

Bharat Heavy Electricals

BUY
Maintained
Rs75

Business revival and diversification on cards

Bharat Heavy Electricals' (BHEL) Q3FY23 revenue grew 2.5% YoY to Rs52.6bn, led by 7% YoY growth in power segment, which was offset by 21% YoY decline in industrial segment revenue. Gross margin contracted 400bps YoY to 30%, but expanded 100bps QoQ. Other expenses declined 97% YoY, which we believe was due to provision reversal. This led to EBITDA growth of 62% YoY to Rs1.4bn. Industrial order intake was impressive at Rs16bn (+142%), which ranged across supply of transformers, propulsion equipment, substations, gas compressors, among others. Power order intake was Rs16.5bn, down 37%. Total order intake was flat at Rs120bn. Orderbook now stands at ~Rs1.03trn (4.5x TTM sales). We await revival in execution in industrial segment. Factoring in lower execution in industrial segment and lower than expected other expense, we adjust our estimates accordingly. Nevertheless, we keep our FY25E EPS unchanged as execution of the recently-won orders will by then gather pace and boost profitability as well. We, therefore, maintain our BUY rating on the stock with target price of Rs100.

- **Muted execution; await pick up in industrial segment execution:** Q3FY23 revenue grew 2.5% to Rs52.6bn. Power segment grew 7% YoY / 4% QoQ to Rs4bn while industrial segment declined 21% YoY / 15% QoQ to Rs9.5bn. 9MFY23 revenue growth is 15% YoY, led by improved execution in power segment. However, industrial execution has remained muted.
- **Lower other expenses lead to profitability improvement:** Gross margin contracted 400bps YoY, but expanded 100bps QoQ to 30%. However, other expenses declined 97% both YoY and QoQ to Rs93mn, which we believe was towards provision reversal. We await further details. This led PAT to grow 117% YoY to Rs310mn supported by lower YoY ETR of 25%.
- **Healthy order intake:** Order inflow in Q3FY23 was flat at Rs32bn, led by 142% YoY growth in industrial order, offset by 37% YoY decline in power segment. Key order wins included supply of rotor and E&M spares for hydro power plants and upgradation of HMI for thermal power plant for power segment. Supply of transformers for locomotives to the Indian Railways, supply of propulsion equipment, substations, gas compressors, among others.
- **Maintain BUY:** For industrial segment, 9MFY23 order intake grew 80% YoY. We await execution pick up in these orders, which along with the recently won power orders are likely to be margin accretive. This, coupled with BHEL's efforts to improve cashflow and reduce receivables, should help build sustainable profitable growth. Risks to our argument include: Delay in ordering activity, and any further increase in raw material prices.

Market Cap	Rs263bn/US\$3.2bn
Reuters/Bloomberg	BHEL.BO/BHEL IN
Shares Outstanding (mn)	3,482.1
52-week Range (Rs)	76/42
Free Float (%)	36.8
FII (%)	8.7
Daily Volume (US\$/'000)	27,715
Absolute Return 3m (%)	(0.2)
Absolute Return 12m (%)	33.0
Sensex Return 3m (%)	0.2
Sensex Return 12m (%)	4.3

Year to Mar (Std)	FY22	FY23E	FY24E	FY25E
Revenue (Rs bn)	212	241	273	317
Net Income (Rs bn)	4	6	13	19
DEPS (Rs)	1.2	1.6	3.6	5.5
% Chg YoY	(115.1)	37.1	122.9	53.8
P/E (x)	63.7	46.4	20.8	13.5
CEPS (Rs)	2.1	2.4	4.4	6.3
EV/E (x)	32.2	22.1	10.8	6.2
Dividend Yield (%)	0.5	0.9	1.9	3.0
RoCE (%)	2.4	2.9	5.0	6.8
RoE (%)	1.5	2.1	4.5	6.8

