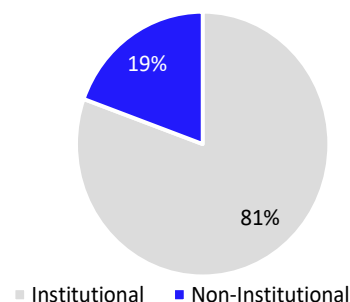
Source: Tadawul Website, Al Rajhi Capital

Figure 27 Free Float Ownership by type of investor (%)



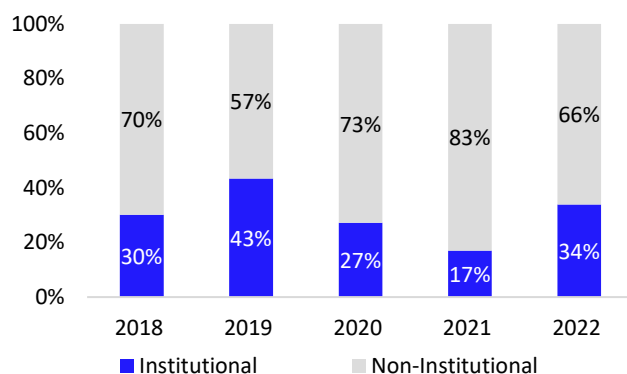
Source: Tadawul Website, Al Rajhi Capital; At the end of September 2023

Figure 28 Free Float ownership split (%)



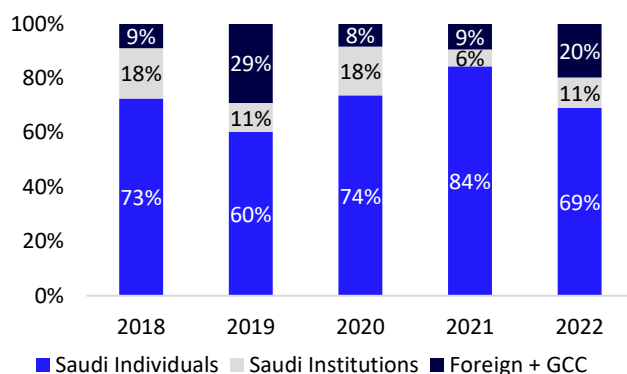
Source: Tadawul Website, Al Rajhi Capital; At the end of September 2023

Figure 29 Trading by type of investor (%)



Source: Tadawul Website, Al Rajhi Capital

Figure 30 Domestic vs foreign Trading (%)



Source: Tadawul Website, Al Rajhi Capital



## Valuation

Our preferred valuation approach to value the company is relative valuation, where we assign an equal weight to price-to-earnings, EV/EBITDA, and price-to-book method. Using the above-mentioned approach, we arrive at a weighted average target price of SAR175/sh. The stock provides a downside of 3.5% from its last closing.

Figure 31 Valuation

Valuation Methodology	Fair Value (SAR)	Weightage	Weighted value per share (RO)	Upside/Downside
Relative Valuation - P/E	157	33%	52	-13%
Relative Valuation - EV/EBITDA	179	33%	60	-1%
Relative Valuation - P/B	191	33%	64	5%
<b>Fair Value (SAR)*</b>		<b>100%</b>	<b>175</b>	
CMP (SAR)			181	4-Dec-23
<i>Upside/(Downside)</i>			-3.5%	

Source: Al Rajhi Capital estimates; \*Target Price is rounded off to SAR175/sh

We believe STG deserves a premium to its peers as it is a monopoly in a growing economy and has tremendous potential to increase its ADTV by launching new products. For the price-to-earnings and EV/EBITDA approach, we have used regional peer companies multiple of 30.2x and 22.2x and assigned a premium of 20% resulting in a value of SAR153/sh and SAR179/sh, respectively. For the price-to-book method, we use a multiple of 6.9x resulting in a value of SAR191/sh. Assigning equal weights, we arrive at our TP of SAR175/sh.

