TURKISH EQUITIES / COMPANY UPDATE

Aselsan

Power of “defensive” growth

We are transferring our coverage of ASELSAN with “Outperform” rating and a 12-month TP of TRY102.00/share, offering 50% upside potential. So far in 2024, the Company has won a slew of new contracts worth USD3.2bn, USD535mn of which being directly or indirectly from international customers, boosting the backlog to USD12.6bn. Regarding only 4Q24, the company reported USD600 million in new contracts, of which USD260 million came from foreign customers. With a constructive outlook for the defense sector amid increasing regional tensions, earnings momentum should be intact in both the long and short-term, making us believe that the current risk-reward trade-off is enticing for investors. Additionally, the growing proportion of defense spending in Türkiye’s budget as well as the NATO's 2%– defense spendings/GDP requirement will continue to give the Company a steady, consistent, and long-term source of revenue. We are forecasting 46% growth in 2025F, after closing 2024 with 53% growth at the top-line, attributable to our expectation of a higher defense budged at home and higher ASELSAN market share in the industry. In the longer-term, the 4 new investments namely, 1) Photon Detector and Nanotechnology Facility, 2) EO FLIR Systems Production Facility, 3) Defense System Technologies Production and Testing Facility ve 4) Radar System Integration and Production Automation Center, which will be ready in the upcoming years, and monetization and capitalization of the R&D investments and international expansion will be the key drivers of the 10.1% USD-terms 5-yr revenue CAGR assumption. As far as operational profitability is concerned, we expect the IAS-29 EBITDA margin to reach 22.4%, and 24.2% (2023: 21.8%) in 2024 and 2025 respectively. On the negatives, even while this allows the company to access low-cost state funding for projects and tax advantages, we anticipate increased financial expenses that will negatively impact the bottom line. Additionally, the heavy CAPEX period for the new investments and the high WC requirement will be FCF dilutive. The stock trades at an EV/EBITDA of 14.0x and 8.9x on our YE24 and YE25 forecasts, implying a 10% and 38% discount to its global peers. With its discounted valuation and solid growth prospects on its better sales mix and margin expansion, we transfer our Coverage with “Outperform” rating.

New contracts keep coming in, book-to-bill ratio to remain high… New contacts in 9M24 amounted to USD3.2bn, with a non-IAS29 book-to-bill ratio of 1.5x, lower than 2023 level of 2.0 but higher than the 5-year average of 1.1x, showing demand is intact, with the all-time-high backlog of USD12.6bn. Regional tensions will serve as the medium-term driver of our forecasts followed by development and serial production projects support, planned investments (air defence systems and guidance kits) and, most importantly, a higher annual defence budget as set out in the Medium Term Plan with a 58% rise over the next 5 years in USD-terms, which will support growth in the mid to long-term. Accordingly, we are forecasting a TRY 5-yr nominal revenue CAGR of 10.1% in USD-terms.

EBITDA margin has surged above historical averages on a more value-added mix: The company’s EBITDA margin is forecasted to end the year with 22.4% level vs. its 10-year average of 21.2%, thanks to a more value-added sales mix and strong order book and capitalization of investments, despite being hurt by strong TRY and high inflation as a net FX earner with TRY-heavy expenditure structure. We expect the current situation to persist in the last quarter of 2024, and forecast a 2024 gross margin of 27.0%, with the OPEX-to-Sales ratio easing to 9.0%, representing a YE24 analyst IAS-29 EBITDA margin of 22.4%. In 2025, we predict a robust TRY trajectory; but, a milder one compared to 2024. As a result, our assumptions will more clearly show the margin improvement brought about by the shift in the sales mix, declining R&D costs in OPEX, growing exports, and lower raw material costs.

Discounted amongst global peers, even though operational profitability metrics are significantly higher than the average industrial metrics… Based on 2024E and 2025E prospective earnings, the stock trades at an EV/EBITDA of 14.0x and 8.9x and the multiple levels imply an average of 10% and 38% discounts to its global peers, respectively. Since ASELSAN's 2025E EBITDA margin is the second highest among its worldwide peers in terms of profitability with its 82% hard currency denominated backlog and rising Türkiye’s dominance in global defence industry, we believe that the current discount is not justified and we transfer our Coverage with “Outperform” rating.

14 November 2024

Outperform

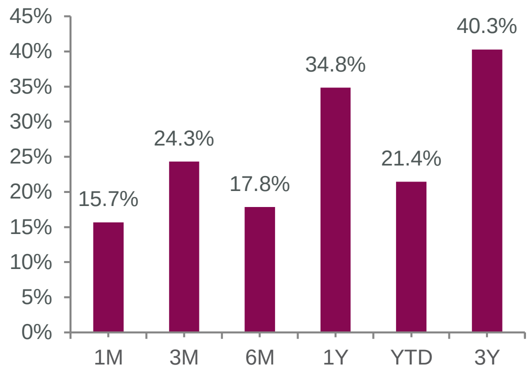
(Transfer of Coverage)

Close Price: TRY 68.00
12M Target Price: TRY102.00
Upside Potential: 50%

Stock data

Bloomberg / Reuters	ASELS TI / ASELS.IS
Mcap (US$mn)	9,037
EV (US$mn)	9,910
Avg. Trd. Vol. (US$mn)	56.8
Free float	26%

Relative Performance to BIST100



Key Data (TRYmn)	2023	R.2023	2024E	R.2024	2025E
Revenues	73,593	104,053	112,825	139,482	165,619
Growth	*69%*		*58%*		*49%*
EBITDA	16,190	22,661	24,902	31,181	39,127
Growth	*71%*		*54%*		*57%*
Net Profit	7,290	10,308	10,247	12,668	14,987
Growth	*469%*		*41%*		*46%*
P/E (x)	21.2		30.3		20.7
EV/EBITDA (x)	10.8		14.0		8.9
P/BV (x)	1.3		2.4		2.1
FCF yield (%)	4%		-1%		1%
Div. yield (%)	0.3%		0.2%		0.3%

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Figure 1 – Summary financials & key metrics (TRYmn)

Income Statement (TLmn)	2023	Restated 2023	2024E	Restated 2024E	2025E
Revenues	**73,593**	**104,053**	**112,825**	**139,482**	**165,619**
Gross Profit	**20,105**	**28,427**	**30,431**	**37,621**	**46,504**
EBITDA	**16,027**	**22,661**	**25,222**	**31,181**	**40,032**
Depreciation	3,402	4,810	4,945	6,113	8,103
EBIT	**12,625**	**17,851**	**20,277**	**25,068**	**31,929**
Net other income	12,349	17,460	2,595	3,208	5,797
Income from investing activities	34	49	53	66	67
Net financial income	-17,797	-25,163	-20,172	-24,938	-22,662
Profit from associates	-1	-2	-2	-3	-3
PBT	**7,210**	**10,194**	**2,751**	**3,401**	**15,128**
Taxes Paid	1,129	1,597	0	0	0
Minority Interest	84	118	113	140	141
Net Profit/(Loss)	**7,290**	**10,308**	**10,247**	**12,668**	**14,987**

Balance Sheet (TLmn)	2023	Restated 2023	2024E	Restated 2024E	2025E
Current assets	**99,020**	**112,242**	**127,685**	**157,852**	**183,574**
Cash equivalents	8,980	10,180	5,254	6,495	12,710
Trade receivables	27,978	31,714	39,257	48,532	54,450
Inventories	43,715	49,552	55,757	68,930	78,322
Other current assets	18,347	20,797	27,417	33,894	38,092
Non-current assets	**105,555**	**119,650**	**131,217**	**162,219**	**155,714**
Tangibles	32,239	36,544	27,439	33,922	30,929
Intangibles	16,504	18,708	16,451	20,338	21,438
Other non-current assets	56,812	64,398	87,327	107,959	103,346
Total assets	**204,576**	**231,892**	**258,902**	**320,071**	**339,288**
Current liabilities	**68,173**	**77,276**	**98,706**	**122,026**	**150,901**
Short-term loans	25,553	28,965	43,568	53,862	52,282
Trade payables	20,194	22,891	30,767	38,037	45,621
Other current liabilities	22,425	25,420	24,370	30,128	52,998
Non-current liabilities	**16,329**	**18,509**	**28,716**	**35,500**	**40,867**
Long-term financial loans	1,535	1,740	4,797	5,930	5,756
Other non-current liabilities	14,794	16,770	23,919	29,570	35,111
Minority Interest	0	0	0	0	0
Shareholders' Equity	**120,074**	**136,107**	**131,480**	**162,544**	**147,520**
Total liabilities and equity	**204,576**	**231,892**	**258,902**	**320,071**	**339,288**

