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## Bharat Electronics (BHAELE)

₹ 179

### Re-rate on sustained order inflows...

Order inflows for Bharat Electronics (BEL) have moved to a new growth trajectory with FY17 order inflows at ~₹ 15000 crore (our estimate: ₹ 12000 crore for the year). We believe it is likely to continue in FY18E and FY19E also. We estimate order inflows in the range of ₹ 12000-15000 crore in FY18E, FY19E. This is on the back of large orders like tactical communication systems ₹ 10000 crore, Akash missile systems ₹ 5000 crore, electronic warfare systems ~₹ 7000 crore, LRSAM & QRSAM ₹ 5000-10000 crore, battlefield management system ~₹ 30000 crore, electronic voting machines (including voter-verifiable paper audit trail) ~₹ 6000 crore. This is like to propel the order backlog to ~₹ 46000 crore by FY19E. Order backlog in FY15 was at ~₹ 21600 crore. Thus, order backlogs are likely to exhibit commendable growth of 20.8% CAGR in FY15-19E. With strong competencies in execution, BEL is likely to deliver a superior topline and bottomline growth in FY17-19E. For now, we keep our estimates unchanged (we will revise post Q4FY17 results) but re-rate the company due to improved visibility on sustainable order inflows.

#### Strong moat, moderate capex to help sustain momentum

BEL has developed strong competency in the area of defence electronics, which is one of the most critical areas for capability building of armed forces. Historically, a large part of defence capital spends (45-60%) has been in this segment. High-end technologies in the electronics segment, long gestation periods, heavy capital requirements, specific requirements of armed forces and secrecy related to defence projects act as key entry barriers in this segment. This gives companies like BEL a strong competitive advantage over any upcoming local and foreign completion. With a planned capex of over ₹ 1500 crore in FY17E-19E, BEL is well placed to capitalise on opportunities in the defence sector.

#### R&D, exports, healthy balance sheet to help sustain momentum

BEL is an R&D-focused company. In FY17E, it is expected to spend ~₹ 775 crore (~9% of sales) on developing new products. New products have historically helped BEL achieve up to 25% of its turnover. This has also given BEL strong competitive advantage over any upcoming local and foreign completion. The management has guided that R&D spend may rise to 12% of sales in coming few years. This, we believe will enable the company to indigenise number of imported technologies. Exports for BEL are likely to be ~₹ 570 crore in FY17E (~6.5% of turnover). With the government's increasing focus on exports, BEL has set-up a dedicated business unit and marketing group to become key supply chain partner of global defence contractors. This is likely to increase exports contribution to 10% of the topline by FY19E. BEL also has a strong balance sheet with near nil debt and cash balance of ~₹ 6000 crore (even after the buyback of ~₹ 2100 crore). With a strong focus on capital allocation, BEL is well-placed to deliver superior return on its deployed capital.

#### Re-rate BEL on accelerated order inflows, strong revenue visibility

Continuous order inflows and BEL's track record in execution give us reasonable confidence about the continued stable performance of the company. Accordingly, we expect BEL to deliver sales and PAT CAGR of 15% and 9%, respectively, in FY16-19E. We re-rate the company due to improved visibility (order book to bill ~5x in FY17E from ~3x in FY15). We value the company at 26x P/E (21x earlier) on FY19E EPS of ₹ 7.8 to arrive at a target price of ₹ 204 per share. We upgrade the stock from HOLD to BUY.

#### Rating Matrix

Rating Matrix	
Rating	: Buy
Target	: ₹ 204
Target Period	: 12 - 15 months
Potential Upside	: 14%

#### What's Changed?

Target	Changed from ₹ 165 to ₹ 204
EPS FY18E	Unchanged
EPS FY19E	Unchanged
Rating	Changed from Hold to Buy

#### Key Financials

₹ Crore	FY16	FY17E	FY18E	FY19E
Revenue	7,295	8,725	9,887	11,058
EBITDA	1,461	1,738	1,809	1,991
EBITDA (%)	20.0	19.9	18.3	18.0
Net Profit	1,358	1,569	1,624	1,753
EPS (₹)	5.7	7.0	7.3	7.8

#### Valuation Summary

(x)	FY16	FY17E	FY18E	FY19E
P/E	31.6	25.5	24.6	22.8
Target P/E	36.1	29.1	28.1	26.0
EV / EBITDA	22.3	19.6	18.5	16.4
P/BV	4.9	5.3	4.7	4.2
RoNW (%)	16	20.9	19.1	18.3
RoCE (%)	22.0	29.0	26.6	25.4

