

Azad Engineering Limited

Company Overview:

Azad Engineering Limited is one of the key manufacturers of the qualified product lines supplying to global original equipment manufacturers (OEMs) in the energy, aerospace and defence, and oil and gas industries, manufacturing highly engineered, complex and mission and life-critical components. The company manufactures complex and highly engineered precision forged and machined components that are mission and life-critical and hence, some of the products has a zero parts per million defects requirement. The company compete with manufacturers from China, Europe, USA and Japan.

Key Highlights:

1. Robust product portfolio: The company products include 3D rotating airfoil/ blade portions of turbine engines and other critical components for (a) gas, nuclear and thermal turbines used in industrial applications or energy generation, and (b) defence and civil aircrafts and spaceships. The demand for such precision, forged and machined components is driven by requirements relating to energy turbines (industrial, gas, nuclear and coal), aircrafts (commercial and military), amongst others. Airfoils/ blades are one of the most critical 3D rotating and stationary parts of a turbine in the compression section. To sustain the high pressure, airfoils/ blades are made up of exotic/ super alloys and manufactured with a unique process designed by the Company.

2. Advanced manufacturing facility: The company has four advanced manufacturing facilities in Hyderabad, Telangana, India, capable of producing high precision forged and machined components with a total manufacturing area of approximately 20,000 square metres. The company also has two manufacturing facilities in the pipeline at (a) Tuniki Bollaram village in Siddipet district, Telangana and (b) Mangampet village in Sangareddy district, Telangana with a total manufacturing area of 94,898.8 square metres and 74,866.8 square metres, respectively. The upcoming manufacturing facility at Tuniki Bollaram village in Siddipet district, Telangana is proposed to have dedicated and exclusive manufacturing for the production of critical and complex components such as airfoils/ blades and other special machined parts for gas and thermal turbines for Mitsubishi Heavy Industries Ltd., one of the long-standing customers.

3. Long-standing relationship with customers: The company has a well-diversified customer base spread across various geographies such as USA, Europe, Japan, Middle East, United Kingdom and China. The company has existing relationships with both Indian and global OEMs. The company's long-standing customer base comprises of leading product OEM companies, key strategic and globally preferred partners such as General Electric and Mitsubishi Heavy Industries Ltd., with whom they have an average relationship of over 10 years.

Valuation: The company is valued at FY23 P/E multiple of 387.2x and 68.6x reported PAT and adjusted PAT respectively, at the upper price band on post-issue capital. The company is a preferred manufacturer of mission & life-critical components serving highly regulated industries with significant entry barriers. It supplies to OEMs with high global market penetration and has long-standing and deep customer relationships. The revenues grew at a CAGR of 43% between FY21-FY23 achieving an adj. RoCE of ~21.2%. It commands an industry leading adjusted EBITDA margin of ~31.6% as of FY23.

| Issue Details | |
|-------------------------------|---|
| Date of Opening | 20 th December 23 |
| Date of Closing | 22 nd December 23 |
| Price Band (Rs) | 499 - 524 |
| OFS (Rs cr) | 500 |
| Fresh Issue (Rs cr) | 240 |
| Issue Size (Rs cr) | 740 |
| No. of shares | 1,48,29,659 – 1,41,22,137 |
| Face Value (Rs) | 2.0 |
| Post Issue Market Cap (Rs cr) | 2,961 – 3,097 |
| BRLMs | Axis Capital, ICICI Securities, SBI Capital Markets, Anand Rathi Advisors |
| Registrar | KFin Technologies Limited |
| Bid Lot | 28 shares and in multiple thereof |
| QIB shares | 50% |
| Retail shares | 35% |
| NIB shares | 15% |
| Employee Reservation | 76,335 equity shares aggregating up to Rs 4 cr |

| Objects of Issue | |
|---|---|
| | Estimated utilization from net proceeds (Rs cr) |
| Funding capital expenditure of the Company | 60.4 |
| Repayment/prepayment, in part or full, of certain borrowings availed by the company | 138.2 |
| General corporate purposes [^] | - |
| Total proceeds from fresh issue | - |

[^] To be finalized upon determination of the Offer Price and updated in the Prospectus prior to filing with the RoC. The amount utilized for general corporate purposes shall not exceed 25% of the Gross Proceeds.

