Azad Engineering
IPO Note
Date: 19.12.2023

Azad Engineering's high entry barrier comes from OEMs' demanding qualification procedures. It's a business that requires more than just money to succeed. The company has a solid track record, a strong business plan, and management experience that has produced positive results in the past. The revenue of the company grew at a CAGR of 43% between FY2021 and FY2023 and PAT margin grew at a CAGR of 49% between FY2021 and FY2023. While, valuation of the company stands at 292.7x P/E which appears fully priced as compared to peers. We recommend to subscribe for listing gains

Issue details

Price Band (in ` per share)	499-524
Issue size (in ` Crore)	740.00
Fresh Issue (in ` Crore)	240.00
OFS (in ` Crore)	500.00
Issue open date	20.12.23
Issue close date	22.12.23
Tentative date of Allotment	26.12.23
Tentative date of Listing	28.12.23
Total number of shares (lakhs)	148.30-141.22
No. of shares for QIBs (50%) (lakhs)	73.75-70.23
No. of shares for NII (15%) (lakhs)	22.12-21.07
No. of shares for S-HNI (1/3rd)	7.37-7.02
No. of shares for B-HNI (2/3rd)	14.75-14.05
No. of shares for retail investors (35%) (lakhs)	51.96-49.16
Minimum order quantity	28
Face value (in `)	2.00
Amount for retail investors (1 lot)	13972-14672
Maximum number of shares for Retail investors at lower Band	392(14 Lots)
Maximum number of shares for Retail investors at upper band	364 (13 Lots)
Maximum amount for retail investors at lower Band- upper band	195608-190736
Minimum number of shares for sHNI (2 Lakhs) at upper band	205,408 (14 Lots)
Maximum number of shares for sHNI (10 Lakhs) at upper band	997,696 (68 Lots)
Minimum number of shares for bHNI at upper band	1,012,368 (69 Lots)
Employee reservation (in lakhs	0.80-0.76
Exchanges to be listed on	BSE, NSE

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About Company

Azad Engineering Limited is a manufacturer of aerospace components and turbines. The company supplies its products to original equipment manufacturers (OEMs) in the aerospace, defense, energy and oil and gas industries. These products are highly engineered, complex, mission critical and vital.
They are one of the key manufacturers of their qualified product lines supplying to global original equipment manufacturers ("OEMs") in the energy, aerospace and defence, and oil and gas industries, manufacturing highly engineered, complex and mission and life-critical components. They manufacture complex and highly engineered precision forged and machined components that are mission and life-critical and hence, some of their products have a "zero parts per million" defects requirement. Their customers include global OEMs across the energy, aerospace and defence and oil and gas industries such as General Electric, Honeywell International Inc., Mitsubishi Heavy Industries, Ltd., Siemens Energy, Eaton Aerospace and MAN Energy Solutions SE

Promoters

- Rakesh Chopdar
- Jyoti Chopdar
- Vishnu Pramodkumar Malpani
- Ronak Jajoo
- Ful Kumar Gautam

Objective of the Offer

- Funding capital expenditure of the Company
- Repayment/prepayment, in part or full, of certain of the borrowings availed by the Company
- General corporate purposes.

Brief Financials

PARTICULARS (Rs. Cr)*	SEPTEMBER 23	FY23	FY22	FY21
Share Capital	9.91	1.65	1.51	1.51
Net Worth	250.53	203.98	120.00	90.89
Revenue	169.53	261.52	199.26	125.03
Profit/(Loss) After Tax	26.88	8.47	29.45	11.5
EPS^ (in Rs)	10.86^	1.79	6.49	2.53
Net Asset Value (Rs)	45.74	42.30	25.58	20.02
P/E#	48.25	292.73	NA	NA
P/B#	11.45	12.38	NA	NA

Source: #calculated at upper price band * Restated consolidated financials ^annualised EPS

