Stock Update

Company Update

Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Bharat Electronics Ltd

Higher order intake to drive sustained long-term growth

Capital Goods	Sharekhan code: BEL

Reco/View: Buy ↔	CMP: **Rs. 173**	Price Target: **Rs. 210** ↑

↑ Upgrade ↔ Maintain ↓ Downgrade

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 31.21

Updated Aug 06, 2023

High Risk

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

Source: Morningstar

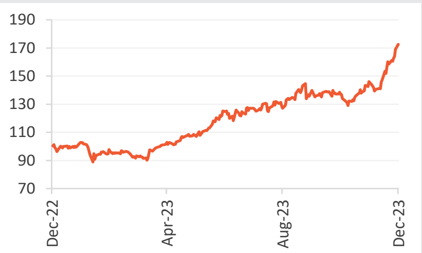
Company details

Market cap:	Rs. 1,26,167 cr
52-week high/low:	Rs. 174/87
NSE volume: (No of shares)	161 lakh
BSE code:	500049
NSE code:	BEL
Free float: (No of shares)	357.2 cr

Shareholding (%)

Promoters	51.1
FII	17.2
DII	24.2
Others	7.5

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	19.9	26.0	38.3	72.0
Relative to Sensex	11.3	19.3	25.4	56.6

Sharekhan Research, Bloomberg

Summary

- Recently, BEL received orders worth ~Rs. 8,801 crore, which helped the company in exceeding management's order intake guidance of Rs. 20,000 crore, which gives strong growth visibility for FY2024 and beyond.
- Higher spending on defence by the government over the next few years with a focus on indigenisation will help company in maintaining growth momentum.
- New non-defence products will help the company diversify its revenue. Further, any breakthrough on the exports front could be a key growth catalyst.
- We expect Revenue/PAT CAGR of ~15% each over FY2023-FY2026E along with a high RoE/RoCE of 22%/21% in FY2026E. We retain Buy with a revised PT of Rs. 210.

Bharat Electronics Limited (BEL) recently won orders worth ~Rs. 8,801 crore, which helped the company in achieving a cumulative order intake worth Rs. 23,176 crore in FY2024, exceeding management's guidance of Rs. 20,000 crore. At the end Q2FY2024, the company's order backlog stood at ~Rs. 68,728 crore (~3.8x TTM revenue). We expect significant growth in the company's order book as the government recently cleared the procurement of defence equipment worth ~Rs. 2.23 lakh crore. BEL has continued to maintain its growth momentum by building on its core strength and delivering defence equipment like missile systems and radar systems. In medium term, we expect the company to receive large orders related to QRSAM, MRSAM, Integrated Air Command and Control System (IACCS), and Drones. New non-defence products like Air Traffic Management Automation System and growth in exports will help the company in diversifying its revenue along with increasing the size of the total addressable market (TAM). The company has developed partnerships with design agencies, academia, start-ups, and global OEMs to maintain its leadership in defence electronics space.

- **Higher-than-expected order intake bodes well for long-term growth:** BEL has received orders worth Rs. 4,522 crore from the Indian Army for various calibres of fuses and has received orders worth Rs. 4,279 crore for various other equipment. The company has received a cumulative order intake worth Rs. 23,176 crores in FY2024, exceeding management's guidance of Rs. 20,000 crore. Management expects the company to achieve 15-17% growth in FY2024. Given higher-than-expected order inflow, we expect the company to maintain double-digit revenue growth rate.
- **Increased domestic defense spending will help in maintaining growth momentum:** The company expects to maintain its growth momentum by building on its core strength and delivering products like missile systems (QRSAM, MRSAM, and LRSAM) and electronics like radar systems. Recently, Defence Acquisition Council cleared the procurement of defence equipment worth ~Rs. 2.23 lakh crore, which will help the company in growing its order book. The upgradation of Su-30 MKI upgrade focuses on procuring equipment from domestic manufacturers, which bodes well for domestic manufacturers like BEL.
- **Higher R&D, exports, and diversification to increase TAM:** BEL is expediting efforts to increase non-defence revenue to diversify its business, which would help in generating additional growth opportunity. Given high-growth opportunities in Medical Electronics and Solutions, BEL has a dedicated vertical for this segment. Creation of IPRs and the acquisition of key technologies have increased BEL's TAM. BEL plans to expand the network of marketing offices to further gain traction in the export business with a focus on Southeast Asia, Europe, Middle East, Africa, and North and South America either through direct engagement with customers or in collaboration with other Indian companies or local partners. The company has developed partnerships with design agencies, academia, start-ups, and global OEMs for developing technologies to meet emerging customer requirements, develop differentiated products, and expand its addressable market.