**Conclusion:** The stock hit a high of SAR204/sh on July 23 and has since come down to SAR181/sh. These are very similar levels to what the stock was trading at the start of the year. STG has underperformed the broader index, which makes sense as ADTV is expected to decrease 23% YoY. However, we believe the trading value to recover in coming years as the interest rates have peaked and are likely to only decrease from here onwards. In addition, STG has launched SSO currently for 4 companies and will gradually expand it. This poses a significant upside risk to our investment case as the derivatives market in the Kingdom remains untapped at the moment and has huge potential. Having said that, the near-term earnings for the company are likely to remain subdued. Hence, we initiate coverage with a “Neutral” rating providing a downside of 3.5% to the last closing price.

## Key Risks

1. Lower than expected ADTV.
2. Investors unwillingness to adopt derivatives.
3. Higher volatility due to retail investors.
4. Unfavorable regulatory changes like reduction in fees structure.
5. Slowdown in IPOs.
6. Failure to lure foreign investors.
7. Decline in oil prices leading to macro weakness.

## Financial Analysis

**Revenue analysis:** From 2017 to 2022, revenues experienced a CAGR of 14%, primarily propelled by the increased trading volume in the equity segment. The historic low-interest rate boosted interest in equity markets during the said period. In FY22, nearly 37 IPOs (18 in the main market) happened in Tadawul. The introduction of single-stock options might potentially elevate trade value, yet only a partial rollout has occurred. Consequently, we maintain a conservative stance in our estimates due to the unknown pace of its effect on trading values. Going forward, we expect revenues to grow at a decent 5-year CAGR of 10% as ADTV normalizes.

**Cost and gross margin analysis:** From 2017–22, the cost of sales grew at a CAGR of 6%, and we expect it to grow at 5% for the period between 2023e-2028e. The cost is expected to be largely driven by salaries, which grew at a CAGR of 12% during 2017–22, and we estimate a growth of 7% between 2023e-28e as the group plans to increase the headcount to cater to new revenue streams. The second largest cost is the CMA fee, which is expected to remain constant. Lastly, we expect depreciation to grow at a CAGR of 3% during 2023e-28e much lower than the historical five-year CAGR of 14%. As most costs are fixed, the company is set to experience the benefit of increased ADTV. Thus, the gross margins are expected to expand to 65% by 2028e.

**Investment Income:** The investment income has shown substantial growth, boasting a 20% CAGR between 2017 and 2022, with a nearly 1.6x surge in 2022 compared to the prior year. This surge is primarily credited to increased returns on time deposits, fuelled by prevailing high-interest rates. As of the end of the 3Q23, the group's investment portfolio reached SAR388 million, a notable achievement. A significant proportion of the group's SAR2.0 bn in cash and equivalents is allocated to time deposits, strategically hedging against the impact of high interest rates on trading volumes, and consequently, the group's top-line revenue. We anticipate a -1% CAGR for the 2023e-2028e period, assuming an eventual normalization of interest rates during this timeframe offset by increasing cash investments.

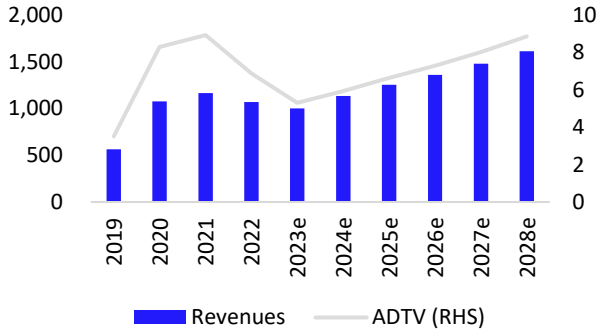
**Working Capital:** Looking ahead to the forecasted period from 2023e-28e, we anticipate the working capital to stabilize and maintain its stability. This projection aligns with the group's efforts toward achieving enhanced working capital efficiency.

**Capex:** The capex as a percentage of sales has spiked in 2022 due to the group's investment into technology as it prepares for expansion into single stock options trading, and co-location services, however, we believe it shall stabilize from 2024e onwards as most of the capex shall be maintenance capex.