Q3FY23 result review and earnings revision

Capital Goods

Target price: Rs100

Earnings revision

(%)	FY23E	FY24E	FY25E
Revenue	↓ 1.0	↓ 1.0	↓ 1.0
EBITDA	↓ 1.9	↓ 5.3	↓ 2.2
EPS	↓ 3.0	↓ 1.1	-

Shareholding pattern

	Jun '22	Sep '22	Dec '22
Promoters	63.2	63.2	63.2
Institutional investors	16.8	19.3	23.2
MFs and others	1.5	3.0	3.2
FIs/Banks	0.3	0.3	0.3
Insurance	10.8	11.2	11.0
FIs	4.2	4.8	8.7
Others	20.0	17.5	13.6

Source: NSE

ESG disclosure score

Year	2020	2021	Chg
ESG score	44.3	51.1	6.7
Environment	26.3	46.5	20.2
Social	24.2	24.2	0.0
Governance	82.4	82.4	0.0

Note - Score ranges from 0 - 100 with a higher score indicating higher ESG disclosures.

Source: Bloomberg, I-sec research

Research Analysts:

Ashwani Sharma

sharma.ashwani@icicisecurities.com
+91 22 6807 7340

Aashna Manaktala

aashna.manaktala@icicisecurities.com
+91 22 6807 7397

Outlook and valuation

We expect awarding of coal-based projects to pick up momentum in next 12-24 months. NTPC has announced the expansion of 6GW in thermal capacity across Talcher, Lara, Singrauli and Darlipalli. In addition, DVC and NLC have announced 3.7GW and 3.4 GW of thermal capacity expansions, respectively.

Besides, non-coal based business is likely to witness strong ordering momentum. We expect ramp-up in Indian Railway's procurement of semi-high speed trainsets for *Vande Bharat* trains and high-HP locomotives for the dedicated freight corridors.

Company's efforts towards diversifying its industrial segment offerings in railway, defence and nuclear segments are reassuring of increasing order intake. We expect industry segment to witness a higher pace in execution due to increasing backlog and short-cycle nature of orders.

We believe with domestic thrust towards manufacturing and company's efforts towards improving its balance sheet, BHEL's business can stage a strong turnaround given its strong technical track record. It is taking cost-control measures and working on reducing receivables, with an increased focus on cashflow.

However, given Q3FY23 margin was below our estimates, we trim our earnings forecast for FY23E and FY24E earnings by 3% and 1%, though our FY25E earnings remain intact. We maintain our **BUY** rating on the stock with target price of **Rs100** (18x FY25E earnings).

Table 1: Earnings revision

(Rs mn)

	FY23E			FY24E			FY25E		
	Earlier	Revised	Change (%)	Earlier	Revised	Change (%)	Earlier	Revised	Change (%)
Revenue	2,42,998	2,40,602	(1.0)	2,75,439	2,72,804	(1.0)	3,20,212	3,17,129	(1.0)
EBIDTA	10,315	10,116	(1.9)	19,549	18,508	(5.3)	27,371	26,766	(2.2)
PAT	5,796	5,623	(3.0)	12,680	12,535	(1.1)	19,275	19,276	0.0

Source: I-Sec research

Table 2: Orderbook break up (by segment)

Rs bn	Q3FY23
Power	861
as % of total	83
Industrial	130
as % of total	13
Exports	46
as % of total	4
Total	1,037