Key metrics	2023	2024E TRY Real	2024E	2025E TRY Real	2025E
Growth					
Revenue growth	10%	8%	53%	19%	47%
EBITDA growth	14%	11%	57%	28%	59%
Net income growth	469%	-1%	41%	18%	46%
Profitability					
Gross Margin	27.3%	27.3%	27.0%	27.0%	28.1%
EBITDA margin	21.8%	21.8%	22.4%	22.4%	24.2%
Net margin	9.9%	9.9%	9.1%	9.1%	9.0%
Return on assets (ROA)	4.2%	5.3%	4.4%	4.7%	4.9%
Return on equity (ROE)	7.3%	9.2%	7.9%	8.8%	10.2%
Return on cap. emp. (ROCE)	6.4%	7.9%	6.5%	6.9%	7.7%
Leverage					
Net Debt	18,107	25,602	43,111	53,296	45,328
Net debt / Equity	0.2	0.2	0.3	0.3	0.3
Net debt / EBITDA	1.1	1.1	1.7	1.7	1.1
EBIT Interest coverage	0.7	0.8	0.7	0.7	1.0
Efficiency					
Total asset turnover	0.4	0.4	0.4	0.4	0.5
Equity turnover	0.6	0.8	0.9	0.9	1.1
WC/Sales	42%	42%	64%	64%	60%
Opex/Sales	10.2%	12.8%	9.0%	14.0%	8.8%

Cash Flow (TLmn)	2023	Restated 2023	2024E	Restated 2024E	2025E
EBITDA	16,190	22,891	24,902	30,786	39,127
Change in working capital	1,832	2,591	15,073	18,634	19,972
Taxes (EBIT x 25%)	1,129	1,597	0	0	0
Capital Expenditures	6,875	9,721	11,862	14,665	16,784
Adjustment	0	0	0	0	0
FCFF	6,353	8,983	-2,033	-2,513	2,370

Source: QNBI Calculations

INVESTMENT THEME

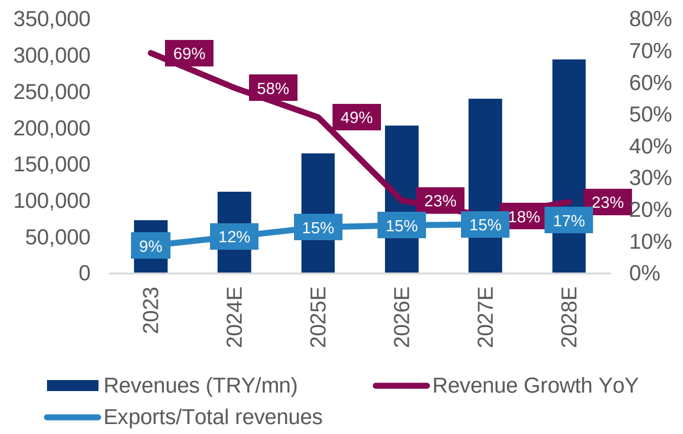
We are transferring our coverage of ASELSAN with "Outperform" rating and a 12-month TP of TRY102.00/share, offering 50% upside potential. So far in 2024, the Company has won a slew of new contracts worth USD3.2bn, USD535mn of which being directly or indirectly from international customers, boosting the backlog to USD12.6bn. Regarding only 4Q24, the company reported USD600 million in new contracts, of which USD260 million came from foreign customers. With a constructive outlook for the defense sector amid increasing regional tensions, earnings momentum should be intact in both the long and short-term, making us believe that the current risk-reward trade-off is enticing for investors. Additionally, the growing proportion of defense spending in Türkiye's budget as well as the NATO's 2%–defense spendings/GDP requirement will continue to give the Company a steady, consistent, and long-term source of revenue growth. We are forecasting 46% growth in 2025F, after closing 2024 with 53% growth at the top-line, attributable to our expectation of a higher defense budged at home and higher ASELSAN market share in the industry. In the longer-term, the 4 new investments namely, 1) Photon Detector and Nanotechnology Facility, 2) EO FLIR Systems Production Facility, 3) Defense System Technologies Production and Testing Facility ve 4) Radar System Integration and Production Automation Center, which will be ready in the upcoming years, and monetization and capitalization of the R&D investments and international expansion will be the key drivers of the 10.1% USD-terms 5-yr revenue CAGR assumption. As far as operational profitability is concerned, we expect the IAS-29 EBITDA margin to reach 22.4%, and 24.2% (2023: 21.8%) in 2024 and 2025 respectively. On the negatives, even while this allows the company to access low-cost state funding for projects and tax advantages, we anticipate increased financial expenses that will negatively impact the bottom line. Additionally, the heavy CAPEX period for the new investments and the high WC requirement will be FCF dilutive. The stock trades at an EV/EBITDA of 14.0x and 8.9x on our non-IAS YE24 and YE25 forecasts, implying a 10% and 38% discount to its global peers. With its discounted valuation and solid growth prospects on its better sales mix and margin expansion, we transfer our Coverage with "Outperform" rating.

New contracts keep coming in, book-to-bill ratio to remain high… New contacts as of September 30th, 2024 have amounted USD3.2bn, with a non-IAS29 book-to-bill ratio of 1.5x, lower than the 2023 level of 2.0 but higher than the 5-year average of 1.1x, demonstrating that demand remains robust with an all-time-high backlog of USD12.6bn. Regional tensions are the medium-term driver of our forecasts, followed by the development and serial production projects support, planned investments, especially in air defense systems and guidance kits, and most importantly, a higher defense budget as set out in the Medium Term Plan, which has a 5-yr USD CAGR of 4%, will support growth in the mid to long-term. Accordingly, we forecast a 5-yr nominal USD revenue CAGR of 10.1%. So far in 4Q24, around USD600mn of new orders have come in, mainly from the Turkish Armed Forces and international clients in the Asia Pacific region. As the 2024 draws to a close, we are expecting the pace of new contracts to gain pace, albeit as a result of elevated regional conflicts such as the Israel-Hamas and Russia-Ukraine wars, while we forecast USD1.5bn of contracts in 4Q24E, pushing total new contracts for 2024 to USD4.7bn. We believe the Company will operate in a more productive environment, not just to receive new contracts but also in terms of deliveries. Accordingly, we expect a higher-than-average book-to-bill ratio for 2024E before easing gradually with the production optimization throughout the years. We forecast a 1.4x IAS29 book-to-bill ratio (non-IAS29: 2.0) for 2024E (currently IAS29 at 1.5x) down from the IAS29 ratio of 1.6x in 2023.

Regarding exports, we are confident that ASELSAN's recent technological advancements have improved the company's standing in the global defense industry and bolstered its competitiveness on a global scale. We have seen an increase in interest from Asia-Pacific nations so far in 2024, particularly following the SAHA EXPO in Istanbul. We therefore anticipate an increase in the proportion of exports in total revenues from 12% in 2024E to 15% in 2025 and 17% in 2030. As far as the export revenues are concerned, after a sharp drop in USD terms in 2023, we expect export growth to get back on track in USD terms, with a 36% YoY USD-terms jump in 2024E followed by a 51% increase in 2025E. The company's announced USD 23% YoY jump in 9M24 has proved that it's not -fragile to the currency movements, thanks to its state-of-the-art technology and advanced products. Furthermore, the Company stands to benefit from indirect export opportunities as Türkiye's presence in the global defense and military equipment market grows. ASELSAN is one of the few that can manufacture a wide variety of capabilities under one roof, and it current has 400 projects and a wide range of products. The Company's extensive product line allows it to sell both directly to customers and as payloads to other companies such as Roketsan (in which ASELSAN holds a 15% stake), Baykar, BMC, and TAI. These companies use the technology produced by ASELSAN in their own products, opening a cross-selling window for all companies in the Turkish defense and aerospace industry.

