PROFITMART

RESEARCH REPORT

13th April 2021

BHARAT DYNAMICS LTD

BSE : BDL **Sector: DEFENCE** **BSE: 541143**

View - BUY

CMP : Rs. 330

Target Price: Rs 450 (In next 12 to 18 mths)

Suggested Buying Range (Between Rs 330 to Rs 345)

BUSINESS BACKGROUND

Bharat Dynamics Ltd (BDL) is one of the leading defence PSU in India, incorporated in 1970 and engaged in the manufacture of Surface to Air missiles (SAMs), Anti-Tank Guided Missiles (ATGMs), under water weapons, launchers, countermeasures and test equipment. BDL has 3 manufacturing facilities located in Hyderabad, Bhanur and Vishakhapatnam. It is the sole manufacturer and supplier in India for SAMs, torpedoes, ATGMs to the Indian armed forces. Additionally, BDL is engaged in the business of refurbishment and life extension of missiles manufactured. It is also the co-development partner with DRDO for the next generation of ATGMs and SAMs.

INVESTMENT HIGHLIGHTS

Steady Financial Performance for FY20 & Q3FY21 –

BDL reported a steady set of FY20 numbers in a difficult year with net sales at Rs 3095 925 crs as compared to a revenue of Rs 3069 crs last year, with EBIDTA placed at Rs 728 crs from Rs 622 crs last year with the PAT placed at Rs 534 crs from Rs 422 crs. BDL declared a dividend of 88% for FY20.

For BDL nine months ended Dec 2020, Revenue was Rs.767 crs with the EBIDTA at Rs 282 crs

Healthy order book indicates strong revenue visibility –

BDL current order book stands at Rs 8100 crs as on Mar2021 comprising the Akash Weapon System, LR SAM, MR SAM, INVAR (3 UBK 20) ATGM and the Konkurs-M ATGM. This puts the revenue visibility for next two years at 2.61x (on FY20 revenues of Rs 3095 crs). Going forward, the strong order book will further help the BDL to boost its top-line

The company management expects exports to be a big focus area for its products going ahead. On a conservative basis the management is targeting Rs 25000 crs order book in the next 3 years ahead largely driven by both domestic and export markets

KEY DATA

FACE VALUE Rs	10.00
DIVD YIELD %	2.40
52 WK HI/LOW	481/147
NSE CODE	BDL
BSE CODE	BDL
MARKET CAP	RS 6709 CRS

SHAREHOLDING PATTERN

PROMOTERS	-	75%
BANKS, MFs & DIIs	-	18%
FIIs	-	%
PUBLIC	-	7%

KEY FUNDAMENTALS

YE	FY21	FY22	FY23
Rev Gr%	-32	43	15
EBIDTA Gr%	-51	68	21
PAT Gr%	-47	60	22
EPS Gr%	-47	60	22
EPS (Rs)	15.33	24.55	30.01
ROE %	11	16	17
ROCE %	9	14	15
P/E(x)		15	12

Long term Drivers for DHFL look good in view of the follow18

BDL enjoys a diversified Product Range –

Milan 2T –

This man portable (infantry) second generation ATGM can destroy tanks fitted with explosive reactive armour, moving and stationary targets. It has a fiber glass logistic container for transformation of 4 missiles, which is highly reliable as no maintenance or pre-fire check is required

Konkurs - M (ATGM) –

This is a second generation, semiautomatic, antitank, tube launched, optically tracked, wire guided and aerodynamically controlled missile designed to destroy moving and stationary armored targets with explosives reactive armours at a range of 75 to 4000 meters. It can be launched either from BMP-II or from ground launcher

Invar (3 UBK 20) (ATGM) –

This is a weapon fired from the gun barrel of a T 90 Tank. The missile has a semi-automatic control system, tele orienting in the laser beam, has a high velocity jamming immune missile with tandem warhead designed to defeat explosive reactive armor and to destroy stationary and moving targets with speed up to 70 Km/hr

Akash –

This is a medium range surface-to-air missile with a multiple target tracking capability

Advanced Light Weight Torpedo (TAL) –

This can be launched from a ship or a helicopter, available as both war shot and exercise model. Also, it has a multiple search pattern capability

Torpedo Counter Measure System (C303) –

This is meant to counter the threat posed to any submarine by any active or passive homing torpedo

Counter Measures Dispensing System (CMDS) –

This is a state of the art chaff and flare dispensing system providing self-protection to the aircraft by passive ECM against radar guided. Protection to the aircraft is achieved by misguiding the missiles by dispensing of chaff and flare payloads

Infra Red Interference Indicator (IRII) –

This is a equipment to detect any IR interference in the field of view of launcher prior to firing of the missile

BDL enjoys modern facilities & infrastructure to deliver quality products in a timely manner –

BDL's infrastructure at manufacturing facilities combined with their vast expertise enables them to cater to the needs of the Indian armed forces in a timely manner

Company's manufacturing facilities are equipped with robotic welding machines, four axis machines, flow forming machines, vaccum furnace for heat treatment, automated electroplating shop, 3D–coordinating measuring machine, climatic chambers and 800G acceleration measuring fixture. BDL's Hyderabad manufacturing unit has been automated for material handling and grain loading of SAMs (Surface to Air Missiles)