| Shareholding Pattern | | |
|---------------------------|--------------------|--------------|
| Pre-Issue | No. of Shares | % |
| Promoter & Promoter Group | 4,28,67,570 | 78.6 |
| Public & Others | 1,16,65,272 | 21.4 |
| Total | 5,45,32,842 | 100.0 |

| Post Issue @Lower Price Band | | |
|------------------------------|--------------------|--------------|
| | No. of Shares | % |
| Promoter & Promoter Group | 3,87,60,055 | 65.3 |
| Public & Others | 2,05,82,406 | 34.7 |
| Total | 5,93,42,461 | 100.0 |

| Post Issue @Upper Price Band | | |
|------------------------------|--------------------|--------------|
| | No. of Shares | % |
| Promoter & Promoter Group | 3,89,56,024 | 65.9 |
| Public & Others | 2,01,56,970 | 34.1 |
| Total | 5,91,12,995 | 100.0 |

Source: RHP, SSL Research

Key Financials

| | FY21 | FY22 | FY23 | 1HFY24 |
|---------------------------------|------|------|------|--------|
| Revenue from operations (Rs cr) | 123 | 194 | 252 | 159 |
| Reported EBITDA (Rs cr) | 28 | 62 | 72 | 53 |
| Reported Profit (Rs cr) | 12 | 29 | 8 | 27 |
| Reported EBITDA Margin (%) | 22.9 | 32.0 | 28.7 | 33.1 |
| Reported PAT Margin (%) | 9.4 | 15.1 | 3.4 | 16.9 |
| Reported EPS (Rs) | 2.3 | 5.9 | 1.7 | 5.4* |
| ROE (%) | 12.7 | 24.5 | 4.2 | 11.7* |
| ROCE (%) | 12.1 | 16.9 | 13.9 | 9.6* |
| Debt / Equity (x) | 1.0 | 1.64 | 1.32 | 1.41* |

* Not Annualized

Source: RHP, SSL Research

Risk Factors

- **Customer concentration risk:** The company derives a significant portion of its revenue accounting for 59.9%, 54.8%, 63.1% and 60.8% of its FY21, FY22, FY23 and 1HFY24 revenue respectively from its top 5 customers. The loss of any of these customers could have a material adverse effect on the business, financial condition, results of operations and cash flows.
- **Raw material sourcing risk:** The company depends on third party suppliers for raw materials, plant, machinery and components, which are on a purchase order basis. The company ordered 63.2%, 61.4%, 66.8% and 83.2% of its raw materials in FY21, FY22, FY23 and 1HFY24 respectively from its top 5 suppliers. Further, the company does not have any exclusive suppliers, and the suppliers could engage with competitors and prioritize supplies of other customers, which could adversely impact the company's ability to procure a sufficient quantity of raw materials, plant, machinery and components at competitive rates.
- **Export risk:** The company generated 82.1%, 78.1%, 80.4% and 89.7% of its FY21, FY22, FY23 and 1HFY24 revenue respectively from outside India. As a result, the company is subject to several complex and regulatory requirements. The concentration of revenue from other countries could adversely affect business, results of operations, financial condition, cash flows and future prospects in case of risks that are specific to each country where the company's customers operate.
- **Competition:** The company faces significant competitive pressures in the business. Any inability to compete effectively would have a material adverse effect on the business, prospects, operations and financial results.

Growth Strategy

- **Strengthen core capabilities:** Continue to strengthen core capabilities across focus industries by expanding existing relationship with customers and acquiring new and more strategic customers across focus industries.
- **Increase penetration and market share:** Increase penetration and market share by leveraging relationship with existing customers and continue to maintain strong record of repeat orders from existing and new customers.
- **Augment manufacturing capabilities:** Continue to augment manufacturing capabilities by organic and inorganic acquisitions and better serve customers, while building scale and delivering state of the art execution.
- **Improve operating efficiencies:** Offer quality products at optimal prices and deploy new technologies to reduce operating costs and improve operative efficiencies.

