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IPO Note – Mazagon Dock Shipbuilders Limited

25-September-2020

RETAIL RESEARCH

Mazagon Dock Shipbuilders Ltd

Issue Snapshot:
Issue Open: Sept 29 – Oct 01, 2020

Price Band: Rs. 135 – 145

Issue Size: 30,599,017 eq shares
(Entirely Offer for sale)

Issue Size: Rs. 413.1 – 443.7 cr

Reservation for:

QIB	Upto 15,126,750 eq sh
Non Institutional	atleast 4,538,025 eq sh
Retail	atleast 10,588,725 eq sh
Employee	Upto 345,517 eq sh

Face Value: Rs 10

Book value: Rs 152.17 (March 31, 2020)

Bid size: - 103 equity shares and in multiples thereof

100% Book built Issue

Capital Structure:

Pre Issue Equity:	Rs. 201.69 cr
Post issue Equity:	Rs. 201.69 cr

Listing: BSE & NSE

Book Running Lead Manager: Yes Securities (India) Ltd, Axis Capital Ltd, Edelweiss Financial Services Ltd, IDFC Securities Ltd, JM Financial Ltd.

Registrar to issue: Alankit Assignments Ltd

Shareholding Pattern

Shareholding Pattern	**Pre issue %**	**Post issue %**
Promoter and Promoter Group	100.0	84.8
Public & Employee	0.0	15.2
Total	100.0	100.0

Source for this Note: RHP

Background & Operations:

Mazagon Dock Shipbuilders Limited (MDSL) is a defence public sector undertaking shipyard under the Department of Defence Production, Ministry of Defence, GoI (MoD) with a maximum shipbuilding and submarine capacity of 40,000 DWT engaged in the construction and repair of warships and submarines for the MoD for use by the Indian Navy and other vessels for commercial clients. It is a wholly owned GoI company, conferred with the 'Mini-ratna-I' status in 2006, by the DPE. It is India's only shipyard to have built destroyers and conventional submarines for the Indian Navy. It is also one of the initial shipyards to manufacture Corvettes (Veer and Khukri Class) in India.

The business divisions in which MDSL operates are (i) shipbuilding and (ii) submarine and heavy engineering. Its shipbuilding division includes the building and repair of naval ships. And are currently building four P-15 B destroyers and four P-17A stealth frigates and undertaking repair and refit of a ship for the MoD for use by the Indian Navy. Its submarine and heavy engineering division includes building, repair and refits of diesel electric submarines. It is currently building/ in the process of delivering four Scorpene class submarines under a transfer of technology agreement with Naval Group as well as one medium refit and life certification of a submarine for the MoD for use by the Indian Navy. Since 1960, MDSL has built a total of 795 vessels including 25 warships, from advanced destroyers to missile boats and three submarines. It has also delivered cargo ships, passenger ships, supply vessels, multipurpose support vessels, water tankers, tugs, dredgers, fishing trawlers, barges and border outposts for various customers in India as well as abroad.

MDSL's shipyard is strategically located on the west coast of India, on the sea route connecting Europe, West Asia and the Pacific Rim, a busy international maritime route. It is headquartered in Mumbai which is also the headquarters of the Western Naval Command of the Indian Navy and are also exploring the possibilities of developing a greenfield shipyard at Nhava, Navi Mumbai with a shiplift, wet basin, workshops, stores and buildings and a ship repair facility spread over an area of 37 acres.

Prior to the company's incorporation in 1934, a small dry dock was constructed in Mazagaon village, Mumbai, to service the ships of the British East India Company in 1774 which was subsequently developed into a ship repair yard and later a ship building yard over the course of two centuries. It was incorporated as a private limited company in 1934 and in the year 1960, the GoI took over the Company to expand its warship development programme designating it as a DPSU under the MoD.

Objects of Issue:

The objects of the Offer are to (i) to carry out the disinvestment of 30,599,017 Equity Shares by the Selling Shareholder constituting 15.17% of MDSL's pre-Offer paid up Equity Share capital ; and (ii) achieve the benefits of listing the Equity Shares on the Stock Exchanges. MDSL will not receive any proceeds from the Offer and all such proceeds will go to the Selling Shareholder.

Competitive Strengths

Only public sector defence shipyard constructing conventional submarines: MDSL is primarily engaged in the defence shipbuilding segment catering to the needs of the MoD. It is India's only shipyard to have built destroyers and conventional submarines for the Indian Navy and in the past constructed two SSK submarines, modernized and refitted four SSK submarines. This has enhanced its capability of handling construction of conventional submarines. It has also entered into a technology transfer agreement with Naval Group, France for Scorpene submarines which are currently manufactured by it. It has also delivered two of the Scorpene submarines, INS Kalvari and INS Khanderi to the MoD. MDSL alongwith the Naval Group has trained its workforce in relation to the construction of such submarines.

World class infrastructure capable of serving the requirements of the Ministry of Defence*:* The infrastructure and facilities available at MDSL's shipyard combined with its vast expertise give a significant edge over its domestic peers. Its facilities currently comprise of three dry docks, two wet basins, three slipways, production shops, assembly shops, module shop with painting chamber for integrated construction, sheet metal shop, pipe shop, machine and fitting shop, ship dry dock and dredging, electrical repair shop and instrumentation shop for shipbuilding division. Its submarine division infrastructure includes shops for fabrication of frame, sub-section assembly and section formation, cradle assembly shop for structural and equipment outfitting and final assembly, one dry dock and submarine section assembly shop. The company also has a shore integration facility which enables it to complete combat system integration off-site prior to onboard installation. It has also constructed a submarine assembly workshop which comprises of two bays and is equipped with two levels of EOT cranes as well as semi goliath cranes.