Industry Review

OVERVIEW OF GLOBAL GDP

The global economy expanded at a compounded annual growth rate of 3.1% from 2010 to 2019. The Covid-19 pandemic crisis of 2020 impacted the growth and the global economy contracted by ~3.3% and entered recession. The pandemic forced the economy to a standstill for almost the entirety of 2020 and some part of 2021. While the pandemic subsided, recovery was hindered further by the Russia-Ukraine war, a downturn in the United States, and challenges in the global supply chain. The world has begun to recover from the economic shocks of the last several years. The global economy is expected to witness a growth rate of 3.0% in 2023. According to IMF, the global slowdown bottomed out in 2022 and the world would likely see a modest growth of ~3% per annum till 2028. Global growth will be led by emerging markets and developing economies, with established economies, particularly the United Kingdom and the Eurozone, expected to increase only at 0.4% and 0.9% in 2023, respectively. Because of its proximity to the war zone and greater sensitivity to swings in energy costs, the Eurozone is projected to suffer the greatest impact on growth. When compared to global GDP growth, emerging markets, and developing economies are predicted to grow at a rate of 4.0% in 2023.

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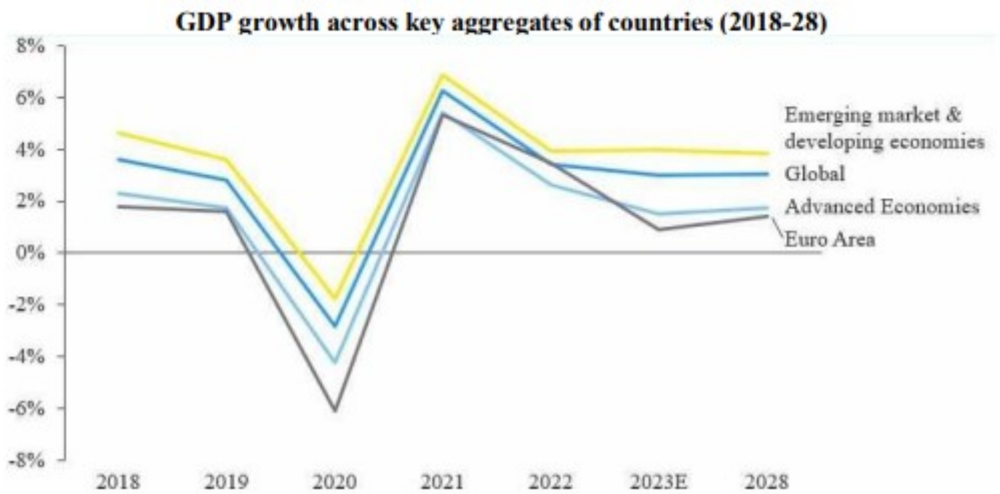

Industry Review

GROWTH OUTLOOK OF KEY ECONOMIES

Outlook on key advanced economies USA is facing an estimated growth rate of 1.8% in 2023 over the previous year which witnessed a 2.1% growth. The economy is witnessing a resilience in consumer demands and industrial production which drives the expansion of the economy. The country is slowly easing out of inflation, which peaked to ~8% in 2022. The inflation has been steadily falling ever since, with the country witnessing lower CPI% at 4.5%, a first post pandemic. CPI eased majorly due to fall in energy prices, but other goods in the CPI basket appear to be impacted as well. But this is still higher than the Federal committees' target of 2% inflation over the long term. The US Federal Open Market Committee meeting of July 2023 indicated a below trend GDP growth and softening of labor markets are required to balance supply and demand and to ease inflation. This indicates possible continuing of the rate hike trend. However, the hiking of rates from 2022 also led to added stress on the country's financial systems, indicated by the recent collapse of Silicon Valley Bank. So, the economy is on a delicate balance between increasing rates to rein in inflation, while ensuring absorbable stress on the banking sector.

UK is facing slower growth rates and the country's growth is projected to witness a marginal growth of 0.4% in the current year. While the economy appeared to be on a path of recovery after a growth of 4.1% in 2022, the high inflation level of 9% in 2022 forced the Bank of England to tighten the policy measures by increasing interest rates. While the market also witnesses higher wages, the pressure it exerts on inflation is gradually expected to come down with loosening of labor markets.

Japan is projected to grow at 1.4% driven by domestic demand and retail demand due to pick-up of tourism post pandemic. The country is witnessing reduction in exports due to weak global demand and hence the lower than global growth rate.

