



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 May 08, 2023

31.21

High Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

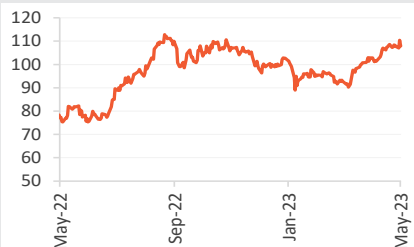
Company details

Market cap:	Rs. 79,677 cr
52-week high/low:	Rs. 115/73
NSE volume: (No of shares)	140.2 lakh
BSE code:	500049
NSE code:	BEL
Free float: (No of shares)	357.4 cr

Shareholding (%)

Promoters	51.1
FII	16.4
DII	25.5
Others	6.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	5.0	13.0	1.0	40.0
Relative to Sensex	1.1	9.1	0.2	25.8

Sharekhan Research, Bloomberg

Bharat Electronics Ltd

Strong Q4, Aiming for broad based growth

Capital Goods

Sharekhan code: BEL

Reco/View: Buy



Upgrade



Maintain



Downgrade

CMP: Rs. 109

Price Target: Rs. 130



Summary

- BEL delivered a strong Q4FY2023 performance with a strong beat on margins and net profit. The company guided for 17% revenue growth in FY2024 and expects OPM to be 21-23%.
- Order backlog stands strong at ~Rs. 60,690 crore (~3.5x revenue). FY2024 order intake expectation is at least ~Rs. 20,000 crore with the likelihood of beat if QRSAM or MRSAM orders kick in.
- Capex of Rs. 700-800 crore in FY2024, R&D expenditure will be at 7% of revenue in the next 1-2 years. BEL is expediting efforts to increase non-defence revenue to diversify its business. Further, any breakthrough on the exports front could be a key growth catalyst.
- We expect Revenue/PAT CAGR of ~16% each over FY23-25E. The stock trades at ~20x FY2025E EPS. We retain a Buy on BEL with a revised PT of Rs. 130.

BEL's consolidated results were ahead of our and street estimates on all fronts, with a strong beat on margins and net profit estimates. Sales grew by 2.2% y-o-y to Rs. 6,479 crores. GPM grew by 628 bps y-o-y to 48.3%, given the decline in raw material cost. Operating profit grew by ~16% y-o-y to Rs. 1,832 crore and OPM rose by 339 bps y-o-y to 28.3% (vs our expectation of 24.9%). Net profit grew by ~20% y-o-y to Rs. 1,382 crores driven by strong operating performance and aided by the lower tax rate. Order backlog stood at Rs. 60,690 crores (up 21% y-o-y), led by strong order inflow in Q4.

Key positives

- Order backlog at ~Rs. 60,690 crore (~3.5x revenue)
- Strong beat on OPM and net profit estimates
- The company provided order inflow guidance of over Rs. 20,000 crore for FY2023. There is also a possibility of awarding a few large orders like QRSAM and MRSAM projects.
- GPM increased by 628 bps y-o-y to 48.3%. OPM increased by 339 bps y-o-y to 28.3%, and net profit increased by ~20% y-o-y.
- Order intake for Q4 has been robust, leading to a strong order book at the end of the quarter.

Key negatives

- Exports' share in revenue is still minuscule at ~2%.
- Non-defence sales share is also low at ~10-11%.

Revision in estimates – We have tweaked our estimates marginally for FY2024-FY2025E.

Management Commentary

- The company is likely to maintain its order inflow at Rs. 20,000 crore in FY2024. However, the company is not factoring in many big-ticket programs like QRSAM and MRSAM projects which are in the pipeline and may be awarded in the current year or next year.
- Revenue growth is expected to be ~17% in FY2024, and the execution will come from the current order book, depending on the delivery timelines. The company is not factoring in any revenue from the order intake in FY2024E.
- As per the company, 75% of its production/revenues are indigenized with 40-45% assistance from DRDO and the rest 25% is through foreign OEMs.
- The company would incur a capex of Rs. 700-800 crore in FY2024. The company would spend on advance electro-optics in Andhra Pradesh, EW factory in Ibrahimpatnam, a defence system integration complex in Nagpur and explosives facility in Pune.
- The company expects gross margins to be at ~40 - 42% for FY2024, while OPM would also be broadly in the 21-23% range.
- Exports revenue in FY2023 came in at US\$ 48mn or Rs. 394 crore and is targeting US\$ 90-100mn in exports in FY2024.
- In FY2023, R&D expense was 6.2% of revenue. However, the company aims to increase the spending to ~7% of revenues.

