

Growth visibility remains strong...

About the stock: Hindustan Aeronautics (HAL), the largest defence PSU in India, is engaged in design, development, manufacture, repair, overhaul, upgrade and servicing of a wide range of products including, aircraft, helicopters, aero-engines, avionics, accessories and aerospace structures.

- The company has delivered revenue, EBITDA and PAT CAGR of 7.4%, 12% and 26.5%, respectively, in FY18-22. In FY22, repair & overhaul contributed ~64% to total revenues while manufacturing contributed ~30%

Q3FY23 Result: EBITDA margins contracted on higher provisions

- Revenue declined 3.8% YoY to ₹ 5665.5 crore on higher base. Sequentially, revenue increased 10.1%
- The EBITDA margin contracted 682 bps YoY to 17.4% on higher provisions; leading to EBITDA de-growth of 30.9% YoY to ₹ 985.4 crore
- PAT rose 23.8% YoY to ₹ 1155.2 crore (due to tax refunds of ₹ 427.4 crore)

What should investors do? We expect HAL to deliver revenue and EBITDA CAGR of 10.3% and 14.8%, respectively, over FY22-25E. PAT is likely to grow at 11.9% CAGR (FY21-25E). Increase in profitability with strong asset turnover is expected to result in healthy return ratios over FY23-25E.

- We continue to remain positive and retain our **BUY** rating on the stock

Target Price and Valuation: We value HAL at ₹ 3300 i.e. 20x PE on FY25E EPS.

Key triggers for future price performance:

- Healthy order book position (₹ 84000 crore; 3.2x TTM revenues) led by large scale orders in manufacturing aircraft/helicopters (LCA, LCH, ALH)
- Continuous order inflows in maintenance, repair & overhaul (MRO) with strong order pipeline in manufacturing for the next three to four years (led by LUH, LCH, ALH, Dornier, HTT-40 and engines for Su-30 & MiG-29)
- LCA Tejas MK1A, largest order in manufacturing, deliveries to IAF expected from FY24E end. Moreover, execution of other key orders and sustained growth in MRO to drive revenue growth in double digits from FY25E

Alternate Stock Idea: We also like Bharat Dynamics (BDL) in the defence space.

- Strong earnings growth of ~25% CAGR expected over FY22-24E led by execution of existing strong order book primarily comprising manufacturing various types of indigenous missiles & torpedoes
- BUY with a target price of ₹ 1010/share



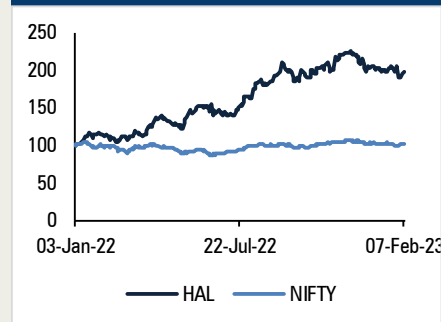
Particulars

Particular	Amount
Market Capitalisation (₹ Crore)	81,090
Total Debt (FY22 - ₹ Crore)	-
Cash (FY22 - ₹ Crore)	14,356
EV (₹ Crore)	66,734
52 Week H/L (Rs)	2813 / 1249
Equity Capital	334
Face Value	10

Shareholding pattern

	Mar-22	Jun-22	Sep-22	Dec-22
Promoter	75.2	75.2	75.2	75.2
FII	4.4	5.6	6.9	7.1
DII	17.0	15.7	13.5	12.7
Others	3.5	3.6	4.5	5.0

Price Chart



Key risks

- Government contract dependence
- Dependence on foreign OEMs for key components

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Key Financial Summary

(₹ crore)	FY20	FY21	FY22	3 Year CAGR (FY19-22)	FY23E	FY24E	FY25E	3 Year CAGR (FY22-24E)
Revenues	21,438	22,882	24,620	5.3	26,158	28,355	33,034	10.3
EBITDA	4,896	5,336	5,409	4.5	6,406	6,983	8,173	14.8
EBITDA margin (%)	22.8	23.3	22.0		24.5	24.6	24.7	
Profit Before Tax	3,969	4,283	5,225	8.8	6,389	6,349	7,319	11.9
EPS (₹)	85.9	97.1	151.9		150.9	143.9	165.3	
P/E (x)	29.1	25.0	16.0		16.1	16.8	14.7	
EV/EBITDA (x)	17.7	13.9	12.3		10.4	9.4	8.0	
RoCE (%)	21.9	29.4	27.4		32.2	29.1	30.1	
RoE (%)	21.0	21.0	26.3		25.4	22.1	22.7	

