## Investment Summary:

We recommend **C2C Advanced Systems Limited (NSE:C2C),** a **₹776Cr.** market cap SME in Aerospace & Défense Industry, trading at **18.17 P/E** vs *Industry Median* **59.08 P/E.** The company's focused domain expertise, coupled with below average pricing, **40%+** Operating Margins and **26% ROCE,** support a long-term thesis of delivering 20% IRR over 5 years, driven by earnings growth, increasing scale and multiple expansion.

## Business Overview:

- The company generates revenue through project-based contracts involving design, development, integration and deployment of defense software and electronics, across C4I Systems, AI/ML driven analytics and embedded hardware-software solutions.
- The profit pool is concentrated in high-value software, system integration and proprietary IP-led solutions which deliver **higher margins** and capital efficiency in comparison to its larger peers which are pure hardware vendors.
- It differentiates itself in the industry by following a vertically integrated, software-first business model which makes it a niche, solutions provider and not a commoditised defence electronics supplier, thus enjoying low threat of substitutes and high barriers to entry.

## Market Mispricing and Value Creation Drivers:

- The market is mispricing the high receivable days as poor collection system, but it should be noted that **Debtor Days** have more than halved from **1048 days** to **349 days** and is supposed to fall further to 270 days as Management quotes in their Concall, **"there's no bad debt".**
- Major driver of Receivables is a first-time NATO-linked contract with milestone-based payments and other specific collections from a USD client impacted by tariffs and a phased bill payment from the Malaysian Navy. All of these pending accounts will be closed and collections will look healthier by 31st March, as per management commentary.
- **FY25 sales jumped 180% YoY** to **₹117.46Cr.** while **PAT rose 135%** YoY to **₹28.83 Cr. EPS** has also expanded from **₹15.85** to **₹21.07.**
- Margin expansion on the back of greater revenue share of proprietary IP **(Current: 30%, Target: 50%),** on top of being largely debt-free for short term capital needs. Thus, we are looking at consistent monthly free cash flow from 2027 onwards, when current capex build-up pays off.
- Strong order book (Overseas: **~$7mn**, Domestic: **~₹100Cr.**) and live proposals/bids cited at **₹1144 crores** with 30% expected conversion.

## Catalysts:

- Low threat of new entrants due to long qualification cycles (2-3 years) and low threat of new substitutes as it is the only provider of full-stack C5ISR and has low competition , with foreign systems restricted on grounds of geopolitics and cost.
- A strong target set by Ministry of Defense to reach **₹50,000Cr.** In defense exports by **2029** places C2C in a very good position to leverage the growing export momentum of the defense sector, considering **93%** of its revenue comes from overseas sales.
- India's deepening defense ties with the US through the **Security of Supply Arrangements (SOSA)** can improve defense trade flows, knowledge sharing, joint operations and other scopes of interoperability, creating new opportunities for C2C.

## Key Risks:

**Risk 1:** High build up of receivables and inventory signalling poor working capital management.
**Mitigation:** Collections are expected to improve as payments worth ₹160crore are expected to be received by end of this fiscal.

**Risk 2:** Payment cycles in India inherently favour foreign OEMs with sovereign letter of credit while domestic vendors have to wait 9–15 months for payments which are tied with obligations like 5% performance bond and 10% retention.
**Mitigation:** The company has aggressively expanded its foreign portfolio of customers, increasing its share to 93% of overall sales. This has not only reduced payment cycles but also created 2 more strategic benefits for the company:
**A.** It is now exposed to a wider market with greater competition from global players like Lockheed Martin, Saab etc. This automatically pushes the firm to achieve higher quality of equipment manufacturing and deployment.
**B.** Balances against foreign exchange risk since a major portion of its components and spare parts are imported.

**Risk 3:** GTM cost per geography is quite high for defense companies and may not guarantee success, thus curtailing scalability.
**Mitigation:** C2C mitigates high global GTM costs by avoiding sales-led expansion and instead focuses on reference-first and platform-driven procurement like its MAGI C5ISR systems which acts as a repeatable software core that can minimise marginal GTM cost, improving scalability.