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Price Band: INR 165-175

ISSUE SUMMARY

Issue Opens	21-Sep-21
Issue Closes	23-Sep-21
Offer Price (INR per share)	165-175
Bid Lot	85 shares
Face Value (INR)	10.0
Pre Issue Shares o/s (mn)	31.0
Offer for Sale (No of sh. mn)	1.7
^Fresh Issue (No of sh. mn)	8.0
^Post Issue shares o/s (mn)	39.0
^*Issue Size (INR bn)	1.7
QIB	=>50%
Non-institutional	<15%
Retail	<35%
^ Issue Size (@INR175)	

POST ISSUE DETAILS

M.Cap @INR175/sh. (INR bn)	6.8
Shareholding pattern	
Promoters	59.7%
Non-Promoters	40.3%

Leading player in Defence/Space: Paras Defence and Space Technologies Ltd (PDSTL) is one of the leading 'Indigenously Designed Developed and Manufactured' (IDDM) category Indian private sector company catering to defence and space optics, defence electronics, EMP protection solutions and heavy engineering. GoI's outlays on these segments is expected to increase at 16% CAGR to over USD14.5bn by 2031.

Optics is key growth driver: Optics is the major focus area for PDSTL with revenue from this segment having increased from 30% in FY19 to 45% in FY21. It is the only Indian company with the design capability for space optics and opto-mechanical assemblies. It constitutes ~67% of the order book (OB; INR3bn) and would be key focus area along with drones.

New product launches to provide diversification: PDSTL is currently developing several new products, such as turnkey submarine periscope, optical/multi/hyper spectral cameras for drones/space, telescopes, anti-drone systems, etc. It has partnered with global technology providers to tap import substitution opportunities under GoI's Atmanirbhar Bharat and 'Make In India' initiatives as well as tap global requirements.

Financials: While PDSTL's Revenue/PAT got impacted due to Covid-19 over FY20-21, EBITDA margins expanded by 254bps to 30.3% over FY19-21 led by better cost management. It has negligible debt on its books which post IPO will further reduce to 0.2x. However it is working capital intensive (~300+ days) and its asset turnover stands at below 1x, thus resulting in suppressed return ratios. With OB/bill at 2x, and contribution from subsidiaries to kick in from FY22 onwards, there is good revenue visibility going ahead

Issue Size: The INR1.7bn IPO consists of fresh issue of INR1.4bn and OFS of INR0.3bn which would result in promoter's stake reducing from 79.4% pre-IPO to 59.7% post-IPO. PDSTL also raised pre-IPO money worth INR0.3bn from various investors. The funds raised will be utilized for capex, debt repayment and funding of working capital.

Valuation & View: We like PDSTL given its complex/wide product portfolio, presence in niche defence space, strong client relationship and high entry barriers. The issue is valued at 1.9x P/BV (peers avg: ~2.4x) on a post issue basis, which is reasonable. We believe PDSTL could benefit from government impetus on the defence and space expenditure. Hence we recommend **Subscribe**. Further given the current buoyant market and high interest for defence stocks, the issue could see **listing gains** as well.

Exhibit 1: Financials & Valuations (INR mn)

Y/E March	FY19	FY20	FY21
Revenue	1,544	1,470	1,433
Growth (%)	NA	-4.8	-2.5
Adj PAT	190	197	158
Growth (%)	NA	3.6	-19.7
EPS (INR)	4.9	5.0	4.0
RoE (%)	12.5	12.1	5.9
P/E	36.0	34.7	43.2

*Calculated on post issue basis, at the upper price band of INR175; Source: RHP, MOFSL

Peer Comparison

Exhibit 2: Valuation matrix

Company	M.Cap. INR Bn	PAT CAGR FY19-21 (%)	EBITDA Margin FY21 (%)	P/E FY21 (%)	P/BV FY21 (%)	EV/EBITDA FY21 (%)
BEL	500	5.8	23.7	14.5	2.8	7.6
HAL	478	17.9	25.2	10.3	2.2	4.6
Bharat Dynamics	74	-22.1	23.0	23.7	2.3	10.3
BEML	59	4.3	5.6	76.1	2.4	30.2
Paras Defence	7	-8.8	30.3	43.2	1.9	14.1

