

BHARAT ELECTRONICS LIMITED | Defence

Soft numbers in Q3, expect decent numbers going forward

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BEL reported earnings of ₹5.98 bn, against a yoy profit of ₹5.83 bn while sequentially it was down by 2% on a high base of Q2. Revenues grew by just 4.7% qoq and 11.8% yoy at ₹41.3 bn. EBITDA de-grew by 0.3% qoq while growing by 3.8% yoy at ₹8.53 bn. On the margins front, EBITDA margins came in at 20.7% which were 100 bps down qoq and 160 bps down yoy. The order book now stands ~₹501 bn providing strong visibility of ~4.4x of TTM revenues. BEL added ~₹36 bn of orders in 9M of FY23 and targets to add ~₹170 bn in Q4 alone on the back of huge order pipeline.

Strong defence order pipeline gives us confidence for long term visibility

BEL boasts of a healthy order book of ₹501 bn, which provides revenue visibility of more than three years. The company gained only ₹36 bn worth orders in 9M, while seems very confident to add ~₹170 bn of orders in the last quarter of the current fiscal, out of which management maintains to add at least ₹50 bn of orders in Q4 through big projects like LRSAM, Akash, Akash Prime, Avionics for air fighters, Sonar ships, Air Defence Fire Control Radar-ATULYA, mountain radars and electronic warfare systems in the near term. About 75-80% of its revenue comes from government orders. BEL rightly targets 15% topline growth in FY 23 and 15-20% target for next two years. The company plans to spend ₹6 bn towards various expansion initiatives, while ~₹10 bn would be spent on R&D (BEL currently has 2,700 engineers and scientists) from FY23 onwards every year. Currently, ~82-85% of revenue comes from indigenous technologies developed either by BEL or Defence Research and Development Organisation (DRDO).

Non-defence segment also to provide significant opportunities

To reduce dependence on defence, BEL has been focusing on diversifying into new and allied business verticals such as Medical Electronics, EVMs, Homeland Security, Metros, Energy Storage, Unmanned system, Space electronics and systems, Software Service (SAAS-opportunity ₹50bn), Ammunition (₹5bn/year opportunity), etc. Along with this, BEL is working on new businesses fetched in Q2 in the form of Civil orders like the Chennai Metro for door screening, Triton deal secured, ATMS (Air Traffic Management System), E-mobility LOI worth ₹80 bn for railways, UP100 smart city, EV charger installation at highways, EV battery packs etc. Non-defence segment contributed 10% of total revenue in Q3 FY23. This segment shall reduce BEL's dependence on defence segment. It expects 20% revenue contribution to come from non-defence in FY24-25 from current 10%. It expects exports to continue to contribute 10% of total revenues as it is expanding presence in international markets and has participated in many tenders.

Key Financials	FY 21	FY 22	FY 23E	FY 24E	FY 25E
Total sales(₹ bn)	140.6	153.1	181.0	210.0	245.0
EBITDA margins (%)	22.6%	21.6%	20.4%	21.3%	22.2%
PAT margins (%)	14.7%	15.3%	15.2%	15.7%	16.2%
EPS (Rs)	2.8	3.2	3.8	4.5	5.4
P/E (x)	33.3	29.2	25.0	20.8	17.3
P/BV (x)	6.4	5.7	4.9	4.4	3.8
EV/EBITDA (x)	20.6	20.4	17.3	14.2	11.6
ROE (%)	19.1%	19.6%	19.6%	20.9%	22.1%
ROCE (%)	22.9%	21.0%	20.3%	22.1%	23.8%
Dividend yield (%)	1.5	1.5	1.8	2.2	2.6

Rating	Buy
Current Market Price (₹)	94
12 M Price Target (₹)	119
Potential upside (%)	27