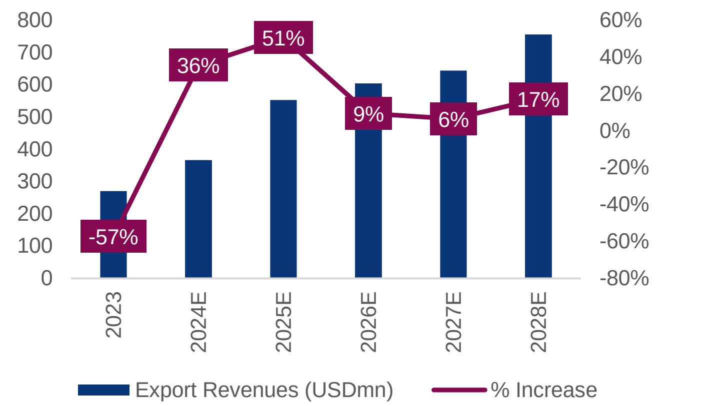
In 2025E, in addition to the tailwinds within the sector, we expect the Company to secure top-line growth with new products and the transition of serial production of existing products. Some of the most exciting new projects are the development and serial production of Layered Air Defense Systems, payloads of Kaan / Kizil Elma / Hürjet / Anka, and Murad Combat Aircraft Radar. The "ÇELİK KUBBE" (Steel Dome) project was completed following the SSİK meeting, which was held under the presidency of the Republic of Türkiye. Air defense systems developed by the Turkish defense industry under the direction of ASELSAN, systems including KORKUT, HİSAR-A+, GÖKDEMİR, GÖKER, GÖKBERK, HİSAR-0+, SİPER, AKINCI, and ATAK, would be able to function in an integrated model with Steel Dome. Within the Steel Dome, in addition to armament systems, there will be radar and electro-optical sensors that precisely monitor, identify, and classify targets. Therefore, it is anticipated that this project, in which ASELSAN will be a key player, would favorably impact the Company's backlog, in our view. Accordingly, we forecast 46.8% growth in revenues to TRY165.6bn and a backlog of USD13.0bn for 2025. We expect the book-to-bill ratio to hold steady in 2024 in 2025 before edging down over the years until it levelling off at 1.3-1.1x throughout our projection period.

Figure 2 – Revenue Projections (TRYmn)



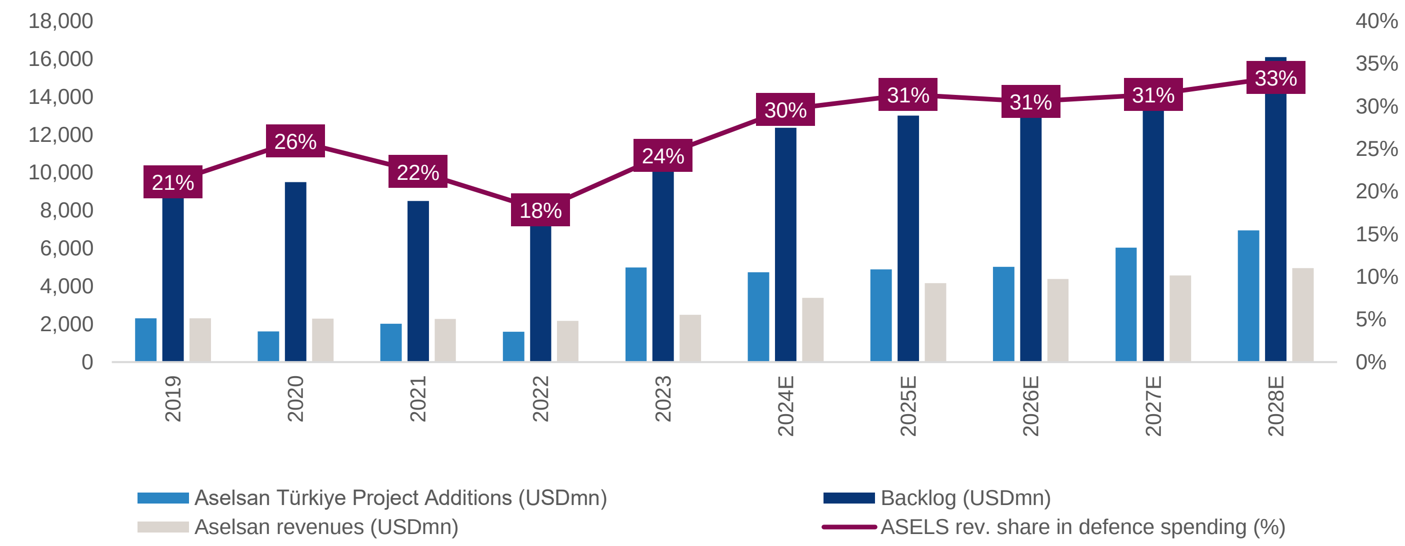
Source: QNBI Calculations, The Company

Figure 3 – Projected Export Revenues (USDmn)



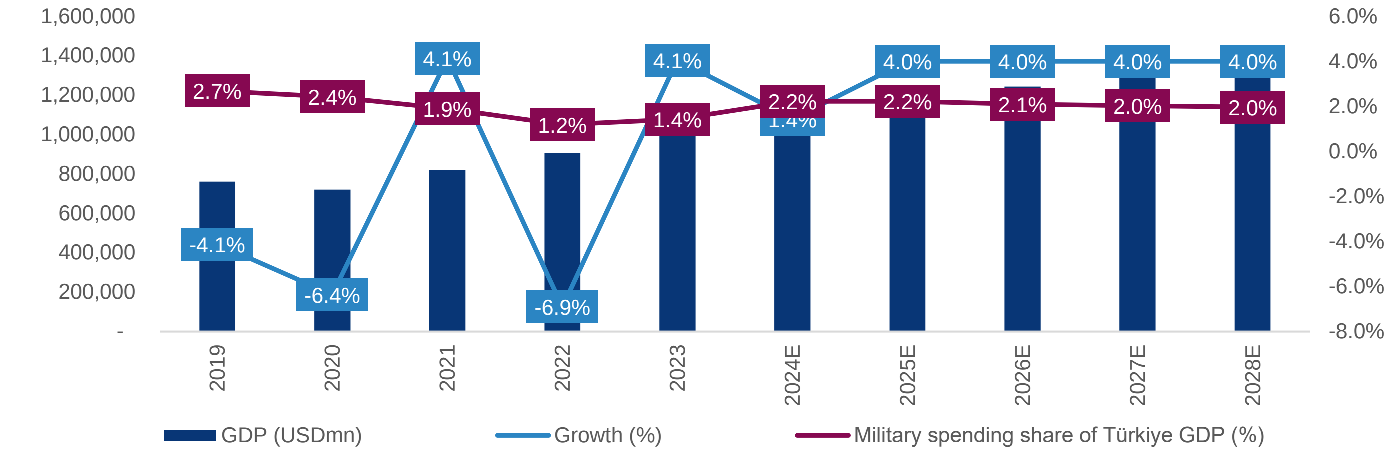
Source: QNBI Calculations, The Company

Figure 4 – ASELSAN's Revenue Share in Türkiye's Defense Spending (USDmn)



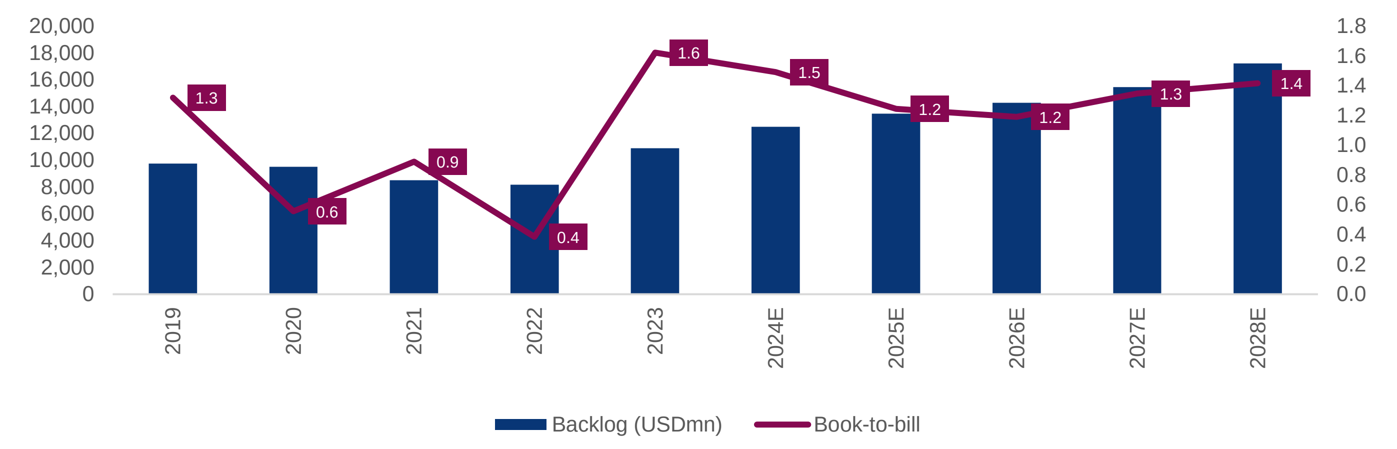
Source: QNBI Calculations, Bloomberg, SASAD

Figure 5 –Türkiye GDP and Military Spending Projections (USDk)



