Cochin Shipyard (COCSHI)

ICICI direct Research

CMP: ₹ 500 | Target: ₹ 580 (16%) | Target Period: 12 months | **BUY**

June 1, 2023

Result Update

Strong order backlog; execution expected to pick up

About the stock: Cochin Shipyard (CSL) was incorporated in 1972 as a Government of India company, with the first phase of facilities coming online in 1982. CSL is the largest shipbuilding and maintenance facility in India.

- The yard has facilities to build vessels up to 1.1 lakh tonnes (lt) and repair vessels up to 1.25 litre annually
- CSL has secured shipbuilding orders from internationally renowned companies from Europe and the Middle East in the recent past

Q4FY23 Results: Below expected performance in the ship-building segment.

- Revenue came in at ₹ 600.1 crore (down 50.5% YoY). Both segments, shipbuilding and ship-repair, witnessed a decline in revenues
- Gross margin was at 13.2% (2385 bps down YoY). At the EBITDA level, the company reported a loss of ₹ 67.1 crore against positive EBITDA of ₹ 296.3 core in Q4FY22
- Adjusted PAT was at -₹ 22.5 crore against ₹ 274.6 crore in Q4FY22 and ₹ 110.4 crore in Q3FY23

What should investors do? Execution is expected to improve significantly over FY24-25E, which would drive revenues. Margins are also expected to improve led by improving performance in the ship repair segment and operating leverage benefits.

- We maintain our **BUY** rating on the stock

Target Price and Valuation: We value CSL at ₹ 580 i.e. 15x P/E (FY25E EPS).

Key triggers for future price performance:

- The order backlog was healthy at ₹ 22132 crore (9.3x FY23 revenues). Majority of large contracts in the order book are expected to witness meaningful execution during FY24 and FY25
- Healthy order book and strong pipeline of projects in the coming two to three years from Indian Navy and other international customers
- Capacity expansion for ship-repair activities to help get more orders in this segment, which is also a higher margin business

Alternate Stock Idea: We also like Bharat Electronics in the defence space.

- Strong order book and healthy pipeline in defence electronics offers strong visibility; diversifying into non-defence to help improve margins
- BUY with a target price of ₹ 135 per share

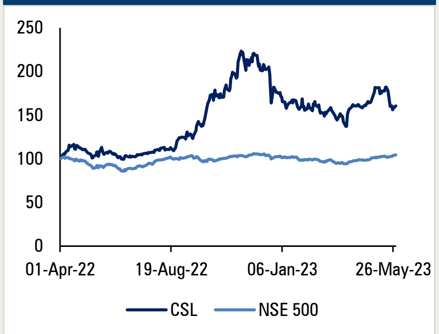
Particulars

Particular	Amount
Market Capitalization	₹ 6538 Crore
Total Debt (FY23)	₹ 132.9 Crore
Cash & Inv (FY23)	₹ 4758 crore
EV (FY23)	₹ 1912 Crore
52 week H/L (₹) (BSE)	687/296
Equity capital	₹ 131.5 Crore
Face value	₹ 10

Shareholding Pattern

	Jun-22	Sep-22	Dec-22	Mar-23
Promoter	72.9	72.9	72.9	72.9
FII	2.8	3.7	6.9	6.3
DII	2.3	2.7	2.2	2.3
Others	22.1	20.7	18.1	18.6

Price Chart



Recent event & key risks

- Receiving orders from Europe
- **Key Risk:** (i) Delays in execution (ii) Delays in order placement

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ICICI Securities – Retail Equity Research

Key Financial Summary

(₹ Crore)	FY20	FY21	FY22	FY23	3 Year CAGR (FY20-FY23)	FY24E	FY25E	2 Year CAGR (FY23E-25E)
Revenues	3,422	2,819	3,191	2,366	(11.6)	3,569	4,393	36.3
EBITDA	709	716	623	248	(29.5)	479	631	59.4
EBITDA margins	20.7	25.4	19.5	10.5		13.4	14.4	
Net Profit	638	611	564	305	(21.8)	406	509	29.3
EPS (₹)	48.5	46.4	42.9	23.2		30.9	38.7	
P/E (x)	10.3	10.8	11.7	21.6		16.2	12.9	
Price / Book (x)	1.8	1.6	1.5	1.5		1.4	1.4	
EV/EBITDA (x)	6.4	6.3	5.6	7.9		8.2	7.4	
RoCE (%)	17.6	14.1	11.4	4.4		7.0	8.5	
RoE (%)	17.1	14.9	12.7	7.9		8.8	10.5	

