



**3R MATRIX**

	+	=	-
Right Sector (RS)	✓	■	■
Right Quality (RQ)	✓	■	■
Right Valuation (RV)	✓	■	■
	+ Positive	= Neutral	- Negative

**What has changed in 3R MATRIX**

	Old		New
RS	■	↔	■
RQ	■	↔	■
RV	■	↔	■

**ESG Disclosure Score**

**NEW**

**ESG RISK RATING**  
Updated Oct 08, 2022 **34.56**

**High Risk**

NEGL	LOW	MED	<b>HIGH</b>	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

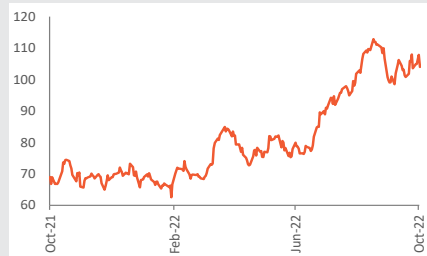
**Company details**

Market cap:	Rs. 76,022 cr
52-week high/low:	Rs. 115/61
NSE volume: (No of shares)	100.8 lakh
BSE code:	500049
NSE code:	BEL
Free float: (No of shares)	119.1 cr

**Shareholding (%)**

Promoters	51.1
FII	17.4
DII	25.6
Others	5.9

**Price chart**



**Price performance**

(%)	1m	3m	6m	12m
Absolute	8.1	18.4	31.2	56.3
Relative to Sensex	3.5	11.4	26.1	58.5

Sharekhan Research, Bloomberg

**Bharat Electronics Ltd**  
**In-line Q2, outlook bright**

<b>Capital Goods</b>	<b>Sharekhan code: BEL</b>		
<b>Reco/View: Buy</b>	↔	<b>CMP: Rs. 105</b>	<b>Price Target: Rs. 130</b>
↑ Upgrade	↔ Maintain	↓ Downgrade	

**Summary**

- ◆ Bharat Electronics Limited's (BEL)'s Q2FY2023 performance was in-line with our and street expectations. While sales growth was satisfactory, the highlight was a sequential improvement in gross and operating margins.
- ◆ Order backlog as on October 01, 2022 was at Rs. 52,795 crore, at ~3.1x its TTM revenue. However, order intake seems to be muted during Q2FY2023.
- ◆ BEL has signed an MoU with Munitions India Limited (MIL), a defence PSU to pursue domestic and export opportunities. It has also bagged an order of ~Rs. 8,060 crore for Li-lon battery packs from Triton Electric Vehicle, India. Further, growing exports (~60% CAGR over FY2022-FY2024E) shall also aid revenue growth.
- ◆ We retain our Buy rating on BEL with an unchanged PT of Rs. 130, considering its improving performance, backed by promising order inflow pipeline in both defence and non-defence verticals.

Consolidated results were in-line with our expectations. Sales grew by ~8% y-o-y to Rs. 3,962 crore (vs our estimate of Rs. 4,052 crore). Gross margins remained flat y-o-y but improved 155 bps q-o-q at 43.6% in Q2FY23. Operating profit was up by just 0.5% y-o-y to Rs 868 crore. OPM came in at 21.9% (vs 23.5% in Q2FY22), down 157 bps y-o-y but improved substantially by 528 bps on a q-o-q basis. Net profit was flat at Rs 624 crore y-o-y. Order backlog stood at Rs. 52,795 crore; providing strong revenue visibility of ~3.1 years on TTM basis. The company had a cash balance of ~Rs 1,000 crore at the end of the quarter.

**Key positives**

- ◆ Positive surprise on operating profit margin front.
- ◆ Order backlog strong at ~Rs. 52,795 crore (~3.1xTTM revenue).

**Key negatives**

- ◆ Tax rate increased from 26.2% in Q2FY2022 to 28% in Q2FY2023.
- ◆ Order intake during the quarter could be muted (as per inferred number).

**Revision in estimates** – We have introduced FY2025E estimates and broadly maintained our estimates for FY2022-FY2024E.

**Our Call**

**Valuation – Maintain Buy with an unchanged PT of Rs. 130:** BEL would play a significant role in the successful implementation of the government's Make in India and Atmanirbhar Bharat initiatives as it is one of the key defence and aerospace players. Further, global defence companies are tying up with indigenous players, as there is a tremendous export potential for engineering services and components sourcing from India, which bodes well for BEL. BEL continues to invest heavily on capex (Rs. 750 crore of capex expected in FY2023) and has considerable expenditure in research and development (R&D, 6-7% of revenues). Further, the company plans to set up a semi-conductor fabrication plant in consortium with Hindustan Aeronautics Limited (HAL) and other companies, which would further reduce dependency on imports in the long term. BEL has strong manufacturing and R&D base, robust order book, healthy order prospects, diversifying revenue stream, and strong balance sheet with improving return ratios. We retain a Buy on the stock with an unchanged price target (PT) of Rs. 130, valuing it on September 2024E EPS.

**Key Risks**

- ◆ Delayed order execution and slower pace of fresh orders can affect revenue growth.
- ◆ Higher raw-material prices and shortage of some key components could affect margins going forward.

**Valuation (Consolidated)**

Particulars	Rs cr			
	FY22	FY23E	FY24E	FY25E
Net Sales	15,368	17,599	19,677	21,857
OPM (%)	8.9	14.5	11.8	11.1
PAT	2,399	2,686	3,186	3,604
Yoy growth	14.3	12.0	18.6	13.1
EPS (Rs.)	3.3	3.7	4.4	4.9
P/E (x)	32.0	28.6	24.1	21.3
EV/EBITDA (x)	24.2	21.2	18.0	16.2
RoCE (%)	17.8	18.6	19.7	19.0
RoE (%)	20.6	20.5	21.5	21.2

Source: Company; Sharekhan estimates

## Decent quarter, OPM beats estimates

BEL's consolidated results were in-line with our expectations with a beat on OPM. Sales grew by ~8% y-o-y to Rs 3,962 crore (vs our estimate of Rs 4,052 crore). The gross profit margins (GPM) remained flat y-o-y but improved 155bps q-o-q at 43.6% in Q2FY23. Operating profit was up by just 0.5% y-o-y to Rs 868 crore. OPM came in at 21.9% (vs 23.5% in Q2FY22) but exceeded our expectations of 20.4%. Further, OPM improved substantially by 528 bps on q-o-q basis. Net profit was flat at Rs 624 crore y-o-y. Order backlog stood at Rs. 52,795 crore; indicating strong revenue visibility of ~3.1 years (on TTM Revenue). The company had a cash balance of ~Rs 1,000 crore at the end of the quarter.

## Recent order win from TEV and MOUs would spur long-term growth

BEL has received a Letter of Intent (LoI) from Triton Electric Vehicle India Pvt Ltd (TEV), a part of Triton Electric Vehicle LLC, USA for procurement of 300 KW lithium-ion (Liion) battery packs for its semi-truck project in India at an estimated value of ~Rs 8060 crore. The battery packs are to be delivered by BEL to Triton in 24 months, commencing from January 2023. The battery packs will be manufactured at Pune unit of BEL. As per the BEL Annual Report FY2022, EV market in India has gained momentum after several policy initiatives such as setting up of a National Mission on Transformative Mobility and Battery Storage, Faster Adoption & Manufacturing of Electric Vehicles EV (FAME II) with an outlay of Rs 10,000 crore, launching of a Phased Manufacturing Programme (PMP) to localise production across the entire EV value chain, etc. Battery cells currently constitute ~35% of EVs' cost. Among the mature storage technologies, Liion batteries are the most versatile and efficient storage devices. The fuel cell technology-based energy storage products are also projected to dominate the future energy storage markets globally, as well as in India. Hence, BEL is actively pursuing opportunities in this domain.

BEL has also signed an MoU with TEV for manufacture of hydrogen fuel cells by BEL with technology transfer from TEV, to meet the requirements of Indian market and mutually agreed export markets. The MoU aims at tapping demand for clean energy solutions for various applications including for E- Mobility, by leveraging government of India's thrust for adoption of clean energy fuels for applications in transport, energy storage etc.

It has also signed an MoU with Munitions India Limited (MIL), to address requirements of Indian defence and export markets in the areas of ammunition, explosives and related systems. MIL is also a defence PSU, under the Ministry of Defence, Government of India. MIL, India's largest manufacturer and market leader, is engaged in the design, development and manufacture of various types of ammunition and explosives including small, medium and high caliber ammunition, mortars, rockets, hand grenades, high explosives and propellants. The MoU aims at leveraging the complementary strengths and capabilities of BEL and MIL under the Make In India initiative.

## Robust long-term outlook

BEL boasts of a healthy order book of Rs. 52,795 crore, which provides revenue visibility of more than three years. More than 90% of its revenue comes from government orders. The company has a promising order inflow pipeline and expects big ticket size orders such as Quick Response Surface to Air Missile (QRSAM), Medium Range Surface to Air Missile (MRSAM), Air Defence Fire Control Radar-ATULYA, mountain radars, and electronic warfare systems in the near term. The company plans to spend Rs. 750 crore towards various expansion initiatives, while ~Rs 1,000 crore would be spent on R&D in FY2023. Currently, ~80-82% of revenue come from indigenous technologies developed either by BEL or Defence Research and Development Organisation (DRDO). The company aims to increase share of non-defence verticals like civil, railways and metro. It expects 15% revenue contribution from non-defence in FY23. It expects exports to contribute 10% of total revenues as it is expanding presence in international markets and have participated in many tenders.

### Results (Consolidated)

Particulars	Q2FY23	Q2FY22	YoY%	Q1FY23	QoQ%
<b>Net sales</b>	<b>3,962</b>	<b>3,678</b>	<b>7.7</b>	<b>3,141</b>	<b>26.1</b>
Operating expenditure	3,093	2,814	9.9	2,618	18.1
<b>Operating profit</b>	<b>868</b>	<b>864</b>	<b>0.5</b>	<b>522</b>	<b>66.2</b>
Other income	74	62	18.3	82	(10.2)
Interest	2	0	257.1	1	71.6
Depreciation	109	99	10.1	99	10.2
PBT	831	827	0.5	504	64.8
Tax	216	216	(0.2)	148	45.9
Reported PAT	615	610	0.8	356	72.6
<b>Adjusted PAT</b>	<b>624</b>	<b>624</b>	<b>(0.1)</b>	<b>366</b>	<b>70.6</b>
Adjusted EPS (Rs.)	0.9	0.9	(0.1)	0.5	70.6
<b>Margin (%)</b>			<b>BPS</b>		<b>BPS</b>
GPM	43.6	43.7	(14.7)	42.0	155.5
OPM	21.9	23.5	(157)	16.6	528
NPM	15.7	17.0	(123)	11.6	410
Effective tax rate	28.0	26.2	181	29.4	(137)

Source: Company; Sharekhan Research

## Outlook and Valuation

### ■ Sector View – AatmaNirbhar Bharat initiative to boost defence manufacturing in India

The government is emphasising on creating an environment to boost the AatmaNirbhar Bharat programme in the defence sector and create a level-playing field for private players, including MSMEs. Completion of defence projects takes longer than envisaged earlier and, hence, the government is planning to incorporate cost-escalation clauses and provide incentives to vendors based on enhanced productivity and performance. Further, hike in foreign direct investment (FDI) to 74% through the automatic route would boost investments in the sector. This is likely to boost investments in the space, as foreign players in the defence sector would look at setting up joint ventures to establish defence manufacturing bases in India, considering the large opportunity with the opening up of the defence sector. The government has also established defence corridors in Tamil Nadu and Uttar Pradesh, which have helped in reducing the dependency on imports.

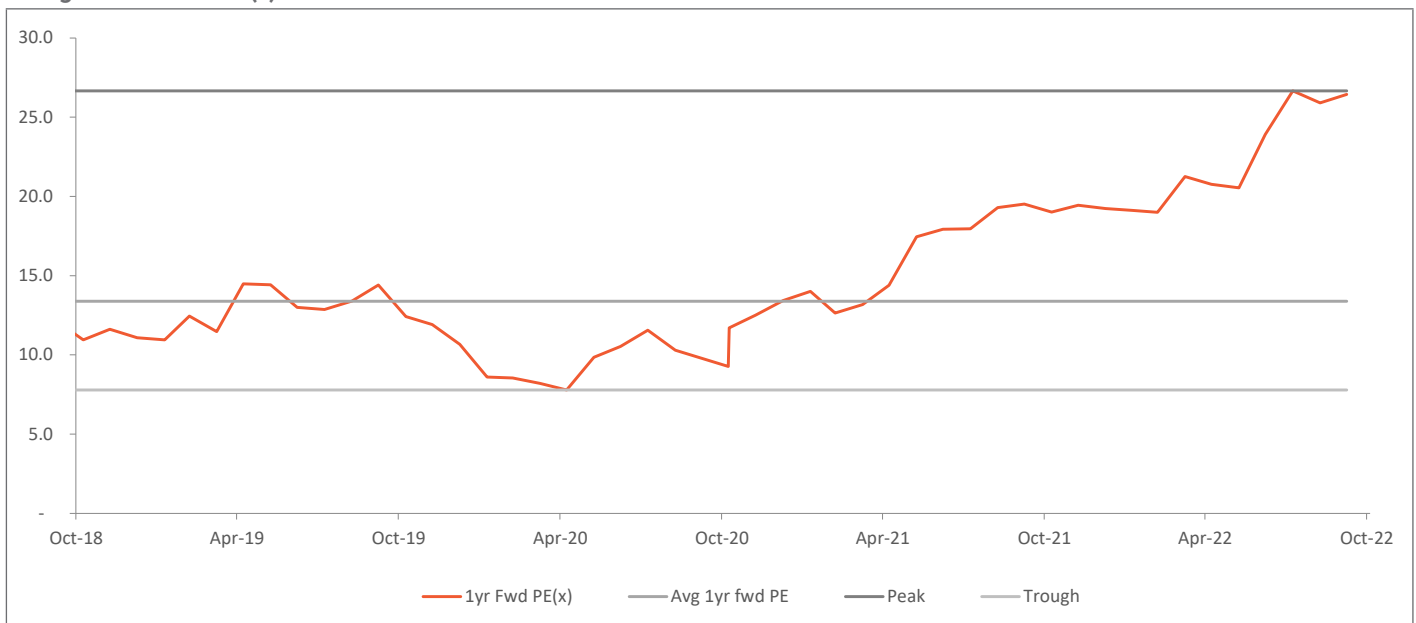
### ■ Company Outlook – Continues to focus on sustainable growth plans

BEL has been continuously focusing on sustainable growth plans and has taken various initiatives such as i) focus on enhancing its R&D capability; ii) enhancing manufacturing capabilities through timely modernisation and expansion of facilities; and iii) enter into joint ventures in existing and emerging businesses to enhance business visibility. The company's order pipeline includes orders for Akash missile system, long-range surface-to-air missile systems, naval equipment, and radar systems. BEL is also into project execution for the development of smart cities and manufacturing of electronic voting machines. In addition, BEL has been focusing on exploring the export (primarily non-defence currently) potential of defence electronics products and systems, which bodes well for revenue diversification. The company targets 10-15% revenue contribution from exports (currently ~2%).

### ■ Valuation – Maintain Buy with an unchanged PT of Rs. 130

BEL would play a significant role in the successful implementation of the government's Make in India and Atmanirbhar Bharat initiatives as it is one of the key defence and aerospace players. Further, global defence companies are tying up with indigenous players, as there is a tremendous export potential for engineering services and components sourcing from India, which bodes well for BEL. BEL continues to invest heavily on capex (Rs. 750 crore of capex expected in FY2023) and has considerable expenditure in research and development (R&D, 6-7% of revenues). Further, the company plans to set up a semi-conductor fabrication plant in consortium with Hindustan Aeronautics Limited (HAL) and other companies, which would further reduce dependency on imports in the long term. BEL has strong manufacturing and R&D base, robust order book, healthy order prospects, diversifying revenue stream, and strong balance sheet with improving return ratios. We retain a Buy on the stock with an unchanged price target (PT) of Rs. 130, valuing it on September 2024E EPS.

#### One-year forward P/E (x) band



Source: Company, Sharekhan Research

## About the company

BEL is a PSU with strong manufacturing and R&D capabilities and robust cost-control measures. The company manufactures electronics, communication, and defence equipment and stands to benefit from enhanced budgetary outlay for strengthening and modernising India's security.

## Investment theme

The government's Make in India and AatmaNirbhar Bharat initiatives along with rising spends for modernising defence equipment will support earnings growth in the coming years, as BEL is one of the key players with strong research and manufacturing capabilities in the defence space in the country. A robust order book provides strong revenue and earnings visibility. BEL is a good play on the defence sector on account of its strong manufacturing and R&D base, good cost control, growing indigenisation, and strong balance sheet.

## Key Risks

- ◆ Delayed order execution and slower pace of fresh orders can affect revenue growth.
- ◆ Higher raw-material prices and shortage of some key components such as semi-conductors could affect execution and earnings going forward.

## Additional Data

### Key management personnel

Mr. Dinesh Kumar Batra	Interim Chairman and Managing Director, Director (Finance)
Mr. Vinay Kumar Katyal,	Interim Director (R&D), Director (Bangalore Complex)
Mr. S Sreenivas	Secretary/Compliance Officer

Source: Company Website

### Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Nippon Life India Asset Management (CPSE ETF)	4.6
2	HDFC Asset Management Co. Ltd.	4.6
3	Kotak Mahindra Asset Management Co. Ltd.	3.6
4	Vanguard Group Inc.	1.7
5	BlackRock Inc.	1.5
6	FMR LLC	1.3
7	Life Insurance Corp. of India	1.3
8	Mirae Asset Global Investments	0.9
9	Canara Robeco Asset Management Co. Ltd.	0.9
10	DSP Investment Managers Ltd.	0.9

Source: Bloomberg old data

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## Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and deteriorating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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