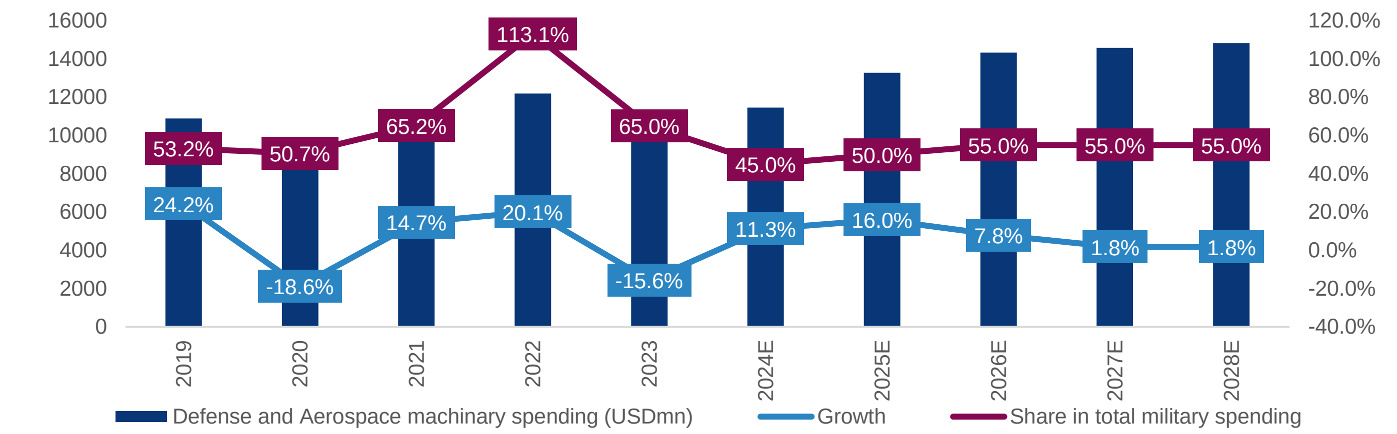
Source: QNBI Calculations, The Company, SSB, SASAD

Figure 6 – ASELSAN's Backlog and Book-to-bill Projections (USDmn)



Source: QNBI Calculations, Bloomberg, SASAD

Figure 7 – Defense and Aerospace Machinery Spending Projection (USDmn)



Source: QNBI Calculations, SASAD

Figure 8 – List of ASELSAN's new contracts as of 10M24

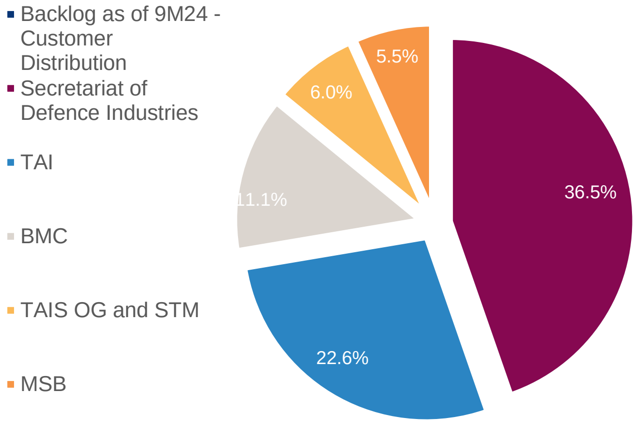
Date	Contract Amount	Currency	TRY Converted Amount	Product	Region / Country
4-Nov	1,210,977,796	TRY	1,210,977,796	Guidance kits	Türkiye
4-Nov	316,000,000	USD	10,870,400,000	Guidance kits	Türkiye
1-Nov	68,000,000	USD	2,339,200,000	Radar Systems and Friend-or-Foe Recognition Systems	Asia Pacific
31-Oct	10,343,050	USD	354,766,615	Electro-Optical Payloads	Asia Pacific - Africa
30-Oct	58,626,094	EURO	2,010,875,024	Payloads of electronic warfare suite, radar systems, and more…	
23-Oct	95,116,802	USD	3,258,045,459	Payloads consisting of friend or foe recognition system, satellite communication systems, and others…	Asia and Africa
3-Oct	26,190,679	USD	896,522,616	Payloads of naval platforms, friend-or-foe recognition system, electronic warfare suite, and others…	Asia Pacific
20-Sep	44,397,467	USD	1,513,065,757	Remote-controlled weapon system	Asia Pacific
19-Aug	60,309,068	USD	2,031,697,848	Avionic suites to the air platforms	Türkiye
14-Aug	32,000,000	EURO	1,177,541,748	Landing craft tank vessels	Türkiye
6-Aug	34,300,000	USD	1,145,421,038	Payloads for naval platforms	Not Specified - International Client
10-Jul	20,265,600	USD	666,815,269	Air defence systems	Not Specified - International Client
8-Jul	59,143,396	EURO	2,087,567,354	Air defence missle subsytems	Türkiye
3-Jul	109,700,953	USD	3,570,063,734	Electronic warfare systems	Türkiye
14-Jun	79,277,900	USD	2,575,746,967	Defence systems	MENA
13-Jun	64,000,000	USD	2,048,000,000	Missile subsystems and seeker production	Türkiye
12-Jun	48,760,000	USD	1,578,112,460	Avionics equipment for Indigenous helicopter project	Türkiye
11-Jun	110,000,000	USD	3,562,108,116	Defence and space related	Türkiye
29-May	421,566,822	EURO	14,732,385,777	Naval warfare systems and payloads of MILGEM 9-12 frigates	Türkiye
13-May	353,863,000	USD	11,387,746,109	Urban securitiy products	Türkiye
10-May	30,000,000	USD	968,493,004	Security systems	Türkiye
18-Apr	36,000,000	USD	1,168,963,165	Air defence systems	Türkiye
28-Mar	34,957,069	USD	1,129,102,901	Defense systems	Asia Pacific
27-Mar	35,130,000	USD	1,131,484,602	Supply of guidance kits and ASELFLIR-500 System	Not Specified - International Client
21-Mar	556,500,000	USD	18,040,338,495	Military equipment	Türkiye
28-Feb	82,000,000	EURO	2,768,845,688	Close-In weapon systems	Türkiye
21-Feb	12,089,000	USD	373,609,447	Land vehicle payloads	Europe
1-Feb	30,524,000	EURO	1,001,036,969	Submarine modernization	Türkiye
30-Jan	20,000,000	EURO	657,969,437	Radar systems	Not Specified - International Client
25-Jan	24,692,633	EURO	812,450,303	Naval systems	Not Specified - International Client
19-Jan	1,690,697,000	TL	1,690,697,000	On Board Signalling Equipment Procurement Project	Türkiye
18-Jan	15,632,304	EURO	512,799,132	Naval air defence systems	Türkiye
5-Jan	21,411,200	USD	638,929,487	Air defense and communication systems	Not Specified - International Client
3-Jan	9,953,500	USD	296,065,461	Defense systems	Not Specified - International Client
2-Jan	58,887,692	USD	1,732,958,764	Intelligent Transportation Systems.	Not Specified - International Client

Source: QNBI Calculations, The Company

Figure 9 – World Military Expenditure Calculated at Constant 2022 prices and Exchange Rates (USDbn)

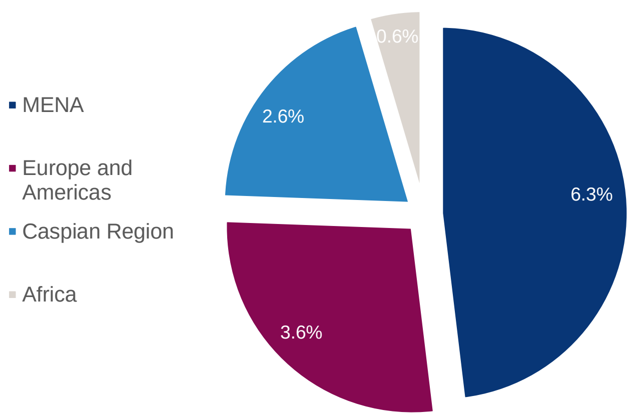
*Source: QNBI Calculations, SIPRI, *2023 USD prices and exchange rate is used*

Figure 10 – ASELSAN's Customer Distribution in Current Backlog (Domestic %)



Source: QNBI Calculations, The Company

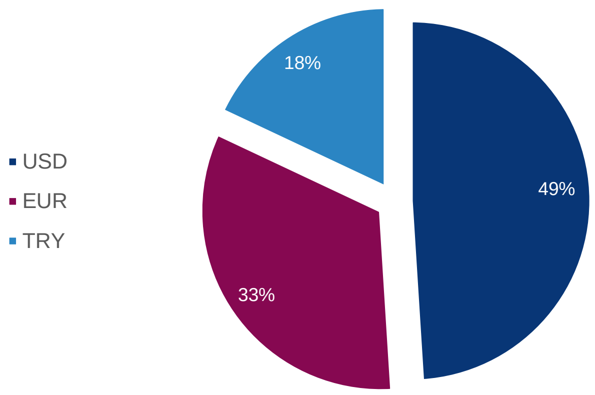
Figure 11 – ASELSAN's Customer Distribution in Current Backlog