**ROE:** The average ROE for 2017-22 was 10%, however, it is largely due to mid-single digit ROE between 2017-19, the returns increased to mid-double digits from 2020 onwards and we estimate an average ROE of 17.6% during 2023-28e.

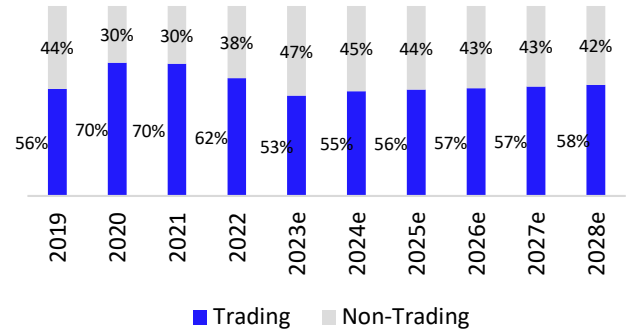
**Debt:** The group, historically devoid of debt, has recently secured debt amounting to approximately SAR16 million during the second quarter of 2023. We believe that this debt acquisition might serve short-term operational necessities, especially considering that the group maintains approximately SAR2.0 billion in cash on its balance sheet. Our forecast anticipates the repayment of this debt starting from 2023 onwards, foreseeing a trajectory where the group continues to remain predominantly unleveraged.

**Figure 32 STG revenues (SARmn) and ADTV (SARbn)**



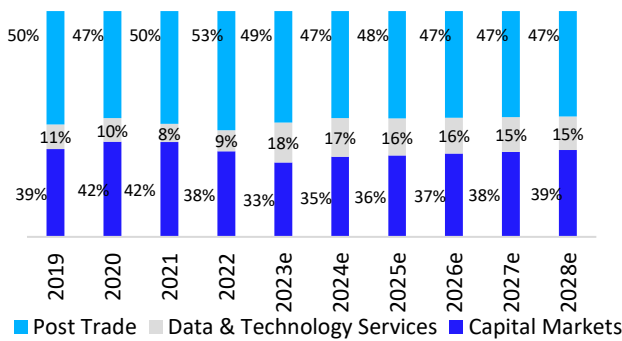
Source: Company Data, Al Rajhi Capital Estimates

**Figure 33 Revenue split by activity**



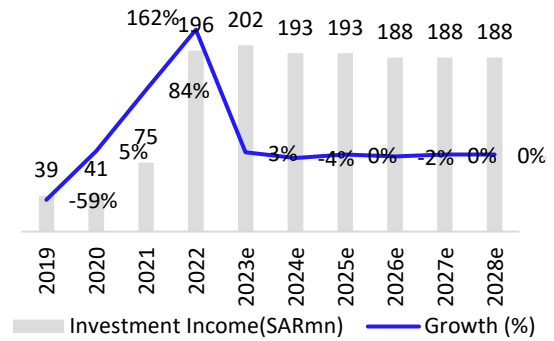
Source: Company Data, Al Rajhi Capital Estimates

**Figure 34 Revenue evolution by segment**



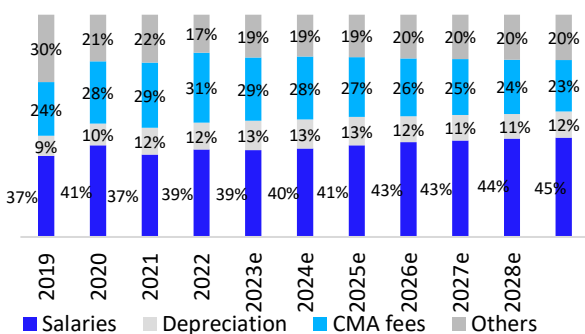
Source: Company Data, Al Rajhi Capital Estimates

**Figure 35 Investment Income**



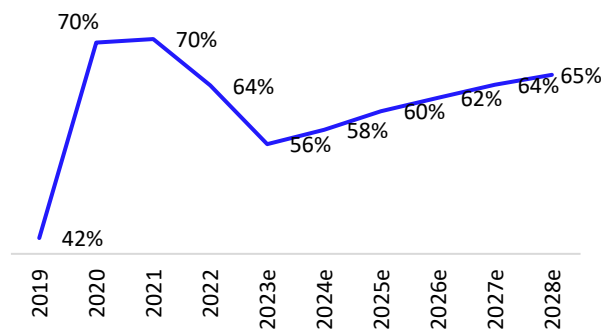
Source: Company Data, Al Rajhi Capital Estimates