Our Call

Valuation – Maintain Buy with a revised PT of Rs. 210: BEL has already exceeded FY2024 order intake guidance and its future order pipeline is promising as large orders like QRSAM or MRSAM are expected to be awarded over the next few quarters. 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 a strong manufacturing and R&D base, robust order book, healthy order prospects, diversifying revenue stream, and strong balance sheet with improving return ratios. The stock is currently trading at 28x its FY2026E EPS. We retain our Buy rating on the stock with a revised price target (PT) of Rs. 210.

Key Risks

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

Valuation (Consolidated) Rs cr

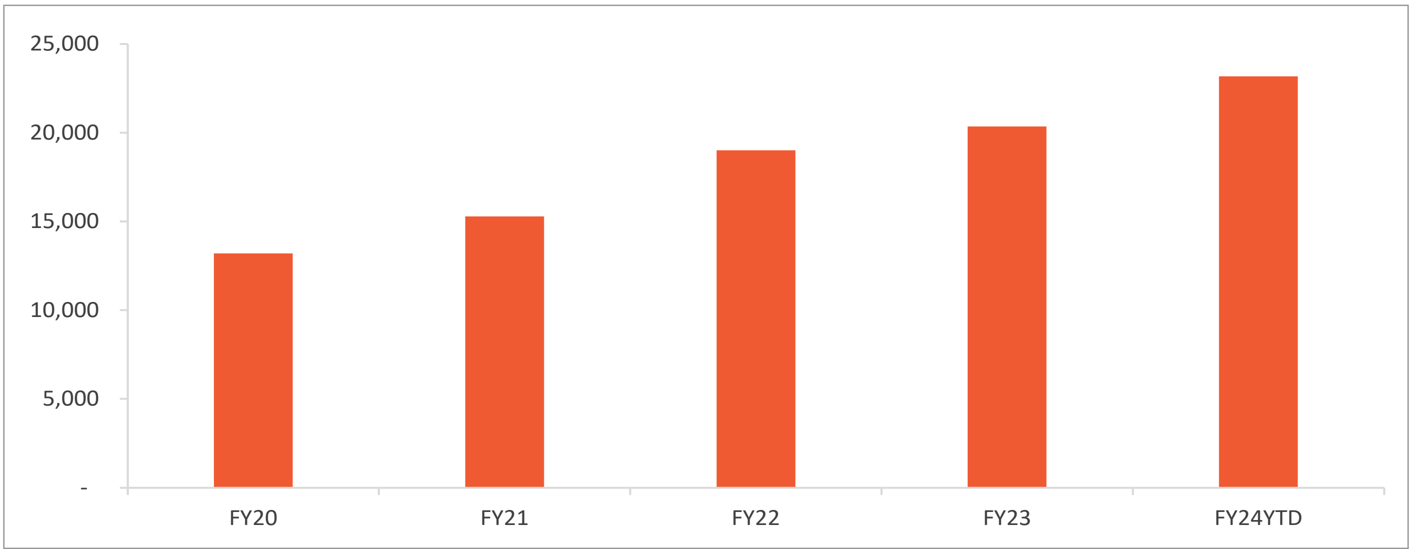
Particulars	FY23	FY24E	FY25E	FY26E
Net Sales	17,734	20,717	23,660	26,648
Operating Profit Margin (%)	23.0	23.1	23.6	23.6
Adjusted PAT	2,984	3,421	4,021	4,537
YoY Growth (%)	24.4	14.6	17.5	12.8
Adjusted EPS (Rs.)	4.1	4.7	5.5	6.2
P/E (x)	42.3	36.9	31.4	27.8
EV/EBITDA (x)	31.8	27.5	23.4	20.7
RoCE (%)	20.3	20.6	20.9	20.6
RoE (%)	22.7	22.7	23.0	22.2