Our Call

Valuation – Maintain Buy with a revised PT of Rs. 130: BEL's Q4FY2023 performance has been very strong. Further, strong order intake has allayed concerns over revenue visibility. BEL has guided for strong revenue growth and margin guidance is also decent. We believe BEL would play a significant role in successfully implementing the government's Make in India and AtmaNirbhar Bharat initiatives as it is a key defence and aerospace player. 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 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 expect Revenue/PAT CAGR of ~16% each over FY23-25E. The stock trades at ~20x FY2025E EPS and we believe there is still room for further upside. We retain a Buy on the stock with a revised price target (PT) of Rs. 130, valuing it on FY2025E EPS.

Key Risks

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

Valuation (Consolidated)

Particulars	FY22	FY23	FY24E	FY25E
Net Sales	15,368	17,734	20,717	23,660
OPM (%)	21.7	23.0	23.1	23.6
PAT	2,399	2,984	3,391	4,006
YoY growth	14.3	24.4	13.6	18.1
EPS (Rs.)	3.3	4.1	4.6	5.5
P/E (x)	28.3	26.7	23.5	19.9
EV/EBITDA (x)	21.6	20.5	17.8	15.1
RoCE (%)	17.8	20.3	20.4	20.8
RoE (%)	20.6	22.7	22.6	23.0

Source: Company; Sharekhan estimates

Strong quarter, the Order book also strengthened on a q-o-q basis

BEL's consolidated results were ahead of our and street estimates on all fronts, with a strong beat on margins and net profit estimates. Sales grew by 2.2% y-o-y to Rs. 6,479 crores. GPM grew by 628 bps y-o-y to 48.3% given decline in raw material cost. Operating profit grew by ~16% y-o-y to Rs1,832 crore and OPM rose by 339 bps y-o-y at 28.3% (vs our expectation of 24.9%). Net profit grew by ~20% y-o-y to Rs. 1,382 crores driven by strong operating performance and aided by the lower tax rate. Order backlog stood at Rs. 60,690 crores (up 21% q-o-q) led by strong order inflow in Q4.

Strong order book, non-defence orders and exports to drive future growth

BEL has a healthy order book of Rs. 60,690 crore, providing revenue visibility for about three years. More than 90% of its revenue comes from government orders. The company has a promising order inflow pipeline. It expects big ticket size orders such as Quick Response Surface to Air Missiles (QRSAM), Medium Range Surface to Air Missile (MRSAM), Air Defence Fire Control Radar-ATULYA, mountain radars, and electronic warfare systems in the near to medium term. The company aims to increase the share of non-defence verticals like civil, railways and metro rail in total revenues. BEL is also trying to get a breakthrough in exports with countries like Egypt, Malaysia, etc and is hopeful of increasing its export share in total revenue.