Source: Company data, I-Sec research

Table 3: Quarterly financial highlights

(Rs mn)	Q3FY23	Q3FY22	YoY(%)	Q2FY23	QoQ(%)	FY22	FY21	YoY(%)
Net Sales	52,634	51,359	2.5	52,026	1.2	2,12,111	1,73,084	22.5
EBITDA	1,443	892	61.7	(2,439)	(159.1)	7,379	(31,352)	-
Margin	2.7	1.7	100bps	(4.7)	743bps	3.5	(18.1)	-
Depreciation	625	741	(15.7)	586	6.6	3,141	4,731	(33.6)
Finance Cost	1,393	860	62.0	1,232	13.0	3,547	3,731	(4.9)
Other Income	989	911	8.5	2,245	(56.0)	3,678	3,698	(0.5)
PBT	414	202	104.7	(2,013)	(120.6)	4,369	(36,115)	-
Tax	104	60	74.4	(2,116)	(104.9)	267	(8,945)	-
tax rate	25.2	29.5		105.1		6.1	24.8	744bps
Reported PAT	310	143	117.4	103	201.3	4,102	(27,171)	-
Adjusted PAT	310	143	117.4	103	201.3	4,102	(27,171)	-
Margin(%)	0.6	0.3	31bps	0.2	39bps	1.9	(15.7)	-
EPS	0.1	0.0		0.0		(7.8)	(4.1)	-
Order intake	32,540	32,700	(0.5)	1,20,040	(72.9)	2,36,930	1,34,724	75.9
Order book	10,36,940	10,70,580	(3.1)	10,63,760	(2.5)	10,25,420	10,20,900	0.4

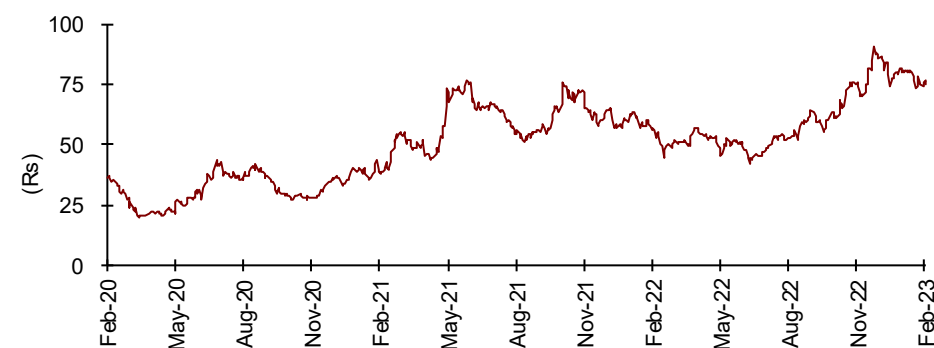
Source: Company data, I-Sec research

Table 4: Quarterly segmental highlights

(Rs mn)	Q3FY23	Q3FY22	YoY(%)	Q2FY23	QoQ(%)	FY22	FY21	YoY(%)
Revenue								
Power	39,921	37,235	7.2	38,144	4.7	1,53,613	1,13,861	34.9
Industrial	9,474	11,955	(20.8)	11,136	(14.9)	47,921	49,095	(2.4)
Total	49,395	49,190	0.4	49,280	0.2	2,93,547	2,81,026	4.5
EBIT								
Power	4,438	3,088	44	(608)	(830.0)	19,492	(12,462)	-
Industrial	(728)	(501)	45.4	514	(241.6)	(390)	(8,505)	-
Total	3,710	2,588	(43.4)	(94)	(4,059.9)	32,370	29,717	8.9
EBIT Margin								
Power	11.1	8.3	282bps	(1.6)	-	12.7	(10.9)	-
Industrial	(7.7)	(4.2)	-	4.6	-	(0.8)	(17.3)	-

Source: Company data, I-Sec research

Price chart



Source: Bloomberg

Financial summary (standalone)

Table 5: Profit and loss statement

(Rs mn, year ending March 31)

	FY22	FY23E	FY24E	FY25E
Total Income	2,12,111	2,40,602	2,72,804	3,17,129
Operating Expenses	2,04,732	2,30,486	2,54,295	2,90,363
EBITDA	7,379	10,116	18,508	26,766
% margins	3.5	4.2	6.8	8.4
Depreciation & Amortisation	3,141	2,603	2,642	2,700
EBIT	4,239	7,514	15,867	24,065
Gross Interest	3,547	4,867	4,659	4,066
Other Income	3,678	4,851	5,506	5,703
PBT before exceptionals	4,370	7,497	16,714	25,702
Add: Extraordinaries/ Exceptionals	-	-	-	-
Add: Share in associates				
PBT	4,370	7,497	16,714	25,702
Less: Taxes	267	1,874	4,178	6,425
Less: Minority Interests				
Net Income (Reported)	4,102	5,623	12,535	19,276
Adjusted Net Income	4,102	5,623	12,535	19,276