Source: Company; Sharekhan estimates

Order intake already above mgmt. guidance

Recently, the company has received orders worth Rs. 4,522 crore from Indian Army for the supply of fuses for various calibres. Apart from this, the company has received orders worth ~Rs. 4,279 for AMC for AEW&C system (Airborne Early Warning & control), Uncooled TI sights, Software Defined Radios, SWIR pay load, Annual Maintenance Contract (AMC) for Integrated Air Command and Control System, Passive Night Vision Binoculars, Electronic Warfare Testers, Medical Systems (Exports), Consumables and Batteries for Electronic Voting Machines (EVMs), Night Vision Devices Spares & Services and AMC of Radars. BEL has cumulatively received orders worth Rs. 23,176 crores in FY2024, which is above management's guidance of Rs. 20,000 crore. The order pipeline is also robust as the company expects orders worth around Rs. 2,500 crore for next-generation offshore patrol vessels (NGOPV) and Rs. 3,000 crore for BMP tank upgrade. Management expects to close these orders by the end of FY2024 or the beginning of FY2025. Management expects the company to achieve 15-17% growth in FY2024. Given higher-than-expected order inflow, we expect the company to maintain double-digit revenue growth rate.

Continued growth in order intake



Source: Company, Sharekhan Research

Future orders to help maintain growth momentum

The company expects to maintain its growth momentum by building on its core strength and delivering products like missile systems (QRSAM, MRSAM and LRSAM), electronics like radar systems, radar upgrades, tank electronics, EO systems, and big upgrade programmes like for tanks BMPs. Recently, Defence Acquisition Council (DAC) cleared the procurement of Light Combat Aircraft, Light Combat Helicopters, anti-tank munitions, indigenous Towed Gun System (TGS), 155mm nubless projectiles, Automatic Target Tracker & Digital Basaltic Computer for tanks and Medium Range Anti-Ship Missiles worth Rs 2.23 lakh crore. Defence Acquisition Council (DAC) also cleared the indigenous upgradation of Su-30 MKI Aircraft. Upgradation of Su-30 MKI focuses on procuring equipment from domestic manufacturers, which bodes well for domestic manufacturers like BEL. These future orders will help company in maintaining growth momentum. Moreover, BEL is expediting efforts to increase non-defence revenue to diversify its business would help in generating additional growth opportunity. Given high-growth opportunities in Medical Electronics and Solutions, BEL has a dedicated vertical for this segment. Recently, the company has received an export order for Medical Systems. Creation of intellectual property rights and acquisition of key technologies has also increased BEL's TAM.

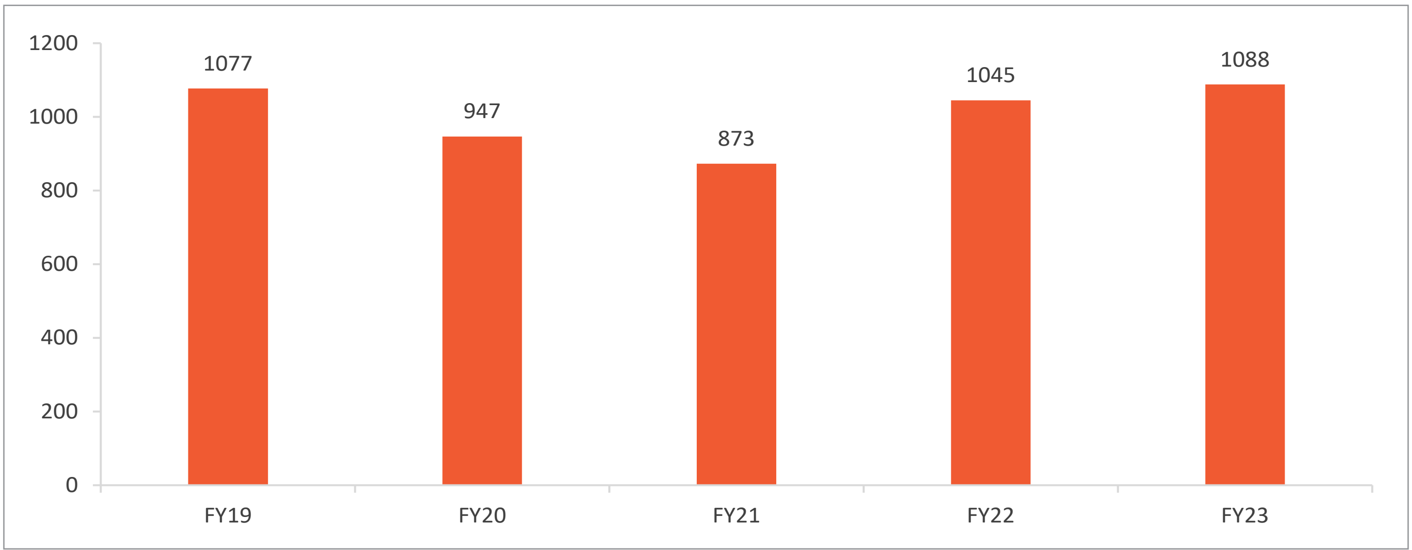
Breakthrough on the exports front could be a key growth catalyst

