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Company update and
recommendation
change

Defence

Target price: Rs153

Target price revision
Rs153 from Rs121

Earnings revision

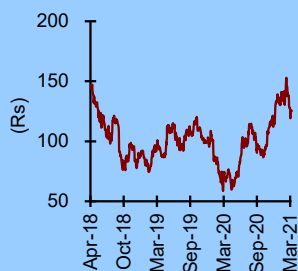
(%)	FY21E	FY22E	FY23E
Sales	↑ 14.4	↑ 14.5	↑ 14.6
EBITDA	↑ 31.3	↑ 23.3	↑ 23.2
EPS	↑ 37.2	↑ 27.1	↑ 26.9

Shareholding pattern

	Jun '20	Sep '20	Dec '20
Promoters	51.1	51.1	51.1
Institutional investors	40.1	41.2	41.6
MFs and others	25.6	25.6	26.3
FIs/Insurance	6.6	5.6	4.6
FIs	7.9	10.0	10.7
Others	8.8	7.7	7.3

Source: BSE India

Price chart



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Bharat Electronics

BUY

Upgrade from REDUCE

Rs126

Strong performance in FY21

Bharat Electronics' (BEL) reported higher than expected FY21 provisional revenues (in-line with guidance) at Rs135bn. This highlights the i) buoyancy in defence budget seen over CY20 ii) BELs' ability to keep diversifying its revenue stream as indicated by the execution mix and iii) BEL's ability to execute in an accelerated manner 30,000 ICU ventilator. We believe, the risks to a constrained defence budget have largely reduced over the events of the past year, specially for defence primes like BEL. Management has earlier guided towards higher capex run rate to achieve double digit revenue growth (10-15% YoY capex growth p.a. from the likely Rs5.5bn in FY21E). We upgrade BEL to BUY from REDUCE with a revised target price of Rs153/share (from Rs121) based on FY23E PE of 15x.

- **FY21E order inflow inline with Guidance at Rs150bn.** FY21 end orderbook stood at Rs530bn. Some of the major orders acquired during the year are ICU ventilators, software defined radios & communication equipment, radars, sonars, torpedo decoy systems, Electronic Warfare systems, Networking & Encryption products, smart cities etc.
- **Execution much higher than expected at Rs135bn (I-Sec Rs 121bn).** This has been driven by ICU Ventilators, Missile Systems (Akash & LRSAM), Gun Upgrades, Various Radars, Various Sonars, Command & Control Systems, Electro-optic systems, Communication & Encryption products, EW Systems, Coastal Surveillance System, Electronic Fuzes, Home Land Security & Smart City Projects, KFON, Avionics Package for LCA etc. BEL achieved export sales of ~ US\$50mn during FY21. Major products exported include Coastal Surveillance System, Trans-Receive (TR) Modules, Bharati Radio, Identification of Friend or Foe-Interrogator (IFFI), Electro-optic system compact multi-purpose advanced stabilization system (EOS CoPASS), Electro-mechanical parts, Radar Finger Printing System (RFPS), Low Band Receivers (LBREC), Spares for Radars etc.
- **Near-term order opportunities.** BEL has already accounted for execution of avionics related to LCA Mk 2 as HAL has received Lol for the same. Key elements of the avionics package for LCA Mk 2 include Fly by Wire Digital Flight Control Computer (DFCC). Future opportunities include Jammer for LCA. Also, LUH and LCH (helicopters) may allow sensors (MAWS and counter-measure dispensers along with HMDS) and weapons to significantly augment BEL's avionics revenue.
- **BEL targets** i) civilian segment (including medical equipments) to increase from 7% of topline to 15% in the next 2-3 years; ii) to increase the current 10% revenue contribution from service sector (including AMCs); iii) capture a pie of the revenue expenditure budget of the Armed Forces via entry into electronic fuses and RF seekers (new complex in Machilipatnam to be commissioned soon); and iv) gain share in the base business, i.e. integration of missile complex (Palasamudram; another separate SBU for QRSAM in Bengaluru), entry into ammunitions, etc.

Market Cap	Rs296bn/US\$4.0bn
Reuters/Bloomberg	BAJE.BO/BHE IN
Shares Outstanding (mn)	2,436.6
52-week Range (Rs)	155/58
Free Float (%)	48.9
FII (%)	10.7
Daily Volume (US\$/'000)	24,488
Absolute Return 3m (%)	4.3
Absolute Return 12m (%)	68.0
Sensex Return 3m (%)	3.4
Sensex Return 12m (%)	75.2

Year to March	FY20	FY21E	FY22E	FY23E
Revenue (Rs mn)	129,677	138,831	154,856	172,780
Net Income (Rs mn)	18,239	19,702	22,481	24,910
Dil. EPS (Rs)	7.5	8.1	9.2	10.2
% Chg YoY	(3.3)	8.0	14.1	10.8
P/E (x)	17.5	16.2	14.2	12.8
CEPS (Rs)	9.0	10.0	11.3	12.5
EV/E (x)	11.0	10.2	8.6	7.5
Dividend Yield (%)	2.1	2.1	2.1	2.1
RoCE (%)	24.5	22.8	23.0	22.4
RoE (%)	18.1	17.4	17.5	17.0

Upgrade to **BUY** from **REDUCE**

We upgrade BEL to **BUY** from **Reduce** with a revised target price of Rs153/share. We value the company as 15x FY23E EPS.