Outlook on key emerging markets

China's economy is facing a slowdown post the pandemic recovery, primarily due to slowing of manufacturing output and decreased domestic demand. Potential for increased exports from the country will also be limited due to slow down in advanced economies such as USA and UK. According to IMF, the country is expected to remain as one of the fastest growing economies in the Asia region in the current year, contributing to ~35% of global growth. However, the economy is expected to slow down in the future due to inherent demographic characteristics and a drag in productivity.

Russian economy faced contraction in 2022 due to wartime sanctions and higher focus on military spends. While EU has stopped the import of oil from Russia, the country has diverted production to other economies. Despite oil revenues, growth will slow down due to continuing global sanctions.

Brazil has had faster-than-expected GDP growth due to agricultural expansion, despite a slowdown in the services sector, which accounts for 70% of GDP, and underperformance in the industrial sector. The Central Bank of Brazil has been raising interest rates to control inflation, which has so far had no effect on consumer spending due to a solid labour market. However, the job market's continuous expansion is not projected to continue, which will have an influence on consumer spending, and growth rates are expected to decline.

The India Opportunity

Macroeconomic Overview of India

GDP GROWTH FOR INDIA

Indian economy had a steady growth over the last few years with the GDP witnessing a compounded annual growth rate of 6.6% from 2010 to 2019. The global pandemic in 2020 led to a 5.8% contraction in the economy. India has recovered from the slump from the pandemic period, with ~7% growth in 2022 and an estimated growth of 6.1% in 2023. In 2022, the Indian economy overtook the UK economy to become the 5th largest in the world. The economic growth is driven by strength of services exports from India. Structural reforms of the government including higher FDI limits, focus on disinvestment have also supported the economy in the recovery post slowdown due to the pandemic. 117 India has been a major driver of global growth in the recent years, especially due to higher inflation and economic slowdown in major economies. With global supply chains getting back to the pre-pandemic order, International Monetary Fund (IMF) predicts that Asia will account for about 70% growth in the world in 2023 and India & China together will contribute towards 50% of global growth.

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Industry Review

INDIAN MANUFACTURING SECTOR

India hasthe potential to become one of the largest manufacturing hubs in the world. It has a large population base with growing income, considerably younger proportion of workforce and business friendly sector policies which provide the opportunity to become a global manufacturer. The World Economic Forum in 2021, identified that India's manufacturing sector can contribute to over US$ 500 billion to the economy in 2030. Due to the COVID-19 pandemic, the country's overall economic activity decreased in 2020. Industrial activity reduced and project completion dates were pushed back. Because of the re-opening and resilience of the domestic manufacturing sector, industrial production recovered strength and returned to a positive trajectory in 2021 after the country emerged from multiple lockdowns. The country's manufacturing sector reportedly employs over 27 million people and the overall contribution of manufacturing to GVA is about 18%. The contribution of manufacturing to GVA has been broadly constant in the past few years, but the absolute GVA from manufacturing has been growing at a CAGR of 2.3% from FY18-FY22.

Index of Industrial Production (IIP) which is an indicator of mining, manufacturing and electricity production has gotten back to pre-pandemic levels. IIP witnessed an accelerated growth in FY22, mainly due to the lower base effect and recovery from FY21 pandemic levels. The manufacturing sector contributes to more than 75% of the IIP in India. For Indian manufacturing sector to pick up pace, the country must shift towards developing competency in niche manufacturing segments and move beyond pure-play cost-advantage. The sector also requires capital investments and strong government policies to attract global manufacturing companies to manufacture in India.

Atma Nirbhar Bharat Abhiyan

In the midst of the COVID-19 epidemic, the Government of India announced the Atma Nirbhar Bharat Abhiyan (or 'Self-reliant India') in May 2020. The campaign's principal goal was to recover from the economic impact of the pandemic and become selfsufficient on five key pillars: economy, technology-driven infrastructure, infrastructure, demand, and demographics. The Indian government unveiled a combined economic package worth INR 20 trillion (approximately 10% of India's GDP) to support a variety of projects aimed at benefiting enterprises, MSMEs, farmers, and the agriculture sector. Reducing import dependence and promoting the growth of domestic manufacturing industry was one of the key emphases of the government in this scheme. Under Atma Nirbhar Bharat, the government also plans to introduce parameters for better quality of output to meet international standards so that Indian products can compete in the global market

Production Linked Incentive (PLI) scheme

India introduced the PLI scheme in 2020 to promote domestic production through subsidies and encourage exports while cutting down on cheap imports. The scheme is available across fourteen key manufacturing sectors including specialty steel, telecom, auto components, drone components etc. It is designed to provide incentives which are linked to investment and turnover size. The government sanctioned over INR 1.9 lakh crore to be periodically utilized for the scheme. The country expects that PLI sectors will attract more FDI inflows due to added incentives especially in food processing, pharmaceuticals, and electronics segments. The government is analyzing the effect of the scheme and depending on the success, it is likely that the scheme will be extended across other manufacturing segments.

