

Public Comments on the Draft Prospectus of Zarea Limited

- 1. First of all, audited statements do not give any cost of sales — not even the technology team or infrastructure, which is in stark contrast to how platform-based companies report data. As a result, gross profits are consistently reported at 100%, which perhaps makes the performance seem more attractive.**

Response:

Zarea's financial statements show a 100% gross profit margin as it does not report "Cost of Sales" due to its usual platform-based model. The cost of sales applies when entities hold inventory directly; as per its core business model, It does not hold inventory, hence does not bear inventory-related costs. Additionally, technology-related expenses are not reflected in its profit or loss statement because development costs are capitalized in line with international accounting standards. While, general and administrative costs are shown in note 18 and selling and distribution costs associated are shown in note 19 of audited financial statements of Zarea Limited. Consequently, the gross profit margin is reported at 100%, which reflects the business model and may differ from conventional companies.

- 2. The company earns revenue by charging a per-transaction fee based on the value of the commodity but there's no mention of what the median commission is. Assuming that the company's median commission is 20%, does this mean that the gross merchandise value of goods sold through Zarea platform is PKR 1.4B?**

Response:

Zarea Limited's revenue model is based on a platform usage fee (PUF), which varies depending on the commodity type and current market dynamics. It does not apply a uniform PUF rate across all commodities, as the nature and demand of each commodity require a tailored approach. This variable fee structure allows it to remain competitive and flexible, ensuring that Zarea meets the specific needs of each sector it serves. While a median commission rate might be estimated, it would not accurately reflect the diverse pricing strategies we employ across commodity categories. This tailored approach helps optimize its platform for a broad range of commodities, supporting sustainable growth and value for its clients.

- 3. 45% of the proceeds are planned for working capital. Why raise growth money then, which is supposed to be for expansion instead of routine operations. Wouldn't debt financing be better in this case?**

Response:

While working capital often supports ongoing operations, for Zarea Ltd, this allocation is strategically tied to its growth objectives. The working capital raised through the IPO is not intended for routine expenses; rather, it will help Zarea enhance market penetration and capture greater market share in the coming years. By boosting liquidity, it can better serve its growing customer base and support increased transaction volumes, all of which contribute to long-term growth. Opting for equity over debt financing aligns with its goal of sustaining a strong, debt-free balance sheet, which supports operational flexibility as it scales. This approach also allows Zarea to reinvest profits from growth rather than channeling cash flows toward debt servicing, ultimately fueling further expansion.

Choosing equity financing over debt for this purpose aligns with our commitment to maintaining a robust, debt-free balance sheet, providing the flexibility needed to scale sustainably. This approach also enables us to reinvest growth profits directly into the business, without the constraints of debt servicing, thereby accelerating our expansion and delivering value to shareholders over the long term. Additionally, this strategy positions Zarea to potentially declare dividend payouts in line with its company's dividend policy, as disclosed in the prospectus.

- 4. Despite working capital getting such a high share of planned proceeds, there's little visibility on what the company's existing scale and model is. Does Zarea Credit have existing customers and what's the average credit amount and duration? Are the sponsors providing this facility from equity at the moment?**

Response:

The working capital requirement reflects anticipated growth in user base, transaction volumes, and platform expansion over the forecast period. Specifically, the transaction volume in agricultural commodities is projected to increase from 1,536 in FY 2024 to 2,458 in FY 2025, requiring Zarea to support a larger scale of operations leading to increase in working capital requirement. Therefore, the working capital consists of the advances to suppliers to be provided for agricultural commodities which are currently being funded through the company's internal cash flows. Please refer to the "section 4.4.1 Working Capital" for updated information.

- 5. General admin plus selling expenses were PKR 51M in FY24 but contains no split of what share went towards technology, logistics, support, etc.**

Response:

The technology related capex is disclosed under note 5 of audited financial statements, general and administration costs are shown in note 18 and selling and distribution costs associated are shown in note 19 of our audited financial statements.

- 6. The entire intangible CAPEX of PKR 18.6M seems to come from a third-party vendor, Alpha ventures. Doesn't Zarea have its own technology team?**

Response:

While Zarea does have an in-house Chief Technology Officer (CTO) and technology team that manages daily operations and routine updates, partnering with specialized companies like Alpha Ventures allows us to access advanced capabilities and efficiently execute complex development projects that drive platform growth. Partnering with third-party technology vendors is a common practice in the e-commerce industry, as it enables companies to leverage specialized resources without over extending their internal teams. For example, eBay has outsourced various aspects of its technology infrastructure, including software development and IT support, to trusted third-party providers. (Reference : Net Solutions. Top 10 Companies That Outsource Software Development. [BLOCKEDnetsolutions\[.\]com/hub/software-development-outsourcing/companiesBLOCKED](https://www.net-solutions.com/hub/software-development-outsourcing/companies)).

