SELL (Maintained)

CMP: **INR 727** Target Price: **INR 500** ▼ -31%

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15 March 2024

India | Equity Research | Q3FY24 concall update

Garden Reach Shipbuilders

Defence

Possibilities aplenty, but priced in

We attended the analyst meet of Garden Reach Shipbuilders (GRSE) to discuss its Q3FY24 results. Key points: 1) Order book stood at INR 236bn, as on end-Dec'23. 2) Revenue growth likely at 25% p.a. over next three years, as P-17A frigates enter peak execution period. 3) Management remains optimistic of securing next-gen corvettes and P-17B frigate orders. 4) Steady margins despite upcoming contracts being competitive in nature. In our view, revenue growth post FY27 shall be contingent on timely award, and GRSE's share in next-gen Corvettes (INR 364bn opportunity) and P-17B frigates (INR 700bn opportunity). Even in a blue sky scenario, we see EPS constrained in the range of INR 60-70/share. Maintain SELL with an unchanged TP of INR 500 (DCF-based methodology).

Order book depletion makes timing of next contracts critical

GRSE's order book as on end-Dec'23 stands at INR 236bn, comprising: 1) P-17A frigates at INR 127bn. 2) Survey Vessel Large (SVL) at INR 10.5bn. 3) Antisubmarine Warfare Shallow Water Crafts (ASWSWC) at INR 50bn. 4) Next-gen Ocean Patrol Vehicles (NGOPV) at INR 33.8bn. Management expects the current order book to deplete by FY28 and peak out in FY26. Management is also optimistic on securing a sizeable chunk of potential orders of Next-gen Corvettes (NGC) and P-17B frigates. The company has experience in building such corvettes and frigates along with facilities and infrastructure in place; it expects orders of NGC and P-17B frigates to be awarded by end-2026 and end-2027, respectively. However, we believe that timely ordering and GRSE's share in them remains critical. Even in a best case scenario, wherein GRSE secures five NGCs and four P-17B frigates, EPS is likely to be constrained between INR 60-70/share through to FY32E.

Various growth vectors in sight

Management mentioned that they are focusing on various revenue streams to maintain growth. These include: 1) Ship repair – revenue potential at INR 0.85-1bn p.a. by end-CY25. 2) Autonomous platforms – currently under development with DRDO. 3) Commercial ship building – discussions underway with various European countries. 4) Naval guns – order worth INR 2.1bn already in place. 5) Potential from co-development of engine with Roll Royce.

Financial Summary

Y/E March (INR mn)	FY23A	FY24E	FY25E	FY26E
Net Revenue	25,611	39,748	50,141	60,884
EBITDA	1,490	2,274	2,834	3,555
EBITDA Margin (%)	0.1	0.1	0.1	0.1
Net Profit	2,281	3,561	4,313	5,432
EPS (INR)	19.9	31.1	37.7	47.4
EPS % Chg YoY	0.2	0.6	0.2	0.3
P/E (x)	36.5	23.4	19.3	15.3
EV/EBITDA (x)	25.0	14.0	1.9	3.1
RoCE (%)	0.1	0.1	0.1	0.1
RoE (%)	0.2	0.2	0.3	0.3

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Market Data

Market Cap (INR)	83bn
Market Cap (USD)	1,005mn
Bloomberg Code	GRSE IN
Reuters Code	GRSE BO
52-week Range (INR)	975 /398
Free Float (%)	26.0
ADTV-3M (mn) (USD)	10.5

Price Performance (%)	3m	6m	12m
Absolute	(12.8)	(8.3)	78.3
Relative to Sensex	(16.5)	(16.6)	52.1

Previous Reports

14-02-2024: Q3FY24 results review
21-11-2023: Q2FY24 results review

Outlook: Ordering uncertainty mars prospects

We believe that GRSE has got significant growth prospects with potential orders for NGC and P-17B frigates in the near future. However, the timing and extent of involvement of GRSE in these contracts remains critical. While management is focusing on several growth vectors at the moment – exports, commercial ship building and other equipment such as naval guns – we believe that such initiatives are still nascent. Factoring in the best possible outcome for GRSE in NGC and P-17B frigate orders and other potential orders flowing in in time, we find EPS constrained between INR 60-70/share. Besides, the potential orders are expected to be on competitive bidding; hence, margins are expected to stay under pressure – though we are factoring in steady margin of 6-7%.

Maintain **SELL** with an unchanged TP of INR 500 (DCF-based methodology). Our TP implies a P/E ratio of 10.5x on FY26E EPS, which is fair given the considerable uncertainties around future orders and current order book peaking out in FY26E.

Key risks

- Repeat order of Frigates
- Earlier than expected ordering of Corvettes and Destroyers
- Higher than expected order quantum of Corvettes and Destroyers

Q3FY24 analyst meet: Highlights

- GRSE aims to maintain its order book position at current level of INR 236bn.
- It is targeting revenue growth of 25% p.a. for next three years.
- **Delivery planned in FY25:** In Q1FY25, one SVL, one ASWSWC and ferry for WB government be delivered. In Q3FY25, one SVL will be delivered and in Q4FY25, one ASWSWC will be delivered.
- **Order book position:** As on Dec'23-end, INR 235.92bn. (P-17A: INR 127bn; ASW: INR 50bn; SVL: INR 10.50bn; NGOPV: INR 33.88bn and others). The current order book will be completed by FY28.
- The company is executing four projects for the Indian Navy (IN), which include: 1) three ships under-17A. 2) Four SVL; 3) Four Anti-Submarine Warfare Shallow Water Craft (ASW-SWC). 4) NGOPV.
- **Project delivery in FY24:** In FY24, GRSE has delivered one ship of large survey vessel in last quarter (got commissioned in Feb'24) and has also delivered passenger cum cargo vessel for the government of Guyana in Apr'23.
- **Physical progress**
    - **P-17A:** First ship achieved 66% completion, two ships achieved 55% completion, three ships achieved 43% completion. GRSE plans to deliver first ship by mid-2025 (Aug'25), second ship in Feb'26 and third ship in Aug'26.
    - **SVL:** Second ship is expected to delivered by May/Jun'24, third ship in Dec'24 and fourth ship in early FY26.
    - **ASW-SWC:** Fifth and sixth ship launched on 13 Mar'24 and of four ships launched earlier; first ship is expected to be delivered by Jun'24 and next ship in every six months, by mid-26 this project will be delivered. First ship achieved

77%, second ship 62%, third ship 62% and fourth ship has achieved at 20% physical progress.

- **NGOPV:** The contract for four ships was signed in Mar'23. Started production of all four ships and achieved ~10% of physical progress. Delivery is expected to start from 2026; one ship in every six months and will complete in 2028.
- **Govt. of West Bengal:** Vessels are expected to be delivered by Apr'24.

- **Ordering in near term**
  - GRSE is L-1 in oceanography research vessel; INR 8.4bn order value, contract expected in Mar'24.
  - GRSE is L-1 in autonomous platform order for MoD: Order value INR 200mn (technology demonstration).
  - GRSE has been declared as L-1 in Govt. of Bangladesh project. Contract is expected to be signed in next three months.
  - Some commercial shipbuilding orders from Germany and Netherlands (contract is expected to be concluded in next three months).
  - GRSE is primary focused on warship building.
- **What is in store (near term opportunities)**
  - IN: Next-gen corvettes; RFP is expected by Jun/Jul'24 (AoN value: INR 360bn for eight ships). To be divided into two shipbuilders and L-1 to get five ships and L-2 to get three ships.
  - Next gen survey vessel: Five vessels (INR 30bn); RFP expected in Q2FY25.
  - Two multipurpose vessel for IN: Order value expected at ~INR 12bn.
  - Five more ocean going patrol vessels; RFP expected in Q1FY25.
  - P-17B project: Seven more vessels (expected order value INR 700bn); AoN has not come yet and is expected in early CY25.
  - Land Platform Dock (LPD): Expected order value INR 400bn (for 2 nos.); clarity on the project is yet to emerge.
- **Capacity expansion**: GRSE plans to increase its shipbuilding capacity from 20 warships currently, to 24 warships.
- **Capex:** It plans to incur INR 0.40-0.50bn capex annually over the next three years.
- **Portable bridges:** Market is modest and GRSE has 65% market share. GRSE has running MOU with BRO for 75 bridges and 40 have already been completed.

Exhibit 1: DCF Valuation

(INR mn)	FY22	FY23	FY24E	FY25E	FY26E	FY27E	FY28E	FY29E	FY30E	FY31E	FY32E
EBITDA	1,407	1,490	2,274	2,834	3,555	4,050	4,052	5,182	6,311	6,216	6,274
Tax	676	771	1,203	1,458	1,836	2,291	2,417	2,633	2,757	2,595	2,582
NOPAT	731	719	1,070	1,377	1,719	1,759	1,635	2,549	3,554	3,621	3,693
Working Capital Change	(117)	4,180	2,973	23,385	(9,495)	91,207	(5,359)	(22,851)	(27,292)	(17,179)	(2,184)
Capex	(548)	(423)	(600)	(600)	(600)	(600)	(600)	(600)	(600)	(600)	(600)
FCF	66	4,477	3,443	24,161	(8,375)	92,367	(4,324)	(20,903)	(24,338)	(14,158)	909
Terminal Value											13,179
Total FCF	66	4,477	3,443	24,161	(8,375)	92,367	(4,324)	(20,903)	(24,338)	(14,158)	14,088
Cost of Equity	11%										
WACC	10%										
Terminal Growth	3%										
NPV of FCFF (FY24E)	54,075										
Net Debt at FY23	(3,090)										
Net Equity value	57,165										
Value per share (INR)	**500**										

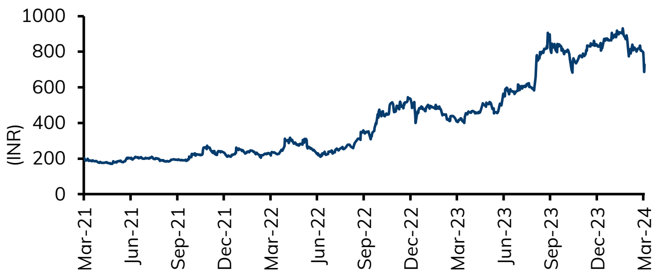
Source: I-Sec research

Exhibit 2: Shareholding pattern

%	Jun'23	Sep'23	Dec'23
Promoters	74.5	74.5	74.5
Institutional investors	10.6	9.3	8.9
MFs and others	6.6	5.3	5.3
FIs/Banks	0.0	0.7	0.7
Insurance	0.0	0.0	0.0
FIIs	4.0	3.3	2.9
Others	14.9	16.2	16.6

Source: Bloomberg

Exhibit 3: Price chart



Source: Bloomberg

Financial Summary

Exhibit 4: Profit & Loss

(INR mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
Net Sales	**25,611**	**39,748**	**50,141**	**60,884**
Operating Expenses	24,121	37,474	47,307	57,329
EBITDA	**1,490**	**2,274**	**2,834**	**3,555**
EBITDA Margin (%)	0.1	0.1	0.1	0.1
Depreciation & Amortization	392	384	376	369
EBIT	1,099	1,890	2,458	3,186
Interest expenditure	65	50	50	50
Other Non-operating Income	2,018	2,924	3,362	4,131
Recurring PBT	**3,052**	**4,764**	**5,771**	**7,267**
Profit / (Loss) from Associates	**-**	**-**	**-**	**-**
Less: Taxes	771	1,203	1,458	1,836
PAT	2,281	3,561	4,313	5,432
Less: Minority Interest	-	-	-	-
Extraordinaries (Net)	-	-	-	-
Net Income (Reported)	**2,281**	**3,561**	**4,313**	**5,432**
Net Income (Adjusted)	**2,281**	**3,561**	**4,313**	**5,432**

Source Company data, I-Sec research

Exhibit 5: Balance sheet

(INR mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
Total Current Assets	99,320	1,11,659	1,43,336	1,47,371
of which cash & cash eqv.	45,983	51,499	77,827	72,387
Total Current Liabilities & Provisions	93,845	1,03,641	1,32,375	1,32,354
Net Current Assets	**5,475**	**8,018**	**10,962**	**15,016**
Investments	-	-	-	-
Net Fixed Assets	5,076	5,292	5,516	5,747
ROU Assets	-	-	-	-
Capital Work-in-Progress	60	60	60	60
Total Intangible Assets	-	-	-	-
Other assets	3,672	3,672	3,672	3,672
Deferred Tax Assets	-	-	-	-
Total Assets	**14,283**	**17,042**	**20,210**	**24,496**
Liabilities				
Borrowings	**-**	**-**	**-**	**-**
Deferred Tax Liability	**145**	**145**	**145**	**145**
provisions	-	-	-	-
other Liabilities	-	-	-	-
Equity Share Capital	1,146	1,146	1,146	1,146
Reserves & Surplus	12,993	15,752	18,919	23,205
Total Net Worth	**14,138**	**16,897**	**20,065**	**24,351**
Minority Interest	-	-	-	-
Total Liabilities	**14,283**	**17,042**	**20,210**	**24,496**

Source Company data, I-Sec research

Exhibit 6: Quarterly trend

(INR mn, year ending March)

	Mar-23	Jun-23	Sep-23	Dec-23
Net Sales	6,012	7,559	8,979	9,231
% growth (YOY)	10.4	30.4	31.7	32.1
EBITDA	204	461	488	487
Margin %	3.4	6.1	5.4	5.3
Other Income	699	706	715	815
Extraordinaries	-	-	-	-
Adjusted Net Profit	525	768	809	884

Source Company data, I-Sec research

Exhibit 7: Cashflow statement

(INR mn, year ending March)

	FY23A	FY24E	FY25E	FY26E
Operating Cashflow	**14,502**	**4,043**	**24,761**	**(7,775)**
Working Capital Changes	13,621	2,973	23,385	(9,495)
Capital Commitments	(423)	(600)	(600)	(600)
Free Cashflow	**14,080**	**3,443**	**24,161**	**(8,375)**
Other investing cashflow	**(16,240)**	**2,924**	**3,362**	**4,131**
Cashflow from Investing Activities	(16,663)	2,324	2,762	3,531
Issue of Share Capital	-	-	-	-
Interest Cost	(53)	(50)	(50)	(50)
Inc (Dec) in Borrowings	3,000	-	-	-
Dividend paid	(727)	(802)	(1,146)	(1,146)
Others	-	-	-	-
Cash flow from Financing Activities	2,203	(852)	(1,196)	(1,196)
Chg. in Cash & Bank balance	**43**	**5,515**	**26,328**	**(5,440)**
Closing cash & balance	27,587	51,499	77,827	72,387

Source Company data, I-Sec research

Exhibit 8: Key ratios

(Year ending March)

	FY23A	FY24E	FY25E	FY26E
Per Share Data (INR)				
Reported EPS	19.9	31.1	37.7	47.4
Adjusted EPS (Diluted)	19.9	31.1	37.7	47.4
Cash EPS	23.3	34.4	40.9	50.6
Dividend per share (DPS)	5.8	7.0	10.0	10.0
Book Value per share (BV)	123.4	147.5	175.2	212.6
Dividend Payout (%)	29.1	22.5	26.6	21.1
Growth (%)				
Net Sales	0.5	0.6	0.3	0.2
EBITDA	0.1	0.5	0.2	0.3
EPS (INR)	0.2	0.6	0.2	0.3
Valuation Ratios (x)				
P/E	36.5	23.4	19.3	15.3
P/CEPS	31.2	21.1	17.8	14.4
P/BV	5.9	4.9	4.2	3.4
EV / EBITDA	25.0	14.0	1.9	3.1
Dividend Yield (%)	0.0	0.0	0.0	0.0
Operating Ratios				
Gross Profit Margins (%)	0.4	0.4	0.4	0.4
EBITDA Margins (%)	0.1	0.1	0.1	0.1
Effective Tax Rate (%)	0.3	0.3	0.3	0.3
Net Profit Margins (%)	0.1	0.1	0.1	0.1
Net Debt / Equity (x)	(3.3)	(3.0)	(3.9)	(3.0)
Net Debt / EBITDA (x)	(30.9)	(22.7)	(27.5)	(20.4)
Fixed Asset Turnover (x)	4.0	5.4	6.3	7.1
Inventory Turnover Days	585	472	387	364
Receivables Days	10	10	9	9
Payables Days	72	47	34	26
Profitability Ratios				
RoCE (%)	0.1	0.1	0.1	0.1
RoE (%)	0.2	0.2	0.3	0.3
RoIC (%)	0.0	(0.1)	0.0	(0.1)

Source Company data, I-Sec research

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