Source: Company, ICICI Direct Research

Key takeaways of recent quarter

Q4FY23 Results

- Revenue came in at ₹ 600.1 crore (down 50.5% YoY); much lower than our estimate of ₹ 1270.5 crore. Both segments, shipbuilding and ship repair, witnessed worse than expected execution and reported decline in revenues
- Ship-building revenue has declined by 52.7% YoY to ₹ 453.8 crore and ship-repair revenue declined 42.1% YoY to ₹ 146.2 crore. Sequentially also, total revenue is down by 6.5% despite being a fourth quarter when execution generally remains better on a QoQ basis (ship building revenue is down 1.6% QoQ while ship-repair revenue is down 18.9% QoQ)
- Gross margin was at 13.2%, contracting significantly from 37% in Q4FY23 and 47% in Q3FY23. At the EBITDA level, the company reported a loss of ₹ 67.1 crore against positive EBITDA of ₹ 296.3 core in Q4FY22 and ₹ 148.8 crore in Q3FY23. We had estimated EBITDA of ₹ 314.5 crore
- EBIT from the ship-building segment was at -₹ 88.3 crore (vs. ₹ 231.3 crore in Q4FY22 and ₹ 112.5 crore in Q3FY23). Ship-repair segment EBIT also declined sharply by 71.6% YoY and 64.8% QoQ to ₹ 20.7 crore. EBIT margin for ship-repair was at 14.2% vs. 28.9% in Q4FY22 and 32.7% in Q3FY23
- The company also mentioned that liquidated damage (LD) charges have been provided by the company for delay in one of the shipbuilding contracts (construction of two 1200 passenger vessels for Andaman & Nicobar Administration). However, the LD charges amount was not mentioned
- Reported PAT came in at ₹ 39.3 crore. However, there was an exceptional item of ₹ 61.8 crore (related to prior period's capex). Adjusted PAT was at -₹ 22.5 crore against ₹ 274.6 crore in Q4FY22 and ₹ 110.4 crore in Q3FY23

Earnings Call Highlights

- Major reasons behind the revenue shortfall were 1) delay in financial closure in the dredger contract, 2) supply chain issues, change in few critical components and delay in arrival of main engines in Anti-Submarine Warfare Shallow Water Craft (ASW-SWC) project, 3) not recognised revenue from eight multipurpose vessels (MPVs) export contract from Europe
- In eight multipurpose vessel contract for European client, CSL was unable to book any revenue from this contract in FY23 as the owner nominated basic designer, which was unable to meet up design schedule as envisaged
- In the Trailing Suction Hopper Dredger (TSHD) contract, which was signed in March 2022 with IHC Holland as the partner, the procedure involved in owner securing overseas funding led to delays in financial closure. Consequently, the contract was effective from November 2022, which impacted the revenue recognition. Moreover, there was also some delay in engineering and construction commencement
- In ASW-SWC contract, the geopolitical situation impacted certain supply chain and thereby impacted production schedule. Also, there was a delay in arrival of engine sets from Europe
- There were some changes in design structure and procurement of sensors. These issues had a significant impact on the outfitting work and led to lower revenue booking
- As there was the need for a change in procurement and installation of two major sensors, the necessity for revision of the accounting estimate was noticed and the revenue shortfall of ₹ 280 crore on account of this was accounted in Q4FY23. However, as per the management, revenue shortfall will be recovered in FY24
- Even in the ship repair segment, there were some challenges in execution of the first major naval refit at the Mumbai ship repair unit

- The shipbuilding order backlog was at ₹ 21432 crore as of March 2023. The order book in ship repair was at ₹ 700 crore
- Out of ₹ 21432 crore order backlog, the defence segment contributes ₹ 17545 crore worth of orders while the balance is from commercial segment including exports
- Largest orders on the book include ₹ 9805 crore contract received recently for next generation missile vessels (NGMVs) from Indian Navy, ₹ 5864 crore worth of pending contract in ASW-SCW Corvette for Indian Navy
- Revenue from the ship-building segment is expected at ₹ 3000 crore in FY24 while ship-repair segment revenue is expected at ₹ 900 crore
- EBITDA margin in ship-building and ship-repair segments are expected at 12-13% and 18-19% respectively. Blended EBITDA margin is expected at 14-15%
- In ASW-SWC contract, three vessels are slated to be launched by November 2023, of which the first vessel will be delivered by November 2024 and two vessels will be delivered every year
- In NGMV contract, the first vessel will be delivered 48 months from now. Post this, one vessel is scheduled to be delivered every year
- The new dry dock project is expected to be commissioned by December 2023. The project has reached physical progress of 76%
- In ship-building, orders worth ₹ 9245 crore are in the pipeline (which are in advanced and request for proposal - RFP stage) which includes NG Offshore Patrol Vessels (NGOPVs), Fast Patrol Vessels (FPV), Commissioning Service Operation Vessels For Europe, etc
- Bids for FPVs and NGOPVs are expected to open in June 2023
- Apart from this, there are orders worth ₹ 35000 crore, which are in request for information (RFI) stage, which includes landing platform dock, Fast Attack Craft (FACs), Fast Interceptor Craft (FICs), etc
- There is a big opportunity in the electric vessels segment from Europe as 2500 vessels are scheduled to be replaced with green vessels as per European Union Emission trading System (EU ETS) scheme
- In ship-repair also, major defence and conversion orders are in the pipeline. MoU between CSL and Lakshadweep Development Corporation is in place and will help regain revenue. Revenue generation from Naval weapons repairs and AMCs for defence vessels are also expected