Source: QNBI Calculations, The Company

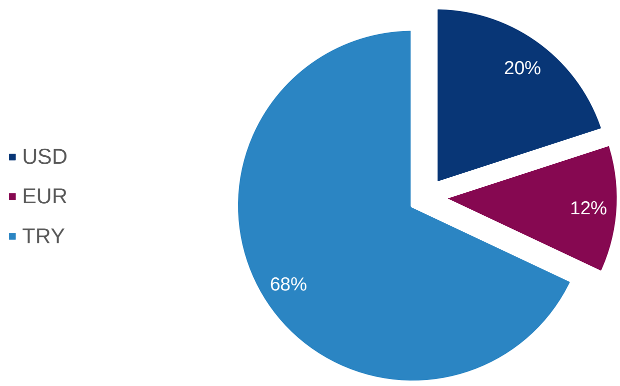
EBITDA margin to surge above historical averages thanks to more value-added mix, strong order book and capitilization of investments, despite being squeezed by strong TRY and high inflation as a net FX earner with expenditure mostly TRY based… As of 9M24, only 18% of the backlog was TRY-based while 68% of the expenditures were denominated in TRY (composed of materials, operating expenses, salaries and investment expenses. In line with the reporting standard, the situation hurts the gross margin given that 9M24 inflation exceeded the increase in Aselsan's FX basket. However, the 9M24 gross margin of 30.9% exceeded the 28.0% realized in 9M23, demonstrated how the mix effect and stable raw material costs have supported profitability. The impact of high inflation against a stable USD/TRY has boosted the OPEX figure, with the 9M24 OPEX-to-Sales ratio rising from 9.8% in 9M23 to 10.9% in 9M24, despite a YoY fall in R&D costs. Accordingly, the IAS-29 EBITDA margin narrowed by 30bps YoY in 9M24 to 23.7% while the non-IAS EBITDA margin was up by around 100bps YoY. We expect this situation to persist in the last quarter of 2024, with a 2024E gross margin of 27.0%, with the OPEX-to-Sales ratio easing to 9.0%, representing to a YE24 analyst IAS-29 EBITDA margin of 22.4%.

Figure 12 – ASELSAN 9M24 Currency Distribution of Current Backlog (%)



Source: QNBI Calculations, The Company

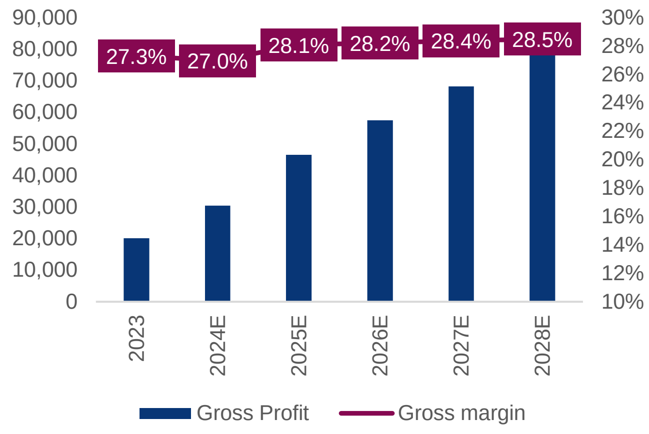
Figure 13 – ASELSAN 9M24 Expenditures Distribution (%)



Source: QNBI Calculations, The Company

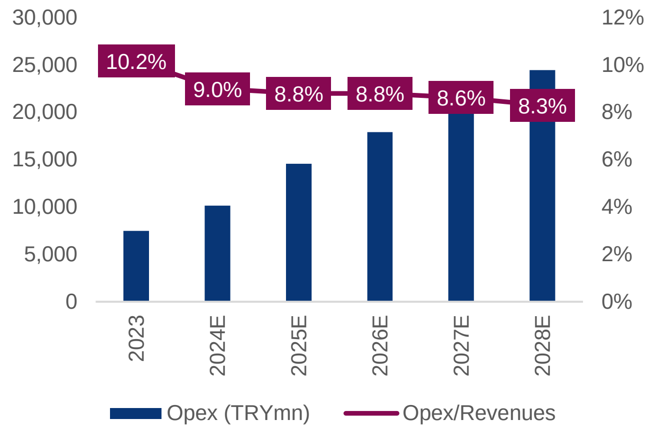
Raw material costs have so far been subdued in the last quarter of 2024, despite rising tensions in the Middle East, although remain somewhat volatile. We expect a smoother trajectory (in USD terms) in 2025 compared to 2024. With price adjustments already in place for 2024 and the assumption of a minimal increase in raw material prices, we do not anticipate much change in ASELSAN's gross margin. We forecast a 110bps improvement in the gross margin for 2025, mainly driven by a change in ASELSAN's sales mix and lower raw material costs. Looking at the OPEX-to-Sales ratio, easing inflation in 2025 will support a normalization in the ratio, as we calculate a decline in the OPEX-to-Sales ratio to 8.8% - still higher than historical averages but down 20bps YoY. Accordingly, we expect the 2025 IAS-29 EBITDA margin to reach 24.2%, reflecting an improvement of around 180bps YoY ahead of a further improvement of 10bps in the margin in 2026. The figures translate to a 5-yr CAGR of 29.8% between 2024-2029 as we expect margins to edge up starting from 2025E.

Figure 14 – Gross Margin Projection (TRYmn)



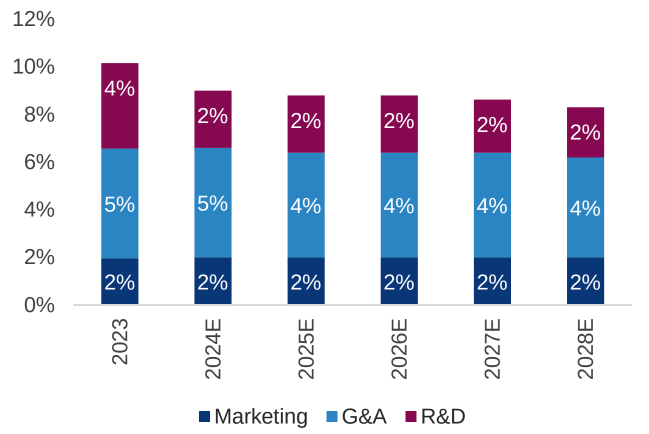
Source: QNBI Calculations, The Company

Figure 15 – OPEX Projection (TRYmn)



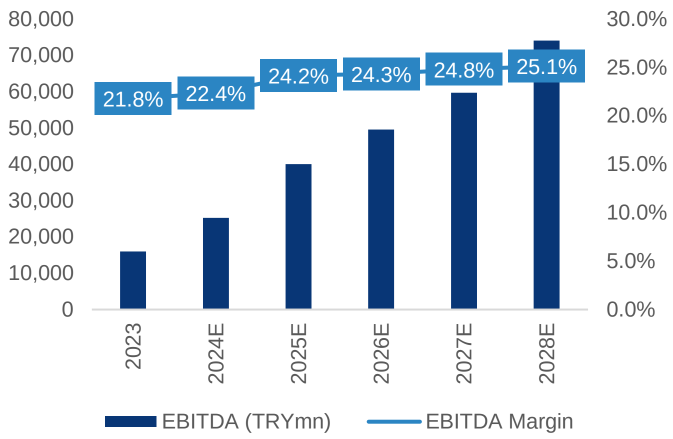
Source: QNBI Calculations, The Company

Figure 16 – OPEX-to-Sales Projection (%)



Source: QNBI Calculations, The Company

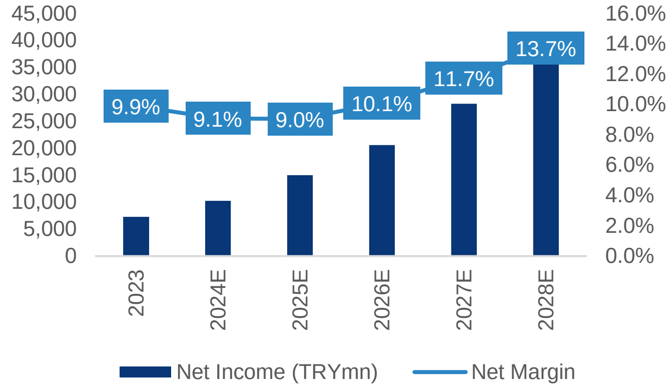
Figure 17 – EBITDA Projection (TRYmn)