Revenue from operations – Product-wise/Geography

| Industry and Product Particulars | FY21 | | FY22 | | FY23 | | 1HFY23 | |
|----------------------------------|-------------------------------|----------------------------------|-------------------------------|---------------------------------|-------------------------------|----------------------------------|-------------------------------|----------------------------------|
| | Revenue from purchase (Rs cr) | % of revenue from operations (%) | Revenue from purchase (Rs cr) | % of revenue from operation (%) | Revenue from purchase (Rs cr) | % of revenue from operations (%) | Revenue from purchase (Rs cr) | % of revenue from operations (%) |
| Energy | 110.5 | 90.1 | 165.1 | 84.9 | 219.0 | 87.0 | 140.9 | 88.8 |
| Airfoil/ blade | 96.2 | 78.4 | 145.8 | 75.0 | 198.0 | 78.7 | 114.3 | 72.0 |
| Non-airfoil | 14.3 | 11.7 | 19.2 | 9.9 | 21.0 | 8.4 | 26.6 | 16.8 |
| Aerospace and defence | 7.6 | 6.2 | 20.3 | 10.4 | 22.5 | 9.0 | 13.7 | 8.6 |
| Air generation system | 1.7 | 1.4 | 8.8 | 4.5 | 3.4 | 1.4 | 5.1 | 3.2 |
| Hydraulic system | 0.3 | 0.2 | 2.2 | 1.1 | 7.5 | 3.0 | 3.5 | 2.2 |
| APU/ engine | 1.9 | 1.5 | 1.2 | 0.6 | 1.9 | 0.8 | 0.7 | 0.5 |
| Airfoil/ blade | 1.4 | 1.1 | 1.8 | 0.9 | 1.3 | 0.5 | 0.8 | 0.5 |
| Engine | 0.3 | 0.3 | 1.4 | 0.7 | 2.0 | 0.8 | 1.0 | 0.7 |
| Generator | 0.2 | 0.2 | 0.5 | 0.2 | 1.9 | 0.7 | 1.5 | 0.9 |
| Engineering charges | 0.0 | 0.0 | 3.0 | 1.6 | 0.0 | 0.0 | 0.0 | 0.0 |
| Propulsion system | 0.0 | 0.0 | 0.0 | 0.0 | 1.9 | 0.8 | 0.4 | 0.3 |
| Structural joints | 0.7 | 0.6 | 0.2 | 0.1 | 0.3 | 0.1 | 0.0 | 0.0 |
| Missile | 0.3 | 0.2 | 0.3 | 0.2 | 0.4 | 0.2 | 0.1 | 0.0 |
| Others | 0.7 | 0.6 | 0.9 | 0.5 | 1.9 | 0.7 | 0.6 | 0.4 |
| Oil and gas | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Drilling services | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Scrap | 2.6 | 2.2 | 7.8 | 4.0 | 9.7 | 3.9 | 3.5 | 2.2 |
| Others | 1.9 | 1.6 | 1.3 | 0.7 | 0.4 | 0.2 | 0.7 | 0.4 |
| Total | 122.7 | 100.0 | 194.5 | 100.0 | 251.7 | 100.0 | 158.7 | 100.0 |

| Country | FY21 | | FY22 | | FY23 | | 1HFY23 | |
|--------------|---------------------------------|------|---------------------------------|------|---------------------------------|------|---------------------------------|------|
| | Revenue from operations (Rs cr) | % |
| Japan | 41.3 | 33.7 | 65.2 | 33.5 | 89.3 | 35.5 | 33.0 | 20.8 |
| USA | 31.3 | 25.5 | 46.7 | 24.0 | 57.9 | 23.0 | 55.7 | 35.1 |
| India* | 22.0 | 17.9 | 43.2 | 22.2 | 49.7 | 19.8 | 16.8 | 10.6 |
| UAE | 9.0 | 7.3 | 17.0 | 8.7 | 22.3 | 8.8 | 17.4 | 11.0 |
| Germany | 8.8 | 7.2 | 6.6 | 3.4 | 15.9 | 6.3 | 3.5 | 2.2 |
| Switzerland | 4.2 | 3.4 | 1.6 | 0.8 | 0.1 | 0.0 | 0.1 | 0.1 |
| UK | 3.5 | 2.9 | 3.6 | 1.8 | 1.2 | 0.5 | 3.9 | 2.5 |
| Hungary | 1.2 | 1.0 | 1.3 | 0.7 | 0.1 | 0.0 | 0.9 | 0.5 |
| France | 0.7 | 0.6 | 8.4 | 4.3 | 15.3 | 6.1 | 20.6 | 13.0 |
| Italy | 0.4 | 0.4 | - | - | - | - | - | - |
| Sweden | 0.4 | 0.3 | - | - | - | - | - | - |
| South Africa | - | - | 0.4 | 0.2 | - | - | - | - |
| Poland | - | - | 0.4 | 0.2 | - | - | 6.8 | 4.3 |
| Saudi Arabia | - | - | - | - | 0.0 | 0.0 | - | - |
| Singapore | - | - | - | - | 0.0 | 0.0 | 0.3 | 0.2 |