Location of facilities promotes closer association with vendors and customers*:* MDSL's shipyard is strategically located in Mumbai on the west coast of India, on the sea route connecting Europe, West Asia and the Pacific Rim, a busy international maritime route. Its customers, being the MoD and Indian Coast Guard and its vendors are based in Mumbai which results in closer co-ordination and greater efficiencies. Further, a majority of its subcontractors are based in and around Mumbai which provides with an ease of access to labour. The location of MDSL's facilities provides a strategic competitive advantage over its peers.

Increase in indigenisation of vessels and implementation of the "Make in India" campaign: MDSL intends to increase the quantum of indigenised components for its warships and submarines in order to give an impetus to the GoI's "Make in India" campaign. In the past, for its warships and submarines, it used to import equipment related to design support, model testing evaluation and simulation, major engineering and weapon equipment and systems, equipment related to planning and project management, installations and system integration, due to non-availability of domestic manufacturers. It has successfully indigenised certain equipment such as sonar dome, ship installed chemical agent detection system, bridge window glass, main batteries for Scorpene submarines, multiple cable transit glands and remote controlled valves with various companies on a no cost no commitment basis.

MDSL had also been assigned 40.52 acres of land by the Government of Kerala for setting up the National Institute of Warship/ Submarine design and Indigeinisation Centre which is currently being used as a head office of National Institute for Research and Development in Defence Shipbuilding. Increase in indigenisation has enabled it to reduce its reliance on third party component manufacturers and the cost of construction for its vessels.

Established track record with strong financial position and strong Order Book: MDSL is a profitable shipyard with profits continuously in the last three Fiscals. Its total income was Rs 42,748.63 million, Rs 50,276.29 million, Rs 52,046.74 million and Rs 55,353.07 million for Fiscals 2017, 2018, 2019 and 2020 respectively. Its profit for the year was Rs 5,982.58 million, Rs 4,961.73 million, Rs 5,324.74 million and Rs 4,770.59 million for Fiscals 2017, 2018, 2019 and 2020 respectively. Further, as of July 31, 2020, its Order Book for shipbuilding and submarines and heavy engineering was Rs 540,740 million comprising of three major shipbuilding projects and two submarine projects.

Experienced board and senior management team and skilfully trained workforce*:* MDSL has a diversified Board with directors having several years of experience in the shipbuilding as well as submarine division and each of its senior management team is experienced in the industry and has been with the Company for an average of more than two decades. It also has a large pool of experienced naval architects, engineers and draftsmen. It continuously train its employees which enable it to service the technical and commercial demands of its customers. Its employees and blue-collar workforce are instrumental to its success including for the quality of its products and services and its ability to operate in a cost-efficient manner, helping it achieve a continuous profit margins, efficient operations, short delivery schedules, relatively lower attrition and fewer employee disputes.

Business Strategy:

Export of products to the international markets*:* MDSL primarily caters to the defence sector in India at present. However, it is in the process of reviving the exports of its defence and commercial products to Latin America, Africa, South East Asia, Middle East and Scandinavian regions and has identified certain defence and civil sectors in such regions. For this purpose, it has entered into agency agreements with sales agents in order to procure customers for its products which it proposes to sell in the identified markets of Europe, Far East, South East Asia, Middle East, Indian Ocean Rim countries, Latin America and Africa regions. It has, in the past, exported its products to Mexico, France, Bahamas and Yemen. It intends to increase its presence globally by establishing an international marketing team to identify potential markets for its business growth.

Focus on ship repair: MDSL's shipbuilding and submarine contracts have a long gestation period. Its revenues under these contracts are dependent on achievement of certain milestones. In order to diversify its revenue streams, it intends to increase its ship repair activities in the future as such activities are for a shorter period of time and result in the early booking of revenues. It has in the past undertaken ship repairs for its clients in the defence and commercial sectors. This will help generate more revenues, increase client base and reduce dependency on the MoD for future orders. The company is in the process of reviving its ship repair operations which will result in augmentation of its revenues and profitability.

Augmentation of infrastructure and enhancing manufacturing capacity: MDSL is currently undertaking capital expenditure for its submarine and heavy engineering division by way of construction of the submarine launch facility and blasting painting chamber. The submarine launch facility which is currently being constructed will enable to execute future submarine orders. It is also leveraging the latest construction methods in order to speed up the construction of its warships. MDSL is planning to dredge the water front to a depth of 3.5 metres below chart datum and create a navigation channel from Angre wet basin to the offshore container terminal of MbPT which will enable it to move the vessels without depending on the tidal conditions throughout the year. It is also exploring acquiring additional land adjacent to its Company, belonging to MbPT for setting up of new facilities. Augmentation of its existing facilities and developments of future facilities will enable to deliver its products on or before the scheduled date of delivery and enable it to cater to future orders.

Industry

Review of the global shipbuilding industry

An overview of the global shipbuilding industry

The global shipbuilding industry comprises construction and modification of ships, offshore vessels and rigs. The broad categories of ships built are:

- Passenger carriers
- Offshore vessels
- Dry bulk carriers
- Tankers (Inclusive of LNG carriers)
- Container ships
- Defence vessels

On average, it takes 15-18 months to build a conventional vessel, i.e., a bulk carrier, tanker or container ship, and 28-32 months to construct a 'liquefied natural gas (LNG)' vessel and an 'offshore rig and support' vessel.

China, South Korea and Japan dominate the industry

Over the past few decades, the shipbuilding industry has shifted from Europe to Asia, due to favourable factors such as cheap labour, competitive manufacturing and steel-making sectors, as well as state support. Typically, a shipyard requires a working capital of around 25-35% of the cost of the ship during the construction period. Moreover, the interest rates offered to shipbuilding yards in these countries are quite low. At the time of sale of ships, the Chinese and South Korean governments provide discounts/subsidies of 5-10% and 15-20%, respectively, thus helping players bid at lower prices against global competition. In 2015, China, South Korea and Japan together accounted for 91% of global deliveries, with China commanding the largest share of 36%, followed by South Korea and Japan at 34% and 21% respectively.