Ease of doing business

India ranks 63rd in the 'Ease of Doing Business' ranking by World Bank. This is a massive improvement over its position just a decade back, when it stood at 142nd rank in 2014. The improvement in ranking is driven by simplification of the business ecosystem through government initiatives such as 'Make in India', 'National Single Window System (NSWS)' etc. Among its South Asian peers, India ranked better in terms of trading across borders ranking including both 'Border compliance' and 'Documentary compliance' that improves cost to export; the country lagged behind China in-terms of time and cost to import and ranked the lowest in terms of time to export. The government has been focusing on initiatives to empower India as an export destination and capitalizing on the opportunities arising out of global China plus one strategy. Thus, improving the overall ease of doing business in the country is a major milestone on the path towards manufacturing success.

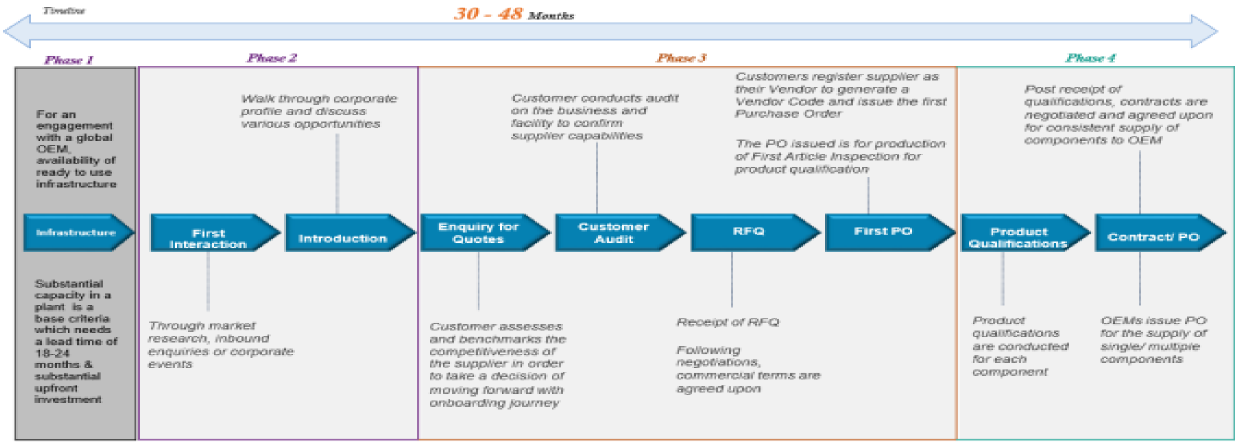
FDII NTO THE MANUFACTURING SECTOR

India is among the top 10 FDI destinations in the world. FDI flows across the world witnessed a degrowth of 12% in 2022 due to global economic conditions and this also reflected in the reduction in FDI inflows into India in FY22 and FY23. Indian manufacturing sector has been consistently accounting for about 20% of total FDI flows into India. In terms of relevant industrial segments, the renewable energy sector attracted US$ 11 Bn worth of FDI in the last 9 years. The defense sector attracted US$ 62 Mn worth of investment since the policy liberalization in 2020, as per InvestIndia website accessed in August 2023. Indian government allows for up to 100% FDI through automatic route in the manufacturing sector

Competitive Strengths

Engineered for success and a preferred name in the manufacturing of highly engineered, complex and mission and lifecritical high precision components for global OEMs despite growing competition from China, Europe, USA and Japan

They are one of the key manufacturers of their qualified product lines supplying to global OEMs primarily engaged in highly regulated industries, including energy, aerospace and defence and oil and gas industries, manufacturing highly engineered, complex and mission and life-critical components. In order to supply there products to their customers, they are required to undergo a part-by-part qualification process with each of them since their products are project and life critical in nature, to satisfy the stringent processes and quality requirements of their customers.



