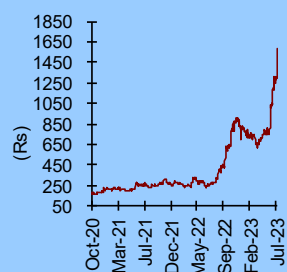


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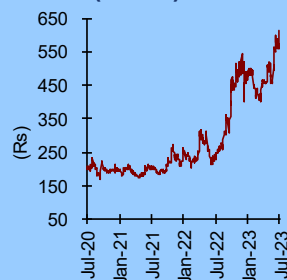
Sector update

Defence

MDSL (SELL)



GRSE (SELL)



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Defence

Rumble of the sea: Potential submarine orders in focus

We have recently seen considerable interest in shipbuilders, particularly Mazagon Dock Shipbuilders (MDSL), as the bidding for P75I project comes closer and the possibility of the order for three additional Scorpene submarines being finalised during PM Modi's visit to France for the Bastille day parade. In our view, the traction around submarine orders worth close to US\$8.6bn is a positive development for MDSL – the only Indian shipbuilder involved in the integration of submarines. The last submarine INS Vagsheer of P75I project is undergoing sea trials and is likely to be delivered in FY24E. Hence, the potential fresh orders come as a shot in the arm for MDSL.

However, the emergence of Spain's Navantia and L&T and Hanwah Ocean as potential bidders for P75I project implies competition to MDSL-ThyssenKrupp Marine Systems (TKMS). Besides, the actual benefits might accrue progressively given these are high-value orders and ordering and execution cycle is prolonged, extending up to 8 years. We will keep a close tab on the developments on this front. Even after factoring in the potential order inflow of Rs450bn on account of submarine orders and Rs100bn on account of MRLC of a submarine, our TP for MDSL works out to Rs600 (DCF based). We maintain SELL rating on the stock.

- **Possible submarine orders on the anvil:** Close on the heels of execution of MoU between MDSL and TKMS to jointly bid for US\$5.6bn P75I project, Hanwah Ocean has expressed keen interest in participating in the project. In another development, L&T has signed an MoU with Spanish shipyard Navantia to jointly bid for the project. Navantia will be offering S80- class submarines and will be competing against TKMS offering of U-214 and Hanwah Ocean's KSS-III submarines. It is noteworthy that Navantia has claimed that its Air Independent Propulsion (AIP) system based on a bioethanol reformer that generates hydrogen to power a fuel cell surpasses the fuel cell-based API system developed by DRDO in terms of performance and stealth capabilities ([Link](#)). Additionally, in order to address the immediate need for underwater vessels, France, through its partner MDSL, has proposed the construction of three additional Scorpene submarines. The proposal is especially important since the P75I programme faces delays. Hence, overall, the ordering of 9 submarines is on anvil, subject to budgetary constraints.
- **Why three extra Scorpene submarines are required at this stage?** Under 1999 plan, Indian Navy was supposed to have 24 ne submarines in service or under construction by CY24, comprising six each under Project 75 (the Kalvari-class), P75I, P76 and P75A (nuclear submarines, nearing the end of development now). However, currently the Indian Navy has just 5 submarines in service while the last one (under P75) has commenced sea trials. The Navy has taken steps like considering refitting 3 out of 4 (Type 209-1500) with AIP and more refits on Simdhughosh-class to keep them longer in operations. However, even with these steps, all of these can last until late 2030s. By that time, the Navy would be having only 12 submarines (under P75 and P75I) resulting in serious gap. Hence, these three extra submarines (Scorpene class) are likely to alleviate some stress, giving enough window to complete Project 75A and Project 76.

- **What it means for MDSL?** Despite the recent euphoria around the MDSL stock as it is likely a major beneficiary of the potential submarine orders, we would keep tab on: 1) Competitive landscape (particularly for P75I); and 2) budgetary constraints as the expected capital outlay on the 9 submarines is almost 45% of the total capital outlay in defence budget for FY24. That said, we note MDSL has the necessary trained manpower including engineers and technicians to undertake the production of one or two additional submarines. Besides, submarines have a long gestation period (almost 8 years), hence, the benefits are evenly spread out. We would wait for more clarity on the bidding process of P75I as well as the actual number of submarines that MDSL might finally get to build. We maintain SELL on MDSL stock with an unchanged DCF-based TP of Rs600.

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