#### Stock Data

Stock Data	
Average Volumes (shares)	441000
Market Capitalization	₹ 39981.9 Crore
Total Debt (FY17E)	₹ 250 Crore
Cash and Investments (FY17E)	₹ 6131.8 crore
EV (FY17E)	₹ 34100.1 Crore
52 week H/L (₹)	1624 / 1009
Equity capital	₹ 223.4 Crore
Face value	₹ 10
MF Holding (%)	12.1
FII Holding (%)	6.6
Promoter Holding (%)	68.2

#### Price Performance

Return (%)	1M	3M	6M	12M
Bharat Electronics	6.4	13.7	34.1	42.5
Centum Electronics	2.6	(7.1)	19.6	0.4
Astra Micro Wave	0.8	(1.2)	0.7	(4.2)

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## Financial summary (Standalone)

Profit and loss statement		₹ Crore			
(₹ Crore)	FY16	FY17E	FY18E	FY19E	
Net Sales	7,154.1	8,479.4	9,674.7	10,820.3	
Other operating income	141.1	245.9	212.8	238.0	
<b>Total Revenue</b>	<b>7,295.2</b>	<b>8,725.3</b>	<b>9,887.5</b>	<b>11,058.3</b>	
Other income	532.2	580.0	605.0	625.0	
<b>Total</b>	<b>7,827.3</b>	<b>9,305.3</b>	<b>10,492.5</b>	<b>11,058.3</b>	
Total Raw Material Costs	3,790.8	4,460.2	5,224.3	5,842.9	
Employee Expenses	1,301.8	1,577.2	1,838.2	2,055.9	
other expenses	741.1	949.7	1,015.8	1,168.6	
<b>Total Operating Expenditure</b>	<b>5,833.7</b>	<b>6,987.0</b>	<b>8,078.3</b>	<b>9,067.4</b>	
<b>Operating Profit (EBITDA)</b>	<b>1,461.4</b>	<b>1,738.3</b>	<b>1,809.2</b>	<b>1,990.9</b>	
Interest	4.5	20.9	44.0	50.0	
PBDT	1,989.1	2,297.4	2,370.2	2,565.9	
Depreciation	168.9	192.0	207.6	232.2	
PBT before Exceptional Items	1,820.2	2,105.4	2,162.5	2,333.7	
Total Tax	455.3	536.9	538.5	581.1	
PAT before MI	1,364.9	1,568.5	1,624.1	1,752.6	
Minority Interest	-	-	-	-	
<b>PAT</b>	<b>1,357.7</b>	<b>1,568.5</b>	<b>1,624.1</b>	<b>1,752.6</b>	
<b>EPS</b>	<b>5.7</b>	<b>7.0</b>	<b>7.3</b>	<b>7.8</b>	

Source: Company, ICICIdirect.com Research

Balance sheet		₹ Crore			
(₹ Crore)	FY16	FY17E	FY18E	FY19E	
Equity Capital	240.0	223.4	223.4	223.4	
Reserve and Surplus	8,493.8	7,294.5	8,296.5	9,377.9	
<b>Total Shareholders funds</b>	<b>8,733.8</b>	<b>7,517.8</b>	<b>8,519.9</b>	<b>9,601.2</b>	
Minority Interest	-	-	-	-	
Other Non Current Liabilities	2.1	7.1	12.1	17.1	
<b>Total Debt</b>	<b>6.2</b>	<b>250.0</b>	<b>275.0</b>	<b>275.0</b>	
<b>Total Liabilities</b>	<b>8,742.1</b>	<b>7,774.9</b>	<b>8,806.9</b>	<b>9,893.3</b>	
Gross Block	2,841.4	3,521.1	4,021.1	4,521.1	
Acc: Depreciation	1,883.0	2,074.9	2,282.6	2,514.8	
Net Block	958.4	1,446.2	1,738.5	2,006.3	
Capital WIP	429.7	250.0	250.0	250.0	
<b>Total Fixed Assets</b>	<b>1,388.1</b>	<b>1,696.2</b>	<b>1,988.5</b>	<b>2,256.3</b>	
Non Current Assets	447.3	447.3	447.3	447.3	
Inventory	4,167.9	4,302.9	4,876.0	5,453.4	
Debtors	3,711.9	4,541.9	5,146.9	5,756.4	
Loans and Advances	599.1	785.3	791.0	884.7	
Other Current Assets	58.1	69.8	79.1	88.5	
<b>Cash</b>	<b>7,332.0</b>	<b>6,131.8</b>	<b>6,710.2</b>	<b>7,615.0</b>	
<b>Total Current Assets</b>	<b>15,868.9</b>	<b>15,831.7</b>	<b>17,603.2</b>	<b>19,797.9</b>	
Current Liabilities	8,118.3	9,562.0	10,564.7	11,815.7	
Provisions	1,161.8	956.2	1,056.5	1,181.6	
<b>Net Current Assets</b>	<b>6,588.8</b>	<b>5,313.5</b>	<b>5,982.0</b>	<b>6,800.6</b>	
<b>Total Assets</b>	<b>8,742.2</b>	<b>7,774.9</b>	<b>8,807.0</b>	<b>9,893.3</b>	