Source: QNBI Calculations, The Company

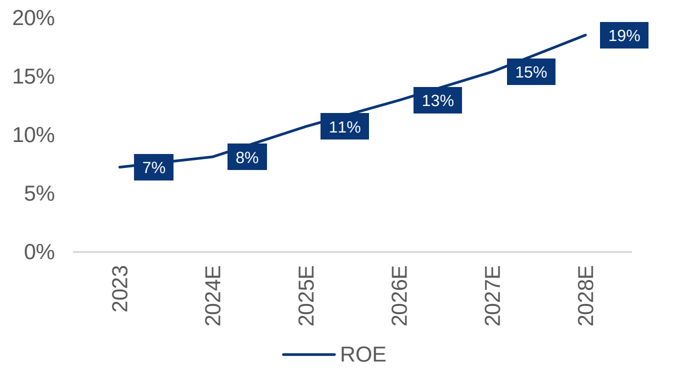
Forecasting the Company to get back on the RoE growth trajectory… ASELSAN posted TL6.1bn net earnings, up 43% YoY in 9M24, corresponding to a net margin of 10.1% vs. the IAS29 unadjusted net income margin of 27.3%. The newly introduced net monetary gain/loss item, which came in at TRY-10.5bn in 9M24, weighed down on net income. Thanks to the TRY7.1bn in deferred tax income, the Company was able to attain a healthy net margin. The TRY5.6bn in financial expenses also squeezed the net margin in 9M24, due to increased debt levels and rising financial expenses in parallel with rising interest rates, even though the Company is less sensitive to rising interest rates compared to our industrials thanks to government incentives. For FY24, we expect substantial financial costs to continue to pressure the bottom-line, with an IAS-29 net profit of TRY10.2bn – up 57.1% YoY in nominal terms. Note that we have incorporated tax incentives into our bottom-line expectations as the Company will not pay any corporation tax until the end of 2028 for R&D expenditures spent between the years as the Company owns 9 R&D centers located Türkiye. In accordance to our expectation of strong earnings momentum, we expect the RoE to reach attractive levels by 2026.

Figure 18 – ASELSAN Net Income Projections (TRYmn)



Source: QNBI Calculations, The Company

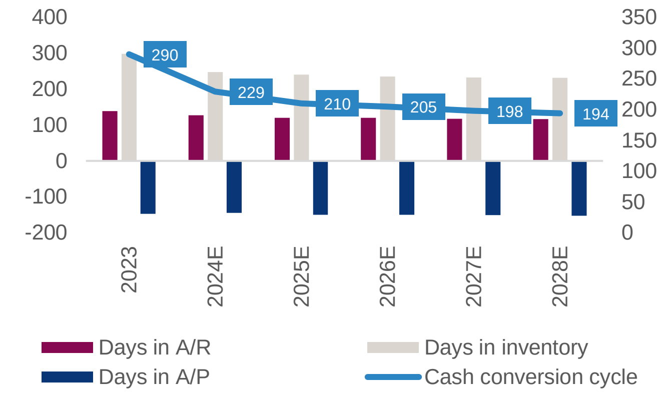
Figure 19 – RoE Forecasts (%)



Source: QNBI Calculations, The Company

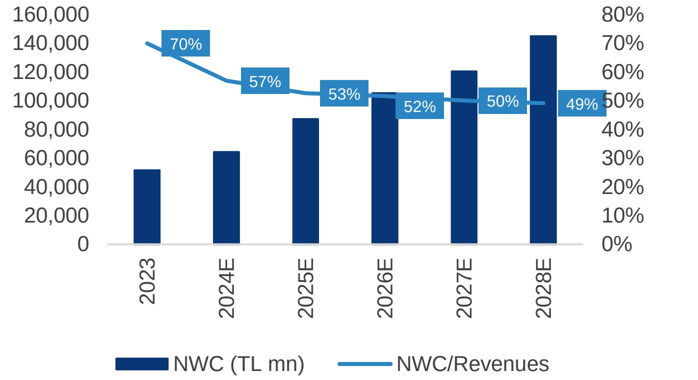
Forecasting an easing in the NWC requirement on the back of an increasing share of exports in total revenues and change in the sales mix… The working capital burden has been depleting the Company's FCFF generation in the past, mainly due to the long inventory days and delayed payments from the major clients. The cash conversion cycle reached 302 days in 9M24, resulting from the increase in the days in inventory of 269 days. The numbers should ease with strong deliveries in the last quarter of 2024, but still, our NWC assumption is one of the major negatives for future FCF generation. To be on the conservative side, we plugged in a 19-day improvement cash-conversion-cycle in 2025 as the export share in total revenue rises to 14% from 12% in 2024E.

Figure 20 – ASELSAN Cash Conversion Cycle Projection (Days)



Source: QNBI Calculations, The Company

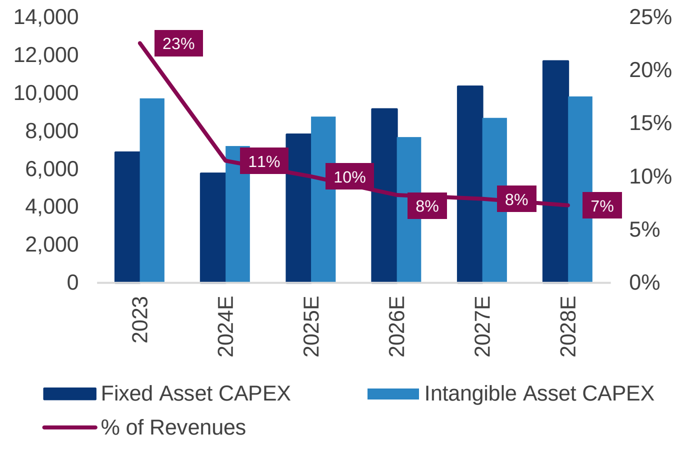
Figure 21 – Net Working Capital Projections (TRYmn)



Source: QNBI Calculations, The Company

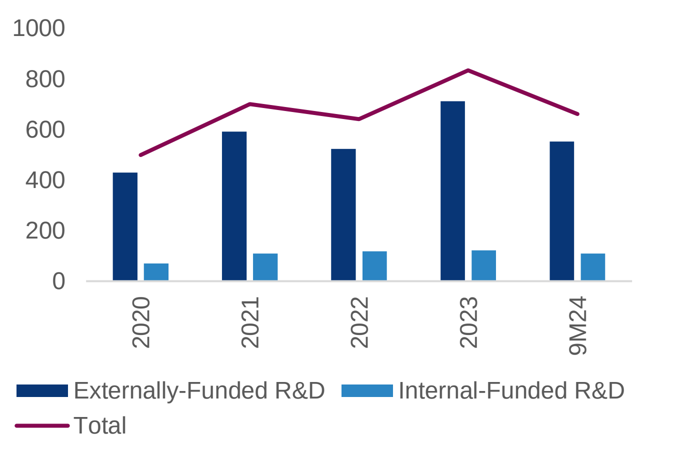
Slightly higher CAPEX period ahead in the short-term, but expecting a milder course of investments once new capacity additions are complete, along with reaching technological maturity… ASELSAN's tangible and intangible investments have expanded over the last four years as the Company has invested heavily in advancing its technology by upgrading or purchasing new state-of-the-art equipment and capacity additions with facility expansions, some of which have been realized as intangible R&D investments. Some of the planned investments which we have incorporated in our CAPEX assumption are the capacity addition to the radar system integration and production automation center, the addition of a platform to the defense system technologies facility and the photon detector and nanotechnology facility. All of these investments are planned as a part of the Company's strategy to meet the rising global needs for products and eventually, capture a higher market share in the global defense industry. Accordingly, we have separately forecasted CAPEX for fixed and intangible assets, in which we have assumed USD175mn of CAPEX in fixed assets and USD200mn in intangible assets for 2025E, translating to 11.9% of total 2025E sales. On the other hand, we expect FCF to remain suppressed in our short-term projections due to high working capital needs, even though the Company will not pay any taxes until 2028YE. Nevertheless, we forecast positive cash flows starting from 2025, mainly derived from the higher than historical margins and tax exemption. We expect FCF of TRY-2.03bn in 2024E, converting to a positive number of TRY2.4bn in 2025 before a recovery in the FCF margin in 2026. Net debt, on the other hand, is on course to increase in the short-term to fund the aforementioned investments, while the net debt/EBITDA ratio remains healthy at 1.1x in 2025E and is expected to remain benign throughout our financial projection.