Source: Company RHP, Bloomberg, MOFSL

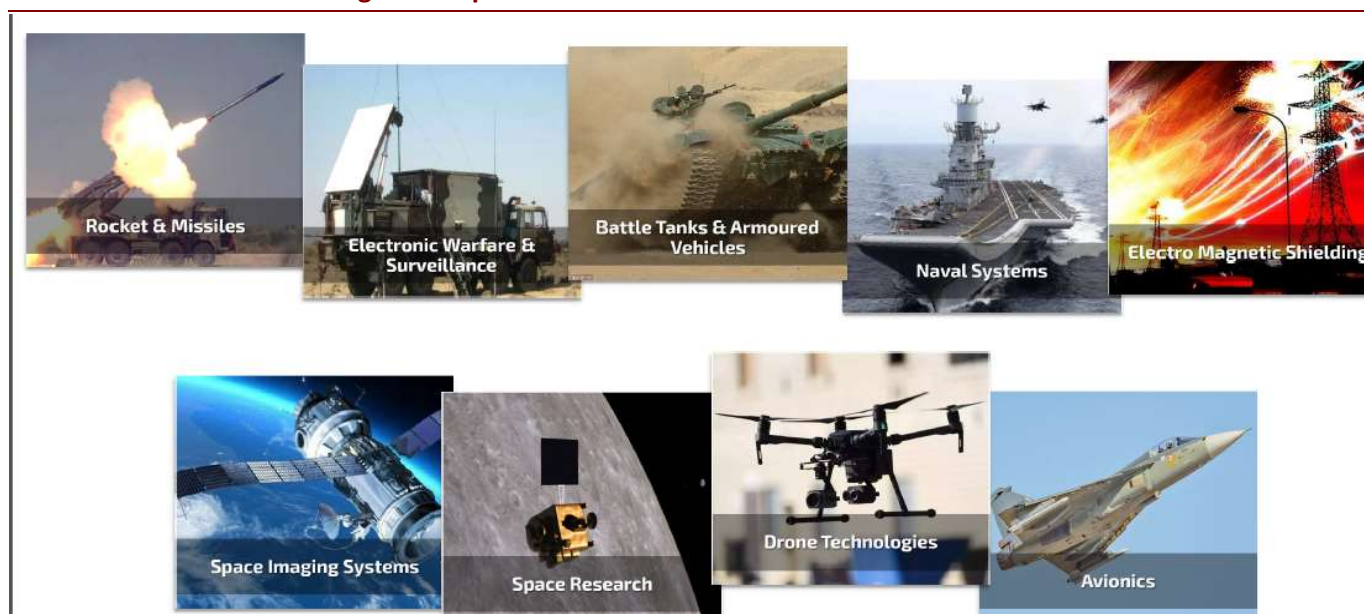
*Price Data as on 20th September, 2021

^Calculated on fully diluted basis at upper price band of INR175

About the Company

Paras Defence (PDSTL) is one of the leading 'Indigenously Designed Developed and Manufactured' (IDDM) category private sector companies engaged in designing, developing, manufacturing and testing of a wide range of defence and space engineering products and solutions. It caters to four major segments of Indian defence sector i.e. defence and space optics, defence electronics, electro-magnetic pulse (EMP) protection solution and heavy engineering. It is also the sole Indian supplier of critical imaging components such as large size optics and diffractive gratings for space applications in India. Its goal is to become one of the leading global companies for optics for defence and space sector. It is well positioned to benefit from the Government's "Atmanirbhar Bharat" and "Make in India" initiatives.

