Diffusion Engineers Ltd

Strong execution and higher backlog; pricing pass-through holds the key

Diffusion Engineers Ltd ("Diffusion") delivered strong revenue growth of 50.7% YoY, supported by industrial demand, higher execution and a growing order book. EBITDA grew a slower 34.5%, weighed down by RM cost inflation pressure (which is usually passed on with one-quarter lag). The sequential PAT decline masks an improvement in operating EBITDA, with lower associate/JV contribution and treasury income affecting the bottom line. Customers are receptive to price revisions, and newer orders are being booked at revised prices, which should help restore margins to prior levels from 4QFY27 onwards, subject to stable RM costs. With a healthy order backlog and sufficient capacity to absorb industry demand, management expects a 20-25% revenue CAGR over the next 3-5 years. We view this growth outlook positively, but margin recovery unproven execution tests. We build in a Revenue/EBITDA/PATAMI CAGR of 23%/31%/23%. **We maintain BUY with a TP of INR 510**.

Key Business Highlights

- **Pricing and Margin Recovery:** Prevailing RM price pressure in tungsten and specialty ferro-alloys, alongside higher energy and logistics costs, has compressed GM% (29.9% vs 37.0% YoY and 31.6% QoQ) ; EBITDA% nonetheless improved marginally QoQ to 13.2% (vs 12.9%), aided by robust execution, with revenue up 14.4% QoQ to INR 125.9Cr (vs INR 110.1Cr). The Tungsten prices have eased from their peaks but remain above earlier levels. Shorter-cycle orders (<6m) carry exposure to fixed-price risk, while longer contracts include price-variation clauses. Most of the current order book has been re-priced and quotation validity has been shortened.
- **Orderbook (OB) and Execution Visibility:** 2QFY27 backlog was INR 227Cr (vs INR 174.1Cr as of 4QFY26), up 30.3%. Heavy Engineering dominates backlog visibility with INR 178Cr OB, while consumables turn faster and are less fully represented in OB (INR 25Cr). Wear Plates/Wear Parts OB at INR 24Cr.
- **New product development to scale up revenue:** New products currently contribute about 1-2% of revenue. Diffusion targets a 10-15% revenue mix from new products on an expanded revenue base. The first vertical roller mill order has been executed for a leading cement manufacturer. The company has closed or is on the verge of closing orders for steel-mill rollers (JSW and JSPL), alternative-fuel shredders and roller presses. Apron feeder conveyors, centrifugal fan casings, hammer mill crushers, tilting runners and vertical roller mill housings are newly commercialised products, where the company sees order traction from core industries such as sugar, steel, power and mining.
- **Railways, Defence and Overseas Expansion**: Diffusion is qualified to manufacture locomotive shells for Indian railways which gives it access to bid for tenders. Defence opportunities are being explored (alongside Tejorup acquisition); however, both these opportunities are long-gestation and would drive growth beyond FY28. The Abu Dhabi facility is moving towards commencement of operations. Turkey is stabilizing and the Philippines remains consistent. Cement customer breakthroughs in Ghana and Nigeria.
- **Capacity, Capex and Sourcing**: Major capex is nearing completion, with phased commissioning expected to add capacity and operating efficiency. 1H capex stood at INR 24.2Cr. Most of the RM sourcing is domestic (85-90%) with certain roller-press forgings/castings imported from China and Europe.

Valuation at a Glance

- **We value Diffusion at 25x FY28F EPS of INR 20.4.** We expect price revisions and operating leverage from higher utilisation to drive margin recovery. Margin pressure is likely to persist in 2H. We have revised our EBITDA margin estimate down by 70bps for FY27F.