**Figure 36 Cost bifurcation**



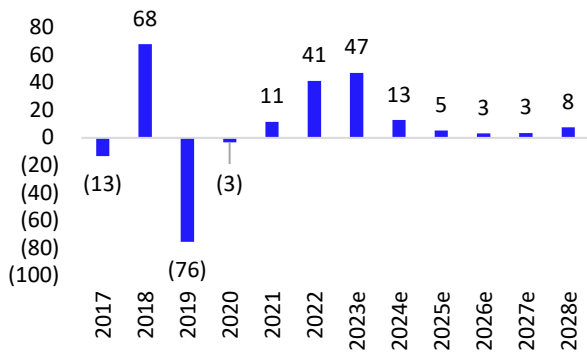
Source: Company Data, Al Rajhi Capital Estimates

**Figure 37 Gross margin evolution**



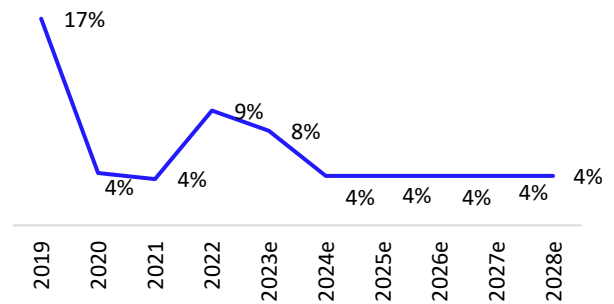
Source: Company Data, Al Rajhi Capital Estimates

**Figure 38 Changes in Working Capital levels (SARmn)**



Source: Company Data, Al Rajhi Capital Estimates

**Figure 39 Capex as % of sales**



Source: Company Data, Al Rajhi Capital Estimates

## Vision 2030 Brief

Saudi Arabia's Vision 2030 is an ambitious and comprehensive blueprint introduced by the Saudi government in 2016. It aims to diversify the country's economy and reduce its dependency on oil revenues while promoting economic development, social progress, and a more dynamic society.

To achieve the objectives, Vision 2030 has launched more than 10 programs which includes wide array of sectors ranging from healthcare, housing to pilgrimage. However, we have identified three main programs as most significant for financial services and banking sector:

### Financial Sector Development Program (FSDP):

The Financial Sector Development Program, initiated in 2018, aims to revolutionize Saudi Arabia's financial landscape, concentrating on banking, insurance, stock, and debt markets. Collaborating closely with SAMA and CMA, the Program enhances accessibility to banking services, fosters a robust financial system through technology and diverse products, and establishes an advanced capital market with international standards. Efforts include regulatory updates, a pioneering FinTech strategy, licensing cutting-edge digital banks, and launching a Financial Academy. Tadawul, the Saudi Capital Market, now ranks among the top 10 globally and features on esteemed indices like MSCI, S&P Dow Jones, and FTSE Russell.

### 2030 Objectives

- Banking Sector Growth:** Targeting a substantial increase in the banking sector, with total assets expected to reach SAR4.6tn by 2030, up from SAR2.6tn in 2019.
- Diversification and Innovation:** Emphasis on diversification, aiming for the stock market to represent 88% of GDP by 2030 (ex-Aramco), and fostering financial innovation with a goal of accommodating 60 financial technology companies by 2030.
- Inclusivity and SME Financing:** Focused on an inclusive financial structure, aiming to increase adult ownership of bank accounts and boost SME financing from banks to 20% by 2030, compared to 5.7% in 2019.
- Insurance Sector Development:** Targeting an increase in gross written premiums to 4.3% of non-oil sector GDP by 2030, up from 1.9% in 2019.
- Digital Transformation:** Aiming for an 80% increase in cashless operations by 2030 to pave the way towards a cashless society.
- Financial Stability:** Prioritizing financial stability aligned with international standards, ensuring the sustainability and empowerment of the financial sector by complying with requirements set by global financial entities.