BDL's Vishakhapatnam manufacturing facility is exclusively engaged in the manufacture of torpedoes

BDL is also in the process of setting up two additional manufacturing facilities at Ibrahimpatnam (near Hyderabad) and Amravati in Maharashtra which shall be used to manufacture SAMs (Surface to Air Missiles) and Very Short Range Air Defence Missiles (VSHORADMs) respectively

Company also intends to automate their production systems at manufacturing facility in Hyderabad to increase the production of SAMs. BDL is also in the process of establishing a test fire range in Rachakonda, Telangana which is believed to result in operational advantages and cost efficiencies

Increase in indigenisation of products & implementation of the "Make in India" policy –

In order to give an impetus to the GoI's "Make in India" policy, company had implemented a vendor development policy in 2015. BDL believes that the implementation of this policy has enabled them to improve their supply chain management in order to meet their long term commitments to their primary customer, the MoD (Ministry of defense) and ensured transparency in identifying and developing new vendors

BDL has tie-ups with various domestic and international Original Equipment Manufacturers (OEMs) for the development of existing and future products. BDL has achieved indigenisation of upto 75 – 90% of the Konkurs-M ATGM and Milan 2T ATGM (Source: F&S Report). The management is constantly evaluating partnerships for transfer of technology to increase the indigenous content of their products. Increase in indigenisation enables to reduce reliance on imports and the cost of the products

BDL intends to leverage their experience to develop new products such as new generation SAMs, ATGMs, and heavy weight torpedoes which enables the company to further increase their revenues. BDL is also joint development partner with the DRDO for the next generation of ATGMs and SAMs. The MoD (Ministry of defence) has identified BDL 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

BDL has also entered into several MoUs and non-disclosure agreements with various companies for developing new products and transfer of technologies.

BDL continues to invest in infrastructure –

The company is continuously investing in infrastructure in terms of their upcoming manufacturing facilities at Ibrahimapatnam and Amravati, which will enable them to cater to the growing demand of the customers. The proposed unit will be utilized to manufacture SAMs

BDL is also planning to automate the production systems at the manufacturing unit in Hyderabad which will result in the increase of production of SAMs. The company is also in the process of establishing a test fire range in Rachakonda, Telangana which will result in operational advantages and cost efficiencies

BDL has entered into several MoUs and non-disclosure agreements with various companies for developing new products and transfer of technologies. Development of new products will help the company to diversify its offerings which will reduce the reliance on current products. It is also the joint development partner with the DRDO (Defence Research and Development Organization) for the next generation of ATGMs and SAMs

The company provides products as per the requirement of the Indian armed forces and is also planning to interact with overseas customers in order to grow its exports. Akash SAM, light weight torpedoes and countermeasure dispensing systems are products to be exported to the international markets

Major Missile procurement and modernisation programs going ahead –

S-400 Triumf Procurement –

India and Russia have reached an agreement worth over US$5bn for procuring the S - 400 Triumf air defence system. The contract is being executed by Russia's arms export monopoly 'Rosboronexport'. The deliveries are expected to be completed within three years from agreement.

Akash Missile Procurement –

The Cabinet Committee on Security (CCS) is set to clear the procurement of Akash missiles for the Air defence systems of the Indian Air Force, enhancing the supersonic missile capability to intercept fighter jets, cruise missiles; ballistic missiles etc.

Barak- 8 –

India's CSS has approved the procurement of MRSAM (Medium range/Long range (Naval version)) SAM systems, further strengthening the defence capabilities to intercept aircraft, UAS and missile systems. Based on the 'Make in India' initiative, IAI has partnered with Indian organisation DRDO for co-development of both long range(Naval) and medium range(Land) versions of the missile. BDL is manufacturing the missiles in India

VSHORADS Procurement –

Field trials for a US$5.2bn weapon systems procurement contract are underway at present. The total contract is for the supply of 5,175 missiles and 1,276 single and multi-launchers with streamlined technology transfer for the Defence Public Sector Undertakings. Three international companies are participating, namely MBDA, Saab and Rosboron export. BDL is the nominated production agency for the program

Barak – I Procurement –

The Indian government has approved the procurement of Barak – 1 missile system. The contract is worth over $ 78Million and will be delivered over a period of 5 years from 2017 onwards

The Guided Missile and Torpedo Market – India

The Indian Guided Missile and Torpedo market landscape consists of two main types of suppliers at present - DPSUs with indigenous Research Development Testing and Evaluation (RDTE) and manufacturing capabilities and foreign players which export their missile systems to India. There is also an emerging category – the Indian private sector teaming up foreign established defence experts to manufacture missile systems in India

The Indian missile market today is dominated by DPSU produced missiles and foreign solutions at present

However, there is a drive within the establishment to indigenize missile production as much as possible in order to extricate the armed forces from any external dependencies for missile systems in the future

At present, indigenous development and manufacturing is carried out by three DPSUs – DRDO, BDL, and BEL