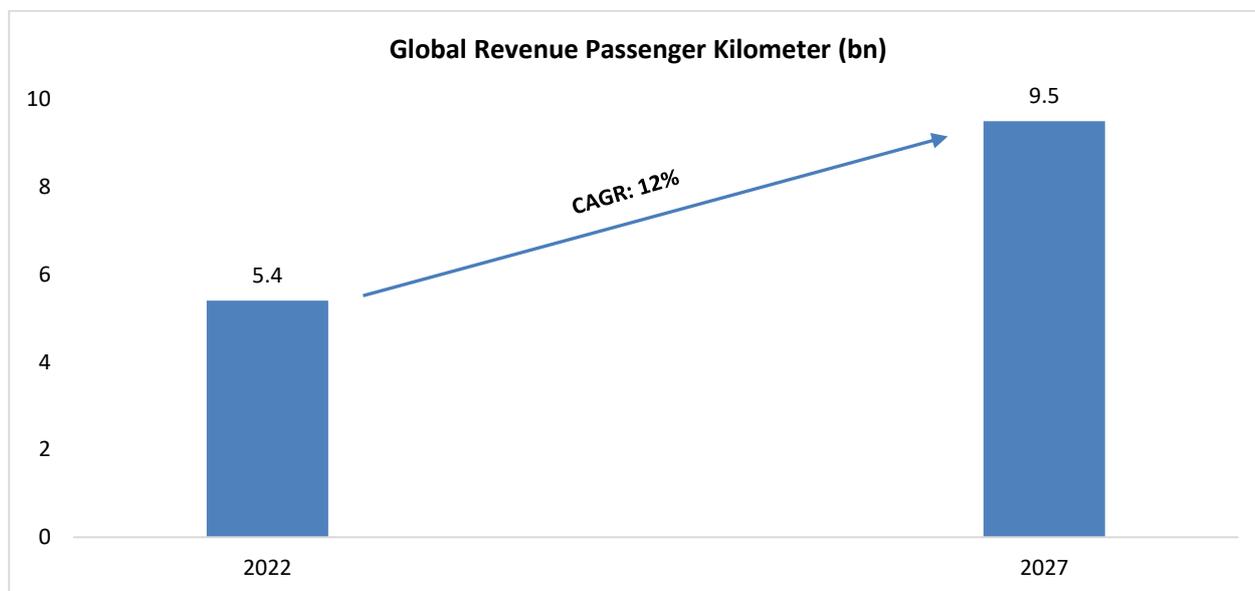
*Includes export incentives

Source: RHP, SSL Research

Industry Overview – Aerospace and Defense Market

Global Air Passenger Traffic Market

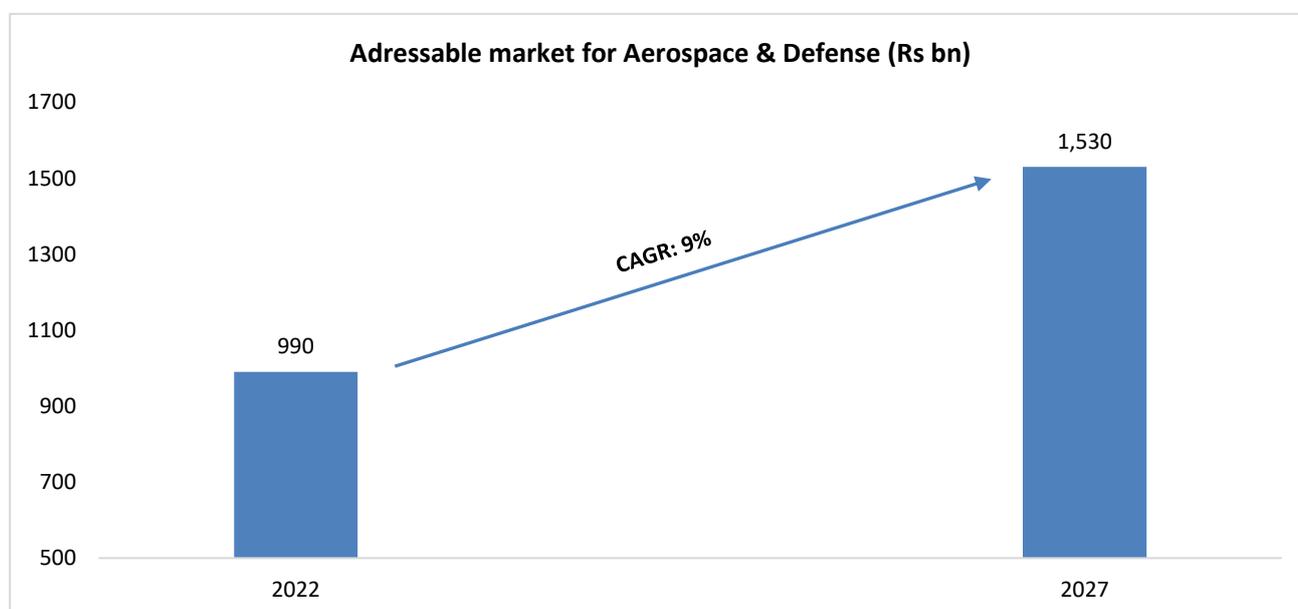
The commercial aircraft industry was facing significant headwinds post the Covid-9 pandemic, recovered in CY22 and CY23. The outlook for global air traffic is positive with Revenue Passenger Kilometer (RPK) expected to increase to 9.5 bn by CY27, growing at a CAGR of 12%.



Source: RHP, SSL Research

Global Addressable Aerospace and Defense Market

The global addressable aerospace and defense components market is valued at Rs 990 bn in CY22 and is expected to grow at a CAGR of 9% to reach Rs 1,530 bn by CY27. As of CY23, GE Aerospace is the player with the largest addressable market size, followed by The Boeing Company & Honeywell International Inc.



Source: RHP, SSL Research