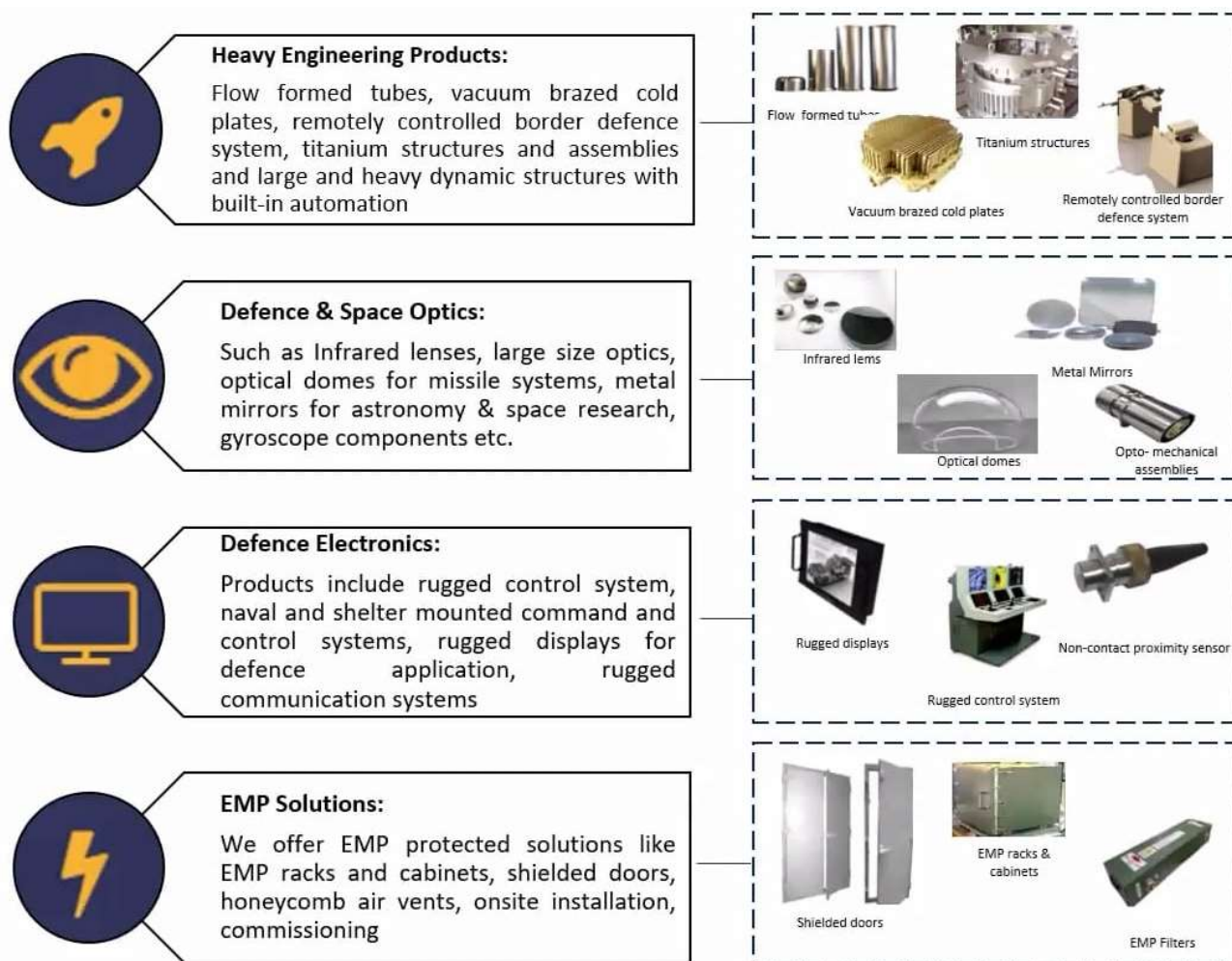
Exhibit 3: Areas & Technologies of Expertise



Source: RHP, MOFSL

In the space sector, PDSTL has established heritage in the earth observation domain by supporting government organizations involved in space research across multiple missions. It is also the sole Indian supplier of diffraction gratings used in hyper-spectral imagers, large size optics (F&S report). Further, the company has been a part of most of the earth observation and space exploration missions since 2018 (F&S Report). Involvement in various space exploration missions has helped PDSTL develop a strong foothold in the Indian space industry by being the sole supplier of optics and opto-mechanical assemblies for these space exploration missions (F&S Report).