Shipbuilding order book

In line with the falling shipyard capacity and stretched finances of owners and banks, the global order book declined for most vessel types in 2015 and 2016. Between 2012 and 2016, the global order book declined at a compound annual growth rate (CAGR) of 8.9%. From their peak values in 2008 and 2009, the order books for container ships, oil tankers, dry bulk carriers and general cargo have declined 46%, 51%, 61% and 82% respectively. This sluggishness was largely because of supply overhang amid low demand, especially in the dry bulk and oil tanker segments.

Shipbuilding deliveries

Deliveries across major shipbuilding countries declined. The number of ships delivered between 2011 and 2015 fell across most major shipbuilding countries. Overall, the total number of ships delivered in tonnage terms decreased at a CAGR of 12.3%.The dry bulk segment saw significant delays and cancellations, as shipping liners postponed deliveries, awaiting market recovery. Deteriorating finances of global shipyards added to the slump, as they were unable to meet working capital requirements and, thus, fulfil orders. Further, to capture the turning tide of rising tanker demand, players looked to convert orders for bulk carriers into tankers. Recently, leading shipbuilding firms, such as New Times Shipbuilding and Hyundai Samho Heavy Industries, have had talks to convert capesize vessels into tankers. China, Japan and the South Korea maintained the dominant share in annual deliveries over the past five years. China and South Korea had their highest individual annual deliveries, in GRT terms, in 2011, while Japan had its highest individual deliveries in 2013. China mostly built dry bulk carriers and had the highest market share in general cargo ships. Japan specialises mostly in bulk carriers, while South Korea dominates the market for container vessels.

Review of the Indian shipbuilding industry

Based on the types of ships built, the Indian shipbuilding industry can broadly be categorised as follows:

i. Large ocean-going vessels catering to overseas and coastal trade;
ii. Medium-sized specialised vessels, such as port crafts, those for fishing, trawlers, offshore vessels, inland and other smaller crafts;
iii. Defence/naval crafts and coast guard vessels.

According to the Statistics of India's Ship Building and Ship Repair Industry of 2014-15, there were 34 dry docks for repairing ships in India, both in the public and private sectors. These dry docks included the 11 dry docks operated by seven major ports. The major ports without dry dock facilities are the Jawaharlal Nehru Port Trust (JNPT), the ports at New Mangalore, Chennai, Ennore, and Haldia Dock Complex of the Kolkata port.

Sector-wise classification

The Indian shipbuilding industry can be divided into following segments:

Public sector shipyards: India's major shipyards have historically been from the public sector. They primarily build merchant-class ships and naval vessels. The Indian shipbuilding industry comprises eight public sector shipyards out of which four naval shipyards come under the purview of India's Ministry of Defence, namely Hindustan Shipyard Ltd, Mazagon Dock Shipbuilders Ltd, Goa Shipyard Ltd and Garden Reach Shipbuilders & Engineers Ltd.

According to the Statistics of India's Ship Building and Ship Repair Industry of 2015-16, as of March 2016, public sector shipyards accounted for around one-third of the total shipbuilding order book in terms of number of ships with outstanding orders for 104 ships amounting to a combined tonnage of 173 thousand DWT. In 2015-16, public sector shipyards delivered a total of 32 ships with a combined tonnage of 48.5 thousand DWT.

Private shipyards: The three listed private-sector shipbuilding companies are Bharati Defence & Infrastructure Ltd (BDIL), ABG Shipyard Ltd and Reliance Defence and Engineering Ltd (RDEL), formerly known as Pipavav Defence and Offshore Engineering Company Limited (PDOECL). Additionally, Larsen & Toubro Ltd is another major private sector player. In addition, there are a number of smaller private shipyards building smaller ships and vessels, including coastal vessels, barges, tugs, patrol ships and fishing ships. As of March 2016, the private sector accounted for around two-thirds of the total shipbuilding order book in terms of the number of ships with outstanding orders for 192 ships amounting to a combined tonnage of 2,569 thousand DWT. In 2015-16, private sector shipyards delivered 23 ships with a combined tonnage of around 94.5 thousand DWT. RDEL accounted for the highest share in terms of tonnage delivered. ABG Shipyard had the largest order book in terms of number of ships and tonnage, followed closely by RDEL.

However, over the last few years, major private players like Reliance Defence and Engineering Ltd, ABG Shipyard, Bharati Defence & Infrastructure Ltd etc. have had to opt for corporate debt restructuring (CDR) due to stressed financial positions. Additionally, the decline in global trade and a liquidity crunch have impacted performance of these shipyards. The execution of existing order book of the private sector in general remains uncertain due to these unresolved issues. The CDR lenders of ABG Shipyard invoked strategic debt restructuring (SDR) provisions in December 2015 with a view to seek out strategic investors to sustain the operations of the company after the plan to restructure loans under CDR did not fructify. On the other hand, Bharati Defence and Infrastructure Limited's debt was sold off to Edelweiss Asset Reconstruction Company (ARC) after its CDR plan also did not work out. Bharati Defence had also approached Board for Industrial & Financial Reconstruction (BIFR) to get itself registered as a sick company. However, RDEL exited the CDR scheme in May 2017 after its refinancing plan was approved by lenders.