Amongst the three BDL is the main player in manufacturing and is the sole manufacturer in India for SAMs, torpedoes, ATGMs. There are many opportunities in the Indian market which will be up for grabs in the future

These opportunities, coupled with the ‘Make in India’ initiative and DPP 2016 has stimulated an interesting market dynamic in India

Frost & Sullivan has estimated the total Indian guided missile and torpedo market to be worth $ 24.49 Billion. 79% of the market valuation remains unaddressed and $19.41 Billion worth of opportunities will emerge in the 2017-26 time-frame

Armed forces modernization and new procurements in terms of fighters, IFVs, submarines, corvettes, frigates etc. will in turn drive procurement of guided missile and torpedo systems

The ballistic missile system segment is expected to remain exclusively with DPSUs / GoI. DPSU players such as BDL have strong track record of guided missile production

BDL enjoys a strong balance sheet with huge scalability potential going ahead –

BDL runs a strong business model covering multiple product segments across multi locations with a efficient working capital management while it continues to invest on a sustained basis largely from its internal accruals.

We expect that going ahead overall bottomline growth in the next 3 years starting FY20 onwards should easily increase at a CAGR of 18-20% and with capex funded largely from internal cash flows.

What is important is that CFO have remained positive since last 3 years totalling Rs 504 crs in FY20 & Rs 74 crs in FY21 despite the covid impact on business while borrowings have been virtually zero in the last 5 years with cash/bank totalling Rs 760 crs as on Sept 2020

New Projects –

Amogha-III: BDL has designed and developed Amogha-III, a 3rd Generation man-portable fire-and-forget Anti-Tank Guided Missile. Field firing test of the missile was conducted at KK Ranges, Ahmednagar from 01 – 03 Feb, 2020.

CMDS Mk-II with AI feature to provide self-protection to the aircraft against previously known missile threat at designated way points

Dispenser for AN-32 aircraft for dispensing flares and chaffs

Tester for 50mm Dispenser Unit (DU) of Su-30 MKI aircraft

Konkurs Launcher Test Equipment (KLTE) Ver. II and Konkurs Missile Test Equipment (KMTE) Ver. II.

KLTE Ver. II is Micro-controller based test equipment to check the serviceability of Konkurs ATGM launchers, whereas, KMTE Ver. II is used to check the serviceability of Konkurs-M ATGMs. User trials have been conducted successfully at 17 Field Ammunition Depot (FAD), Ludhiana and 510 Army

Business Outlook & Stock Valuation –

On a rough cut basis, in FY21E, Topline is expected to touch Rs 2100 crs, followed by Rs 3000 crs in FY22E and Rs 3450 crs in FY23E.

On the bottomline level we expect the company to record a PAT of Rs 281 crs in FY21E which is expected to bounce back to Rs 450 crs in FY22 and Rs 550 crs in FY23.

Thus on a conservative basis, BDL should record a EPS of Rs 15 for FY21E. For FY22E and FY23E our expectation is that earnings traction for BDL would continue to be strong wherein we expect a EPS of Rs 25 and Rs 30 respectively.

Also another attractive point for BDL is that EPS growth over the next three years between FY21 to FY23 is expected to average 25% plus YoY but valuation multiples look quite low at 12x on FY23E.

Also the company holds cash/Investments to the tune of Rs 760 crs as on Sept 20 making its net debt free as on Sept 20.

On a EV/EBIDTA basis the stock trades at 10x & 8x on FY22 and FY23 which looks very low for a well established player enjoying good profitability, and a monopolistic hold on its key products with strong operating cash flows and being net cash positive

The company management is confident of improving EBIDTA margins in going ahead via operational efficiency and better product mix.

Looking at BDL's steady financial track record, strong product domain and dominant market share and strong promoters we expect the stock to get re rated in future.

Hence we believe that the BDL stock should be purchased at the current price for a price target of around Rs 450 over the next 18 months.

FINANCIALS

For the Year Ended March RsCrs	FY19	FY20	FY21	FY22	FY23
Net Sales	3069.34	3095.19	2100.00	3000.00	3450.00
EBIDTA	622.11	727.56	357.00	600.00	724.50
EBIDTA %	20.27	23.51	17.00	20.00	21.00
Interest	4.23	4.65	4.00	4.00	3.50
Depreciation	82.50	96.43	98.00	112.70	129.61
Non Operational Other Income	135.98	115.97	120.00	115.00	110.00
Profit Before Tax	671.36	742.45	375.00	598.30	701.40
Profit After Tax	422.58	534.90	281.00	450.00	550.00
Diluted EPS (Rs)	23.06	29.18	15.33	24.55	30.01
Equity Capital	183.28	183.28	183.28	183.28	183.28
Reserves	2085.26	2423.54	2554.54	2844.54	3219.54
Borrowings	1.82	2.17	3.00	3.00	3.00
GrossBlock	1220.00	1291.00	1366.00	1466.00	1566.00
Investments	3.71	3.71	3.71	3.71	3.71

Source Company our Estimates

KEY CONCERNS

Drop in orders from the Govt can impact business negatively ahead for BDL

Lack of export orders can also slow down the progress for BDL

Disclaimer –