Exhibit 4: Diversified Business Verticals & Products



Source: RHP, MOFSL

From time to time, PDSTL enters into contracts with third parties in India and outside India for partnering in relation to development of certain products or sourcing components. For instance, PDSTL has entered into teaming agreements with companies such as HPS GmbH, Invent GmbH, and Kley France for securing contracts and manufacturing of products. These agreements are typically short term and are entered for a period of one or two years. Further, company has also entered into a partnership agreement with S-TEC Corporation for collaboration in relation to offering products and solutions for aircraft component manufacturing. PDSTL has also partnered with Canada based PreditMedix to manufacture Safe Entry Station. These provide AI based detection of symptoms of Infectious diseases including COVID.

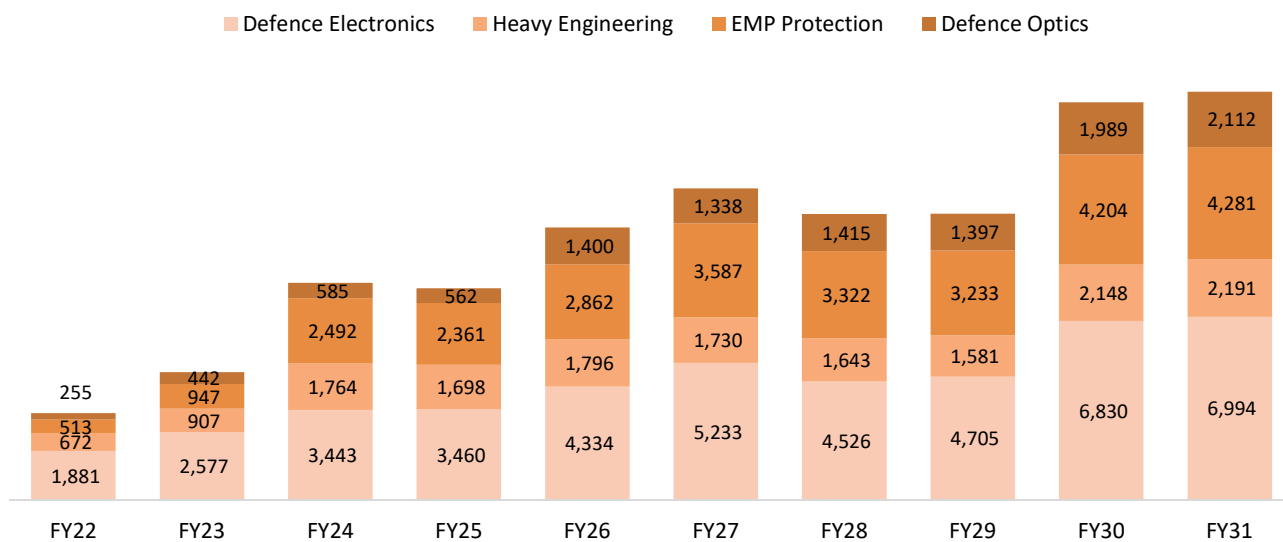
Exhibit 5: Partnerships & Associates



Source: RHP, MOFSL

Recently, the MoD has announced the Defence Acquisition Procedure, which focuses on significantly boosting indigenous production and turning India into a global manufacturing hub of weapons and military platforms. This is expected to provide a boost to indigenous defence companies such as PDSTL and we believe that with the expertise and technological know-how that the company has, it is poised to take advantage of the expected growth in India's defence industry. The outlays by the Indian Government on the four segments where PDSTL is present is expected to increase from ~USD3.2b in 2021 to over USD14.5b by 2031 due to extensive fleet re-capitalization, C4ISR orientation and greater indigenous supply preferences.