Key Business Highlights

Particulars (INR Cr)	FY24A	FY25A	FY26A	FY27F	FY28F
Revenue	**278**	**335**	**407**	**487**	**618**
EBITDA	39	47	57	68	97
EBITDAM (%)	14.0%	14.1%	14.1%	13.9%	15.8%
EBIT	42	51	65	75	103
Adj PAT	**31**	**36**	**50**	**57**	**76**
PATM%	11.0%	10.7%	12.4%	11.7%	12.4%
AEPS	**10.9**	**9.6**	**13.5**	**15.2**	**20.4**
RoCE %	18.5%	13.0%	15.0%	15.3%	18.1%
RoE %	16.1%	9.7%	12.4%	12.5%	14.6%
P/E (x) at CMP	38.4x	43.8x	31.1x	27.7x	20.6x

Source: Incred Estimates

Result Update

BUY

Stock Data

CMP (INR)	420
Target	510
Upside (%)	21%
BSE code	544264
NSE code	DIFFNKG
Bloomberg Code	DIFFNKG:IN
Face Value	10.0
Market Capitalization (Cr)	1,572
1M Average Daily Volume	92,534
52-week H/L	520/217
Free Float %	29.24%

Shareholding Pattern (%)

Period	Jun'26	Sep'26
Promoters	69.76	69.76
FII	0.72	1.18
DII	8.42	8.45
Others	20.31	19.82

Estimates

	Old		New	
	FY27F	FY28F	FY27F	FY28F
EBITDA	71	97	69	97
EBITDA%	14.6	15.8	13.9	15.8
PATAMI	58	76	56	76
EPS	15.5	20.4	15.2	20.4

Price Chart



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Valuation Thesis

We maintain a BUY rating with a revised TP of INR 510, based on 25x FY28F EPS of INR 20.4.
Our FY28F EPS is based on:

- Revenue of INR 617.5Cr driven by stronger execution with newly commissioned capacity and a healthy order backlog providing visibility (23% CAGR).
- EBITDA of INR 97.3Cr (15.8% margin). With price-revision and operating leverage from existing capacity, we expect a 170bps margin expansion over FY26 (14.2%), subject to RM price stability. The FY27F EBITDA margin has been revised down by 70bps to 13.9% on GM pressure
- PATAMI of INR 76.3Cr (12.4% margin). Higher depreciation to weigh on the bottom line.

Source: Incred Research, Company disclosures

Summary of Financials

Profit and Loss Statement

Particulars (INR Cr)	FY24A	FY25A	FY26A	FY27F	FY28F
Revenue from Operations	278	335	407	487	618
Material Consumed & Mfg Expenses	186	223	274	331	414
Gross Profit	92	112	133	156	204
GPM (%)	*33.3%*	*33.5%*	*32.7%*	*32.0%*	*33.0%*
Employee Benefits Expense	36	42	48	57	66
Other Expenses	18	23	27	32	40
EBITDA	39	47	57	68	97
EBITDAM (%)	*14.0%*	*14.1%*	*14.1%*	*13.9%*	*15.8%*
D&A Expense	5	5	7	9	12
Other Income	7	9	15	16	17
EBIT	42	51	65	75	103
EBITM (%)	*15.0%*	*15.2%*	*16.1%*	*15.3%*	*16.6%*
Finance Costs	2	2	2	3	3
Share of P/L from Associates	1	-2	3	2.00	-
PBT	41	47	65	74	99
Total Tax Expenses	10	11	15	17	23
PAT	31	36	50	57	76
Minority	0.1	0.1	0.1	0.1	0.1
PATAMI	31	36	50	57	76
PATM%	*11.0%*	*10.7%*	*12.4%*	*11.7%*	*12.4%*
EPS	10.9	9.6	13.5	15.2	20.4