BEL plans to expand the network of marketing offices to further gain traction in the export business with a focus on Southeast Asia, Europe, Middle East, Africa, and North and South America either through direct engagement with customers or in collaboration with other Indian companies or local partners. The company has set a target of achieving \$90 million in exports, of which the company has already sold more than \$27 million worth of products in H1FY2024. Apart from defence equipment, the company is currently exploring civil and medical equipment opportunities globally.

Continued investment in R&D

The company has developed partnership with design agencies, academia, start-ups, and global OEMs for developing technologies to meet emerging customer requirements, develop differentiated products, and expand its addressable market.

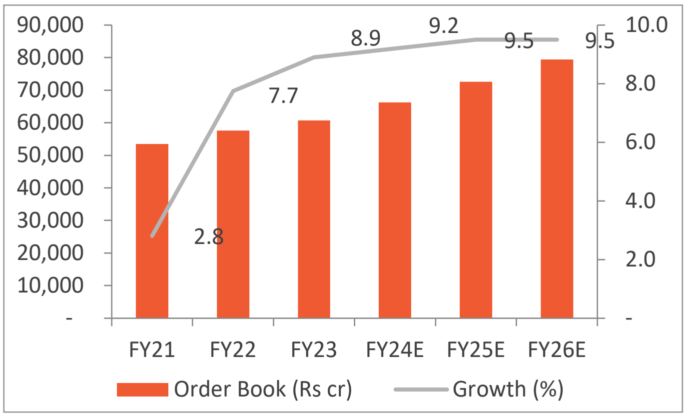
Investment in R&D



Source: Company, Sharekhan Research

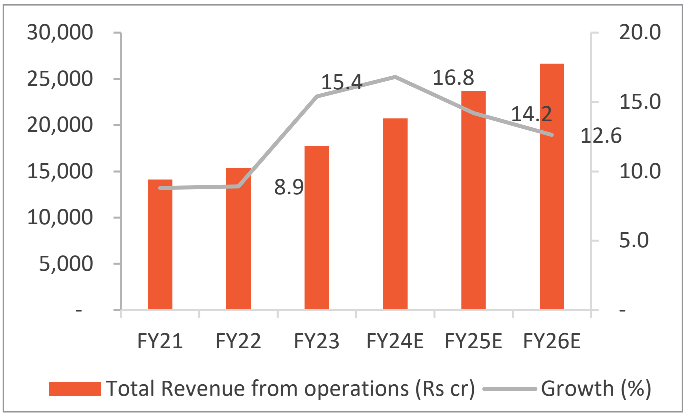
Financials in charts