Exhibit 1: Variance Analysis

	Q4FY23	Q4FY23E	Q4FY22	YoY (%)	Q3FY23	QoQ (%)	
Revenue	600.1	1270.5	1212.5	-50.5	641.7	-6.5	Execution remained poor YoY in both ship building & ship repair segments
Other Income	71.2	59.2	111.8	-36.3	23.2	207.1	
Total Revenue	671.3	1329.7	1324.3	-49.3	664.8	1.0	
Total Raw Material Costs	521.0	710.2	763.4	-31.8	339.9	53.3	
Employee Expenses	89.9	118.5	84.7	6.2	85.1	5.7	
Other expenses	54.0	122.8	50.7	6.4	65.8	-18.0	
Provision for losses & exp.	2.3	4.5	17.4	-86.7	2.2	6.3	
Operating Profit (EBITDA)	-67.1	314.5	296.3	-122.6	148.8	-145.1	
EBITDA margin (%)	-11.2%	24.8%	24.4%	-3561 bps	23.2%	-3436 bps	Margin contracted sharply on poor execution
Interest	-1.5	12.5	11.7	-112.6	12.3	-112.1	
Depreciation	10.9	19.5	17.6	-38.2	19.2	-43.3	
Total Tax	17.2	86.4	99.5	-82.7	30.1	-42.7	
PAT	39.3	255.3	274.6	-85.7	110.4	-64.4	

Key Metrics	Q4FY23	Q4FY22	YoY (%)	Q3FY23	QoQ (%)	
Revenue (Segment-wise)						
Shipbuilding	453.8	959.8	-52.7	461.4	-1.6	Delay in execution impacted ship-building revenues
As a % of Sales	75.6%	79.2%		71.9%		
Shiprepair	146.2	252.7	-42.1	180.3	-18.9	Ship repair performance also remained muted
As a % of Sales	24.4%	20.8%		28.1%		
EBIT (Segment-wise)						
Shipbuilding	-88.3	231.3	-138.2	112.5	-178.5	
EBIT Margins(%)	-19.4%	24.1%		24.4%		
As a % of EBIT	1313.1%	60.0%		73.7%		
Shiprepair	20.7	72.9	-71.6	59.0	-64.8	
EBIT Margins (%)	14.2%	28.9%		32.7%		
As a % of EBIT	-308.6%	18.9%		38.6%		

Source: Company, ICICI Direct Research

Exhibit 2: Change in Estimates

	FY23	FY24E			FY25E		
(₹ Crore)	Actual	Old	New	Change(%)	Old	New	Change(%)
Revenue	2365.8	3353.8	3568.8	6.4	3954.6	4392.5	11.1
EBITDA	248.4	654.0	478.9	-26.8	771.2	631.3	-18.1
EBITDA Margin (%)	10.5	19.5	13.4	-608 bps	19.5	14.4	-513 bps
PAT	304.7	540.3	406.3	-24.8	629.1	509.4	-19.0
EPS (₹)	23.2	41.1	30.9	-24.8	47.8	38.7	-19.0

Source: ICICI Direct Research, Company

Financial Summary

Exhibit 3: Profit and loss statement ₹ crore

(₹ Crore)	FY22	FY23	FY24E	FY25E
Revenue	3,191	2,366	3,569	4,393
% Growth	*13.2*	*(25.9)*	*50.8*	*23.1*
Other income	262	212	210	220
Total	3,453	2,578	3,779	4,613
% Growth	*14.7*	*(25.4)*	*46.6*	*22.1*
Raw Mtl costs	2,026	1,557	2,470	3,053
Employee Expenses	311	334	360	391
other expenses	183	217	250	307
Total Operating Exp.	2,568	2,117	3,090	3,761
EBITDA	623	248	479	631
% Growth	*(13.1)*	*(60.1)*	*92.8*	*31.8*
Interest	47	35	40	40
PBDT	838	425	649	811
Depreciation	70	69	100	123
PBT & Except. items	769	357	549	688
Total Tax	202	114	143	179
PAT before MI	564	305	406	509
PAT	564	305	406	509
% Growth	*(7.7)*	*(46.0)*	*33.3*	*25.4*
EPS	43	23	31	39