Figure 22 – ASELSAN CAPEX Projection (TRYmn)



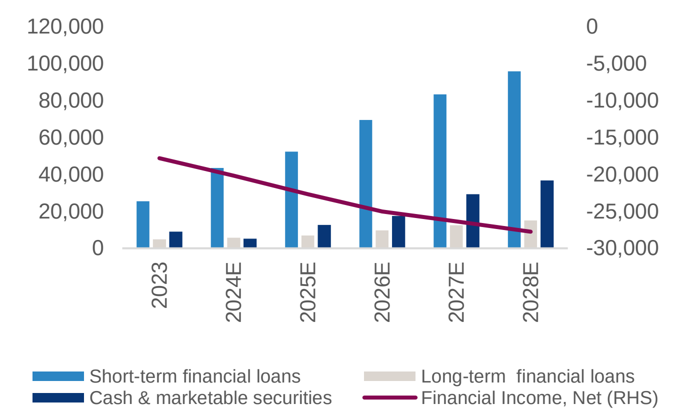
Source: QNBI Calculations, The Company

Figure 23 – R&D Funding (USDmn)



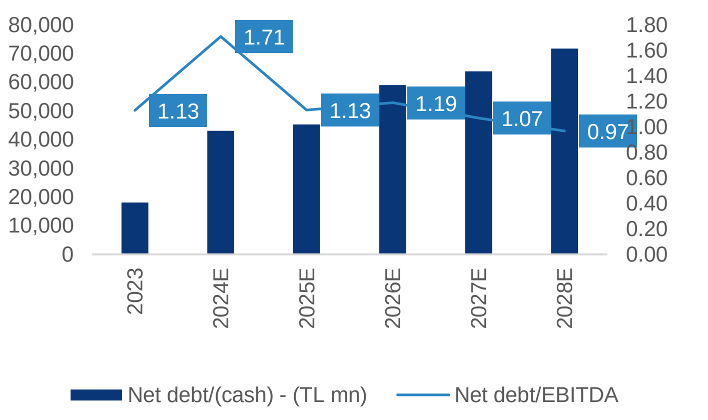
Source: QNBI Calculations, The Company

Figure 24 – Financial Snapshot (TRYmn)



Source: QNBI Calculations, The Company

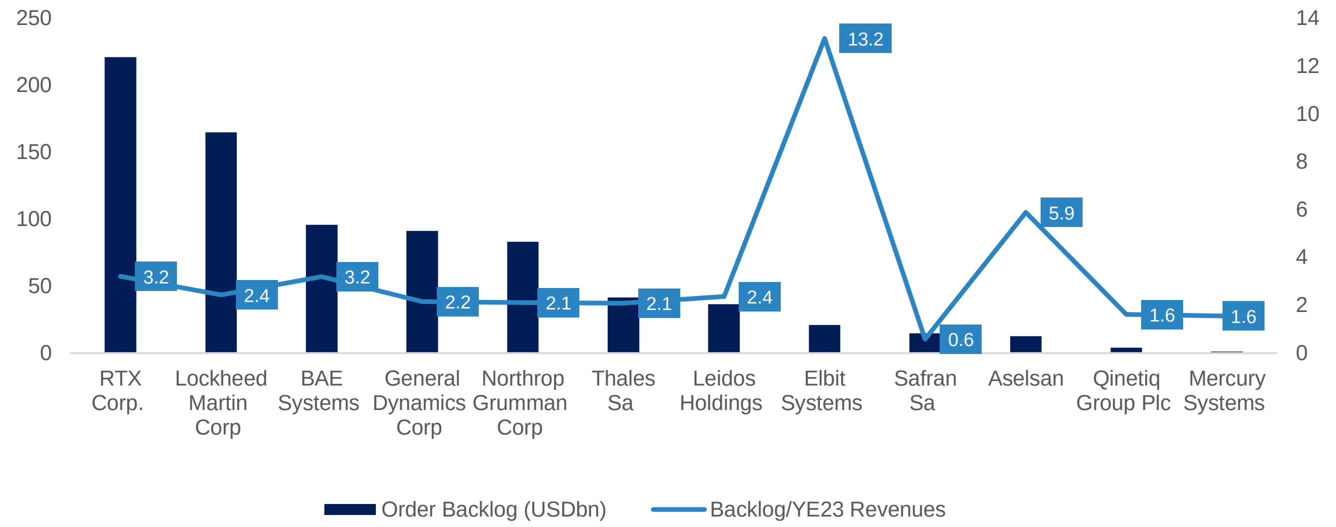
Figure 25 – Net Debt Projection (TRYmn)



Source: QNBI Calculations, The Company

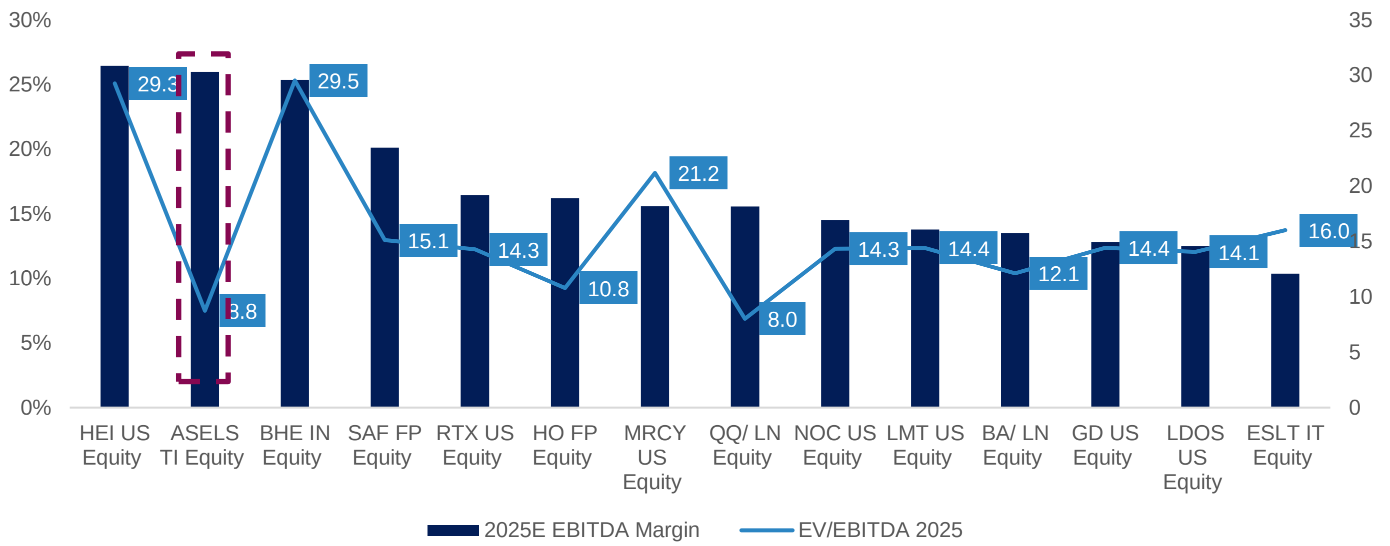
Discounted amongst global peers, even though operational profitability metrics are significantly higher than the average industrial metrics… Based on 2024E and 2025E our prospective earnings the stock trades at an EV/EBITDA of 13.6x and 8.7x and the multiple implying an average respective discount of 12% and 40% to its global peers, respectively. Since ASELSAN's 2025E EBITDA margin is the second highest among its worldwide peers in terms of profitability with its 82% hard currency denominated backlog and rising Türkiye's dominance in global defense industry, we believe that the discount is not justified.

Figure 26 – **Order Backlog Comparison vs. Peers**



Source: QNBI Calculations, Bloomberg, Company Presentations

Figure 27 – **EBITDA Margin and EV/EBITDA Comparison vs. Peers**



Source: QNBI Calculations, Bloomberg

Valuation

We valued ASELSAN using a 70-30 blended DCF and relative valuation methodology and found a 12-month target price of TRY 102.04/share. Our 12-month TP offers 51% upside potential at the latest close. In our DCF valuation model, we have incorporated an average weighted-average cost of capital (WACC) of ≈20% for our long-term valuation horizon, based on a 47.5% cost of borrowing, 45.2% cost of equity (40% risk-free rate, 5.5% equity risk premium and a 0.94 stock beta) for 2024, which is assumed to decline until 2028. Finally, we set a terminal growth rate of 13%. We have not used the P/E multiple in our relative valuation as we believe the IAS-29 practice offers a misleading impression of the net income figure, and would therefore be not be instructive for our valuation.

Note that we have incorporated a non-IAS valuation which is based on nominal terms in our relative valuation method as well.