Exhibit 6: GoI's outlay on the four segments to grow at 16% CAGR to USD14.5b (USD m)



Source: RHP, MOFSL

Paras derive most of its revenues under the contracts from the Government arms and associated entities such as defence public sector undertakings and government organizations involved in space research. Its customer base includes Government arms and notable Indian public and private sector companies including BEL, HAL, Bharat Dynamics, etc.

Exhibit 7: Diversified Customer Base

Source: RHP, MOFSL

PDSTL have two manufacturing facilities in Maharashtra, located at Nerul in Navi Mumbai and Ambernath in Thane. It have diversified products and solutions mainly due to R&D and technological capabilities. Its research activities are focused on creating new products and solutions which are customized to meet customer expectations and end-user preferences and also improving production processes and improving the quality of its existing products. With R&D capabilities, it is currently developing several new products and solutions, such as hyper spectral space camera, ARINC-818 based avionic display, naval periscopes and optical solar reflectors.

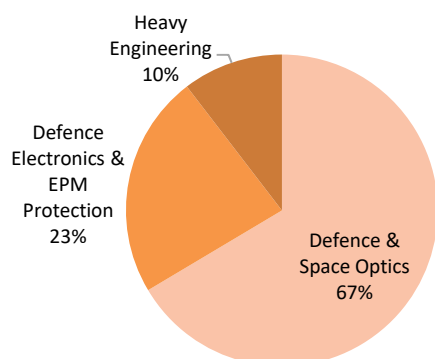
Exhibit 8: New Products & solutions

Future Activities	Description
Turnkey Submarine Periscope	It is a high performance sighting system designed to perform under extreme submarine environment making it magical marvel.
Optical/Multi/Hyper Spectral Cameras	Dron payload cameras are high end imaging cameras providing exceptional imaging capabilities under dynamic moving condition. It is used in various applications like homeland security, agriculture, industrial, etc.
Large Sized Flow formed tubes	Paras is proactively investing in one of its kind manufacturing setup to manufacture large sized flowform tubes which are used in space rockets
Optical Solar Reflectors	OSRs are used for radiators on spacecrafts.
Complete Avionic Suite with Auto Pilot	Complete Avionic Suite (Glass Cockpit) for FAR - 23 Aircraft
Large Deployable Antenna	LDA (Un-furlable) for space application
CFRP Structures	Use for space application

Source: RHP, MOFSL

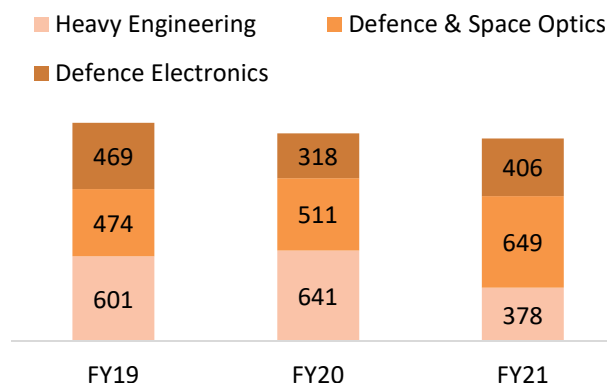
Story in Charts

Exhibit 9: Order Book as on Q1 FY22 (%)