Stock Data

FV (₹) :	1
Total Market Cap (₹ bn) :	687
Free Float Market Cap (₹ bn) :	333
52-Week High / Low (₹) :	115 / 62
2-Year High / Low (₹) :	115 / 39
1 Yr Avg. Dly Traded Volume (in lakh)	125
BSE Code / NSE Symbol	500049 / BEL
Bloomberg :	BHE IN

Shareholding Pattern

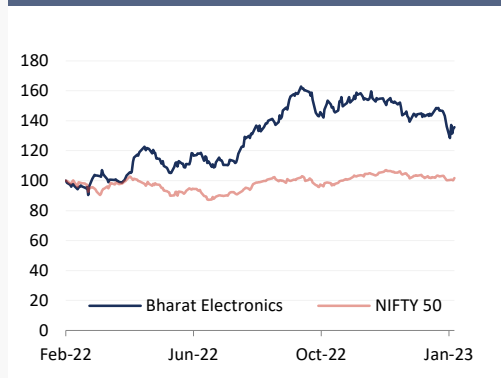
(%)	Dec-22	Sep-22	Jun-22	Mar-22
GOI	51.14	51.14	51.14	51.14
FPIs	17.28	17.36	15.99	16.77
MFs	20.56	21.19	22.42	21.74
Insurance	3.51	3.55	4.45	4.31
Others	7.51	6.76	6.00	6.04

Source: BSE

Price Performance

(%)	1M	3M	6M	1YR
BEL	-6.4%	-14.5%	1.8%	35.6%
Nifty 50	-2.1%	-1.1%	2.7%	1.7%

* To date / current date : February 03, 2023

BEL vs Nifty 50

Margin Outlook remains good

BEL has a strong indigenous portfolio of products (82-85%), which has reduced dependence on imports and other commodity prices. Also, BEL intends to add nearly 1,000 employees for new competencies. It intends to reduce employee cost without compromising on R&D (7% of topline). Furthermore, now that the chip shortage issue is behind them, we can expect strong surge in order delivery leading to higher capacity utilisation thus providing operating leverage. In Q2, the GOI has announced to localise 411 defence related goods. This step shall surely lead to higher indigenization leading to higher margin performance of the defence sector in totality. Also reducing dependence on nominated programs through higher contribution from services, non-defence and exports orders shall augur well for the margins. Additionally, BEL has a seasonally lumpy Q4, where financials witness an unusual jump, during which maximum orders are executed and topline as well as margin performance is elevated. Therefore, we believe that margins in FY23E should be in the 20-21% range. For FY24E and FY25E as well we expect margins to be better on improved product mix and stable input costs.

Outlook and Valuation

BEL reported subdued Q3 FY23 numbers. It is leveraging its past R&D investments and change in defence ministry's stance on import ban and increasing its levels of indigenization. Its impetus on outsourcing low-value-addition functions is further helping in improving and de-risking its cost structure. 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 is expected to utilize the above cost savings to increase its spending on R&D (7% of topline) and capex (₹6bn per annum over the next 3-4 years) and enter new markets.

BEL has been able to negate the overhang of lower margin in nomination-based contracts by increasing the quantum of exports and non-defence. It is also focusing on up-skilling its workforce and adding to employee count (100 per year taking up to 2600 employees currently with 40% engineers) in new areas with good growth prospects. Its strong order book, well-defined and distinct order pipeline gives us a very strong visibility over mid to long term despite 9M FY23 being a period of lower order offtake. BEL's new initiative in non-defense streams and emphasis on exports is expected to gain momentum soon and contribute meaningfully to the topline. On the back of decent topline and margin performance, huge cash surplus, comfortable WC cycle and rich return ratios, we maintain our BUY rating on the stock with a TP of ₹119 (22x rolled over FY25E earnings).

