

Pick-up in execution to drive growth...

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 7.9%, 10.9% and 19%, respectively, in FY20-23. In FY23, repair & overhaul contributed ~70% to total revenues while manufacturing contributed ~18%

Q4FY23 Result: EBITDA margin improves on better contract mix.

- Revenue increased 8.1% YoY to ₹ 12494.7 crore. Sequentially, revenue increased 120.5% as Q4 remains better in terms of execution
- The EBITDA margin improved 435 bps YoY to 26.0% on better contract mix; leading to EBITDA growth of 29.8% YoY to ₹ 3245.8 crore
- PAT declined 8.8% YoY to ₹ 2831.2 crore due to higher depreciation

What should investors do? We expect HAL to deliver revenue and EBITDA CAGR of 10.8% and 10%, respectively, over FY23-25E. PAT is likely to grow at 6.5% CAGR (FY23-25E). 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 ₹ 3610 i.e. 22x PE on FY25E EPS.

Key triggers for future price performance:

- Healthy order-book position (~₹ 82000 crore; 3x FY23 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 will 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 ~24% CAGR expected over FY22-25E led by execution of existing strong order-book primarily comprising manufacturing various types of indigenous missiles & torpedoes
- BUY with a target price of ₹ 1215/share



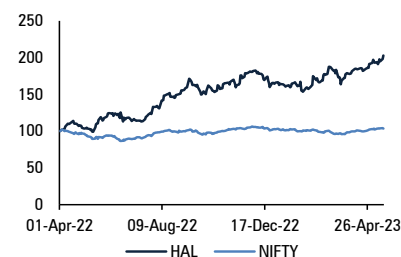
Particulars

Particular	Amount
Market Capitalisation (₹ Crore)	1,03,561
Total Debt (FY23 - ₹ Crore)	-
Cash (FY23 - ₹ Crore)	20,317
EV (₹ Crore)	83,244
52 Week H/L (Rs)	3168 / 1629
Equity Capital	334
Face Value	10

Shareholding pattern

	Jun-22	Sep-22	Dec-22	Mar-23
Promoter	75.2	75.2	75.2	71.7
FII	5.6	6.9	7.1	9.1
DII	15.7	13.5	12.7	13.9
Others	3.6	4.5	5.0	5.3

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	FY23	3 Year CAGR (FY19-23)	FY24E	FY25E	3 Year CAGR (FY23-25E)
Revenues	21,438	22,882	24,620	26,927	7.9	28,905	33,041	10.8
EBITDA	4,896	5,336	5,409	6,679	10.9	6,935	8,078	10.0
EBITDA margin (%)	22.8	23.3	22.0	24.8		24.0	24.4	
Adjusted PAT*	2,873	3,246	3,887	4,838	19.0	4,757	5,483	6.5
EPS (₹)	85.9	97.1	151.9	174.3		142.2	164.0	
P/E (x)	37.2	32.0	20.4	17.8		21.8	18.9	
EV/EBITDA (x)	22.3	18.1	16.5	12.5		12.2	10.1	
RoCE (%)	21.9	29.4	27.4	27.8		27.6	28.6	
RoE (%)	21.0	21.0	26.3	24.7		20.9	21.6	

Q4FY23 & FY23 Result – Key Highlights

- Revenue for the quarter came in at ₹ 12494.7 crore (up 8.1% YoY); a little better than our estimate of ₹ 12067.0 crore. Sequentially, revenue increased 120.5% as execution remains better in Q4. The revenue for FY23 came in at ₹ 26927.5 crore (up 9.4% YoY), largely in line with the provisional revenue of ₹ 26500 crore reported by the company. The growth remains in single digits for this year as a large part of the order book is yet to see meaningful execution
- Gross margin was at 61.9% (vs. our estimate of 56%); improved from 59.9% in Q4FY22. This was mainly on account of lower raw material cost, which increased just 2.6% YoY. FY23 gross margin was at 62.5% vs. 59.4% in FY22
- EBITDA margins came in at 26.0% (vs. estimate of 25%); improving 435 bps YoY. This was mainly on account of a decline in others cost (down 4.8% YoY). FY23 EBITDA margin was at 24.8% (up 284 bps YoY). Thus, on account of better margins, EBITDA grew 29.8% YoY (up 229.4% QoQ) to ₹ 3245.8 crore (better than our estimate of ₹ 3020.1 crore). FY23 EBITDA is up 23.5% YoY at ₹ 6679.2 crore
- Reported PAT of ₹ 2831.2 crore (vs. our estimate of ₹ 2934.1 crore) was down 8.8% YoY; mainly on account of higher depreciation (+176% YoY). The company has mentioned that development expenditure of ₹ 585.2 crore (for HT-40 aircraft) has been amortised against the revenue recognised during the period. However, there was a tax refund to the tune of ₹ 722.9 crore during the quarter related to earlier years. FY23 PAT was at ₹ 5827.7 crore (up 14.7% YoY)

