

## Recommendation

**SUBSCRIBE**

## Issue Details

Face Value:	₹10
Public Issue	~57.64 lakh Shares
Employee Reservation	20,000 Shares
Price Band* :	₹270-275
Issue Size#	~₹156 Cr
Bid lot	50 Equity shares
Issue Type:	100% Book building

Post Issue Market Cap#: ~₹571 Cr; Note: # - at upper band, \* retail and employee discount of Rs12

% Shareholding	Pre IPO	Post IPO
Promoter	88.5	63.9
Public	11.5	36.1

Source: RHP

Share Reservation	% of Issue
QIB	50
NII	15
Retail	35

## Company Management

Mr. Karunakar Reddy Baddam	MD
Mr. Sudarshan Chiluveru	CFO

## Issue Managers

BRLMs	Aryaman Financial Services Ltd.
Registrar	Bigshare Services Pvt. Ltd.

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## Company Overview

Apollo Micro Systems (AMS) designs, manufactures and supplies electronic and electro-mechanical solutions. It caters to defence, space, transport and home land security for Ministry of Defence, Govt. controlled Public Sector Undertakings (PSUs) and private sector. It has participated in several indigenous missile programmes, underwater electronic warfare and underwater missiles amongst others. The defence system supplies are classified into On-Board Systems (on Weapon or Vehicle) and Ground support (associated or communicates with On-Board) equipment. AMS' key products include defence avionics systems, defence naval systems, defence aerospace systems and satellite space systems.

## Offer Details

The offer consists of Fresh Issue of 5.8mn shares (aggregating up to ~₹156cr) at the upper end of the price band. A discount of ₹12 is offered for eligible employees (20,000 shares reservation) and retail investors. The proceeds will be used for working capital (WC) requirements (~₹119cr) and general corporate purposes (~₹37cr).

## Our View

We believe that AMS' execution capabilities and ability to develop new technologies are visible in its 54% revenue CAGR over FY13-17. AMS is well placed to capitalize on both defence and non-defence opportunities that are on the anvil led by various Government initiatives. The proceeds should fund the WC requirements for AMS. At the upper price band, the company commands PE multiple of 32.2x on FY17E EPS (post dilution). This is, in-line with other defence sector companies i.e. – BEL and Astra Microwave. Considering the high traction expected in the defense sector for AMS, we recommend SUBSCRIBE on the issue.

## Financial Summary

Standalone ₹cr.	FY14	FY15	FY16	FY17	1HFY18
Revenue	73	108	159	211	109
EBITDA Margin (%)	13.9	16.7	15.9	19.2	17.7
Adj. PAT	5	7	10	18	7
EPS (₹)*	2.6	3.6	4.8	8.5	3.4
P/E*	107.1	76.7	57.1	32.2	--
P/BV*	20.8	16.4	12.7	9.0	--
EV/EBITDA*	59.6	34.6	25.2	16.0	--
RONW (%)*	24.8	23.9	25.1	32.8	--

Source: Company, IIFL Research; \*EPS & Ratios at higher end of the price band, on post IPO shares

## Key Points

### Proven track record and R&D capabilities

The company's participation in several defence, ships and space programmes and proven track record of order execution have given it a competitive edge. The company enjoys strong brand equity on account of its longstanding presence and continuous improvement and adoption of technologies. The company has been able to do so via continuous investments in product research and development. We believe that its association with Ministry of Defence and other Govt. PSU programmes should enable it to garner larger repeat orders.

### Government measures provide support to revenue outlook

As per the RHP, defense expenditure in India is expected to increase and currently, 60% of India's defence requirements are met through imports. ESDM (Electronic System, Design and Manufacturing) sector in India too relies heavily on imports. Govt's 'Make in India' initiative aims to achieve 70% indigenization, and the Defence Offset policy will involve private participation, especially at the MSME level. This, along with non-defence opportunities arising out of the Digital India program, would provide ample opportunities for AMS.

### Plans to capitalize on build to print (BTP) opportunity in defence

In BTP business, the customer provides work instructions, assembly drawings, etc., which is used in building its parts along with the specification of component's functional requirements. Apollo has established BTP business vertical with existing infrastructure and skills sets. This vertical has helped in generating incremental revenue and profits with low working capital cycle. Thus, the company expects BTP to be a strong revenue driver in the defence electronics space.

## Key Risks

### High dependence on PSUs and Government entities

The company has significant dependence on various PSUs and Government entities for projects. Change in Government's stance on defence policies could adversely affect its financials.

### Working capital intensive business

Delay in receipts of dues and high advance payment requirements may put stress on the balance sheet.

## Recommendation Parameters for Fundamental/Technical Reports:

- Buy – Absolute return of over +10%
- Accumulate – Absolute return between 0% to +10%
- Reduce – Absolute return between 0% to -10%
- Sell – Absolute return below -10%

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