Financial Snapshot

| INCOME STATEMENT | | | |
|------------------------------------|-------------|-------------|-------------|
| (Rs cr) | FY21 | FY22 | FY23 |
| Revenue from Operations | 123 | 194 | 252 |
| YoY growth (%) | - | - | 29.4 |
| Cost Of Revenues (incl Stock Adj) | 14 | 21 | 30 |
| Gross Profit | 109 | 174 | 222 |
| Gross margins (%) | 88.7 | 89.3 | 88.0 |
| Employee Cost | 33 | 46 | 59 |
| Other Operating Expenses | 48 | 65 | 90 |
| Reported EBITDA | 28 | 62 | 72 |
| Adjusted EBITDA | 37 | 63 | 80 |
| Reported EBITDA margins (%) | 22.9 | 32.0 | 28.7 |
| Other Income | 2 | 5 | 10 |
| Net Interest Exp. | 5 | 14 | 52 |
| Depreciation | 9 | 13 | 17 |
| Exceptional Items | 0 | 0 | 0 |
| PBT | 16 | 40 | 13 |
| Tax | 5 | 11 | 5 |
| Reported PAT | 12 | 29 | 8 |
| Adjusted PAT | 20 | 33 | 45 |
| Reported PAT margin (%) | 9.4 | 15.1 | 3.4 |
| Reported EPS | 2.3 | 5.9 | 1.7 |