Q3FY23 Result – Key Highlights

- Revenue for the quarter came in at ₹ 5665.5 crore (down 3.8% YoY); lower than our estimate of ₹ 6032.1 crore. The de-growth during the quarter was likely on account of muted execution in manufacturing contracts (which account for 75% of the total order book) as a large part of this order book is yet to see meaningful execution. Sequentially, revenue increased 42%. For 9MFY23, revenue was up 10.5% YoY, mainly on account of substantial growth seen during Q1FY23
- Gross margin was at 56.1% (vs. our estimate of 51%); improved from 49.6% in Q3FY22. This was mainly on account of lower raw material cost, which declined 16.2% YoY
- EBITDA margins came in at 17.4% (vs. estimate of 24.3%); down 682 bps YoY despite an improvement in gross margins. This was mainly on account of a significant increase in others cost (up 149.5% YoY). The provisions amount in others cost was at ₹ 808.5 crore, up 129% YoY. The 9MFY23 EBITDA margin was at 23.8% against 22.3% for 9MFY22
- EBITDA declined 30.9% YoY (down 39.2% QoQ) to ₹ 985.4 crore (I-direct estimate of ₹ 1465.4 crore). The 9MFY23 EBITDA was up 18% YoY at ₹ 3433.4 crore
- Reported PAT of ₹ 1155.2 crore was up 23.8% YoY. However, it includes a refund of ₹ 427.4 crore related to favourable orders in income tax (it includes ₹ 176.9 crore in other income and ₹ 250.5 crore of tax refunds). Adjusting for this refund, net profit for the quarter was at ₹ 727.7 crore
- Order backlog was at ₹ 84000 crore (3.2x TTM revenues). Implied order inflows during 9MFY23 were at ₹ 16278 crore

Exhibit 1: Variance Analysis

	Q3FY23	Q3FY23E	Q3FY22	YoY (%)	Q2FY23	QoQ (%)	Comments
Operating Income	5,665.5	6,032.1	5,891.9	-3.8	5,144.8	10.1	Revenue declined YoY on higher base and muted growth in manufacturing contracts
Other income	497.2	160.0	196.8	152.7	259.1	91.9	
Total Revenue	6,162.7	6,192.1	6,088.7	1.2	5,403.9	14.0	
Raw materials costs	2,489.7	2,955.7	2,972.1	-16.2	1,841.0	35.2	
Employees Expenses	1,132.8	1,144.7	1,069.3	5.9	1,144.7	-1.0	
Other Expenses	1,057.6	466.3	423.9	149.5	537	96.8	
Total Expenditure	4,680.1	4,566.7	4,465.3	4.8	3,523	32.8	
EBITDA	985.4	1,465.4	1,426.6	-30.9	1,621.6	-39.2	
EBITDA margins (%)	17.4	24.3	24.2	-682 bps	31.5	-1413 bps	Higher provision expenses impacted EBITDA margin
Interest	2.1	0.4	0.8		0.4		
Depreciation	268.9	375.0	373.5	-28.0	252.0	6.7	
Tax	57.8	312.5	313.8	-81.6	409.4	-85.9	
PAT	1,155.2	937.5	933.4	23.8	1,221.2	-5.4	

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

₹ Crore)	FY23E			FY24E			FY25E		
	Old	New	% Change	Old	New	% Change	Old	New	% Change
Revenue	26,227	26,158	-0.3	28,355	28,355	0.0	33,034	33,034	0.0
EBITDA	6,425	6,406	-0.3	6,983	6,983	0.0	8,173	8,173	0.0
EBITDA Margin (%)	24.5	24.5	-1 bps	24.6	24.6	0 bps	24.7	24.7	0 bps
PAT	4,439	5,048	13.7	4,813	4,813	0.0	5,526	5,526	0.0
EPS (₹)	132.7	150.9	13.7	143.9	143.9	0.0	165	165.3	0.0

Source: ICICI Direct Research

Financial Summary

Exhibit 3: Profit and loss statement ₹ crore

(₹ Crore)	FY22	FY23E	FY24E	FY25E
Revenue	24,620	26,158	28,355	33,034
% Growth	7.6	6.2	8.4	16.5
Other income	984.9	1,200.0	700.0	700.0
Total Revenue	25,613	27,364	29,064	33,751
% Growth	10.2	6.8	6.2	16.1
Total Raw Material Costs	10,001	10,594	13,469	15,698
Employee Expenses	4,604	4,708	4,962	5,781
other expenses	4,606	4,450	2,941	3,382
Total Operating Expenditure	19,211	19,752	21,372	24,861
Operating Profit (EBITDA)	5,409	6,406	6,983	8,173
% Growth	1.4	18.4	9.0	17.0
Interest	58	3	1	1
PBDT	6,335	7,602	7,682	8,872
Depreciation	1,111	1,229	1,333	1,553
PBT before Exceptional Items	5,225	6,373	6,349	7,319
Total Tax	145	1,342	1,537	1,793
PAT before MI	5,080	5,048	4,813	5,526
PAT	5,080	5,048	4,813	5,526
% Growth	56.5	(0.6)	(4.7)	14.8
EPS	151.9	150.9	143.9	165.3