Earnings call highlights

- Order backlog was at ₹ 81785 crore as of FY23 end. Order inflows were at ₹ 25990 crore during the year, which includes manufacturing contracts for 70 HTT -40, six Do-228 Aircraft & PSLV launch vehicles and repair & overhaul (RoH) contracts of ~₹ 16,600 crore
- Key orders in the pipeline for the next six to 10 months, which are in advanced stages include 25 advanced light helicopters (ALH) Dhruva, 12 light utility helicopters (LUH), 12 Sukhoi-30 MKI, 240 AL-31 engines for Sukhoi-30 MKI aircraft and 80 engines for Mig-29 aircraft. Total estimated cost of these orders is at ~₹ 48000 crore
- There are a few more orders (where acceptance of necessity has already been accorded and RFPs are likely to floated in the next two years) are nine ALHs for Indian Coast Guard and 60 Utility Helicopter Marine (UHM). Total cost of these are expected at ₹ 36000 crore
- In the longer term (three to five years), key orders in the pipeline are 145 LCH, 175 LUH, 36 HTT-40, 60 Dornier upgrades (for IAF and Navy). Total cost of these orders is expected at ₹ 65000 crore
- Repair & overhaul (RoH) inflow is expected at ₹ 17000-18000 per annum
- Revenue guidance for FY24E was maintained at 8-9%. For FY25, revenue growth is expected to be in double digits mainly led by execution of LCA Tejas MK1A. From FY26 onwards, revenue growth is likely to stabilise at 12-13%
- EBITDA margin (including other income) is expected at 26-27% in the coming periods
- The company has delivered these projects in FY23: seven ALH, two LCA, six AL-31 engines, eight LCH and two Dornier
- Tejas LCA MK1A deliveries will start from February 2024. Three LCA are expected to be delivered in FY24 and 16 per annum from FY25 onwards.

The company is also in process of ramping up production capacity of these aircraft post which production can be increased further from 16

- On the exports front, the company is in talks with a few countries where it has submitted the proposals for the platforms like LCA, ALH, LCH and LUH. These countries include Philippines, Argentina, Sri Lanka, Egypt, Maldives, Thailand and Nigeria. Out of these countries, talks are in advanced stages with Philippines and Argentina. If the deal gets closed with any of these countries, initial order size can be US\$150 mn

Exhibit 1: Variance Analysis

	Q4FY23	Q4FY23E	Q4FY22	YoY (%)	Q3FY23	QoQ (%)	Comments
Operating Income	12,494.7	12,067.0	11,561.1	8.1	5,665.5	120.5	Muted growth in manufacturing contracts but better execution in repair & overhaul contracts
Other income	722.2	520.1	500.7	44.3	497.2	45.3	
Total Revenue	13,216.9	12,587.1	12,061.8	9.6	6,162.7	114.5	
Raw materials costs	4,756.1	5,280.4	4,637.3	2.6	2,489.7	91.0	
Employees Expenses	1,615.0	1,474.6	1,402.7	15.1	1,132.8	42.6	
Other Expenses	2,877.7	2,291.9	3,021.4	-4.8	1,058	172.1	
Total Expenditure	9,248.9	9,046.9	9,061.3	2.1	4,680	97.6	
EBITDA	3,245.8	3,020.1	2,499.8	29.8	985.4	229.4	
EBITDA margins (%)	26.0	25.0	21.6	435 bps	17.4	858 bps	Increase in share of repair & overhaul led to improvement in margins
Interest	55.3	2.1	42.1		2.1		
Depreciation	1,055.6	410.4	382.5	176.0	268.9	292.6	
Tax	12.5	193.5	-528.1	-102.4	57.8	-78.4	
PAT	2,831.2	2,934.1	3,105.1	-8.8	1,155.2	145.1	

Source: Company, ICICI Direct Research

Exhibit 2: Change in Estimates

(₹ Crore)	FY24E			FY25E		
	Old	New	% Change	Old	New	% Change
Revenue	28,356	28,905	1.9	33,035	33,041	0.0
EBITDA	6,983	6,935	-0.7	8,173	8,078	-1.2
EBITDA Margin (%)	24.6	24.0	-64 bps	24.7	24.4	-29 bps
PAT	4,813	4,757	-1.2	5,526	5,483	-0.8
EPS (₹)	143.9	142.2	-1.2	165.3	164.0	-0.8

Source: ICICI Direct Research, Company

Financial Summary

Exhibit 3: Profit and loss statement				
	₹ crore			
(₹ Crore)	FY22	FY23	FY24E	FY25E
Net Sales	24,620	26,927	28,905	33,041
Other operating income	-	-	-	-
Revenue	24,620	26,927	28,905	33,041
% Growth	7.6	9.4	7.3	14.3
Other income	984.9	1,670.1	1,250.0	1,300.0
Total Revenue	25,613	28,607	30,162	34,355
% Growth	10.2	11.7	5.4	13.9
Total Raw Material Costs	10,001	10,102	13,730	15,701
Employee Expenses	4,604	4,910	5,261	5,716
other expenses	4,606	5,236	2,979	3,546
Total Operating Expenditure	19,211	20,248	21,970	24,963
Operating Profit (EBITDA)	5,409	6,679	6,935	8,078
% Growth	1.4	23.5	3.8	16.5
Interest	58	58	2	2
PBDT	6,335	8,291	8,183	9,376
Depreciation	1,111	1,785	1,908	2,115
PBT before Exceptional Items	5,225	6,507	6,275	7,262
Total Tax	145	682	1,519	1,779
PAT before MI	5,080	5,828	4,757	5,483
Minority Interest	-	-	-	-
PAT	5,080	5,828	4,757	5,483
% Growth	56.5	14.7	(18.4)	15.3
EPS	151.9	174.3	142.2	164.0