Our key DCF model assumptions are as follows;

- We are forecasting moderate revenue growth for 2024 in nominal terms given the strong base in 2023 and steady trajectory in exchange rates. Upcoming Investments will significantly support the top-line in the mid and long-term, and we forecast a non-IAS29 CAGR of 27.1% between 2024-2029.
- We have assumed that margins will remain high and hover over historical averages for 2025E. Therefore, our forecasts conservatively point to a strong nominal EBITDA growth of 57% for 2025E, to be followed by a 29.5% nominal CAGR growth between 2024-2029. Our non-IAS EBITDA forecast points to an EBITDA margin of 27.7% for 2025E and 27.9% in 2026E, and expanding further after 2028E when the majority of the investments are completed.
- While the FCF will become more attractive in the future, in the short-term we believe the high CAPEX trajectory and high NWC requirement will deplete the cashflow. ASELSAN will not pay corporation tax until the end of 2028E (thanks to R&D incentives), which we have incorporated in our DCF valuation. With new capacity coming onstream and the period of high CAPEX in 2024 and 2025 drawing to a close, we expect a surge in the FCF margin and forecast a positive cashflow of TR16.4bn and TRY26.4bn in 2026 and 2027, corresponds to FCFF margins of 9.4%, and 12.9%, respectively.
- Based on 2024 prospective earnings, the stock trades at a P/E of 29.4x and EV/EBITDA of 13.6x, but looking at 2025 prospective earnings, the Company trades at a P/E of 20.1x and EV/EBITDA of 8.7x, trading at a severe discount compared to its global peers.

Figure 28 – Summary of DCF Model

ASELS (TRYmn)	2024E	2025E	2026E	2027E	2028E	2029E	2030E	2031E	2032E	2033E
Revenues	94,754	141,407	173,943	205,411	251,649	314,640	394,338	483,425	556,091	630,637
y/y growth	*58%*	*49%*	*23%*	*18%*	*23%*	*25%*	*25%*	*23%*	*15%*	*13%*
EBIT	20,277	31,929	39,570	47,521	59,514	75,885	96,954	119,990	138,027	156,530
EBITDA	24,902	39,127	48,485	58,360	72,428	90,803	114,528	140,548	162,208	184,394
y/y growth	*54%*	*57%*	*24%*	*20%*	*24%*	*25%*	*26%*	*23%*	*15%*	*14%*
EBITDA Margin	*26%*	*28%*	*28%*	*28%*	*29%*	*29%*	*29%*	*29%*	*29%*	*29%*
Inc./dec. in W/C	15,073	19,972	15,037	12,690	20,377	27,809	34,731	37,958	29,865	29,746
CAPEX	11,862	16,784	17,021	19,233	21,734	24,559	27,752	31,360	35,436	40,043
Taxes paid	0	0	0	0	0	12,557	17,423	22,758	26,857	31,040
FCFF	**-2,033**	**2,370**	**16,427**	**26,437**	**30,317**	**25,878**	**34,623**	**48,473**	**70,050**	**83,566**
WACC	39.7%	30.3%	23.7%	21.5%	19.4%	19.3%	19.3%	19.3%	19.4%	19.5%
PV of FCFF	**93,077**									
Terminal growth rate	*13%*									
Terminal Value	1,453,059									
PV of Terminal Value	**244,012**									
Value of Firm	**337,090**									
Minority Interest	286									
Net debt @ 3Q24	29,788									
Equity Value	**307,016**									

Source: QNBI Estimates

Figure 29 – Peer Analysis

Country	Company Name	BB Ticker	Market Cap	P/E 24	P/E 25	EV/EBITDA 24	EV/EBITDA 25
US	RTX Corp.	RTX US Equity	159,828	21.5	19.6	15.7	14.3
US	General Dynamics Corp	GD US Equity	84,140	21.9	19.0	16.1	14.4
US	Heico Corporation	HEI US Equity	30,368	69.2	58.9	32.5	29.3
US	Leidos Holdings	LDOS US Equity	25,703	19.4	18.5	14.3	14.1
US	Lockheed Martin Corp	LMT US Equity	130,806	20.7	19.7	15.0	14.4
US	Northrop Grumman Corp	NOC US Equity	75,846	20.1	18.6	15.3	14.3
UK	Qinetiq Group Plc	QQ/ LN Equity	3,345	14.5	12.9	8.6	8.0
UK	BAE Systems	BA/ LN Equity	53,917	20.2	17.9	13.3	12.1
India	Bharat Electronics	BHE IN Equity	25,774	46.1	38.7	35.1	29.5
US	Mercury Systems	MRCY US Equity	2,502	103.6	46.9	30.1	21.2
France	Safran Sa	SAF FP Equity	102,360	32.8	26.7	17.4	15.1
France	Thales Sa	HO FP Equity	35,689	19.0	16.8	11.9	10.8
Median				**21.1**	**19.3**	**15.5**	**14.4**
Türkiye	ASELSAN	ASELS TI Equity	8,740	29.4	20.1	13.6	8.7
Discount/Premium				**44%**	**7%**	**-10%**	**-38%**

Source: QNBI Calculations, Bloomberg

Figure 30 – Valuation Summary

	Weight	Implied Equity Value
DCF-Driven 12M Target Value	70%	446,708
Peer Analysis Implied Value	30%	474,088
70-30 DCF and relative valuation blended equity value		454,922
Participations		10,373
Total Target Equity Value		**465,294**
# of shares outstanding		4,560
Target Price		**102.04**
Current Share Price		68.00
Upside / Downside		**50%**

Source: QNBI Calculations, Bloomberg

QNB Invest Rating System

We employ a relative scale in our rating system (i.e. Market **Outperform, Neutral, Underperform**) in order to better present relative value propositions and more actively pursue long vs. short ideas at the BIST. The relevant benchmark is the broader Turkish stock market, using the BIST-100 index as a basis. The ratings also incorporate a certain degree of relativity within the analyst's own stock coverage universe due to asymmetric return expectations among the industries under our BIST coverage. The rating system combines analysts' views on a stock relative to the sectors under coverage, and the sector call relative to the market, together providing a view on the stock relative to the market.

Individual ratings reflect the expected performance of the stock relative to the broader market over the next 6 to 12 months. The assessment of expected performance includes a function of near-term company fundamentals, industry outlook, confidence in earnings estimates and valuation, and other factors.

An essential element of our rating methodology involves benchmarking a 12-month expected return against the cost of equity. We set a required rate of return for each stock, calculated from our risk-free rate and equity risk premium assumptions. The price target for a stock represents the value that the stock is expected to reach or sustain over the performance horizon of 12 months, according to the view of the analyst.

We have separated the stocks under our coverage into two groups, mainly with respect to their liquidity (market cap, free float market cap and historical average daily trading volume) as small-cap stocks exhibit different risk/return characteristics to more-liquid large-caps. For the purposes of the relative stock rating, however, stocks within each group will be considered on an unweighted basis with regard to their market capitalization.

For a stock to be assigned an **Outperform** rating, the implied return *must* exceed the required rate of return by at least 5 percentage points over the next 12 months for our larger-cap stock coverage, or by 10 percentage points for the small-cap group. For a stock to be assigned an **Underperform** rating, the stock must be expected to underperform its required return by at least 5 percentage points over the next 12 months. Stocks between these bands will be classified as **Neutral**.

When the potential upside of an *average* stock in our coverage exceeds its required rate of return (i.e. the market upside exceeding the implied average cost of capital), a greater number of stocks would fall into the aforementioned Outperform (Buy) category, illustrating the significance of the "relative return" concept (vis-à-vis absolute return) in picking better investment ideas with a positive alpha. The same holds true when the potential upside of an *average* stock in our coverage falls short of its required rate of return.

In this regard, as a supplemental methodology, we rank the stocks in our coverage according to their notional target price with respect to their current market price, and then categorise the top group (approximately 40-50% of the companies under coverage) as Outperform, the next 40-50% as Neutral and the lowest 10-20% (and no less than 10%) as Underperform.

It should be noted that the expected returns on some stocks may at times fall outside the relevant ranges of the applicable respective rating category because of market price movements and/or other short-term volatility or trading patterns. Such interim deviations from specified ranges are permitted but becomes subject to review.

Also note that the analyst's short-term view may occasionally diverge from the stock's longer-term fundamental rating.

Outperform. We expect the stock to outperform the BIST-100 over the next 6 to 12 months.

Neutral (Market Perform). We expect the stock to broadly perform in line with the BIST-100 index over the next 6 to 12 months. (Although we would normally have a neutral assessment of stocks in this category, if a stock has gone through a period of market underperformance, it would be an indication that the stock may be expected to improve its performance relative to market averages in the coming period, and vice versa).

Underperform. We expect the stock to underperform the BIST-100 over the next 6 to 12 months.

N/R. Not Rated.

U/R. Under Review.

Analyst Certification

The following analysts hereby certify that the views expressed in this research report accurately reflect their own personal views regarding the securities and issuers referred to therein and that no part of their compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in the research report: **Can Alagöz, Tolga Han.**

Unless otherwise stated, the individuals listed on the cover page of this report are research analysts.

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