Shipbuilding capacity

The shipbuilding capacity of public sector shipyards remained fairly stable during 2011-12 to 2015-16, even as Goa Shipyard's capacity declined to 4,500 DWT from 10,000 DWT in 2014-15. On the other hand, the private sector's shipbuilding capacity increased at a CAGR of around 3% over 2011-12 to 2015-16. Capacity enhancement of the private sector was on account of new players - L&T entered in 2013-14 with a capacity of 30,000 DWT, Sembmarine Kakinada Ltd started operations in 2014-15 with a capacity of 50,000 DWT, and Chidambaranar Shipcare Private Ltd set up a capacity of 3,500 DWT at its shipbuilding facility. During the same five-year period, the capacity addition to the shipbuilding capacity of private sector was higher vis-a-vis the public sector.

The shipbuilding order book declined during 2013-14 to 2015-16, due to minimal new orders on account of persistent supply overhang and weak global trade. During 2011-12 to 2015-16, the bulk cargo segment accounted for the largest share in terms of capacity. Its share rose significantly in 2012-13, because RDEL's orders were reclassified from bulk cargo to dry cargo. The 'others' vessel category in the chart above also includes the vessel orders for clients engaged in the defence sector. Defence vessels are low on DWT (a metric more suited for commercial vessels) and usually have longer completion timelines, thus occupying the shipyards' capacities for a longer duration compared with commercial vessels. Between 2011-12 and 2015-16, the order book of public sector shipyards was lower than that of private sector shipyards due to the presence of defence vessels in their order book. However, order book execution of private shipyards remains uncertain on account of stressed financial position of major players like ABG Shipyard, RDEL and BDIL.

The public sector dominated the Indian shipbuilding industry up to 1999-00. However, following the opening up of the sector to private players, the industry has witnessed healthy growth in the order book. As per industry interactions, commercial vessels in the order book of private sector players have either been cancelled or put on hold. Additionally, the majority of ship orders for clients engaged in the defence sector are with public sector players. As of 2015-16, Indian shipbuilders had orders for 296 ships, totalling a tonnage capacity of 2.74 million DWT. Of these, 69 ships, with a combined capacity of 1.359 million DWT, were export orders.

In terms of DWT, domestic orders form a greater share of the public sector order book, while that of the private sector is evenly distributed between domestic and export orders. Considering the order book as of March 2016, the average tonnage per ship was higher for export orders compared with domestic orders. Although private sector companies received larger proportion of export orders compared with the public sector, these orders have been on the books for quite some time, and these players have not received any significant new export orders recently. The public sector was limited in its ability to take up large export orders with its capacities occupied primarily with defence orders. As on March 31, 2016, GSL is the only public sector company with export orders in its order book. As on March 31, 2016, RDEL and BDIL are the major players in the private sector with majority of their export orders in the dry and bulk cargo segments.

Warship building industry in India

Naval shipbuilding is a key segment of the Indian shipbuilding industry. It is characterised by value addition of 65% during construction of ships, which is contributed by ancillary industries such as steel producers, main engine builders, and equipment suppliers. Growth of the domestic shipbuilding sector, which imports 45% of its input requirement, can provide a major trigger for large-scale indigenisation of heavy-engineering products and ancillaries.

Traditionally, even as naval ancillary components have been acquired from outside India, the actual shipbuilding activity has been carried out indigenously. However, over the years, the government has focused on greater indigenisation of even defence equipment. The domestic shipbuilding industry primarily caters to two sub-segments: the Indian Navy and Indian Coast Guard. Currently, its fleet consists of aircraft carriers, amphibious transport dock, landing ship tanks, destroyers, frigates, nuclear-powered attack submarine, conventionally powered attack submarines, corvettes, mine countermeasure vessels (MCMVs), large offshore patrol vessels, fleet tankers and various auxiliary vessels and small patrol boats. The Indian Coast Guard’s fleet comprises patrol vessels, patrol boats, patrol craft and a hovercraft.

Review of government policies for shipbuilding industry in India

The government has taken some key initiatives to develop and promote the country’s shipbuilding industry. In December 2015, the Cabinet approved the new shipbuilding policy, which aims to provide financial assistance to shipbuilders and grant infrastructure status for the industry. The government has set aside Rs 40 billion to implement the scheme over 10 years.

Key features of the policy

• Grants financial assistance to both state-owned and private shipbuilders on each ship they build, except for smaller boats and fishing vessels.
• Quantum of financial assistance would be scaled down by three percentage points every three years, starting with 20% in first three years, 17% in next three, 14% in subsequent three years and 11% in the tenth year.
• Assistance will be given on contract or fair price, whichever is lower.
• Both state-owned and private yards will get assistance only after they construct and hand over a ship to its buyer.
• The right of first refusal is given to Indian shipyards for government purchases, implying that even if the shipyard is not the lowest bidder, an option is provided to the yard to match the lowest foreign bid and secure the contract.
• Grants infrastructure status to shipbuilding and ship-repair industry, thereby entitling it to various government incentives and tax benefits.

Review of government policies specific to defence shipbuilding industry in India

The Indian government has taken steps to encourage defence shipbuilding in the country. According to PIB, in June 2016, Foreign Direct Investment (FDI) Policy in defence sector has been reviewed. As per the updated policy, FDI of up to 49% is allowed under automatic route and above 49% under Government route wherever it is likely to result in access to modern technology or for other reasons to be recorded. To further the ease of process of approvals, the Government has abolished Foreign Investment Promotion Board (FIPB).Moreover, the government is working on Strategic Partnership Model for creating capacity in the private industry on a long term basis and a policy document shall be released shortly for selection of strategic partners. In line with the government’s vision of 'Make in India', Indian Navy has prepared a guideline document, titled ‘Indian Naval Indigenisation Plan (INIP), 2015-2030,’ to enunciate the need for developing various advanced systems for its platforms. This plan states that the domestic industry can play a vital role in meeting the sophisticated needs of the armed forces through cost-effective utilisation of its know-how and existing infrastructure, in pursuance of the government’s vision of ‘Make in India'. However, the following factors hinder the Indian shipbuilding sector from becoming competitive with foreign players: Equipment costs constitute 50-55% of shipbuilding cost. Indian shipbuilders import 65-70% of equipment, including steel, due to absence of ancillary companies manufacturing the equipment in the country. This increases the cost burden of the shipbuilders. Labour is another major cost, accounting for about 10-15% of total cost. Lower labour cost compared with China, South Korea and Japan could aid in increasing competitiveness ahead of greater indigenisation.