BEL Q4FY23 conference call highlights

- ♦ **Order inflow guidance:** The company has received order inflows of above Rs 20,000 crore in FY23 and expects to maintain the same levels for FY24. However, the company is not factoring in many big ticket programs like QRSAM and MRSAM projects which are in the pipeline and may be awarded in current year or next year. Other orders are the Akash Missile ground support system which could be around Rs. 4,500 crore and other shipbuilding programs like the Next-Generation Offshore Patrol Vessel program (NGOPV) and Next Generation Missile Vessels (NGMV) will be to the tune of Rs. 5,000 crore to Rs. 6,000 crore. Shakti Electronic Warfare System is orders of Rs. 5,000 crore.
- ♦ **Revenue guidance:** Revenue growth is expected to be ~17% in FY2024 and the execution will come from the current order book depending on the delivery timelines. The company is not factoring in any revenue from the order intake in FY2024E.
- ♦ **Revenue mix:** Defence contributed 87% to FY2023 revenues, followed by 10.6% from non-defence and 2.4% from exports. The company expects a marginal rise in non-defence share this year. Areas like metro, railways and ATS will take time to fructify but the company has been developing capabilities in ATS, railways, metro, etc and it has signed MoUs with various entities such as Airport Authority of India (AAI) and Delhi Metro Rail Corporation (DMRC), etc.
- ♦ **75% indigenization has been achieved at the company level:** As per the company, 75% of its orders are self-designed with 40-45% assistance from DRDO, and the rest 25% is through foreign OEMs.
- ♦ **Capex guidance:** In FY2023, capex was around Rs. 500 crore. The company would incur a capex of Rs 700-800 crore in FY2024. The company would spend on advance electro-optics in Andhra Pradesh, EW factory in Ibrahimpatnam, defence system integration complex in Nagpur and an explosives facility in Pune.
- ♦ **Margin guidance:** The company expects gross margins to be at ~40 - 42% for FY24, while OPM would also be broadly in the 21-23% range.
- ♦ **Aims US\$ 90- 100 mn exports in FY2024E:** Export revenue in FY23 came in at US\$ 48mn or Rs. 394 crore and BEL is targeting US\$ 90-100mn in exports in FY24.
- ♦ **Aims to take R&D expenditure to 7% of sales:** In FY2023, R&D expense was 6.2% of revenue. However, company aims to increase the spending to ~7% of revenues.

Results (Consolidated)

Rs cr

Particulars	Q4FY23	Q4FY22	YoY %	Q3FY23	QoQ %
Net sales	6,479	6,340	2.2	4,153	56.0
Operating expenditure	4,647	4,762	(2.4)	3,290	41.3
Operating profit	1,832	1,578	16.1	863	112.2
Other income	66	64	3.5	59	12.8
Interest	2	4.3	(42.1)	10	(74.7)
Depreciation	114	106	7.4	106	7.5
PBT	1,782	1,531	16.4	806	121.0
Tax	415	385	7.9	203	104.3
Reported PAT	1,366	1,147	19.2	603	126.6
Adjusted PAT	1,382	1,154	19.7	613	125.4
Adjusted EPS (Rs.)	1.89	1.58	19.7	0.8	125.4
Margin(%)			BPS		BPS
GPM (%)	48.3	42.0	628	41.7	652
OPM (%)	28.3	24.9	339	20.8	748
NPM (%)	21.3	18.2	312	14.8	657
Effective tax rate (%)	26.0	25.1	88	26.0	-

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - AatmaNirbhar Bharat initiative to boost defence manufacturing in India

The government is emphasising 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, a 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 reduce the import dependency.