Order book growth trend



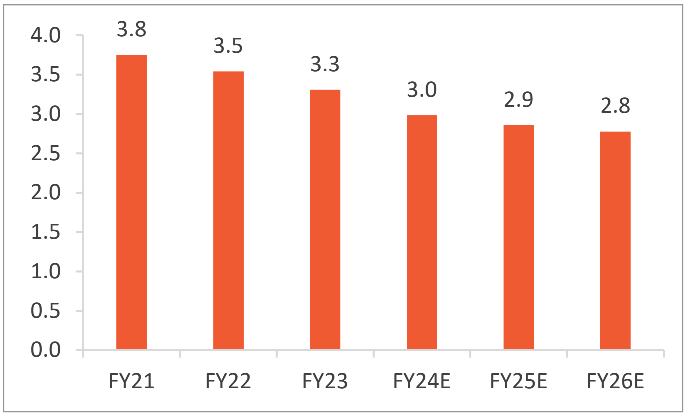
Source: Company, Sharekhan Research

Revenue growth trend



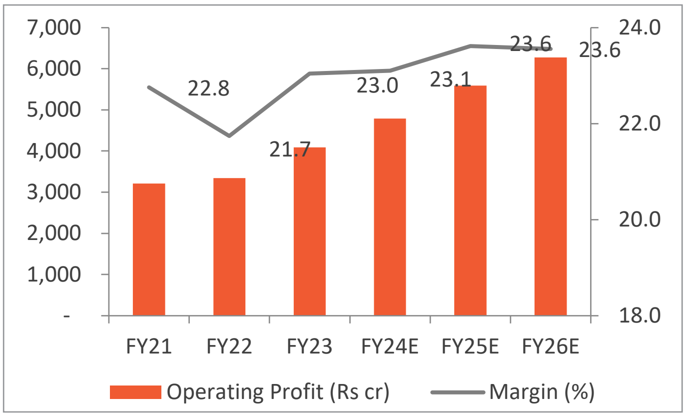
Source: Company, Sharekhan Research

Order book to revenue ratio



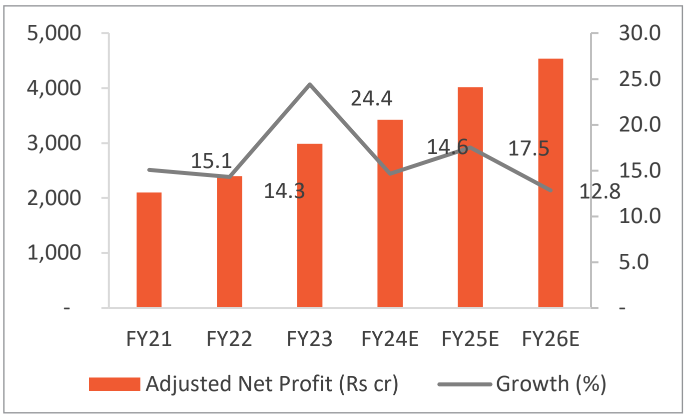
Source: Company, Sharekhan Research

Operating profit and margin trend



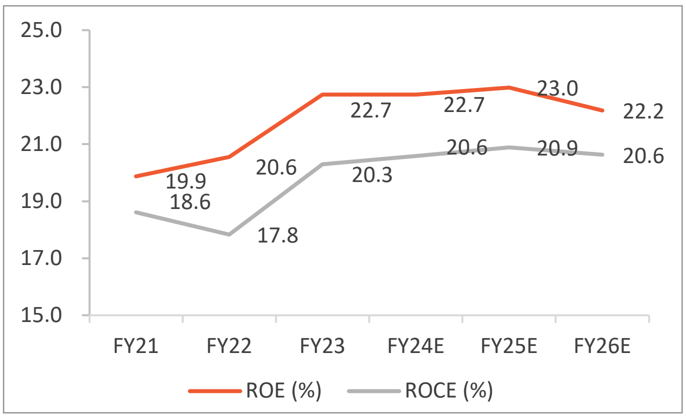
Source: Company, Sharekhan Research

Net profit growth trend



Source: Company, Sharekhan Research

Return ratios trend (%)



Source: Company, Sharekhan Research

Outlook and Valuation

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

The government emphasises 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. Completing defence projects take longer than envisaged earlier and, hence, the government plans 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 increase 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 ample 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 import dependency.