| BALANCE SHEET | | | |
|---|------------|------------|------------|
| (Rs cr) | FY21 | FY22 | FY23 |
| Assets | | | |
| Net Block | 121 | 144 | 217 |
| Capital WIP | 0 | 24 | 38 |
| Other Non current Assets | 9 | 69 | 51 |
| Current Assets | | | |
| Inventories | 34 | 57 | 86 |
| Trade receivables | 53 | 75 | 119 |
| Cash and Bank Balances | 17 | 18 | 53 |
| Other Current Assets | 22 | 18 | 26 |
| Total Current Assets | 126 | 168 | 284 |
| Current Liabilities & Provisions | | | |
| Trade payables | 37 | 43 | 48 |
| Other current liabilities | 28 | 30 | 19 |
| Short-term provisions | 1 | 1 | 2 |
| Total Current Liabilities | 66 | 73 | 68 |
| Net Current Assets | 60 | 94 | 215 |
| Total Assets | 190 | 331 | 521 |
| Liabilities | | | |
| Share Capital | 2 | 2 | 2 |
| Reserves and Surplus | 89 | 118 | 202 |
| Total Shareholders Funds | 91 | 120 | 204 |
| Total Debt | 88 | 197 | 301 |
| Long Term Provisions | 1 | 2 | 3 |
| Net Deferred Tax Liability | 10 | 12 | 14 |
| Total Liabilities | 190 | 331 | 521 |

| Cash Flow (Rs cr) | FY21 | FY22 | FY23 |
|--|------|------|------|
| Cash flow from Operating Activities | 4 | 21 | -10 |
| Cash flow from Investing Activities | -35 | -114 | -101 |
| Cash flow from Financing Activities | 24 | 96 | 126 |
| Free Cash Flow | -16 | -96 | -96 |

| RATIOS | | | |
|-------------------------------------|-------|------|-------|
| | FY21 | FY22 | FY23 |
| Profitability | | | |
| Return on Assets (%) | 4.5 | 7.3 | 1.4 |
| Return on Capital (%) | 12.1 | 16.9 | 13.9 |
| Return on Equity (%) | 12.7 | 24.5 | 4.2 |
| Margin Analysis | | | |
| Gross Margin (%) | 88.7 | 89.3 | 88.0 |
| EBITDA Margin (%) | 22.9 | 32.0 | 28.7 |
| Net Income Margin (%) | 9.4 | 15.1 | 3.4 |
| Short-Term Liquidity | | | |
| Current Ratio (x) | 1.1 | 1.1 | 1.9 |
| Quick Ratio (x) | 0.8 | 0.7 | 1.3 |
| Avg. Days Sales Outstanding (x) | 156 | 140 | 172 |
| Avg. Days Inventory Outstanding (x) | 102 | 108 | 125 |
| Avg. Days Payables | 111 | 80 | 69 |
| Fixed asset turnover (x) | 1.0 | 1.3 | 1.2 |
| Debt-service coverage (x) | 0.3 | 0.3 | 0.2 |
| Long-Term Solvency | | | |
| Total Debt / Equity (x) | 1.0 | 1.6 | 1.3 |
| Interest Coverage Ratio (x) | 4.0 | 3.9 | 1.3 |
| Valuation Ratios | | | |
| EV/EBITDA (x) | 94.7 | 44.6 | 38.9 |
| P/E (x) | 225.8 | 88.2 | 306.5 |
| P/B (x) | 28.6 | 21.6 | 12.7 |

Source: RHP, SSL Research

Peer Comparison

| | Azad Engineering Limited | MTAR Technologies Ltd. | Paras Defence and Space Technologies Ltd. | Dynamic Technologies Ltd | Triveni Turbines Ltd |
|-----------------------------------|--------------------------|------------------------|---|--------------------------|----------------------|
| CMP | 524.0 | 2,243.7 | 745.4 | 4,455.0 | 415.3 |
| Sales (Rs cr) | 251.7 | 573.0 | 214.0 | 1,316.0 | 1,248.0 |
| EBITDA (Rs cr) | 72.3 | 154.0 | 56.0 | 184.0 | 235.0 |
| Adjusted EBITDA (Rs cr) | 80.0 | - | - | - | - |
| Net Profit (Rs cr) | 8.5 | 104.0 | 36.0 | 43.0 | 193.0 |
| Adjusted PAT (Rs cr) | 45.0 | - | - | - | - |
| Market Cap (Rs cr) | 3,097.5 | 6,901.5 | 2,907.1 | 3,025.6 | 13,201.4 |
| Enterprise Value (Rs cr) | 3,313.2 | 7,135.5 | 2,919.4 | 3,466.6 | 12,844.4 |
| EBITDA Margin (%) | 28.7 | 26.9 | 26.2 | 14.0 | 18.8 |
| Net Margin (%) | 3.4 | 18.2 | 16.8 | 3.3 | 15.5 |
| P/E(x): Based on the Reported PAT | 365.6 | 66.4 | 80.8 | 70.4 | 68.4 |
| P/E (x): Based on Adjusted PAT | 68.6 | - | - | - | - |
| EV/EBITDA | 45.8 | 46.3 | 52.1 | 18.8 | 54.7 |
| RoE (%) | 4.2 | 17.9 | 9.1 | 9.2 | 21.5 |
| RoCE (%) | 13.9 | 22.2 | 13.2 | 10.4 | 28.7 |