Quarterly Financial Snapshot

YE Mar (₹ mn)	Q3 FY23	Q2 FY23	% qoq	Q3 FY22	% yoy
Total net sales	41,310	39,458	4.7%	36,937	11.8%
RM cost	24,157	22,383	7.9%	22,002	9.8%
Employee cost	5,674	5,955	-4.7%	5,039	12.6%
Other expenses	2,944	2,563	14.9%	1,675	75.8%
EBITDA	8,535	8,557	-0.3%	8,221	3.8%
EBITDA Margins %	20.7%	21.7%	(100 bps)	22.3%	(160 bps)
Other income	575	750	-23.4%	593	-3.1%
Depreciation	1,008	1,042	-3.3%	929	8.5%
Interest	97	17	459.2%	2	5305.6%
PBT	8,004	8,248	-2.9%	7,884	1.5%
Tax	2,017	2,138	-5.7%	2,050	-1.6%
PAT	5,988	6,110	-2.0%	5,834	2.6%
PAT margins %	14.5%	15.5%	(100 bps)	15.8%	(130 bps)
Exceptional items	-	-	N/A	-	N/A
Adjusted PAT	5,988	6,110	-2.0%	5,834	2.6%
APAT margins %	14.5%	15.5%	(100 bps)	16.0%	(130 bps)

Source: Company, LKP Research

Income Statement

(₹ mn)	FY 21	FY 22	FY 23E	FY 24E	FY 25E
Total Revenues	1,40,638	1,53,138	1,81,000	2,10,000	2,45,000
Raw Material Cost	78,278	89,025	1,04,075	1,19,490	1,37,935
Employee Cost	19,407	21,094	28,055	31,500	35,525
Other Exp	11,142	9,926	11,946	14,280	17,150
EBITDA	31,811	33,092	36,924	44,730	54,390
EBITDA Margin(%)	22.6%	21.6%	20.4%	21.3%	22.2%
Depreciation	3,663	3,802	4,240	4,828	5,788
EBIT	28,148	29,291	32,684	39,902	48,602
EBIT Margin(%)	20.0%	19.1%	18.1%	19.0%	19.8%
Other Income	1,261	2,336	4,100	4,200	4,400
Interest	61	49	190	150	150
PBT	29,348	31,578	36,594	43,952	52,852
PBT Margin(%)	20.9%	20.6%	20.2%	20.9%	21.6%
Tax	8,694	8,089	9,149	10,988	13,213
Adjusted PAT	20,654	23,489	27,446	32,964	39,639
APAT Margins (%)	14.7%	15.3%	15.2%	15.7%	16.2%
Exceptional items	0	0	0	0	0
PAT	20,654	23,489	27,446	32,964	39,639
PAT Margins (%)	14.7%	15.3%	15.2%	15.7%	16.2%

Key Ratios

YE Mar	FY 21	FY 22	FY 23E	FY 24E	FY 25E
Per Share Data (₹)					
Adj. EPS	2.8	3.2	3.8	4.5	5.4
CEPS	3.3	3.7	4.3	5.2	6.2
BVPS	14.8	16.4	19.1	21.6	24.6
DPS	1.4	1.4	1.7	2.0	2.4
Growth Ratios(%)					
Total revenues	8.8%	8.9%	18.2%	16.0%	16.7%
EBITDA	22.6%	21.6%	20.4%	21.3%	22.2%
EBIT	18.2%	4.1%	11.6%	22.1%	21.8%
PAT	15.1%	13.7%	16.8%	20.1%	20.2%
Valuation Ratios (X)					
PE	33.3	29.2	25.0	20.8	17.3
P/CEPS	28.3	25.2	21.7	18.2	15.1
P/BV	6.4	5.7	4.9	4.4	3.8
EV/Sales	4.7	4.4	3.5	3.0	2.6
EV/EBITDA	20.6	20.4	17.3	14.2	11.6
Operating Ratios (Days)					
Inventory days	127.6	132.0	134.0	136.0	138.0
Receivable Days	170.0	145.5	150.0	160.0	165.0
Payables day	110.4	103.1	105.0	100.0	98.0
Net Debt/Equity (x)	0.00	0.00	0.00	0.00	0.00
Profitability Ratios (%)					
ROCE	22.9%	21.0%	20.3%	22.1%	23.8%
ROE	19.1%	19.6%	19.6%	20.9%	22.1%
Dividend payout ratio	49.5%	43.6%	45.0%	45.0%	45.0%
Dividend yield	1.5	1.5	1.8	2.2	2.6

Balance Sheet

(₹ mn)	FY 21	FY 22	FY 23E	FY 24E	FY 24E
Equity and Liabilities					
Equity Share Capital	2,437	2,437	7,309	7,309	7,309
Reserves & Surplus	1,05,642	1,17,406	1,32,501	1,50,631	1,72,433
Total Network	1,08,079	1,19,843	1,39,810	1,57,940	1,79,742
Total debt	0	0	0	0	0
Long term provisions	14,074	18,001	20,001	21,501	23,501
Deferred tax assets/liabilities	649	615	615	615	615
Other long term liabilities	82	721	721	721	721
Current Liab & Prov					
Trade payables	42,533	43,245	52,068	57,534	65,781
Short term provs+ borrow	3,425	4,156	4,156	4,156	4,156
Other current liabilities	1,21,689	1,47,919	1,51,919	1,55,919	1,59,919
Total current liab & provs	1,67,647	1,95,320	2,08,144	2,17,609	2,29,856
Total Equity & Liabilities	2,90,531	3,34,499	3,69,290	3,98,386	4,34,434
Assets					
Net block	24,227	24,545	30,306	31,477	37,689
Capital WIP	3,507	3,986	4,986	5,986	6,986
Intangible assets under devt	4,430	5,296	5,296	5,296	5,296
Non current investments	13,667	15,843	15,843	15,843	15,843
Long term loans and adv	5,028	6,480	6,480	6,480	6,480
Other non current assets	3,908	6,778	6,778	6,778	6,778
Total fixed assets	54,766	62,928	69,689	71,860	79,072
Cash, cash equiv & bank deposits	50,082	74,991	77,372	81,375	86,262
Inventories	49,153	55,396	66,449	70,449	74,449
Trade receivables	65,515	61,034	74,384	92,055	1,10,753
Other current assets	71,016	80,151	81,401	82,651	83,901
Total current Assets	2,35,766	2,71,571	2,99,606	3,26,530	3,55,366
Total Assets	2,90,531	3,34,499	3,69,290	3,98,386	4,34,434

Cash Flow

(₹ mn)	FY 21	FY 22	FY 23E	FY 24E	FY 25E
PBT	29,348	31,578	36,594	43,952	52,852
Depreciation	3,663	3,802	4,240	4,828	5,788
Interest	58	18	190	150	150
Chng in working capital	22,659	15,507	-10,830	-11,955	-9,702
Tax paid	-5,323	-8,024	-9,149	-10,988	-13,213
Other operating activities	644	-1,264	0	0	0
Cash flow from operations (a)	51,034	41,616	21,045	25,987	35,875
Capital expenditure	-4,677	-5,535	-11,000	-7,000	-13,000
Chng in investments	-1,678	-2,231	0	0	0
Other investing activities	-19,331	-40,840	32,601	0	0
Cash flow from investing (b)	-25,686	-48,606	21,601	-7,000	-13,000
Free cash flow (a+b)	25,348	-6,989	42,646	18,987	22,875
Inc/dec in borrowings	-83	0	0	0	0
Dividend paid (incl. tax)	-10,227	-10,233	-12,351	-14,834	-17,837
Interest paid	-58	-18	-190	-150	-150
Other financing activities	0	-521	4,872	0	0
Cash flow from financing (c)	-10,755	-10,772	-7,668	-14,984	-17,987
Net chng in cash (a+b+c)	14,593	-17,761	34,978	4,003	4,888
Closing cash & cash equivalents	30,155	12,394	47,372	51,375	56,262

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