### 2025 commitments

- Banking Sector Growth:** Targeting a substantial increase in total assets of the banking sector to SAR3.5tn by 2025, up from SAR2.6tn in 2019, to ensure necessary growth in the financial services sector.
- Diversification and Digital Innovation:** Aiming to diversify the financial services sector by increasing the stock market's market value to 80.8% of GDP by 2025 (from 66.5% in 2019) and debt instruments to 24.1% of GDP (from 14% in 2019).
- Inclusive Financing for SMEs:** Committed to inclusivity by boosting the share of SME financing in banks to 11% by 2025, up from 5.7% in 2019, aiming to provide better financial access and support for small and medium-sized enterprises.
- Insurance Sector Development:** Aiming to increase gross written premiums as a percentage of non-oil GDP to 2.4% by 2025, compared to 1.9% in 2019, contributing to the growth of the private sector.

5. **Digital Transformation:** Aiming for non-cash transactions to constitute 70% by 2025, up from 36% in 2019.

### Opportunities in capital markets

1. **Growth in Debt/fixed income market:** KSA markets are highly dependent upon banking sector for financing. The size of Fixed income issuances was only SAR537bn by the end of October 2023. The program aims to reduce dependency upon banks which could result in increasing size of fixed income market in the kingdom.
2. **Reducing market cap concentration:** By the end of 2019, the top 10 listed companies (ex-Aramco) accounted for 60% of the market capitalisation, the program aims to reduce the concentration which presents an opportunity in terms of new IPOs.
3. **Institutional trading activity:** The ratio of assets locally managed is 16.9% to GDP in 2019. This also affects the nature of trading activity in the stock market, as the share of institutional investment trading is low, at 41% in 2019 (37% in 9M23).

### Public Investment Fund Program

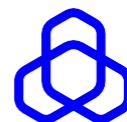
Launched in 2017, the Program revolves around maximizing the Public Investment Fund's (PIF) impact, serving as the catalyst for Saudi Arabia's economic diversification. This initiative spearheads global investments, positioning the Kingdom as an esteemed global partner. With the PIF amassing US\$700bn in assets by July 2022, creating 500,000 jobs and establishing 79 companies like the Saudi Coffee Company, the Program actively supports local industries. Furthermore, through five transformative giga-projects — NEOM, ROSHN, the Red Sea project, Qiddiya, and Diriyah — the Kingdom is redefining its future, emphasizing technological innovation, modern living, tourism, entertainment, and cultural heritage.

### Privatization Program

The Privatization Program, initiated in 2018, aims to bolster Saudi Arabia's economy by identifying government assets for privatization across various sectors like transport, health, education, and municipal affairs. By enacting the Saudi Privatization Law and establishing the National Center for Privatization and Public Private Partnership (NCP), the Program facilitates privatization frameworks, asset preparation, and develops a pipeline for sector privatization or private sector involvement.

### Capital Market Authority (CMA) strategic plan

The CMA, Saudi Arabia's financial market regulator, oversees exchanges, depository centers, and clearinghouses. Its 2021-2023 strategic plan aligns with Vision 2030 aspirations, aiming to position Saudi capital markets regionally and globally. Divided into four pillars, the strategy focuses on funding facilitation, encouraging investments, promoting confidence through reinforced regulations, and capacity building. Initiatives include boosting market depth, supporting private listings, developing sukuk and debt markets, enabling digital fund distribution, and enhancing market participant awareness. These pillars aim to diversify STG's offerings, promote capital formation, ensure market stability, and bolster overall growth.