The data is based on FY23 financial data.

For Azad Engineering Limited the Market cap, PE(x), and EV/EBITDA (x) are calculated on post-issue equity share capital based on the upper price band.

CMP as on 15th December'23.

Source: RHP, SSL Research

SBICAP Securities Limited

(CIN): U65999MH2005PLC155485 | Research Analyst Registration No INH000000602

SEBI Registration No.: Stock Broker: INZ000200032 | CDSL: IN-DP-314-2017 | NSDL: IN-DP-NSDL-369-2014 | Research Analyst: INH000000602

Portfolio Manager: INP000004912 | IRDA/RW/IR2/2015/081 | IRDA/RW/IR1/2016/041 | IRDA: CA0103

Registered & Corporate Office: Marathon Futorex, A Wing, 12th Floor, N. M. Joshi Marg, Lower Parel, Mumbai-400013.

For any information contact us:

022-6854 5555**E-mail: helpdesk@sbicapsec.com | Web: www.sbisecurities.in****DISCLOSURES & DISCLAIMERS:**

Analyst Certification: The views expressed in this research report ("Report") accurately reflect the personal views of the research analysts ("Analysts") employed by SBICAP Securities Limited (SSL) about any and all of the subject issuer(s) or company(ies) or securities. This report has been prepared based upon information available to the public and sources, believed to be reliable. I/We also certify that no part of my/our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

The Analysts engaged in preparation of this Report or his/her relative:-

- (a) do not have any financial interests in the subject company mentioned in this Report; (b) do not own 1% or more of the equity securities of the subject company mentioned in the report as of the last day of the month preceding the publication of the research report; (c) do not have any material conflict of interest at the time of publication of the Report.

The Analysts engaged in preparation of this Report:-

- (a) have not received any compensation from the subject company in the past twelve months; (b) have not managed or co-managed public offering of securities for the subject company in the past twelve months; (c) have not received any compensation for investment banking or merchant banking or brokerage services from the subject company in the past twelve months; (d) have not received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past twelve months; (e) has not received any compensation or other benefits from the subject company or third party in connection with the Report; (f) has not served as an officer, director or employee of the subject company; (g) is not engaged in market making activity for the subject company.

| Name | Qualification | Designation |
|------------------|--------------------------------|--|
| Sudeep Shah | MMS-Finance | DVP- Technical & Derivative Research |
| Sunny Agrawal | B.E, MBA (Finance) | DVP - Fundamental Research |
| Rajesh Gupta | PGDBM (Finance), MA (Bus. Eco) | AVP - Fundamental Research |
| Monica Chauhan | C.A. | Research Analyst - Equity Fundamentals |
| Harsh Vasa | CA | Research Analyst - Equity Fundamentals |
| Sumeet Shah | B.E., CFA | Research Analyst - Equity Fundamentals |
| Sweta Padhi | MBA (Finance) | Research Analyst - Equity Fundamentals |
| Uday Chandgothia | B-Tech, MBA (Finance) | Research Associate - Equity Fundamentals |
| Gautam Updhyaya | MBA (Finance) | Research Analyst - Equity Derivatives |
| Vinayak Gangule | BE (IT) | Research Analyst - Equity Technicals |
| Pratik Patni | BSc (Biotech Entire) | Research Analyst- Equity Derivatives |
| Ghanshyam Gupta | MBA (Finance) | Research Analyst- Currency Derivative |
| Sagar Peswani | B.Tech (ECE) | Research Associate - Equity Technicals |
| Kalpesh Mangade | B.Com | MIS Analyst - Retail Research |

For other Disclosures please visit: https://bit.ly/R_disclaimer02