Therefore, this strategic collaboration allows Zarea's internal teams to focus on core operational needs, while Alpha Ventures contributes the specific technical expertise required for larger-scale development initiatives.

- 7. Only 10M out of 75M marketing spend is meant for digital media while the biggest chunk is earmarked for traditional. Not only is the split quite strange for an e-commerce company, the amount seems rather low for growth marketing. What's the current cost of customer acquisition?**

Response:

Primary customer base of Zarea Limited consists of SMEs and retailers, and have found that traditional media channels are more effective for reaching and engaging this audience. While digital media is essential, traditional media provides a wider reach and helps build trust within communities that may be less digitally engaged. This balanced approach ensures Zarea's message resonates with SMEs across different regions, enhancing brand awareness and credibility. The current allocation allows it to reach a broader audience at an optimal cost, supporting sustainable growth. Additionally, customer acquisition in this market is influenced by regional preferences, variable levels of digital adoption, and trust-building efforts that require longer engagement times compared to markets where digital acquisition is dominant. This means that while some marketing activities yield immediate results, others contribute indirectly by building brand credibility over time, making it harder to isolate exact costs per new customer acquisition in a single figure. We have further provided additional breakdown of marketing spend in "section 4.4.4 Marketing.

- 8. Human resource costs appear to be rather low as typically the salaries of any experienced c-level executive is significantly higher than PKR 425,000 provided in the estimates.**

Response:

Please see revised disclosure with additional details in prospectus "section 4.4.6 Human resource". Costs provided are as per market standards.

- 9. 12 of the 27 employees are key management? How big is the tech and sales team?**

Response:

Please refer to organizational chart added in prospectus in "section 3.5 Company Organogram"

- 10. Are loans from sponsors convertible to equity or some other instrument? Because debt ratios give a value of zero.**

Response:

Yes, loans from sponsors are converted into equity through a rights issuance, as detailed in the "Section 2.11 summary of related party transaction" of the prospectus.

- 11. Asset turnover seems quite low for a trading marketplace.**

Response:

The asset turnover ratio for Zarea reflects its operational model and strategic investments, which differ from typical trading marketplaces. Zarea's focus is on increasing transaction volumes and enhancing platform efficiency, which will continue to drive revenue growth and improve asset turnover over time.

- 12. DDR5 is a RAM, not a PC, as indicated in the prospectus, and doesn't cost as much either.**

Response:

The intended reference was to a complete, high-performance PC build, specifically Build PC G-8.9.8 | DDR5 BEAST RYZEN 9 9950X WITH RTX 4080 SUPER , which includes DDR5 RAM as part of the setup. This has been updated in the prospectus.

13. Website analytics data differs significantly from estimates by platforms such as Similarweb and SEMrush. Are the reported numbers audited by any third party? Secondly, the screenshots attached don't seem to be from Google Analytics.

Response:

The website analytics data presented in Zarea's reports is sourced directly from Google Analytics, a trusted and industry-standard tool that provides accurate, real-time insights into website traffic and user engagement. As Google Analytics collects first-party data directly from Zarea's website, it offers a more precise reflection of user interactions than third-party platforms like Similarweb or SEMrush, which use estimation models that may not fully capture Zarea's specific traffic dynamics. Given the reliability of Google Analytics, this data is not subject to third-party auditing. We can also confirm that the screenshots are from our verified Google Analytics account.

14. Peer comparison to listed companies is given on the basis of valuation but it's not apples to apples as the stock exchange has no e-commerce company.

Response:

Comparison to e-commerce companies has also been provided in "section 4A (viii) Peer group analysis of ZL". However, please refer to section 4A where the following disclosure is given/added.

"There are no listed competitor of Zarea and the above listed peer companies are not directly comparable to Zarea thus no direct comparison can be drawn in terms of financial performance".

15. For a platform-based company that is supposed to be asset light, why exactly is Zarea utilizing so much money on capex like cars, trucks, etc.?