Source: Company, ICICIdirect.com Research

Cash flow statement		₹ Crore			
Profit after Tax	1,357.7	1,568.5	1,568.5	1,752.6	
Depreciation	168.9	192.0	192.0	232.2	
Interest	4.5	20.9	20.9	50.0	
<b>Cash Flow before WC changes</b>	<b>1,531.1</b>	<b>1,781.4</b>	<b>1,781.4</b>	<b>2,034.8</b>	
Changes in inventory	(798.5)	(135.0)	(573.1)	(577.4)	
Changes in debtors	74.2	(830.0)	(605.0)	(609.5)	
Changes in loans & Advances	152.9	(186.2)	(5.7)	(93.7)	
Changes in other current assets	(4.6)	(11.7)	(9.3)	(9.4)	
<b>Net Increase in Current Assets</b>	<b>(575.9)</b>	<b>(1,162.9)</b>	<b>(1,193.1)</b>	<b>(1,289.9)</b>	
Changes in creditors	1,590.5	1,443.6	1,002.7	1,251.0	
Changes in provisions	385.1	(205.6)	100.3	125.1	
<b>Net Inc in Current Liabilities</b>	<b>1,975.6</b>	<b>1,238.1</b>	<b>1,103.0</b>	<b>1,376.1</b>	
<b>Net CF from Operating activities</b>	<b>2,930.8</b>	<b>1,856.5</b>	<b>1,691.3</b>	<b>2,121.1</b>	
Changes in deferred tax assets	(34.5)	-	-	-	
(Purchase)/Sale of Fixed Assets	(646.2)	(500.0)	(500.0)	(500.0)	
<b>Net CF from Investing activities</b>	<b>(964.2)</b>	<b>(495.0)</b>	<b>(495.0)</b>	<b>(495.0)</b>	
Dividend and Dividend Tax	(489.6)	(574.1)	(589.5)	(636.2)	
<b>Net CF from Financing Activities</b>	<b>(516.2)</b>	<b>(2,561.7)</b>	<b>(617.9)</b>	<b>(721.3)</b>	
<b>Net Cash flow</b>	<b>1,450.4</b>	<b>(1,200.2)</b>	<b>578.4</b>	<b>904.8</b>	
Opening Cash/Cash Equivalent	5,881.5	7,332.0	6,131.8	6,710.2	
<b>Closing Cash/ Cash Equivalent</b>	<b>7,332.0</b>	<b>6,131.8</b>	<b>6,710.2</b>	<b>7,615.0</b>	

Source: Company, ICICIdirect.com Research

Key ratios		(Year-end March)			
	FY16	FY17E	FY18E	FY19E	
<b>Per Share Data</b>					
EPS	5.7	7.0	7.3	7.8	
Cash per Share	30.5	27.5	30.0	34.1	
BV	36.4	33.7	38.1	43.0	
Dividend per share	1.7	2.1	2.2	2.4	
Dividend payout ratio	0.3	0.3	0.3	0.3	
<b>Operating Ratios</b>					
EBITDA Margin	20.0	19.9	18.3	18.0	
PAT Margin	19.0	18.5	16.8	16.2	
<b>Return Ratios</b>					
RoE	15.5	20.9	19.1	18.3	
RoCE	22.0	29.0	26.6	25.4	
RoIC	242.4	163.5	120.6	116.5	
<b>Valuation Ratios</b>					
EV / EBITDA	22.3	19.6	18.5	16.4	
P/E	31.6	25.5	24.6	22.8	
EV / Net Sales	4.5	3.9	3.4	3.0	
Sales / Equity	0.8	1.2	1.2	1.2	
Market Cap / Sales	5.5	4.6	4.0	3.6	
Price to Book Value	4.9	5.3	4.7	4.2	
<b>Turnover Ratios</b>					
Asset turnover	5.2	4.6	4.2	4.3	
Debtors Turnover Ratio	1.9	2.1	2.0	2.0	
Creditors Turnover Ratio	1.0	1.0	1.0	1.0	
<b>Solvency Ratios</b>					
Debt / Equity	0.0	0.0	0.0	0.0	
Current Ratio	0.9	0.9	0.9	0.9	
Quick Ratio	0.5	0.5	0.5	0.5	

Source: Company, ICICIdirect.com Research

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