

BHARAT DYNAMICS – IPO RECOMMENDATION – SUBSCRIBE



Sole Manufacturer Of Critical Missile Equipment

Due to government's new defence policies, more opportunities will open up for the company but its status as a nominated production agency will change to that of a competitive bidder

Incorporated in 1970 and promoted by the Government of India, Bharat Dynamics (BD) is a leading defence public sector undertaking company engaged in the manufacture of surface-to-air missiles (SAMs), anti-tank guided missiles (ATGMs), underwater weapons, launchers, countermeasures and test equipment. The company primarily caters to the requirements of the Indian armed forces.

BDL is the sole manufacturer in India for SAMs, torpedoes and ATGMs. It is also the sole supplier of SAMs and ATGMs to the Indian armed forces. Additionally, company is engaged in the business of refurbishment and life extension of missiles.

Company aims to offer products such as Akash SAM, light weight torpedoes and countermeasure dispensing system to the international markets in near future. BDL is also exploring possibilities of technology transfer with Thales, which is an established global player with respect to the StarSTREAK missile system and working with L&T for development of naval launcher systems

The company has 3 manufacturing facilities located in Hyderabad (Telangana), Bhanur (Telangana) and Vishakhapatnam (Andhra Pradesh). Hyderabad and Bhanur facilities manufacture SAMs, ATGMs, Countermeasures and testing equipment's while Vishakhapatnam manufacturing facility is exclusively engaged in the manufacture of torpedoes.

It is in the process of setting up two new plants – one at Hyderabad, AP, and another at Amaravati, Maharashtra -- which will be utilised to manufacture new generation of SAMs and ATGMs and is expected to be operational by FY 20-21. Its Astra missiles technology completed final development trials in Sept 17 and was cleared for production for an initial order of 50 missiles.



It intends to automate production systems at its manufacturing facility in Hyderabad to cater to the growing demand of production of SAMs, Very Short Range Air Defence Missiles (VSHORADMs) and 3rd Generation ATGMs

It is also in the process of establishing a test fire range in Rachakonda, Telangana which will result in operational advantages and cost efficiencies. It has also established various technological labs such as RF labs, laser labs, aerodynamic labs and seeker labs to develop seeker technologies.

The company has over 3165 full-time employees, which includes 863 engineers and has its own internal R&D centre. The company will also focus on further improving its own R&D in order to improve productivity and efficiency of operations and thereby lower costs. R&D expenses have grown at a CAGR of 23.60% from Rs 22.7 crore for the FY 2015 to Rs 34.70 for the FY 2017.

Its first export order is expected to be executed in FY 2019 and from thereon, exports will rise. It has all the licenses in place for establishing its footprint in global defence arena.

Company's current order book as of January 31, 2018 is Rs. 10543 crore, It expects Rs 2000 crore average order inflow just from long-range SAMs and medium-range SRMs every year for the next four years. Cash Balance as on 31 Jan 2018 stands at a healthy Rs 1300 crore.

The Offer and the Objects

The offer comprises of offer for sale by Government of India of 22451953 shares, which at lower price band of Rs 413 per share, works out to Rs 927.27 crore and at higher price band of Rs 428, the issue size works out to Rs 960.94 crore. The minimum bid lot is 35 equity shares and in multiples of 35 equity shares.

The objects of the issue is to carry out the divestment program of Government of India apart from the benefits of listing the equity shares on the BSE and the NSE and to enhance its visibility and brand image and provide liquidity to its existing shareholders. Government of India will hold 87.8% of total paid up equity share capital of the company post listing.

Strengths

The company is a dominant player in defence sector and has over four decades of experience in manufacturing missiles and countermeasures and its allied equipment. The Ministry of Defence (MoD) has identified it as the production agency and the lead integrator for one of the new generation of SAMs and the nominated agency for the third generation of ATGMs

Under the ambit of the 'Make in India' initiative, investment procedure, license applications, declarations and other processes has been streamlined to boost investor confidence. This will augur well for future investments and orders for the sector in general and for the company in particular.

It has tie-ups with various domestic and international Original Equipment Manufacturers (OEMs) for the development of existing and future products and has achieved indigenisation of upto 90% of the Konkurs-M ATGM and Milan 2T ATGM.

Strong in house R&D. BD is the co-development partner with the Defence Research and Development Organisation (DRDO) for the next generation of ATGMs and SAMs. The company has established a missile development group with the objective to design and develop missiles



Weaknesses

In view of the policies of the Government of India such as the opening of foreign direct investment in the defence sector to encourage competition, the company's status as a nominated production agency will transition to that of a competitive bidder and due to such procurement policy and competition it may suffer loss of new business or lower margins.