Modernisation programme for DPSUs

Currently, all major Indian warships and submarines under construction are being built in Indian shipyards. These include both DPSUs and private shipyards. MDL and GRSE are engaged in building complex weapon-intensive vessels such as destroyers, stealth frigates and corvettes. GSL and HSL have the capability to build various categories of vessels, such as patrol vessels, tankers, landing platform docks, survey vessels, tugs and barges. MDL is also constructing submarines for Indian Navy. The government has introduced a modernisation programme for DPSUs. Following are the provisions for each DPSU under the programme: Mazagon Dock Shipbuilders Ltd: has undertaken a modernisation programme at a cost of Rs 9 billion (of which Rs 8 billion was provided by Government of India and the rest from internal accrual). The modernisation included the following facilities:

• Module workshop with two 50T EOT crane and retractable roof designed for fabrication of large hull blocks, substantially pre-outfitted within a covered environment.

• Goliath crane with a capacity of 300 tonne with a span of 138 meter straddling over two slipways and the module shop.

• New wet basin equipped with about 27,000 sq. meters of area to accommodate two large frigates and two submarines for outfitting.

• Cradle assembly shop, used for fabrication and pre-outfitting of cradle structure in unit block assemblies. With the programme, MDL is aiming at a paradigm shift in warship construction, i.e., construction from unit assembly to block assembly, enabling integrated modular construction. This would substantially reduce the construction/building period. Post-modernisation, MDL capacity for ship building has increased from eight warships to 10 warships since 2014 and submarine capacity has increased from six submarines to 11 submarines since 2016. The submarine-building capacity has been further enhanced by construction of additional submarine section assembly workshop of 9,900 square meters. The workshop comprises of two bays, equipped with two levels of EOT Cranes as well as semi goliath cranes, which will facilitate fabrication as well as assembly of submarine units simultaneously.

A review of the Indian ship repairing industry

Size of the industry

According to a report published by the Ministry of Shipping at the India Maritime Summit 2016, the global ship repair market is estimated to be around USD 12 billion. Shipyards in Singapore, Bahrain, Dubai and Middle East account for a major share of this market. These locations have achieved a dominant position despite higher cost of ship repair services compared to other Asian countries, largely because of availability of skilled workforce and latest technology. This has helped these shipyards attract demand from other low-cost locations like India, Malaysia and Indonesia. The report also estimates Indian ship repair industry’s market potential to be around USD 1.5 billion (~ Rs 102 billion). Considering the earnings from ship repairs for all major shipyards in India (as per the Statistics of India’s Ship Building and Ship Repair Industry of 2015-16), the size of Indian ship repair industry in 2015-16 stood at Rs 9,434 million. Overall earnings significantly jumped in 2012-13 on the back of MDL’s high-ticket value orders, repairs and fabrication orders for offshore assets taken up by RDEL during the year. The segment grew at CAGR of 13.4% during 2011-12 to 2015-16, even as growth stagnated post 2013-14.

Ship repairing capacity

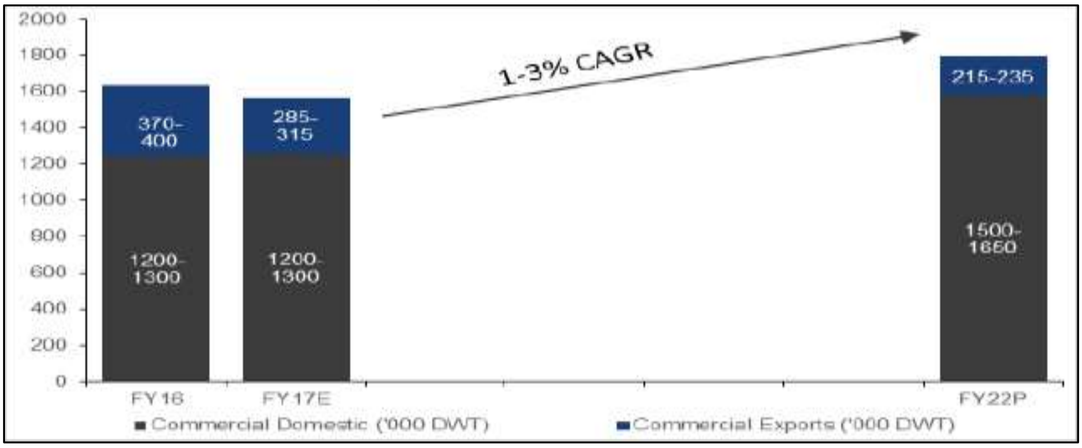
Ship repairing capacity of public sector shipyards remained fairly stable during 2011-12 to 2015-16. Private sector’s capacity improved on account of commencement of operations of two new shipyards, viz., Larsen & Toubro Ltd with 30,000 DWT and Sembmarine Kakinada with 54,000 DWT capacity. However, RDEL accounts for more than half of total ship repairing capacity available across Indian shipyards.

Dry dock and ship repairing facilities at major ports

Kandla, Mumbai, Mormugao, Cochin, V O Chidambaranar, Visakhapatnam, Paradip and Kolkata are the major ports in India. The Kolkata port has four dry docks; the rest have one each. The Mormugao and Visakhapatnam ports have eight workshops each, while the Paradip port has only one. In terms of dimensions, the Mumbai port is the largest. All major ports have cranes, except the V O Chidambaranar port; the Kolkata port has six cranes.