Earnings change

We have adjusted for FY21 earnings. Higher base for FY21E allows for higher FY22/23E revenues and earnings as well. We have kept the capex low for FY21E as we are not sure of the final spend possible in FY21.

Table 1: Earnings change

(Rs mn)

	New			Old			Change (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Revenue	138,831	154,856	172,780	121,331	135,256	150,828	14.4	14.5	14.6
EBITDA	29,903	33,913	37,578	22,768	27,496	30,513	31.3	23.3	23.2
PAT	19,702	22,481	24,910	14,365	17,682	19,625	37.2	27.1	26.9
TP			153			121			

Source: Company data, I-Sec research

Key risks

Continued strength in order inflows from the base business (Indian defence) can help future execution and reduce the necessity for diversification.

Cause of concern is the extent of cashflow pressures – part of which was observed from H1FY21 consolidated cashflows. We expect these pressures to moderate in the medium term with ease in defence budgetary allocation.

Financial summary

Table 2: Profit & Loss statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Operating Income	129,677	138,831	154,856	172,780
Operating Expenses	102,132	108,927	120,943	135,202
EBITDA	27,545	29,903	33,913	37,578
% margins	21.2	21.5	21.9	21.7
Depreciation & Amortisation	3,719	4,647	5,047	5,447
Gross Interest	36	18	18	18
Other Income	994	751	873	873
Recurring PBT	24,784	25,989	29,721	32,986
Less: Taxes	-	-	-	-
Add: Share of profit from associates	321	263	263	263
Recurring Net Income	18,239	19,702	22,481	24,910

Source: Company data, I-Sec research

Table 3: Balance sheet

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Assets				
Total Current Assets	187,381	201,284	221,143	244,486
of which cash & cash eqv.	16,809	15,920	29,070	37,745
Total Current Liabilities & Provisions	142,120	141,823	145,292	149,405
Net Current Assets	45,261	59,461	75,851	95,081
Investments	1,621	1,621	1,621	1,621
Strategic/Group	1,621	1,621	1,621	1,621
Other Marketable	-	-	-	-
Net Fixed Assets	27,126	29,479	28,432	26,985
Capital Work-in-Progress	8,280	4,371	4,463	4,554
Goodwill	19,076	19,104	19,143	19,193
Total Assets	101,364	114,036	129,509	147,434
Liabilities				
Borrowings	507	507	507	507
Deferred Tax Liability	-	-	-	-
Government Grants	-	-	-	-
Minority Interest	142	170	208	259
Equity Share Capital	2,437	2,437	2,437	2,437
Reserves & Surplus				
Net Worth	100,715	113,360	128,794	146,668
Total Liabilities	101,364	114,036	129,509	147,433

Source: Company data, I-Sec research

Table 4: Cashflow statement

(Rs mn, year ending March 31)

	FY20	FY21E	FY22E	FY23E
Operating Cashflow	22,646	23,381	26,448	29,289
Working Capital Changes	3,058	(15,089)	(3,240)	(10,555)
Capital Commitments	(7,466)	(3,091)	(4,091)	(4,091)
Free Cashflow	18,238	5,200	19,117	14,643
Investing Cashflow	(6,490)	(2,340)	(3,218)	(3,218)
Issue of Share Capital	-	-	-	-
Buyback of shares	-	-	-	-
Inc (Dec) in Borrowings	(250)	-	-	-
Others	(9,835)	(6,841)	(6,841)	(6,841)
Extraordinary Items	-	-	-	-
Chg. in Cash	9,130	(889)	13,150	8,675

Source: Company data, I-Sec research

Table 5: Key ratios

(Year ending March 31)

	FY20	FY21E	FY22E	FY23E
Per Share Data (in Rs.)				
EPS(Basic Recurring)	7.5	8.1	9.2	10.2
Diluted Recurring EPS	7.5	8.1	9.2	10.2
Recurring Cash EPS	9.0	10.0	11.3	12.5
Dividend per share (DPS)	2.8	2.8	2.8	2.8
Book Value per share (BVPS)	41.3	46.5	52.9	60.2
Growth Ratios (%)				
Operating Income	6.6	7.1	11.5	11.6
EBITDA	(5.2)	8.6	13.4	10.8
Recurring Net Income	(3.3)	8.0	14.1	10.8
Valuation Ratios (x)				
P/E	17.5	16.2	14.2	12.8
P/CEPS	14.5	13.1	11.6	10.5
P/BV	3.2	2.8	2.5	2.2
EV / EBITDA	11.0	10.2	8.6	7.5
EV / FCF	16.6	58.4	15.2	19.3
Operating Ratios (%)				
Raw Material/Sales	54.7	53.4	54.6	55.3
SG&A/Sales	8.0	9.4	8.8	8.7
Other Income / PBT	4.0	2.9	2.9	2.6
Effective Tax Rate	27.7	25.1	25.1	25.1
NWC / Total Assets	0.4	0.5	0.6	0.6
Inventory Turnover	1.8	1.4	1.5	1.5
Asset Turnover	1.3	1.2	1.2	1.2
Net D/E Ratio (x)	(0.2)	(0.1)	(0.2)	(0.3)
Return/Profitability Ratios (%)				
Recurring Net Income Margins	14.1	14.2	14.5	14.4
RoCE	24.5	22.8	23.0	22.4
RoNW	18.1	17.4	17.5	17.0
Dividend Pay-out Ratio	37.4	34.6	30.3	27.4
EBITDA Margins	21.2	21.5	21.9	21.7

Source: Company data, I-Sec research

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