## Key Financials

Figure 40 Income Statement

Income Statement (SARmn)	2023E	2024E	2025E
Sales	1,002	1,138	1,256
<i>y-o-y growth</i>	-6.5%	13.6%	10.3%
Cost of Sales	(446)	(483)	(500)
<i>y-o-y growth</i>	14.9%	8.4%	3.5%
<b>Gross Income</b>	<b>557</b>	<b>655</b>	<b>756</b>
<i>y-o-y growth</i>	-18.6%	17.7%	15.4%
<i>margins</i>	55.5%	57.6%	60.2%
General and administrative expenses	(265)	(290)	(314)
<b>Operating Income</b>	<b>290</b>	<b>365</b>	<b>442</b>
<i>y-o-y growth</i>	-32.1%	25.9%	21.1%
<i>margins</i>	28.9%	32.1%	35.2%
Investments and other	220	221	218
Financing Expense	(4)	(4)	(4)
Income from Affiliate	(45)	0	0
<b>Net income before tax</b>	<b>460</b>	<b>582</b>	<b>656</b>
Zakat & Tax	(61)	(61)	(64)
<i>tax rate</i>	13.4%	10.5%	9.8%
<b>Net Income</b>	<b>399</b>	<b>521</b>	<b>592</b>
<i>y-o-y growth</i>	-6.1%	30.7%	13.7%
<i>margins</i>	39.8%	45.8%	47.2%
EPS	3.3	4.3	4.9
DPS	2.5	3.3	3.7

Source: Al Rajhi Capital estimates

Figure 42 Cash Flow Statement

Cash Flow Statement (SARmn)	2023E	2024E	2025E
Net Cash Flows from Operating Activities	479	623	690
Cash Flows from Investing Activities	(73)	(68)	(75)
Cash Flows from Financing Activities	(345)	(417)	(462)
<b>Net Change in cash &amp; cash equivalents</b>	<b>61</b>	<b>137</b>	<b>152</b>

Source: Al Rajhi Capital estimates

Figure 41 Balance sheet

Balance Sheet (SARmn)	2023E	2024E	2025E
Cash & Cash Equivalents	2,180	2,317	2,469
Deposits with SAMA	3,629	3,629	3,629
Receivables, Net	110	114	117
Prepaid expenses and other assets	89	94	98
Investments in associates and joint ventures	268	268	268
<b>Total Current Assets</b>	<b>6,276</b>	<b>6,422</b>	<b>6,581</b>
Property and equipment	158	180	210
Right of Use Assets	174	159	143
Investments	388	388	388
Other Non-Current Assets	596	605	613
<b>Total Non-Current Assets</b>	<b>1,315</b>	<b>1,331</b>	<b>1,353</b>
<b>Total Assets</b>	<b>7,591</b>	<b>7,754</b>	<b>7,934</b>
<b>Liabilities and Equity</b>			
Short-term Debt & Leases	10	1	1
Trade Payable	14	15	17
Accrued expenses and other liab.	235	255	264
Margin Deposits from clearing participants	3,608	3,608	3,608
Other Current Liabilities	120	121	122
<b>Total Current Liabilities</b>	<b>3,988</b>	<b>4,002</b>	<b>4,013</b>
Long-Term Debt & Leases	157	166	178
Employees' end of service benefits	91	101	111
Other Non-Current Liabilities	172	172	172
<b>Total Non-Current Liabilities</b>	<b>421</b>	<b>439</b>	<b>461</b>
<b>Total Liabilities</b>	<b>4,408</b>	<b>4,441</b>	<b>4,474</b>
<b>Total Equity</b>	<b>3,182</b>	<b>3,313</b>	<b>3,461</b>
<b>Total liabilities and equity</b>	<b>7,591</b>	<b>7,754</b>	<b>7,934</b>

Source: Al Rajhi Capital estimates

Figure 43 Key Ratios

Ratios	2023E	2024E	2025E
Dividend Payout	75%	75%	75%
ROA	5%	7%	8%
ROE	13%	16%	17%
Asset turnover	0.1x	0.1x	0.2x
P/E	54.6x	41.8x	36.8x
EV/EBITDA	44.6x	35.7x	30.2x
P/BV	6.8x	6.6x	6.3x
Dividend yield	1.4%	1.8%	2.0%

Source: Al Rajhi Capital estimates



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"Neutral": We expect the share price to settle at a level between 10% below the current share price and 10% above the current share price on a 12 month time horizon.

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