Source: Company data, I-Sec research

Table 6: Balance sheet

(Rs mn, year ending March 31)

	FY22	FY23E	FY24E	FY25E
Assets				
Total Current Assets	3,11,526	3,43,057	3,83,378	4,39,048
of which cash & cash eqv.	71,537	82,904	1,05,290	1,36,005
Total Current Liabilities & Provisions	2,49,570	2,78,890	3,13,569	3,60,044
Net Current Assets	61,955	64,167	69,809	79,005
Investments	6,697	6,697	6,697	6,697
Other Non-Current Assets				
Net Fixed Assets	28,294	26,999	25,857	24,657
Goodwill				
Total Assets	96,947	97,862	1,02,363	1,10,359
Liabilities				
Borrowings	47,801	45,801	43,801	41,801
Deferred Tax Liability	(2,20,566)	(2,20,566)	(2,20,566)	(2,20,566)
Minority Interest				
Equity Share Capital	6,964	6,964	6,964	6,964
Face Value per share (Rs)	2.0	2.0	2.0	2.00
Reserves & Surplus	2,62,748	2,65,663	2,72,164	2,82,160
Net Worth	2,69,712	2,72,627	2,79,128	2,89,124
Total Liabilities	96,947	97,862	1,02,363	1,10,359

Source: Company data, I-Sec research

Table 7: Cashflow statement

(Rs mn, year ending March 31)

	FY22	FY23E	FY24E	FY25E
Operating Cashflow	7,191	8,754	14,877	20,918
Working Capital Changes	417	9,940	15,362	20,170
Capital Commitments	(2,356)	(1,307)	(1,500)	(1,500)
Free Cashflow	5,251	17,387	28,739	39,589
Cashflow from Investing	3	-	-	-
Activities				
Issue of Share Capital				
Buyback of shares				
Inc/(Dec) in Borrowings	(1,553)	(2,000)	(2,000)	(2,000)
Interest paid	52	(529)	300	1,058
Dividend paid	1,676	3,492	4,652	7,932
Extraordinary Items/Others	(908)	(6,983)	(9,305)	(15,864)
Chg. in Cash & Bank balance	4,523	11,367	22,386	30,715

Source: Company data, I-Sec research

Table 8: Key ratios

(Year ending March 31)

	FY22	FY23E	FY24E	FY25E
Per Share Data (in Rs)				
Diluted adjusted EPS	1.2	1.6	3.6	5.5
Recurring Cash EPS	2.1	2.4	4.4	6.3
Dividend per share (DPS)	0.4	0.6	1.4	2.2
Book Value per share (BV)	77.5	78.3	80.2	83.0
Growth Ratios (%)				
Operating Income	22.5	13.4	13.4	16.2
EBITDA	(123.5)	37.1	83.0	44.6
Recurring Net Income	(115.1)	37.1	122.9	53.8
Diluted adjusted EPS	(115.1)	37.1	122.9	53.8
Diluted Recurring CEPS	(132.3)	13.6	84.5	44.8
Valuation Ratios				
P/E	63.7	46.4	20.8	13.5
P/CEPS	36.1	31.8	17.2	11.9
P/BV	1.0	1.0	0.9	0.9
EV / EBITDA	32.2	22.1	10.8	6.2
EV / Operating Income	1.1	0.9	0.7	0.5
EV / Op. FCF (pre -Capex)	31.2	12.0	6.6	4.1
Operating Ratios				
Raw Material/Sales (%)	69.7	69.2	68.7	69.2
SG&A/Sales (%)	10.8	10.9	10.4	9.8
Other Income / PBT (%)	84.2	64.7	32.9	22.2
Effective Tax Rate (%)	6.1	25.0	25.0	25.0
NWC / Total Assets (%)	(9.9)	(19.1)	(34.7)	(51.6)
Inventory Turnover (days)	118.8	118.8	118.8	118.8
Receivables (days)	54.8	54.8	54.8	54.8
Payables (days)	140.4	137.1	136.6	139.3
Net D/E Ratio (x)	(0.1)	(0.1)	(0.2)	(0.3)
Return/Profitability Ratios (%)				
Recurring Net Income Margins	1.9	2.3	4.6	6.1
RoCE	2.4	2.9	5.0	6.8
RoNW	1.5	2.1	4.5	6.8
Dividend Payout Ratio	34.0	40.0	40.0	40.0
Dividend Yield (%)	0.5	0.9	1.9	3.0
EBITDA Margins	3.5	4.2	6.8	8.4