Quarterly P&L

Particulars (INR Cr)	2QFY27	2QFY26	YoY	1QFY27	QoQ
Revenue from Operations	125.9	83.6	*50.7%*	110.1	*14.4%*
Material Consumed & Mfg Expenses	88.2	52.7	*67.5%*	75.3	*17.1%*
Gross Profit	37.7	30.9	*22.0%*	34.8	*8.4%*
GPM (%)	*29.9%*	*37.0%*		*31.6%*	
Employee Benefits Expense	12.8	12.1	*6.0%*	12.6	*1.5%*
Other Expenses	8.3	6.5	*28.1%*	8.0	*3.1%*
EBITDA	16.6	12.4	*34.5%*	14.2	*17.5%*
EBITDA (%)	*13.2%*	*14.8%*		*12.9%*	
D&A Expense	1.9	1.6		1.9	
Other Income	1.9	3.0		4.1	
EBIT	16.7	13.8	*20.9%*	16.4	*1.7%*
EBITM (%)	*13.2%*	*16.5%*		*14.9%*	
Finance Costs	0.8	0.5		0.7	
Share of P/L from Associates	-0.6	-0.6		4.5	
PBT	15.2	12.7	*20.3%*	20.1	*-24.4%*
Total Tax Expenses	2.5	2.5		3.5	
PAT	12.8	10.2	*25.4%*	16.7	*-23.5%*
Minority	0.1	0.1		0.1	
PATAMI	12.7	10.1	*25.6%*	16.6	*-23.7%*
PATM%	*10.1%*	*12.1%*		*15.1%*	
EPS	3.4	2.7	*25.6%*	4.4	*-23.7%*

Balance Sheet

Particulars (INR Cr)	FY24A	FY25A	FY26A	FY27F	FY28F
PP&E (incl CWIP)	92	101	133	187	187
Non-Current Investments	29	35	43	43	43
Other Non-Current Assets	7	10	11	11	11
Total Non-Current Assets	128	145	187	241	241
Inventories	53	68	74	105	128
Trade Receivables	67	85	128	134	169
Cash & Bank Balances	8	127	98	62	104
Short Term Loans	15	12	11	11	11
Other Current Assets	5	8	13	16	22
Total Current Assets	148	300	324	327	434
Total Assets	276	444	510	568	675
Equity Share Capital	28	37	37	37	37
Other Equity	163	331	368	417	485
Minority Interest	0.3	0.4	0.5	0.6	0.7
Total Equity	191	369	406	455	523
Long Term Borrowings	-	-	-	-	-
Deferred Tax Liabilities	5	6	6	6	6
Total Non-Current Liabilities	6	7	6	6	6
Short Term Borrowings	34	23	29	34	43
Trade Payables	31	28	47	46	69
Short-Term Provisions	1	2	3	3	3
Other liabilities	12	15	21	24	31
Total Current Liabilities	78	68	99	107	146
Total Liabilities	85	75	105	113	152
Total Equity and Liabilities	276	444	510	568	675

Cashflow Statement

Particulars (INR Cr)	FY24A	FY25A	FY26A	FY27F	FY28F
Profit before tax	41	47	65	74	99
Depreciation & amortisation expense	5	5	7	9	12
Finance Cost	2	2	2	3	3
Operating Profit before WC Changes	44	54	67	86	115
Decrease/Increase in Inventories	(2)	(15)	(5)	(32)	(23)
Decrease/Increase in Receivables	3	(18)	(43)	(5)	(36)
Decrease/Increase in Payables	6	(2)	18	(1)	23
Decrease/Increase in Other assets	3	(3)	(5)	(3)	(6)
Decrease/Increase in Other Liabilities	2	3	6	4	7
Income Tax Paid	(10)	(11)	(14)	(17)	(23)
Net cash from Operating Activities	36	9	23	32	57
Cash Flow from Investing Activities					
Purchase of Fixed Assets	(32)	(12)	(19)	(63)	(12)
Increase in Investments	(10)	(5)	(8)	-	-
Other Investing Activities	6	(1)	(13)	-	-
Net Cash from Investing Activities	(36)	(18)	(40)	(63)	(12)
Cash Flow from Financing Activities					
Finance costs paid	(2)	(2)	(2)	(3)	(3)
Change in Borrowings	(14)	(11)	5	5	9
Proceeds from Issue of Shares	20	144	-	-	-
Dividend Paid	(2)	(2)	(6)	(8)	(9)
Other Financing Activities	(0)	-	(9)	-	-
Net Cash used in Financing Activitie	3	129	(12)	(5)	(3)
Net increase in Cash & Cash Equivale	3	119	(29)	(36)	43
Cash & Cash Equivalents Beginning	5	8	127	98	62
Cash & Cash Equivalents Ending	8	127	98	62	104

Source: Incred Estimates

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