Response:

These allocations are strategic investments that support key aspects of Zarea's operations, enhancing both sales outreach and logistics capabilities. The cars are designated for sales team, enabling them to engage effectively with clients, expand Zarea's customer base, and strengthen relationships across various regions, which is crucial for its growth. The trucks, meanwhile, are a targeted investment to bolster Zarea's logistics operations, adding unique competitive advantages to its e-commerce marketplace model. This approach allows it to meet customer demands more efficiently, ensuring timely deliveries and an overall improved service experience. These strategic investments will not only enhance Zarea's financial performance but also position Zarea more competitively in the market, enabling it to deliver a high standard of service.

Query -1: GP margin & technology capitalization

Your response mentioned that Zarea's financial statements show a 100% gross profit margin as it does not report "Cost of Sales" due to its platform-based model, where it does not hold inventory directly and, therefore, avoids inventory-related costs.

However, this interpretation raises questions:

While the cost of goods sold (COGS) applies to inventory-holding entities, the cost of sales for Zarea cannot be zero since it operates an online platform requiring technological and operational resources. Costs related to maintaining and running the platform e.g., server costs, software maintenance, and other technology expenditures must be reflected in the profit and loss statement.

You stated that technology-related expenses are not reflected in the profit or loss statement because they are capitalized per international accounting standards. However, it is extremely strange and against all the norms of accounting that the entirety of costs is capitalized. Does this mean Zarea is also capitalizing the day-to-day operational costs, say with running email accounts or any software subscriptions. If such as the logic then every single platform-based company would have 100% gross margins since the provided logic dictates that no technology expenses be booked in P&L.

Secondly, it also contradicts the provided answer as well stating that Zarea has a CTO and an in-house tech team. If that's the case, how exactly is the cost not reflected in cost of sales? Because by the very definition, it falls under that and certainly cannot be capitalized.

Response:

Zarea's financial statements show a 100% gross profit margin as it does not report 'Cost of Sales' due to its platform-based model. Cost of Sales applies when entities hold inventory directly; as per its core business model, Zarea does not hold inventory therefore, does not incur inventory-related costs.

For further clarity, please consider the following:

In accordance with IAS 38: Intangible Assets, costs related to the development of internally generated intangible assets are categorized into two phases:

1. Research Phase: Expenses incurred during this phase are required to be expensed as they do not meet the criteria for capitalization.
2. Development Phase: Costs incurred in this phase can be capitalized if they meet specific criteria, including:
 - Technical feasibility of completing the intangible asset.
 - The intent and ability to complete and use or sell the asset.
 - Probable future economic benefits generated by the asset.
 - Availability of adequate resources to complete development.
 - Reliable measurement of the expenditure.

In line with this guidance, only costs directly attributable to the development of Zarea's intangible assets that meet the recognition criteria outlined in IAS 38 have been capitalized. Conversely:

- Payroll costs related to administrative support functions or routine updates pertaining to technology are expensed under Note 18: Administrative Expenses, as they do not directly contribute to the creation of an intangible asset.
- Recurring website maintenance costs, which do not result in enhancements or further development of the intangible asset and are not part of direct costs, are also expensed under Note 18.

This approach ensures full compliance with IAS 38, maintaining a clear and transparent distinction between capitalized development costs and expensed administrative and general costs which have been reported in line with international accounting standards.

Query-2: Median commission

Your response regarding the median commission seems to demonstrate a lack of understanding of the question. We didn't suggest that the commission rate was uniform or ask for the standard cut but rather a median value. Surely, with lots of commodities and different structure for each, there must be a median and range available, where transparency is needed. Again, hardly any platform-based company around the world have a flat fee per transaction, but they do still provide the median or average take-rates. If

there's any trouble, we can help you find examples to shed light on how reporting for tech companies is usually done.

Response

Zarea Limited Charges platform usage fee in range of 1%-10%. It varies depending on the commodity and current industry dynamics. This fee is flexible allowing Zarea to remain competitive.

Query- 3: Google Analytics data and third party audit

Given the reliability of Google Analytics, Zarea confirmed that the data provided is sourced directly from its verified Google Analytics account. There are two points here: generally, credible third-party platforms are within a certain standard deviation of first-party data even if there are differences each period. Secondly, and more importantly, the audit from an external authority brings in far more transparency than self-reported screenshots, which the market deserves.

Response:

Zarea relies on Google Analytics as a trusted and widely recognized industry-standard tool for tracking traffic and user behavior. The data provided is sourced directly from Zarea's verified Google Analytics account, ensuring accuracy and reliability. Google Analytics is used globally by leading businesses and organizations due to its robust tracking capabilities, adherence to international standards, and consistent methodology, which eliminates the need for additional third-party audits in this context.

Furthermore, Google Analytics data is already neutral and automated, reducing the risk of bias or manipulation. The platform's tools and reporting systems undergo continuous updates and improvements by Google to meet industry standards, ensuring data integrity. As such, the analytics data provided directly from the platform offers a sufficient, credible, and transparent representation of Zarea's traffic and user metrics.

Query-4: Allocation of Proceeds

It goes against the fundamentals of business that the company plans to use more expensive equity instead of the cheaper debt to offer financing. Why isn't the management seeking a cheaper source of funding to fuel expansion, especially now that the interest rates are coming down. With strong profits and exceptional margins, can't the company manage interest and principal costs comfortably while using the proceeds towards better growth avenues?

In addition to it, there is a need for greater transparency, including full disclosure of agreements and associated concerns. The major shareholder, in practice, is a single individual who will own 76% of the shares (directly and indirectly), enabling them to secure approvals unilaterally.

This raises corporate governance concerns, as minority shareholders risk being sidelined.

Outsourcing and Financial Strategy: It would be more logical to outsource services. In a declining interest rate environment, leasing logistics and utilizing debt for growth could be a better approach.

Valuation Concerns: The valuation appears questionable. Profitability numbers require review as the gross profit is equal to net profit, and for 2024, net profit is shown to exceed gross profit.

Valuation assumptions suggest a multiple of 6-7 times EPS. However, the forecasted multiples for exit and their relation to the local market are unclear.

Dividend and Exit Strategy: A significant portion of cash is likely to be distributed as dividends, primarily benefiting the individual holding 76% equity. This would adversely impact the per-share value and the current ratio, leaving the minority shareholders at a disadvantage.

If minority investor decides to exit, clarity is required on the multiple at which the exit would occur, given that a major chunk of dividends would already have been taken by the majority shareholder.

Response:

Choosing equity financing over debt for this purpose aligns with Zarea's commitment to maintain a robust, debt-free balance sheet, providing the flexibility needed to scale sustainably. This approach also enables Zarea's to reinvest operating cash flows directly into the business growth, without the constraints of debt servicing, thereby accelerating Zarea's expansion and delivering value to shareholders over the long term. Consequently, this strategy positions Zarea to potentially declare dividend payouts in line with its company's dividend policy in future, as disclosed in the prospectus.

Zarea Limited is fully committed to comply with all regulatory requirements and adhering to the highest standards of **corporate governance** in accordance with applicable laws. As a public limited company, the Board of Directors consists of seven highly professional members, including experienced independent directors. The Board is further supported by dedicated Audit and HR Committees, which ensure transparency, regulatory compliance, and the implementation of robust governance practices. Notably, the Chairmen of both the Audit and HR Committees are independent directors, further reinforcing the objectivity and accountability of these critical oversight functions.

In line with the Companies Act, 2017, and the Code of Corporate Governance applicable to listed companies, all material decisions are presented to the Board for thorough review and approval. This governance framework ensures that no single individual has undue influence over decision-making. Consequently, the question of domination by a single person or unilateral decision-making does not arise, as all significant decisions are made collectively by the Board in accordance with established policies and procedures.

Please refer to the section 4A in prospectus for clarity on **valuation**.

The issue is being offered at a Price-to-Earnings ("PE") multiple of **9.21x** at a Floor Price of PKR 16/- per Ordinary Share based on the TTM earnings as of 30th **September** 2024 compared to industry average of **24.12** times. As per 3MFY25 management accounts of Zarea Limited, the EPS is PKR 0.54 per share which translates to an annualized EPS of PKR 2.16 hence at Pre-issue Price-to-Earnings ("PE") multiple of 7.41x.

Please refer to the section 6.8 in prospectus for clarity on **profit margins**.

Please refer to the section 6.12 in prospectus for clarity on **dividend payouts**. Zarea operates under a robust corporate governance framework, where all material decisions, including dividend declarations, are subject to Board review and approval. Independent directors on the Board ensure that minority shareholders' interests are adequately represented.

While the majority shareholder holds a significant equity stake, all dividend payouts are proportional to shareholding, ensuring equitable distribution in compliance with corporate laws. Zarea is committed to enhancing shareholder value through reinvestment in growth, which will contribute to higher valuation multiples over time, benefiting all shareholders, including those seeking to exit. The company remains committed to long-term value creation while safeguarding the interests of minority shareholders, maximizing shareholder wealth over time.