Source: Company data, I-Sec research

This report may be distributed in Singapore by ICICI Securities, Inc. (Singapore branch). Any recipients of this report in Singapore should contact ICICI Securities, Inc. (Singapore branch) in respect of any matters arising from, or in connection with, this report. The contact details of ICICI Securities, Inc. (Singapore branch) are as follows: Address: 10 Collyer Quay, #40-92, Ocean Financial Tower, Singapore - 049315, Tel: +65 6232 2451 and email: navneet_babbar@icicisecuritiesinc.com, Rishi_agrawal@icicisecuritiesinc.com.

"In case of eligible investors based in Japan, charges for brokerage services on execution of transactions do not in substance constitute charge for research reports and no charges are levied for providing research reports to such investors."

New I-Sec investment ratings (all ratings based on absolute return; All ratings and target price refers to 12-month performance horizon, unless mentioned otherwise)

BUY: >15% return; **ADD:** 5% to 15% return; **HOLD:** Negative 5% to Positive 5% return; **REDUCE:** Negative 5% to Negative 15% return; **SELL:** < negative 15% return

ANALYST CERTIFICATION

I/We, **Ashwani Sharma, MBA; Aashna Manaktala, BTech, MBA (Finance)**; authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report. Analysts are not registered as research analysts by FINRA and are not associated persons of the ICICI Securities Inc. It is also confirmed that above mentioned Analysts of this report have not received any compensation from the companies mentioned in the report in the preceding twelve months and do not serve as an officer, director or employee of the companies mentioned in the report.

Terms & conditions and other disclosures:

ICICI Securities Limited (ICICI Securities) is a full-service, integrated investment banking and is, inter alia, engaged in the business of stock brokering and distribution of financial products.

ICICI Securities is Sebi registered stock broker, merchant banker, investment adviser, portfolio manager and Research Analyst. ICICI Securities is registered with Insurance Regulatory Development Authority of India Limited (IRDAI) as a composite corporate agent and with PFRDA as a Point of Presence. ICICI Securities Limited Research Analyst SEBI Registration Number – INH000000990. ICICI Securities Limited SEBI Registration is INZ000183631 for stock broker. ICICI Securities is a subsidiary of ICICI Bank which is India's largest private sector bank and has its various subsidiaries engaged in businesses of housing finance, asset management, life insurance, general insurance, venture capital fund management, etc. ("associates"), the details in respect of which are available on www.icicibank.com.

ICICI Securities is one of the leading merchant bankers/ underwriters of securities and participate in virtually all securities trading markets in India. We and our associates might have investment banking and other business relationship with a significant percentage of companies covered by our Investment Research Department. ICICI Securities and its analysts, persons reporting to analysts and their relatives are generally prohibited from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover.

Recommendation in reports based on technical and derivative analysis centre on studying charts of a stock's price movement, outstanding positions, trading volume etc as opposed to focusing on a company's fundamentals and, as such, may not match with the recommendation in fundamental reports. Investors may visit icicidirect.com to view the Fundamental and Technical Research Reports.

Our proprietary trading and investment businesses may make investment decisions that are inconsistent with the recommendations expressed herein.