Long-standing and deep customer relationships

There company has existing relationships with both Indian and global OEMs. There long-standing customer base comprises leading product OEM companies, key strategic and globally preferred partners such as General Electric and Mitsubishi Heavy Industries, Ltd., with whom they have an average relationship of over 10 years. Further, their integrated manufacturing and supply chain solutions together with their scale of operation technical know-how, value added design and engineering expertise, allows them to cater to several Indian and global OEMs. They serve a broad range of customers both in the Indian and overseas markets. The table below sets out the details of their total 211 revenue from contracts with customers with geographical location outside India

	Six months period ended September 30, 2023	Fiscal 2023	Fiscal 2022	Fiscal 2021
Outside India (in ₹ million)	1,423.79	2,023.08	1,518.17	1,007.33
Outside India % (in %)	89.69	80.38	78.07	82.08

Experienced promoters and leadership team:

The promoter Rakesh Chopdar has more than 25 years of experience in precision engineering industry. He has developed healthy relationship with the customers through timely execution, consistent quality and achieving requisite certifications for the processes followed. Business operations are led by professionals having an average experience of more than 16 years in their individual field of expertise and having played key roles in Siemens, Godrej Aerospace, Toshiba, and Mercedes India.

Established relationships with reputed OEMs:

The company has running long-term contracts with reputed customers in domestic & export markets. The business can be broadly divided into two business verticals – Energy and Aerospace. The company is a supplier to established and known OEMs like GE, Mitsubishi, BHEL, Siemens, Toshiba etc in the energy segment and Honeywell, GE Aviation, Boeing, Eaton, HAL etc in the Aerospace segment. The export sales are well diversified to regions such as US, UK, Europe, Japan, and Middle East. The market for turbine blades is valued around ₹ 12,600 crores. AEPL has obtained 1200+ product qualifications and 45+ process qualifications in last 10 years which provides it an edge over competition as product and process qualification is capital and time consuming. The company is one of the four major global players offering similar products

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Risk Factors

Market Risks: Fluctuations in demand for engineering products and services due to economic conditions or industry-specific factors can impact the company's revenue and profitability.

Technological Changes: Rapid advancements in technology can render existing products obsolete or require significant investments in research and development to stay competitive.

Supply Chain Disruptions: Dependence on a complex supply chain makes companies vulnerable to disruptions, such as shortages of raw materials, transportation issues, or geopolitical events.

Regulatory Compliance: Changes in regulations or compliance requirements, especially in the engineering and manufacturing sectors, can pose challenges and necessitate adjustments to operations.

Financial Risks: Economic downturns, fluctuations in interest rates, or unfavorable currency exchange rates can affect the company's financial stability.

Project Risks: If Azad Engineering Limited is involved in project-based work, project delays, cost overruns, or contractual disputes can pose risks to profitability.

Peer Comparison

Name of the company	Total Revenue (in Rs Cr)	Face Value (Rs per share)	EPS (in Rs)	Return on Net Worth (%)	NAV(Per share Rs)	P/E	P/B
Azad Engineering	261.52	2	1.79	4.32	42.30	292.73	12.38
MTAR Technologies	593.28	10	33.62	16.72	201.13	66.71	11.15
Paras Defence and Space Technologies Limited	230.65	10	9.25	8.69	10.60	80.60	85.79
Dynamatic Technologies	1325.53	10	67.32	7.93	79.47	65.84	55.79
Triveni Turbine	1290.17	1	5.97	25.41	25.47	69.38	16.31

*P/E Ratio and P/B has been computed based on the closing market price of equity shares on the website of NSE as of December 15, 2023

Our View

Azad Engineering's high entry barrier comes from OEMs' demanding qualification procedures. It's a business that requires more than just money to succeed. The company has a solid track record, a strong business plan, and management experience that has produced positive results in the past. The revenue of the company grew at a CAGR of 43% between FY2021 and FY2023 and PAT margin grew at a CAGR of 49% between FY2021 and FY2023. While, valuation of the company stands at 292.7x P/E which appears fully priced as compared to peers. We recommend to subscribe for listing gains

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