The business environment in many of its principal operating segments requires extensive design and development expenses to keep pace with rapid technological and market changes in the guided missile manufacturing sector. However, with the MoD and the Indian armed forces opting to phase out the upgrade of its defence systems and go for ordering new missiles with superior technology, the company would need to invest more in research, design and development to manufacture indigenous missiles to remain competitive. Its future growth depends on adapting existing products to new requirements and introducing new products that achieve acceptance of the MoD and the Indian armed forces. Moreover, research, design and development programmes may not guarantee and produce successful results, and its new products may not achieve market acceptance, create additional revenue or become profitable.

The Company or its technical collaborators may engage in certain transactions in or with countries or persons that are subject to U.S. and other sanctions.

Valuation

For FY 2017, net sales were up 18% to Rs 4832.76 crore. The OPM stood at 11.8% down by 60 bps thus restricting the OP growth to 11% to Rs 568.24 crore. Other income stood at Rs 229.82 crore down by 40%. Lower other income is due to lower interest income and buyback of shares. Thus, PBIDT was down by 11% to Rs 798.05 crore.

Interest cost was up by 5% to Rs 3.68 crore while depreciation was higher by 17% to Rs 62.19 crore. Thus, PBT stood at Rs 732.19 crore down by 13% YoY. After paying total tax of Rs 241.87 crore, PAT for FY 2017 stood at Rs 490.32 crore, down 13%.

For half year ended September 2017, net sales stood at Rs 1805.68 crore with OPM of 13.6% resulting in an OP of Rs 245.02 crore. Other income stood at Rs 74.79 crore. Interest cost was at Rs 1.55 crore and depreciation stood at Rs 30.25 crore thus resulting in PBT of Rs 288.01 crore. After providing for total tax of Rs 115.42 crore, PAT stood at Rs 172.59 crore. **Due to seasonality of business, half yearly earnings cannot be annualised.**

Valuation

At higher price band of Rs 428, the P/E on FY 17 EPS (on current diluted equity of Rs 183.28 crore) of Rs 26.8 works out to 16. There are no listed players engaged in the manufacturing of missiles in India. Due to the nature of its business, there can be volatility in quarterly earnings and it has to maintain secrecy about its plans at the cost of investor friendliness, which may affect the P/E that it can command. **However taking into account the fact that is a sole manufacturer with strong growth prospects, we recommend a SUBSCRIBE to the IPO.**

Bharat Dynamics: Issue highlights	
Offer for sale (in Rs crore)	
- On lower price band	927.27
- On upper price band	960.94
Total Issue size for fresh issue (in no of shares in lakhs)	2.25
Price Band (Rs)	413-428*
Bid size (in no of shares)	35.00
Post issue share capital (Rs crore)	183.28
Post-issue Promoter & Group shareholding (%)	87.8%
Issue open date	13-03-2018
Issue closed date	15-03-2018
Listing	BSE, NSE
Rating	47/100

- Discount of Rs 10 to retail investors

Bharat Dynamics: Standalone Financials					
	1403(12)	1503(12)	1603(12)	1703(12)	1709(06)
Net Sales	1783.46	2840.82	4078.76	4832.76	1805.68
OPM (%)	4.6%	9.7%	12.6%	11.8%	13.6%
OP	82.24	274.90	513.25	568.24	245.02
Other in.	499.96	439.03	384.76	229.82	74.79
PBDIT	582.19	713.93	898.01	798.05	319.81
Interest	0.45	3.32	3.52	3.68	1.55
PBDT	581.75	710.61	894.49	794.38	318.26
Dep.	39.45	66.68	53.22	62.19	30.25
PBT	542.30	643.93	841.27	732.19	288.01
Tax (including Deferred Tax)	182.18	200.38	279.20	241.87	115.42
PAT	360.12	443.55	562.07	490.32	172.59
EPS (Rs)*	19.6	24.2	30.7	26.8	#
<p>*EPS is on post issue equity capital of Rs 183.28 crore of face value of Rs 10 each # EPS not annualised due to seasonality of business Figures in crore Source: Capitaline Database</p>					

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Registered Office:	124 Viraj, S.V.Road, Khar (W), Mumbai 400 052. Tel. (022) 4082 4082, Fax (022) 2649 7997. research@lmspl.com , www.latinmanharlal.com
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