ICICI Securities Limited has two independent equity research groups: Institutional Research and Retail Research. This report has been prepared by the Institutional Research. The views and opinions expressed in this document may or may not match or may be contrary with the views, estimates, rating, and target price of the Retail Research.

The information and opinions in this report have been prepared by ICICI Securities and are subject to change without any notice. The report and information contained herein is strictly confidential and meant solely for the selected recipient and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form, without prior written consent of ICICI Securities. While we would endeavour to update the information herein on a reasonable basis, ICICI Securities is under no obligation to update or keep the information current. Also, there may be regulatory, compliance or other reasons that may prevent ICICI Securities from doing so. Non-rated securities indicate that rating on a particular security has been suspended temporarily and such suspension is in compliance with applicable regulations and/or ICICI Securities policies, in circumstances where ICICI Securities might be acting in an advisory capacity to this company, or in certain other circumstances.

This report is based on information obtained from public sources and sources believed to be reliable, but no independent verification has been made nor is its accuracy or completeness guaranteed. This report and information herein is solely for informational purpose and shall not be used or considered as an offer document or solicitation of offer to buy or sell or subscribe for securities or other financial instruments. Though disseminated to all the customers simultaneously, not all customers may receive this report at the same time. ICICI Securities will not treat recipients as customers by virtue of their receiving this report. Nothing in this report constitutes investment, legal, accounting and tax advice or a representation that any investment or strategy is suitable or appropriate to your specific circumstances. The securities discussed and opinions expressed in this report may not be suitable for all investors, who must make their own investment decisions, based on their own investment objectives, financial positions and needs of specific recipient. This may not be taken in substitution for the exercise of independent judgment by any recipient. The recipient should independently evaluate the investment risks. The value and return on investment may vary because of changes in interest rates, foreign exchange rates or any other reason. ICICI Securities accepts no liabilities whatsoever for any loss or damage of any kind arising out of the use of this report. Past performance is not necessarily a guide to future performance. Investors are advised to see Risk Disclosure Document to understand the risks associated before investing in the securities markets. Actual results may differ materially from those set forth in projections. Forward-looking statements are not predictions and may be subject to change without notice.

ICICI Securities or its associates might have managed or co-managed public offering of securities for the subject company or might have been mandated by the subject company for any other assignment in the past twelve months.

ICICI Securities or its associates might have received any compensation from the companies mentioned in the report during the period preceding twelve months from the date of this report for services in respect of managing or co-managing public offerings, corporate finance, investment banking or merchant banking, brokerage services or other advisory service in a merger or specific transaction.

ICICI Securities or its associates might have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the companies mentioned in the report in the past twelve months.

ICICI Securities encourages independence in research report preparation and strives to minimize conflict in preparation of research report. ICICI Securities or its associates or its analysts did not receive any compensation or other benefits from the companies mentioned in the report or third party in connection with preparation of the research report. Accordingly, neither ICICI Securities nor Research Analysts and their relatives have any material conflict of interest at the time of publication of this report.

Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

ICICI Securities or its subsidiaries collectively or Research Analysts or their relatives do not own 1% or more of the equity securities of the Company mentioned in the report as of the last day of the month preceding the publication of the research report.

Since associates of ICICI Securities and ICICI Securities as a entity are engaged in various financial service businesses, they might have financial interests or actual/beneficial ownership of one percent or more or other material conflict of interest in various companies including the subject company/companies mentioned in this report.

ICICI Securities may have issued other reports that are inconsistent with and reach different conclusion from the information presented in this report.

Neither the Research Analysts nor ICICI Securities have been engaged in market making activity for the companies mentioned in the report.

We submit that no material disciplinary action has been taken on ICICI Securities by any Regulatory Authority impacting Equity Research Analysis activities.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject ICICI Securities and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

This report has not been prepared by ICICI Securities, Inc. However, ICICI Securities, Inc. has reviewed the report and, in so far as it includes current or historical information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed.