

March 02, 2017

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Rating	Not Rated
Price	Rs552
Target Price	NA
Implied Upside	NA
Sensex	28,840
Nifty	8,900

(Prices as on March 02, 2017)

Trading data

Market Cap. (Rs bn)	145.2
Shares o/s (m)	263.0
3M Avg. Daily value (Rs m)	1,018.8

Major shareholders

Promoters	49.88%
Foreign	19.08%
Domestic Inst.	18.43%
Public & Other	12.61%

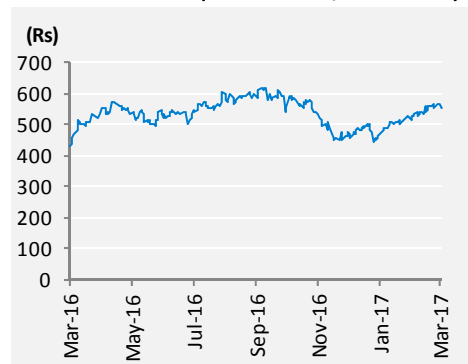
Stock Performance

(%)	1M	6M	12M
Absolute	7.8	(7.3)	30.2
Relative	5.4	(8.8)	8.8

How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2018	NA	91.2	NA
2019	NA	103.1	NA

Price Performance (RIC: RLIN.BO, BB: RELI IN)



Source: Bloomberg

We Attended Reliance defence and Engineering analyst meet (RDEL) where the company showcased the opportunity and their preparedness to benefit from the opportunity. Management sounded optimistic regarding the defence opportunities and believes that defence business could become a leading business vertical of Reliance Infrastructure going ahead. It has entered into strategic partnerships and has set up the infrastructure in place. The size of opportunity over next 15 years is estimated at ~ Rs15tn. It has put in place a team of 2000 professionals and over 200 senior management team to execute the vision. The current order book for the Defence segment is ~ Rs57bn to be executable by 2021. While opportunity size for defence business continues to be large over the next decade, however long lead time for order finalization continues to be a near term impediment. We believe RDEL along with L&T/BEL/TATA will be key beneficiaries form large defence opportunity.

- **Rs15tn worth of opportunity over next 15 years:** India is the largest importer of defence products accounting for 14% of the total global imports in 2016 and imports about 70% of the country's total requirement. Huge opportunity for import substitution along with government making conducive business environment for Private Sector participation under "Make In India" would be a great tailwind for private sector in defence sector going ahead. The capital acquisitions of defence hardware in next 10 years is expected to be ~Rs 15 tn (Aerospace - Rs 5.2tn/ Naval - Rs 3.5tn/ Land systems - Rs 6.0tn/ Security - Rs 300bn). Additionally the offset export opportunity is also estimated at Rs77bn. RDEL expects orders worth Rs300bn each to be finalized in both FY17 and FY18.

Contd...2

Key financials (Y/e March)

	2013	2014	2015	2016
Revenues (Rs m)	226,307	189,599	162,794	166,273
Growth (%)	(6.2)	(16.2)	(14.1)	2.1
EBITDA (Rs m)	29,586	31,672	20,279	32,662
PAT (Rs m)	22,468	19,137	18,002	19,746
EPS (Rs)	85.4	72.8	68.5	75.1
Growth (%)	41.6	(14.8)	(5.9)	9.7

Profitability & Valuation

	2013	2014	2015	2016
EBITDA margin (%)	13.1	16.7	12.5	19.6
RoE (%)	8.0	6.2	5.1	5.3
RoCE (%)	8.6	8.1	7.8	9.2
EV / sales (x)	1.5	2.0	2.3	2.2
EV / EBITDA (x)	11.7	11.7	18.7	11.1
PE (x)	6.5	7.6	8.1	7.4
P / BV (x)	0.6	0.6	0.6	0.5

Source: Company Data; PL Research

- Strategic tie -ups with global majors to capitalize on growth opportunities:** RDEL has received 27 industrial licenses for manufacturing of various defence hardware / equipments. It has also formed several strategic partnerships and Joint Ventures with global defence majors like Dassault Aviation to focus on Aviation in Aerospace sector, Rafael (Israel) to focus on Air to Air missiles, Air Defence Systems and Large Aerostats. It has signed strategic partnership with Antonov, Ukraine for Transport Aircraft. RDEL is setting up manufacturing facility in Mihan (Nagpur) & Bhopal for Aero segment and Indore SEZ for Land Systems.
- Targeting Naval opportunity through Pipav:** RInfra has acquired management control of Pipavav Defence Offshore and Engineering Company Limited (PDOECL) now renamed as Reliance Defence and Engineering Limited (RDEL). Reliance Shipyard at Pipavav has the largest Dry Dock in India. Reliance Shipyard has world class infrastructure facility to undertake all types of construction / refit / life cycle support of Warships, Submarines, Commercial vessels (including large bulk carriers), Oil & Gas platforms / rigs. Currently, Reliance Shipyard is the only Shipyard in India capable of building a new Aircraft Carrier of 65,000 Ton and above. The naval defence market size is likely to be more than Rs3.50trn in the next 15 years. RDEL has strategic partnerships with the global majors like, DCNS, SAAB, SAFRAN and Thales.
- Capital intensity not as high as perceived:** The management highlighted that contrary to popular perception the sector is not as capital intensive as perceived to be. It cited few examples of required capex in programs like the Rafel fighter jet program (Total capex requirement of ~Rs11bn and equity requirement of ~Rs1.65bn), Landing Platform Docks (LPD)(Rs1bn of additional capex) and P-75 Submarines(Rs1bn of additional capex). It highlighted that the return becomes even more attractive when one considers the life cycle cost of the programme.

Exhibit 1: List of Industrial licences won by RDEL

 AEROSPACE	 NAVY	 LAND SYSTEMS
<ul style="list-style-type: none"> ▪ Aircraft & Helicopters ▪ Missiles ▪ Avionics ▪ Simulators ▪ Radar & Radio Equipment ▪ Aviation MRO ▪ Medium Transport Aircraft ▪ Guided ammunition 	<ul style="list-style-type: none"> ▪ Hull Penetrators, Propulsion Systems ▪ Sonars, Electro Optical & C4I Systems ▪ Torpedos / Rockets/ AUV ▪ Electronic Warfare Systems ▪ Radars, Jammers ▪ Night Vision Devices ▪ Sensors, Navigation Systems & Surveillance Equipment 	<ul style="list-style-type: none"> ▪ Heavy Weapons, Heavy machine guns, Air Defence, Guns, Mortars, Multi barrel rocket launchers ▪ Revolvers, Shotgun, Light Machine gun, Pistols ▪ Tanks, Armoured Vehicles, Infantry Combat Vehicles (ICV), Armoured Personnel Carrier (APC)

Source: Company Data, PL Research

Exhibit 2: Break up of Rs15tn capex opportunity

Air Force	5.2
Naval	3.5
Army	6.0
Security	0.3

Source: Company Data, PL Research

Exhibit 3: Likely ordering size over next 3 years

2017	
LPD-4Nos	200
ASW-8 Nos	100
Total	300
2018	
NGC- 7 Nos	175
NGMV-6nos	120
Total	300
2019	
IAC-2	900
P-75(I)-12 nos	1200
Total	2100

Source: Company Data, PL Research

Exhibit 4: Aero space Defense Business(Rsbn)

Particulars	No.	Value
Single Engine fighter aircraft	200	1500
Twin Engine fighter aircraft	90	900
Deck based fighter aircraft for Navy	57	600
UAV/Aerostat	1000	500
AN32/Avro aircraft requirement	150	400
Airborne Warning and control systems	6	150
Medium range maritime aircraft	15	100
Medium heavy helicopters	200	750
Light utility helicopters	600	150
Naval utility helicopters	100	150
Sub total		5200

Source: Company Data, PL Research

**Exhibit 5: Land Defence Business(Rsbn)**

Artillery	360
Missile Systems	950
Combat Vechicals & Upgrades	2110
Small Arms	220
Helicopters	60
UAV's	60
Communication Systems	750
Miscellaneous	1700
Ammuniations	140
Security systems	350
Total	6700

Source: Company Data, PL Research

Income Statement (Rs m)