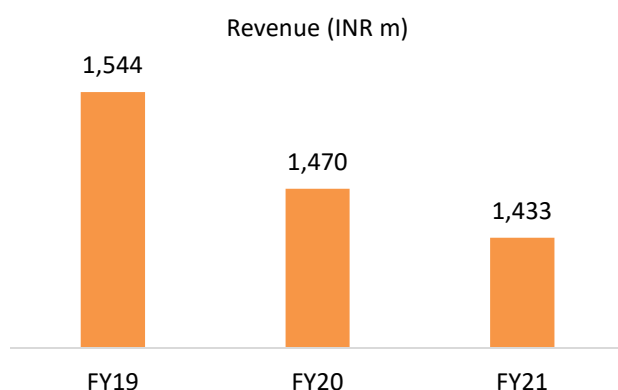
Source: RHP, MOFSL

Exhibit 10: Revenue by Business Verticals (INR m)



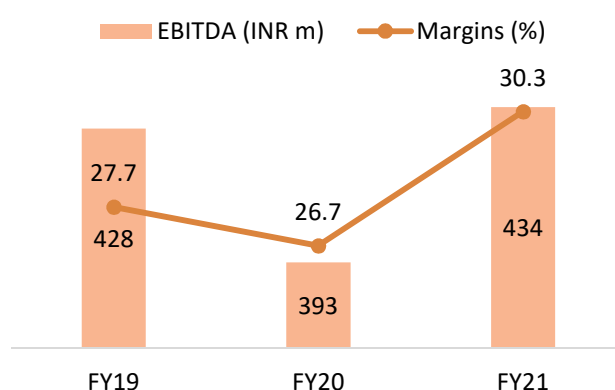
Source: RHP, MOFSL

Exhibit 11: Revenue impacted over FY20-21 due to Covid-19



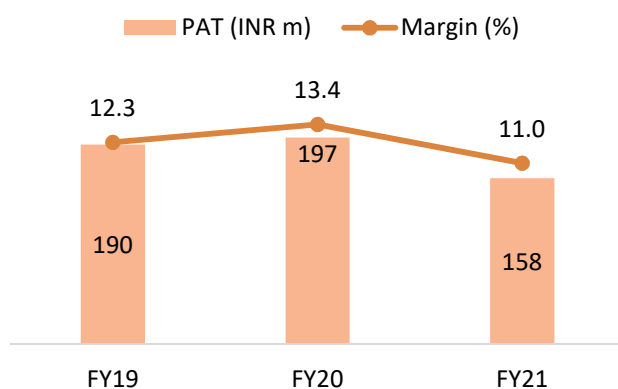
Source: RHP, MOFSL

Exhibit 12: EBITDA margins improve by 254bps despite subdued revenue



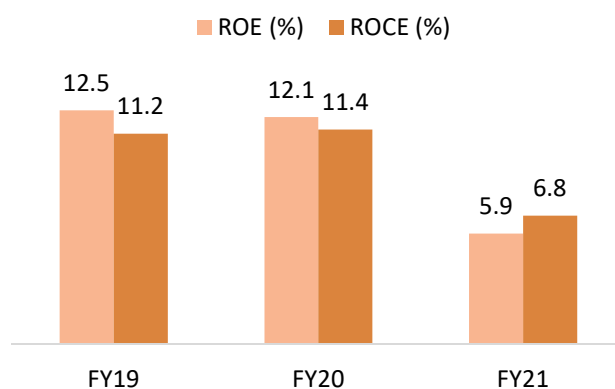
Source: RHP, MOFSL

Exhibit 13: PAT trend



Source: RHP, MOFSL

Exhibit 14: Weak Return ratios due to high WC requirement



Source: RHP, MOFSL

Risk and concerns

- PDSTL is largely dependent on contracts from GoI and associated entities including defence PSUs and government organizations involved in space research. Any reprioritization/termination of existing contracts, or any adverse change in the GoI's defence/space related policies will have an adverse impact on the business.
- The company has executed various agreements with third parties, including in relation to securing contracts and manufacturing of products. Any termination of contract may adversely affect the business.
- Many of PDSTL contracts contain performance obligations that require innovative design capabilities, are technologically complex or involve developmental costs.
- Given the nature of the business, the working capital requirement is very high (~300+ WC days), which leads to negative free cash flow.
- The contracts are fixed price in nature. Thus as a result of cost overruns, delays in delivery or failures to meet contract specifications may have an adverse effect.