Source: Company, ICICI Direct Research

Exhibit 4: Cash flow statement				
	₹ crore			
(₹ Crore)	FY22	FY23	FY24E	FY25E
Profit after Tax	5,080	5,828	4,757	5,483
Depreciation	1,111	1,785	1,908	2,115
Interest	58	58	2	2
Cash Flow before WC change	6,249	7,670	6,666	7,599
Changes in inventory	2,326	2,199	(2,502)	(2,549)
Changes in debtors	1,027	(78)	(824)	(793)
Changes in loans & Advances	(0)	0	-	-
Changes in other current asse	(1,413)	(1,380)	(436)	(662)
Net Increase in Current Asset	2,562	(922)	(5,099)	(5,623)
Changes in creditors	302	577	270	487
Changes in provisions	1,121	1,721	1,054	1,121
Net Inc in Current Liabilities	(382)	5,805	2,731	4,462
Net CF from Operating activiti	8,429	12,553	4,298	6,439
Changes in deferred tax asset	(513)	(560)	-	-
(Purchase)/Sale of Fixed Asse	(1,118)	(1,440)	(1,200)	(1,200)
Net CF from Investing activiti	123	(5,131)	366	(1,263)
Dividend and Dividend Tax	(1,338)	(1,338)	(1,505)	(1,672)
Net CF from Financing Activiti	(1,375)	(1,460)	(5,681)	(2,869)
Net Cash flow	7,178	5,961	(1,017)	2,306
Opening Cash/Cash Equivalen	7,178	14,356	20,317	19,300
Closing Cash/ Cash Equivalen	14,356	20,317	19,300	21,606

Source: Company, ICICI Direct Research

Exhibit 5: Balance Sheet				
	₹ crore			
(₹ Crore)	FY22	FY23	FY24E	FY25E
Equity Capital	334.4	334.4	334.4	334.4
Reserve and Surplus	18,979	23,238	22,423	25,038
Total Shareholders funds	19,313	23,572	22,758	25,373
Other Non Current Liabilities	12,262.4	10,926.0	12,500.0	12,500.0
Total Debt	-	-	-	-
Total Liabilities	33,369	36,377	37,158	39,774
Gross Block	10,628	12,284	13,170	14,370
Acc: Depreciation	4,700	6,485	8,393	10,507
Net Block	5,928	5,799	4,778	3,863
Capital WIP	949	637	950	950
Total Fixed Assets	9,239	8,728	8,128	7,213
Non Current Assets	2,797	5,141	5,172	5,235
Inventory	14,347	12,149	14,650	17,200
Debtors	4,642	4,719	5,543	6,337
Loans and Advances	8	8	8	8
Other Current Assets	2,809	4,189	4,625	5,287
Cash	14,356	20,317	19,300	21,606
Total Current Assets	44,994	51,877	55,959	63,888
Current Liabilities	2,558	3,135	3,405	3,893
Provisions	1,263	1,347	1,347	1,265
Total Current Liabilities	25,023	30,827	33,558	38,021
Net Current Assets	19,971	21,050	22,401	25,867
Total Assets	33,369	36,377	37,158	39,774

Source: Company, ICICI Direct Research

Exhibit 6: Key ratios				
(Year-end March)	FY22	FY23	FY24E	FY25E
EPS	151.9	174.3	142.2	164.0
Cash per Share	429.3	607.6	577.2	646.1
BV	577.6	704.9	680.6	758.8
Dividend per share	40.0	40.0	45.0	50.0
Dividend payout ratio	26%	23%	32%	30%
EBITDA Margin	22.0	24.8	24.0	24.4
PAT Margin	20.6	21.6	16.5	16.6
RoE	26.3	24.7	20.9	21.6
RoCE	27.4	27.8	27.6	28.6
RoIC	86.7	150.3	145.4	158.3
EV / EBITDA	16.5	12.5	12.2	10.1
P/E	20.4	17.8	21.8	18.9
EV / Net Sales	3.6	3.1	2.9	2.5
Sales / Equity	1.3	1.1	1.3	1.3
Market Cap / Sales	4.2	3.8	3.6	3.1
Price to Book Value	5.4	4.4	4.6	4.1
Asset turnover	1.3	1.1	1.3	1.3
Debtors Turnover Ratio	4.8	5.8	5.6	5.6
Creditors Turnover Ratio	10.2	9.5	8.8	9.1
Debt / Equity	-	-	-	-
Current Ratio	2.1	1.7	1.8	1.9
Quick Ratio	0.7	0.7	0.7	0.8

Source: Company, ICICI Direct Research

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