Source: Company, ICICI Direct Research Note: FY23E EPS is factoring in tax refunds of ₹ 427 crore received by the company in Q3FY23

Exhibit 4: Cash flow statement ₹ crore

(₹ Crore)	FY22	FY23E	FY24E	FY25E
Profit after Tax	5,080	5,048	4,813	5,526
Depreciation	1,111	1,229	1,333	1,553
Interest	58	3	1	1
Cash Flow before WC change	6,249	6,280	6,147	7,080
Changes in inventory	2,326	(1,061)	(1,294)	(4,114)
Changes in debtors	1,027	(375)	(421)	(1,350)
Changes in loans & Advances	(0)	-	-	-
Changes in other current asse	(1,413)	(68)	42	(468)
Net Increase in Current Asset	2,562	(2,702)	(3,021)	(7,482)
Changes in creditors	302	166	229	668
Changes in provisions	1,121	(564)	377	1,102
Net Inc in Current Liabilities	(382)	1,850	2,035	4,812
Net CF from Operating activiti	8,429	5,427	5,160	4,410
Changes in deferred tax asset	(513)	-	-	-
(Purchase)/Sale of Fixed Assε	(1,118)	(1,200)	(1,200)	(1,200)
Net CF from Investing activitie	123	(969)	(1,237)	(1,278)
Dividend and Dividend Tax	(1,338)	(1,471)	(1,605)	(1,839)
Net CF from Financing Activiti	(1,375)	(4,615)	(2,802)	(3,036)
Net Cash flow	7,178	(156)	1,122	97
Opening Cash/Cash Equivalen	7,178	14,356	14,200	15,322
Closing Cash/ Cash Equivalen	14,356	14,200	15,322	15,419

Source: Company, ICICI Direct Research

Exhibit 5: Balance Sheet ₹ crore

(₹ Crore)	FY22	FY23E	FY24E	FY25E
Equity Capital	334.4	334.4	334.4	334.4
Reserve and Surplus	18,979	19,453	21,465	23,957
Total Shareholders funds	19,313	19,787	21,799	24,291
Other Non Current Liabilities	12,262.4	12,500.0	12,500.0	12,500.0
Total Debt	-	-	-	-
Total Liabilities	33,369	34,106	36,118	38,610
Gross Block	10,628	11,827	13,027	14,227
Acc: Depreciation	4,700	5,930	7,262	8,815
Net Block	5,928	5,897	5,765	5,412
Capital WIP	949	950	950	950
Total Fixed Assets	9,239	9,247	9,115	8,762
Non Current Assets	2,797	2,828	2,864	2,942
Inventory	14,347	15,408	16,702	20,816
Debtors	4,642	5,017	5,438	6,788
Loans and Advances	8	8	8	8
Other Current Assets	2,809	2,877	2,836	3,303
Cash	14,356	14,200	15,322	15,419
Total Current Assets	44,994	47,541	51,683	59,261
Current Liabilities	2,558	2,723	2,952	3,620
Provisions	1,263	1,265	1,265	1,265
Total Current Liabilities	25,023	26,872	28,907	33,719
Net Current Assets	19,971	20,668	22,777	25,543
Total Assets	33,369	34,106	36,118	38,610

Source: Company, ICICI Direct Research

Exhibit 6: Key ratios

(Year-end March)	FY22	FY23E	FY24E	FY25E
EPS	151.9	150.9	143.9	165.3
Cash per Share	429.3	424.7	458.2	461.1
BV	577.6	591.7	651.9	726.4
Dividend per share	40.0	44.0	48.0	55.0
Dividend payout ratio	26%	29%	33%	33%
EBITDA Margin	22.0	24.5	24.6	24.7
PAT Margin	20.6	19.3	17.0	16.7
RoE	26.3	25.4	22.1	22.7
RoCE	27.4	32.2	29.1	30.1
RoIC	86.7	92.6	87.2	74.6
EV / EBITDA	12.3	10.4	9.4	8.0
P/E	16.0	16.1	16.8	14.7
EV / Net Sales	2.7	2.6	2.3	2.0
Sales / Equity	1.3	1.3	1.3	1.4
Market Cap / Sales	3.3	3.1	2.9	2.5
Price to Book Value	4.2	4.1	3.7	3.3
Asset turnover	1.3	1.3	1.3	1.4
Debtors Turnover Ratio	4.8	5.4	5.4	5.4
Creditors Turnover Ratio	10.2	9.9	10.0	10.1
Debt / Equity	-	-	-	-
Current Ratio	2.1	2.4	2.4	2.5
Quick Ratio	0.7	0.8	0.8	0.8

Source: Company, ICICI Direct Research Note: FY23E EPS is factoring in tax refunds of ₹ 427 crore received by the company in Q3FY23

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