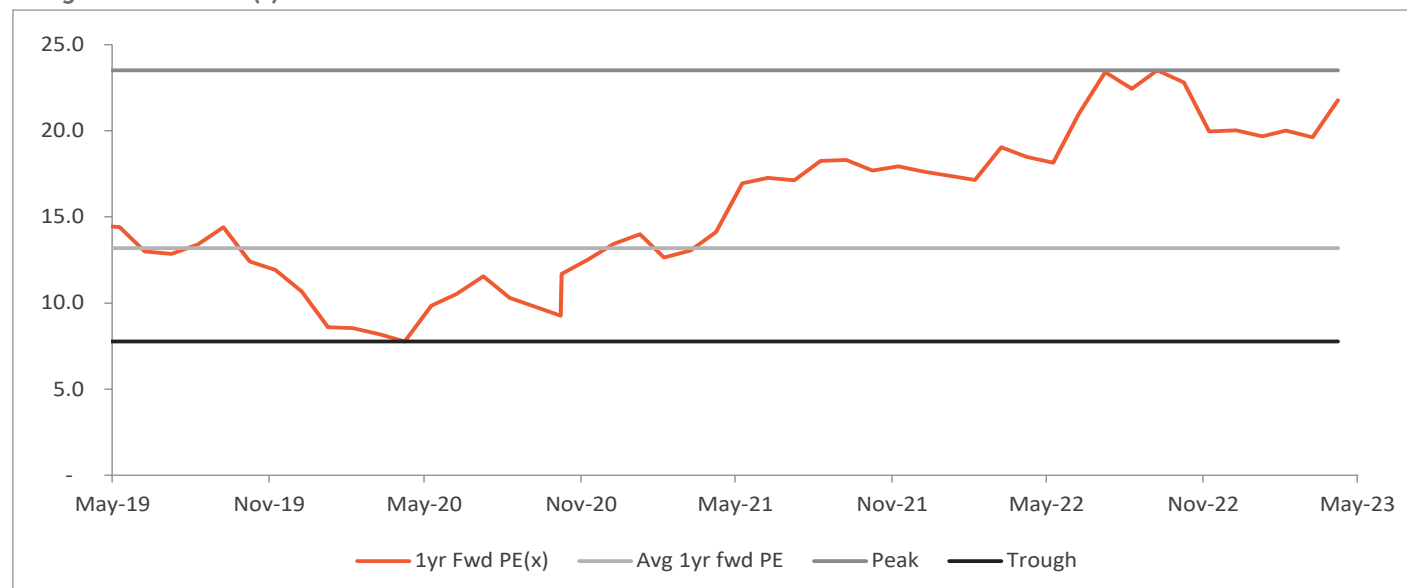
■ Company outlook - diversification and a strong order pipeline would boost growth

BEL has been continuously focusing on sustainable growth plans and has taken various initiatives such as i) Focusing on enhancing its R&D capability, ii) Enhancing manufacturing capabilities through timely modernisation and expansion of facilities; and iii) Entering into joint ventures in existing and emerging businesses to enhance business visibility. Order pipeline includes orders for Medium Range Surface - To - Air Missile (MRSAM)- Rs. 20,000 crore, Quick Reaction Surface-to-Air Missile (QRSAM) – Rs. 20,000 crore, Akash Prime Rs. 4,500 crores; etc. 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 a revised PT of Rs. 130

BEL's Q4FY2023 performance has been very strong. Further, strong order intake has allayed concerns over revenue visibility. BEL has guided for strong revenue growth and margin guidance is also decent. We believe BEL would play a significant role in successfully implementing the government's Make in India and AtmaNirbhar Bharat initiatives as it is a key defence and aerospace player. 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 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 expect Revenue/PAT CAGR of ~16% each over FY23-25E. The stock trades at ~20x FY2025E EPS and we believe there is still room for further upside. We retain a Buy on the stock with a revised price target (PT) of Rs. 130, valuing it on FY2025E EPS.

One-year forward P/E (x) band



Source: Sharekhan Research

About 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 benefits 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 spending 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 because of its strong manufacturing and R&D base, good margin trajectory, cost efficiency, 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 critical components such as semiconductors could affect execution and earnings going forward.

Additional Data

Key management personnel

Mr. Bhanu Prakash Srivastava	Executive Director-Chairperson-MD
Mr. Vinay Kumar Katyal	Executive Director
Mr. Damodar S Bhattad	Director (Finance) & Chief Financial Officer (CFO)

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Nippon Life India Asset Management	4.25
2	Kotak Mahindra Asset Management Company	3.51
3	HDFC Asset Management Company Limited	3.01
4	Vanguard Group Incorporation	1.74
5	BlackRock Incorporation	1.60
6	FMR LLC	1.32
7	Canara Robeco Asset Management Company	1.25
8	DSP Investment Managers Private Limited	1.07
9	Mirae Asset Global Investments Company	1.04
10	ICICI Prudential Asset Management Company Limited	0.84

Source: Bloomberg

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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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