Indian commercial and warship building industry

India’s commercial order book to grow at a modest pace of 1-3% CAGR over next 5 years



Domestic commercial cargo order book to remain weak

In the past, the Indian commercial shipbuilding industry primarily catered to the dry bulk segment amongst cargo vessels. A majority of these orders were with private players such as ABG Shipyard. Sluggish demand and economic slowdown in 2013-14 resulted in cancellation of bulk carrier orders and piling up of inventory and work-in-progress (WIP), leaving companies in a state of financial distress.

Given the improved macroeconomic environment and increasing imports of coal and iron ore to China, fears of a depression in dry bulk segment's freight space over the next two years has subsided. This, coupled with increasing second-hand asset prices, will slowly improve new building demand as utilisation of existing assets keeps improving. This is expected to slowly add to the global commercial cargo shipbuilding order book. Major shipping companies like SCI and Great Eastern Shipping are currently taking advantage of low secondhand asset prices which will come into play as and when freight demand picks up. This will limit the new building demand even post-freight improvement. However, as demand picks up, orders are more likely to flow in to major shipyards in China, Japan and Korea, who are currently battling with underutilised capacities, and then trickle down to Indian shipyards. Thus, the domestic commercial cargo order book is expected to remain weak in the near term.

Domestic commercial non-cargo order book to pick up by 2021-22
Oversupply in the offshore segment is expected ease by 2021-22, with improvement in offshore rig utilisations, backed by improvement in E&P spending. However, offshore shipping companies, too, are taking advantage of low second-hand asset prices to improve their fleet composition, so they can cater to offshore demand when the market improves. The requirement of dredgers is expected to rise substantially, considering the government's emphasis on developing water transportation facilities in the country and improving the existing coastal movement, and it is expected to add to the existing capital and maintenance dredging requirements for major and minor ports in India. Historically, Indian yards have accounted for an insignificant contribution to the new dredgers market. However, with major players ramping up technological capabilities, orders for smaller dredgers are expected to flow in to domestic players' order books by 2021-22. With the improvement in vessel traffic at Indian ports, requirement for tugs and other port crafts are also expected to be substantial, further boosting the domestic non-cargo order book. Majority of orders for non-cargo vessels were historically catered to by private players like ABG Shipyard, BDIL, L&T, and RDEL. The uncertain business position of ABG Shipyard and BDIL has caused a downside risk to the non-cargo segment order book.

Defence shipbuilding order book to grow 8-10% CAGR over the next 5 years
Indian shipbuilding industry's order book is expected to receive a boost on account of Indian Navy and Coast Guard's ambitious ship acquisition plans- the forces plan to have fleets of 200 ships each till 2020-21. However, constrained capacities of the defence public sector undertakings and weak financial position of private players having defence shipbuilding licenses can prove to be an impediment to the execution of this plan. Ship orders from the navy are expected to have a larger share of this order book in terms of DWT, compared with the Indian Coast Guard. In case of the Indian Navy, the orders expected are: warship vessels like corvettes, submarines, etc. as well as patrol vessels and crafts. The category-wise vessel composition of both the Indian Navy and the Indian Coast Guard fleet is expected to remain constant over the next five years.

Other key drivers for the Indian ship repairing industry continue to look positive Strategic positional advantage
India's strategic position along the east bound and west bound international trade routes offers an opportunity to cater to vessels plying on these routes. A main container route connecting America and Europe to the East passes very close to the Indian coastline, presenting a major opportunity for repairs

Capacity additions
• The Ministry of Shipping had announced Rs 2.7 billion financial aid for the development and modernisation of Cochin Shipyard Ltd in 2014. Of this, Rs 1.2 billion will be used for setting up a new dry dock yard. It is in the process of adding one more dry dock of size 310 x 75/60 x 13 M. This large dry dock will also enable it to undertake repairs of vessels such as LNG carriers, semi-submersibles, jack up rigs, drill ships, etc.
• Full commissioning of the international ship repair facility at Cochin port with state of the art facilities will enable positioning of Cochin as a major ship repair hub. This is targeted to enhance Cochin Shipyard's ship repair capability by 70-90 ships per annum.
• Phase 3 and 4 of development - expansion and upgradation of infrastructure at Goa Shipyard Ltd – are under progress. This is expected to enhance its capabilities for defence ship repair.
• The construction of floating dry dock facility at V O Chidambaranar port is in the feasibility study phase. This will enhance its capacity to carry out underwater repairs of tugs, launch boats and other watercrafts.
• The project to modernise ship repairing facilities at Kolkata dock is expected to improve its capabilities to service both Indian and foreign vessels. The project is still in the planning stages.
• There is a proposal underway for refurbishment of the existing Hughes dry dock at Mumbai port. This project aims at providing adequate wet berth facilities to complement dry docks to cater to afloat repairs.
• In order to create adequate dry docking facilities and maintenance capacities for vessels plying through Andaman and Nicobar waters, a project to create a ship repair facility(ship lift/slipway) capable of handling 5000 DWT vessels is underway, and is in the pre-feasibility stage (Source: Maritime India Summit 2016: Advantage Maritime India document)

Diversification from core ship building business
The slowdown in commercial ship building is expected to drive Indian shipyards to an increased focus towards ship repairs to keep their capacities utilised.

Tax exemptions

With service tax and excise duty exemptions granted for ship repairs, Indian shipyards will now be able to better compete with major ship repair yards in Colombo, Dubai, Oman, Singapore, and China. This should bring in additional revenue from foreign vessels carrying cargo to Indian ports over the next five years.

Increased vessel traffic due to Sagarmala project

As per the national perspective plan of Sagarmala project, coastal and inland waterways traffic is expected to shoot up 15 times over the next 20 years. Similarly, capacity augmentation is expected to result in a five times rise in traffic capacity, from the existing 350 million tonnes. This is expected to bring in additional ship repair business.

Defence repair orders

A major boost is expected to come from defence (Navy and Coast Guard) refitting and modernisation initiatives, which will increase the average repair revenue. Moreover, the indigenisation plan is expected to encourage all sectors of the industry to come forward and participate in indigenous development of weapons, sensors, and other high end equipment for the Indian Navy, which will further improve repair and maintenance revenue in the long run.

Key Concerns:

- The continuing effect of the COVID-19 pandemic on business and operations is highly uncertain and cannot be predicted.
- MDSL predominantly depend on the MoD for defence orders and has mostly been awarded such orders on a nomination basis by the MoD for use by the Indian Navy. There is no assurance that future defence orders will be awarded to it by the MoD.
- Imposition of liquidated damages and invocation of performance bank guarantees / indemnity bonds by the customers could impact results of operations
- Any decline, delay or reprioritisation of funding under the Indian defence budget or that of customers including the MoD for use by the Indian Navy could adversely affect MDSL’s ability to grow or maintain its sales, earnings, and cash flow.
- MDSL or its technical collaborators may engage in certain transactions in or with countries or persons that are subject to U.S. and other sanctions.
- Revenues from the MoD contracts including the submarine refit contracts are subject to the satisfaction of certain milestones and are subject to termination. Its inability to fund such contracts at the time of inception or any termination of any of its contracts with the MoD could have a material adverse effect on its financial condition and results of operations.
- Any delays in procurement, nomination or any other decision – making by MDSL’s customer and collaborators may result in time and cost overruns in completion of its shipbuilding and submarine projects, which may have an adverse effect on the business, financial condition and results of operations.
- Future growth and expansion is limited by the location at which MDSL operate.
- MDSL may be subject to penalties in the event it is unable to justify the alleged non-compliance with respect to the Mazdock Modernisation project.
- MDSL’s future growth and expansion is limited by its current infrastructure.
- Earnings and margins may vary based on the mix of contracts and programs, performance, and MDSL’s ability to control costs.
- There are outstanding legal and tax proceedings involving the Company and Directors. Any adverse decision in such proceedings may expose MDSL to liabilities or penalties and may adversely affect the business, financial condition, results of operations and cash flows.
- Any failure to comply with the provisions of the MoD contracts could have an adverse effect on the business operations, financial conditions and results of operations.
- MDSL’s entire business operations are based out of a single yard at Mumbai. The loss of, destruction, or shutdown of, operations at its shipyard in Mumbai will have a material adverse effect on its business, financial condition and results of operations.

- MDSL is subject to a number of procurement rules and regulations of the MoD regulations and other rules and regulations. Its business and its reputation could be adversely affected if it fails to comply with applicable rules.

- The interests of the GoI as MDSL's controlling shareholder may conflict with interests as a shareholder. The GoI has significant influence over its actions and can issue directives with respect to the conduct of its business or its affairs. Any change in GoI policy or goodwill could have a material adverse effect on the financial condition and results of operations.

- MDSL incur additional expenditure due to siltation at the waterfront surrounding its Company.

- MDSL is subject to extensive government regulation and require certain approvals and licenses in the ordinary course of business, and the failure to obtain, maintain or renew them in a timely manner may materially adversely affect the operations.

- Current Order Book may not necessarily translate into future income in its entirety. Some of its current orders may be modified, cancelled, delayed, put on hold or not fully paid for by its customers, which could adversely affect the results of operations.

- The manufacturing processes for MDSL's products are complex and involve some hazards.

- MDSL is dependent on the MbPT for certain basic services required for daily operations. Further, if its relationship with the MbPT is negatively affected in any manner or if the MbPT is unable to provide these services in the future, it may have an adverse impact on its operations.

- MDSL is subject to stringent labour laws and its workmen are unionised under a number of trade unions. Any labour disputes or unrests could lead to lost production, increased costs or delays which could lead to penalties.

- MDSL commence execution of its shipbuilding and submarine construction contracts prior to finalization of the design and specifications for its ships and submarines. Delays in finalization of the design and specifications of its shipbuilding and submarine construction projects or any modifications thereto may have a material adverse effect on its business, financial condition and the results of operations.

- Dependency on suppliers for timely delivery of raw materials, equipment and components and non – adherence to the agreed timelines may adversely affect the delivery timelines

- Highly dependent on the expertise of key managerial personnel and its skilled workforce and management for its operations. Inability to retain such workforce or replace such management may have an adverse effect on the business, financial condition and the results of operations

- Damage to the information technology equipment may adversely affect MDSL's ability to access its back – up information critical for its business on a timely basis which may cause an adverse effect on the business, financial condition and the results of operations.

- Financing agreement contains certain restrictive covenants for certain activities that limit the company's flexibility in operating business.

- High dependency on foreign sources for equipment, weapons, sensors and propulsion systems

- MDSL may face claims and incur additional rectification costs for defects and warranties in respect of its vessels which could have a negative impact on its business, financial condition and results of operations.

- Shipbuilding and submarine – building expose MDSL to potential liabilities that may not be covered by insurance.

- MDSL face the risk of unsatisfactory quality of work performed by its subcontractors which could result in a negative impact on its business, reputation, financial condition and results of operations.

- MDSL's business is expected to become more diversified and its historical results of operations may not be indicative of its future performance. Failure to successfully implement its new business model, execute its new business strategies or develop new business may materially and adversely affect the business, financial condition, results of operations and prospects.

- MDSL is subject to risks arising from currency exchange rate fluctuations, which could adversely affect the business, financial condition and results of operations.