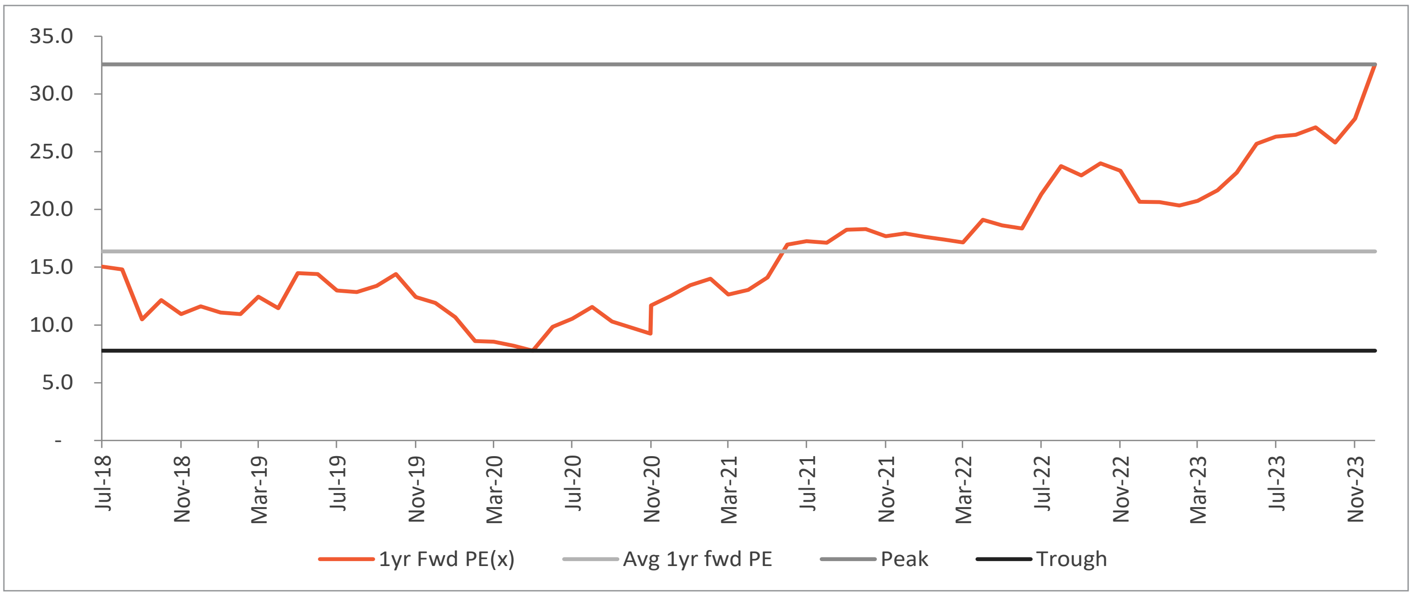
■ Company outlook - Diversification and a strong order pipeline would boost growth.

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. Long-term order pipeline includes high -value orders such as Medium Range Surface-To-Air Missile (MRSAM) - Rs. 15,000-20,000 crore, Quick Reaction Surface-to-Air Missile (QRSAM) – Rs. 20,000 crore. 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% revenue contribution from exports (currently ~2%) in the long term.

■ Valuation - Maintain Buy with a revised PT of Rs. 210

BEL has already exceeded FY2024 order intake guidance and its future order pipeline is promising as large orders like QRSAM or MRSAM are expected to be awarded over the next few quarters. 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 a strong manufacturing and R&D base, robust order book, healthy order prospects, diversifying revenue stream, and strong balance sheet with improving return ratios. The stock is currently trading at 28x its FY2026E EPS. We retain our Buy rating on the stock with a revised PT of Rs. 210.

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 plays well in 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.

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	3.91
2	Kotak Mahindra Asset Management Co	3.48
3	HDFC Asset Management Co Ltd	2.62
4	Vanguard Group Inc/The	1.95
5	BlackRock Inc	1.83
6	Canara Robeco Asset Management Co	1.37
7	FMR LLC	1.18
8	DSP Investment Managers Pvt Ltd	1.14
9	UTI Asset Management Co Ltd	0.85
10	ICICI Prudential Asset Management	0.83

Source: Bloomberg

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 detoriating 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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by BNP PARIBAS

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