Source: Company, ICICI Direct Research

Exhibit 4: Cash flow statement ₹ crore

(₹ Crore)	FY22	FY23	FY24E	FY25E
Profit after Tax	564	305	406	509
Depreciation	70	69	100	123
Interest	47	35	40	40
CF before WC changes	681	409	546	672
Changes in inventory	128	(67)	(175)	(78)
Changes in debtors	(37)	52	(199)	(64)
Changes in loans & Adv	(18)	(72)	(54)	(37)
Changes in other CA	167	316	(759)	(535)
Net Increase in CA	240	229	(1,187)	(715)
Changes in creditors	(59)	(160)	145	120
Changes in provisions	(43)	(82)	121	123
Net Inc in CL	532	1,575	(560)	188
CF from Operatons	1,453	2,212	(1,201)	145
Changes in deferred tax assets	5	11	-	-
(Purchase)/Sale of FA	(261)	(381)	(550)	(550)
CF from Investing	(198)	(342)	(550)	(550)
Dividend & Dividend Tax	(220)	(224)	(243)	(276)
CF from Financing	(199)	(252)	(286)	(319)
Net Cash flow	1,056	1,619	(2,036)	(724)
Opening Cash/Cash Eq	2,150	3,206	4,825	2,789
Closing Cash/ Cash Eq	3,206	4,825	2,789	2,065

Source: Company, ICICI Direct Research

Exhibit 5: Balance Sheet ₹ crore

(₹ Crore)	FY22	FY23	FY24E	FY25E
Equity Capital	132	132	132	132
Reserve and Surplus	4,262	4,292	4,494	4,724
Total Shareholders funds	4,393	4,423	4,626	4,856
Minority Interest	-	-	-	-
Total Debt	**123**	**133**	133	133
Total Liabilities	**4,913**	**4,966**	**5,168**	**5,398**
Gross Block	**1,262**	**1,304**	2,457	3,707
Acc: Depreciation	292	361	461	584
Net Block	970	943	1,996	3,123
Capital WIP	1,264	1,602	1,000	300
Total Fixed Assets	2,234	2,546	2,996	3,423
Non Current Assets	360	334	334	334
Inventory	306	373	548	626
Debtors	390	338	538	602
Loans and Advances	35	107	161	198
Other Current Assets	1,876	1,561	2,320	2,855
Cash	**3,213**	**4,758**	**2,789**	**2,065**
Total Current Assets	5,820	7,137	6,355	6,346
Current Liabilities	376	216	362	481
Provisions	522	440	561	684
Net Current Assets	2,319	2,060	1,838	1,641
Total Assets	**4,913**	**4,940**	**5,168**	**5,398**

Source: Company, ICICI Direct Research

Exhibit 6: Key ratios

(Year-end March)	FY22	FY23	FY24E	FY25E
Per Share Data				
EPS	42.9	23.2	30.9	38.7
Cash per Share	244.2	361.7	212.0	157.0
BV	334.0	336.3	351.6	369.2
Dividend per share	16.8	17.0	18.5	21.0
Dividend payout ratio	39%	73%	60%	54%
Operating Ratios				
EBITDA Margin	19.5	10.5	13.4	14.4
PAT Margin	16.3	11.8	10.8	11.0
Return Ratios				
RoE	12.7	7.9	8.8	10.5
RoCE	11.4	4.4	7.0	8.5
RoIC	20.9	6.8	8.2	8.2
Valuation Ratios				
EV / EBITDA	5.6	7.9	8.2	7.4
P/E	11.7	21.6	16.2	12.9
EV / Net Sales	1.1	0.8	1.1	1.1
Sales / Equity	0.7	0.5	0.8	0.9
Market Cap / Sales	2.1	2.8	1.8	1.5
P/BV	1.5	1.5	1.4	1.4
Turnover Ratios				
Asset Turnover Ratio	2.5	1.8	1.5	1.2
Debtors Turnover Ratio	8.6	6.5	8.1	7.7
Creditors Turnover Ratio	7.9	8.0	12.3	10.4
Solvency Ratios				
Debt / Equity	0.0	0.0	0.0	0.0
Current Ratio	2.8	3.5	3.8	3.6
Quick Ratio	2.5	2.9	3.2	3.1

Source: Company, ICICI Direct Research

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