- MDSL is subject to compulsory expropriation by the GoI of any critical technology developed by it which may have an adverse effect on the business, financial condition and results of operations.
- If MDSL is unable to establish and maintain an effective system of internal controls and compliances, its business and reputation could be adversely affected
- Business is substantially affected by prevailing economic, political and other prevailing conditions in India.
- Foreign investors are subject to foreign investment restrictions under Indian law, which may adversely affect the market price of MDSL's Equity Shares.

Balance Sheet

Particulars (Rs in Million)	FY20	FY19	FY18	FY17
Non-current assets				
Property, plant and equipment	8312.5	7873.2	6769.1	5440.5
Capital work-in-progress	799.61	887.7	853.8	984.3
Other intangible assets	171.5	229.9	284.1	213.5
Financial Assets				
Investments	4841.8	4306.7	4291.5	3835.9
Trade receivable	156.1	157.8	159.3	160.5
Loans	68.9	66.6	89.5	87.0
Other financial assets	1534.5	1435.2	34.0	34.0
Deferred tax assets (net)	4116.6	5819.8	5521.7	5068.3
Non-current tax assets (net)	2259.3	1933.8	2067.3	1811.3
Other non-current assets	6517.5	4990.1	3195.2	1388.1
Total Non Current Assets	**28778.3**	**27700.8**	**23265.5**	**19023.4**
Current assets				
Inventories	46226.9	37,903.03	37,859.69	40,286.56
Financial Asset				
Trade receivables	14587.7	14728.9	11133.8	8117.0
Cash and cash equivalents	4832.8	7296.8	3735.9	1428.8
Bank Balances other than Cash and Cash Equivalents	53150.0	67400.0	68160.0	82200.0
Loans	21.1	42.9	9.1	10.2
Others	1781.0	2213.0	1105.4	1476.7
Contract assets	554.7	9013.1	7379.4	11632.4
Assets held for sale	2.2	20.7	0.1	0.2
Other current assets	59725.6	42160.2	41055.0	29736.4
Total current Assets	**180882.0**	**180778.6**	**170438.2**	**174888.2**
Total Assets	**209660.3**	**208479.3**	**193703.7**	**193911.7**
EQUITY AND LIABILITIES				
Equity				
Equity share capital	2016.9	2241.0	2241.0	2490.0
Other Equity	28674.4	29928.2	26099.5	27411.5
Total Equity	**30691.3**	**32169.2**	**28340.5**	**29901.5**
Non-current liabilities				
Financial liabilities				
Trade payables	156.1	157.8	159.3	160.5
Others	360.1	355.3	372.7	385.5
Other long-term liabilities	1694.6	1578.4	1597.4	1669.5
Long-term provisions	12150.7	11977.6	12063.7	12121.1
Total Non current liabilities	**14361.5**	**14069.0**	**14193.0**	**14336.6**
Current liabilities				
Trade payables				
Total outstanding dues to micro enterprises and small enterprises	200.7	186.8	134.2	131.6
Others outstanding dues	47507.2	28985.7	23776.5	9131.8

Others	1364.6	2367.0	2578.7	1747.1
Contract liability	113831.2	129499.4	123380.8	137595.6
Other current liabilities	436.3	220.6	98.8	251.1
Short-term provisions	1267.6	981.7	1201.2	816.3
Total Current Liabilities	**164607.5**	**162241.1**	**151170.2**	**149673.6**
Total Liabilities	**178969.0**	**176310.2**	**165363.2**	**164010.2**
Total Equity and Liabilities	**209660.3**	**208479.3**	**193703.7**	**193911.7**

Profit & Loss

Particulars (Rs in Million)	FY20	FY19	FY18	FY17
Revenue from Operations	49776.5	46139.6	44703.6	35190.8
Other Income	5576.6	5907.2	5572.7	7557.8
Total Income	**55353.1**	**52046.7**	**50276.3**	**42748.6**
Total Expenditure	**47096.8**	**43531.6**	**43156.6**	**33933.4**
Cost of materials consumed	25031.7	25571.2	26928.9	21400.8
Procurement of base and depot spares	3622.3	6080.5	917.2	348.7
Sub-contract	7440.9	1759.1	3227.0	1101.9
Employee benefits expense	7929.3	6894.7	8857.0	7288.4
Power and fuel	165.2	192.6	226.2	260.4
Other expenses	2520.9	2644.6	2808.1	2941.0
Provisions	386.5	388.9	192.2	592.2
PBIDT	**8256.3**	**8515.2**	**7119.7**	**8815.2**
Interest	92.6	90.8	90.8	93.1
PBDT	**8163.6**	**8424.4**	**7028.9**	**8722.1**
Depreciation	686.8	643.3	524.8	416.6
PBT	**7476.9**	**7781.1**	**6504.1**	**8305.5**
Exceptional items	123.2	0.0	0.0	0.0
Tax (incl. DT & FBT)	**3516.8**	**3077.3**	**2568.3**	**2877.2**
Tax	1804.3	3321.1	2915.2	2930.7
Adjustment of tax relating to earlier years	9.3	54.3	106.4	0.0
Deferred Tax	1703.2	-298.1	-453.3	-53.5
Reported Profit After Tax	**3836.9**	**4703.8**	**3935.7**	**5428.3**
Share of Profit /(loss) in Associates	933.7	620.9	1026.0	554.3
Adj.PAT	**4770.6**	**5324.7**	**4961.7**	**5982.6**
EPS (Rs.)	23.7	23.8	22.1	24.0
Equity	2016.9	2241.0	2241.0	2490.0
Face Value	10.0	10.0	10.0	10.0
OPM (%)	5.4	5.7	3.5	3.6
PATM (%)	9.6	11.5	11.1	17.0

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