Financials

Income Statement

(INR m)

Y/E March	FY19	FY20	FY21
Net Sales	1,544	1,470	1,433
Change (%)	NA	-4.8	-2.5
Total Expenditure	1,116	1,078	999
% of Sales	72.3	73.3	69.7
EBITDA	428	393	434
Margin (%)	27.7	26.7	30.3
Depreciation	94	97	97
EBIT	334	296	337
Int. and Finance Charges	94	98	124
Other Income	28	20	13
PBT	268	218	226
Tax	78	21	68
Tax Rate (%)	29.2	9.8	30.2
Reported PAT	190	197	158
Adjusted PAT	190	197	158
Change (%)	NA	3.6	-19.7
Margin (%)	12.3	13.4	11.0

Source: Company RHP, MOFSL

Balance Sheet

(INR m)

Y/E March	FY19	FY20	FY21
Share Capital	57	284	299
Reserves	1,467	1,442	1,768
Net Worth	1,524	1,726	2,066
Debt	761	971	937
Deferred Tax (Net)	278	235	231
Total Capital Employed	2,563	2,932	3,235
Net Fixed Assets	1,683	1,578	1,566
Capital WIP	26	49	5
Investments	1	1	11
Current Assets	1,588	1,796	2,045
Inventory	645	604	747
Debtors	832	976	949
Cash and Bank Balance	19	44	83
Loans and Advances & OCA	92	172	266
Curr. Liability & Provisions	735	492	392
Account Payables	533	270	153
Current Liabilities	184	207	226
Other Long Term Liab. & Provs.	18	14	13
Net Current Assets	853	1,304	1,653
Misc Expenditure	-	-	-
Appl. of Funds	2,563	2,932	3,235

Source: Company RHP, MOFSL

Key Ratios

Y/E March	FY19	FY20	FY21
Basic (INR)			
EPS	4.9	5.0	4.0
Cash EPS	7.3	7.5	6.5
BV/Share	39.1	44.3	93.2
DPS	0.0	0.0	0.0
Valuation (x)			
P/E	36.0	34.7	43.2
Cash P/E	24.1	23.2	26.8
P/BV	4.5	4.0	1.9
EV/Sales	4.9	5.3	4.3
EV/EBITDA	17.7	19.7	14.1
Dividend Yield (%)	0.0	0.0	0.0
Return Ratios (%)			
RoE	12.5	12.1	5.9
RoCE	11.2	11.4	6.8
Working Capital Ratios			
Fixed Asset Turnover (x)	0.9	0.9	0.9
Asset Turnover (x)	0.6	0.5	0.3
Inventory (Days)	153	150	190
Debtor (Days)	197	242	242
Creditor (Days)	126	67	39

Source: Company RHP, MOFSL

*All ratios calculated on fully diluted basis at the upper price band of INR175

Cash Flow Statement**(INR m)**

Y/E March	FY19	FY20	FY21
OP/(Loss) before Tax	268	218	226
Depreciation	94	97	97
Finance Cost	94	98	124
Income Taxes paid	-70	-70	-69
(Inc)/Dec in WC	-514	-384	-340
CF from Operations	-127	-42	38
Others	7	16	5
CF from Operating (Net)	-121	-26	43
(Pur)/Sale of FA	-97	-40	-53
(Pur)/Sale of Investments	-	-	-11
Interest/Dividend received	1	2	1
Bank Deposits	-	-10	-
CF from Investments	-96	-49	-63
Proceeds from borrowings	185	189	-130
Issue of equity shares	-	-	319
Interest Paid	-81	-95	-106
Dividend Paid	-	-	-
Others	110	-8	-30
CF from Fin. Activity	214	86	54
Net Inc/Dec of Cash	-2	11	34
Opening Balance	4	2	15
Closing Balance	2	15	51

Source: Company RHP, MOFSL

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	> - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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