Y/e March	2013	2014	2015	2016
Net Revenue	226,307	189,599	162,794	166,273
Raw Material Expenses	105,668	96,456	94,183	84,883
Gross Profit	120,639	93,143	68,612	81,390
Employee Cost	11,419	10,674	12,095	13,406
Other Expenses	79,634	51,320	36,403	35,593
EBITDA	29,586	31,672	20,279	32,662
Depr. & Amortization	5,511	5,341	8,328	10,010
Net Interest	16,874	20,574	25,834	30,209
Other Income	10,585	12,651	16,531	19,511
Profit before Tax	17,785	18,408	13,836	11,954
Total Tax	2,026	2,743	700	3,463
Profit after Tax	15,759	15,664	13,136	8,491
Ex-Od items / Min. Int.	2,881	3,472	4,865	5,718
Adj. PAT	22,468	19,137	18,002	19,746
Avg. Shares O/S (m)	263	263	263	263
EPS (Rs.)	85.4	72.8	68.5	75.1

Cash Flow Abstract (Rs m)

Y/e March	2013	2014	2015	2016
C/F from Operations	26,359	44,116	32,903	67,660
C/F from Investing	(76,871)	(59,374)	(17,245)	(57,359)
C/F from Financing	41,631	17,211	(17,075)	(10,926)
Inc. / Dec. in Cash	(8,881)	1,952	(1,417)	(624)
Opening Cash	13,089	3,983	5,655	4,221
Closing Cash	3,983	5,655	4,221	3,635
FCFF	(22,489)	1,552	6,526	33,112
FCFE	51,794	83,906	54,446	126,734

Key Financial Metrics

Y/e March	2013	2014	2015	2016
Growth				
Revenue (%)	(6.2)	(16.2)	(14.1)	2.1
EBITDA (%)	8.8	5.3	(35.4)	61.0
PAT (%)	0.0	(14.8)	(5.9)	9.7
EPS (%)	41.6	(14.8)	(5.9)	9.7
Profitability				
EBITDA Margin (%)	13.1	16.7	12.5	19.6
PAT Margin (%)	7.0	8.3	1.2	5.1
RoCE (%)	8.6	8.1	7.8	9.2
RoE (%)	8.0	6.2	5.1	5.3
Balance Sheet				
Net Debt : Equity	0.8	0.8	0.9	0.8
Net Wrkng Cap. (days)	(45.7)	(62.6)	(48.4)	(117.7)
Valuation				
PER (x)	6.5	7.6	8.1	7.4
P / B (x)	0.6	0.6	0.6	0.5
EV / EBITDA (x)	11.7	11.7	18.7	11.1
EV / Sales (x)	1.5	2.0	2.3	2.2
Earnings Quality				
Eff. Tax Rate	11.4	14.9	26.4	29.0
Other Inc / PBT	59.5	68.7	624.3	163.2
Eff. Depr. Rate (%)	3.1	3.2	3.3	3.6
FCFE / PAT	2.3	4.4	3.0	6.4

Source: Company Data, PL Research.

Balance Sheet Abstract (Rs m)

Y/e March	2013	2014	2015	2016
Shareholder's Funds	261,210	265,909	269,745	276,758
Total Debt	206,142	232,333	240,297	222,288
Other Liabilities	43,490	38,076	29,518	27,294
Total Liabilities	510,842	536,319	539,559	526,339
Net Fixed Assets	212,571	210,903	227,782	242,015
Goodwill	748	589	589	589
Investments	100,340	141,182	142,476	161,212
Net Current Assets	79,237	85,188	77,786	41,983
Cash & Equivalents	4,924	6,504	5,351	4,711
Other Current Assets	37,579	49,939	54,841	27,289
Current Liabilities	154,118	152,958	168,912	193,181
Other Assets	118,695	99,046	91,516	81,129
Total Assets	510,842	536,319	539,559	526,339

Quarterly Financials (Rs m)

Y/e March	Q4FY16	Q1FY17	Q2FY17	Q3FY17
Net Revenue	44,693	70,986	69,729	58,157
EBITDA	12,239	10,362	11,391	11,802
% of revenue	27.4	14.6	16.3	20.3
Depr. & Amortization	2,756	3,260	3,729	5,182
Net Interest	7,943	10,108	10,459	11,474
Other Income	5,057	7,150	6,396	8,099
Profit before Tax	6,188	4,144	4,455	3,244
Total Tax	448	1,005	(257)	309
Profit after Tax	6,150	3,139	3,856	2,935
Adj. PAT	6,150	3,139	3,856	2,935

Source: Company Data, PL Research.

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