

BHARAT HEAVY ELECTRICALS

APRIL 2016

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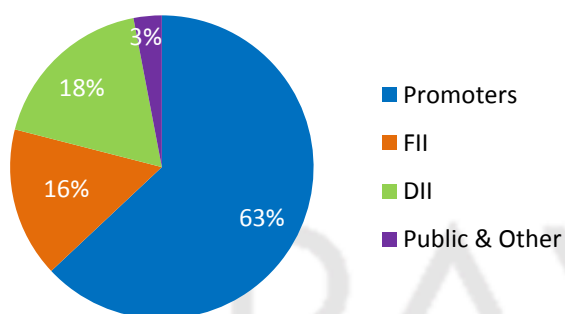
Rating Accumulate

Target Price Rs 168/-

CMP Rs 112/-

Potential upside 50%

Shareholders



Market Data

No of shares	2448 mn
Fee float	37%
market cap	Rs 295 bn
52 week high/low	Rs 290/ Rs 90
Avg daily vol	4.3 mn shares
bloomberg code	BHEL IB Equity

HIGHLIGHTS :

Key negatives:

- (1) Continued weak execution, higher raw material costs and increased provisioning for slow moving projects;
- (2) Deteriorating quality of order book with highershare of EPC (low margin and higher risk) projects at 45% and super critical projects (higher imported content due to JDU# from Alstom and Siemens taking the raw material costs higher);and
- (3) Exclusion of slow moving orders worth Rs 36 bn taking the order backlog down again in Q3.

Key positives:

- (1) Receivables went down from ~Rs 380 bn in Mar'15 to ~Rs359 bn in Dec'15;
- (2) Management is targeting reduction in material cost through renegotiation with its suppliers; and
- (3) Pipeline of orders looks strong and the company expects to get further orders worth Rs80 bn in FY16 (YTD order inflow atRs 350 bn).

Execution and margin woes continue

BHEL's Q3FY16 disappointed with EBITDA loss of Rs16.4bn due to negative operating leverage (revenue down 14% YoY), higher material costs (65% of sales vs. 54% YoY) and higher provisions for slow moving projects from domestic private sector. Order inflow was Rs61bn (down 9% YoY). However, combined with two large orders received post Q3, company has booked total order inflow of Rs 350 bn year to date (vs. 310 bn in FY15).

Order pipeline remains strong:

In the power segment, BHEL is L1 in ~9 GW of domestic orders and expects finalization of ~2.1 GW worth of orders in Q4 in addition to 9.9 GW it has booked so far in FY16 (7 GW in FY15). Management expects reduction in slow moving orders from current Rs 326bn (total order book of Rs 1.1 trn) post SEB reforms.

Financial summary consolidated				
Y/E March	FY15	FY16E	FY17E	FY18E
Sales	295420	269626	321168	363239
EBITDA	27851	-7776	19196	27588
Adj PAT	17421	-5133	14827	20513
Con EPS	0	4.2	8.7	11.2
EPS	7.1	-2.1	6.1	8.4
Change Yoyo	-38	-129.5	-388.9	38.4
P/E	16.9	-57.4	19.9	14.4
ROE	5.5	-1.6	4.7	6.4
EV/E	7.1	-21.4	9.5	7
DPS	2	2	3	3

Key drivers			
Rs ban	FY16E	FY17E	FY18E
Order inflow	464	480	492
Backlog	1207	1348	1457
margin	-2.80%	5.80%	7.40%

Rs mn	15-Dec	14-Dec	% chg	15-Sep	% chg	FY16E	FY15	% Chg
Net sales	53256	61980	-14.1	59380	-10.3	279036	304830	-8.5
EBITDA	-16387	2938	0	-4742	0	-7776	27851	-127.9
Other income	1706	2741	-37.8	3733	-54.3	10626	9010	17.9
PBIDT	-14682	5679	0	-1009	0	2850	36861	-92.3
Depreciation	2255	2564	-12.1	2249	0.2	9782	10773	-9.2
Interest	52	52	0	44	19.7	400	917	-56.4
PBT	-16989	3062	0	-3302		-7332	25172	
Tax	-5969	936	0	-1253		-2200	7751	
Adjusted PAT	-11020	2126	0	-2049		-5133	17421	
Extra ordinary income/exp	0	0	0	0		6528	-956	
Reported PAT	-11020	2126	0	-2049		-3423	14193	
No of shares	2448	2448	0	2448		2448	2448	
EBITDA Margin%	-30.8	4.7	0	-8		-2.8	9.1	
PBIDT Margin%	-27.6	9.2	0	-1.7		1	12.1	
EPS	-4.5	0.9	0	-0.8		-2.1	7.1	

New Emission norms to impact BHEL's competitiveness negatively: According to the management, the new emission norm is an opportunity for BTG suppliers. However, it will increase the cost of the boiler by Rs 5-7 mn/MW from current Rs 15mn/MW. To meet the new norms for NOx and SOx, BHEL would need to add a FGD and an SCR. BHEL has tied up with MHI for FGD and is developing its own SCR. As per our channel checks, BHEL's boiler technology supplier Alstom

(now GE) has aggressive plans for India. Also, L&T's boilers are at NOx levels of ~110 mg vs. BHEL at ~500 mg, resulting in higher cost for BHEL impacting its competitiveness for future projects.

Profit and loss				
Y/E March	FY15	FY16E	FY17E	FY18E
Net sales	295420	269626	321168	363239
other operating income	9410	9410	9410	9410
total operating income	304830	279036	330578	372650
cost of goods sold	-177666	-179551	-198530	-218533
gross profit	127164	99485	132047	154116
gross margin%	43	36.9	41.1	42.4
total operating expenses	-99313	-107262	-112851	-126528
EBITDA	27851	-7776	19196	27588
EBITDA Margin	9.4	-2.9	6	7.6
depreciation	-10773	-9782	-10270	-10570
EBIT	17078	-17559	8926	17018
Net interest	-917	-400	-400	-400
other income	9010	10626	12655	12686
profit before tax	25172	-7332	21181	29305
total taxation	-7751	2200	-6354	-87191
tax rate	30.8	30	30	30
profit after tax	17421	-5133	14827	20513
minorities	0	0	0	0
profit/loss associate	0	0	0	0
adjusted net profit	17421	-5133	14827	20513
adj PAT Margin	5.9	-1.9	4.6	5.6
net non recurring items	-3228	1710	0	0
Reported net profit	14193	-3423	14827	20513

Balance sheet				
Y/E March	FY15	FY16E	FY17E	FY18E
Paid up capital	4895	4895	4895	4895
Reserves and surplus	313744	304593	310829	322752
Net worth	318639	309489	315725	327647

Borrowings	610	610	610	610
Other noncurrent liabilities	0	0	0	0
Total liabilities	662464	651672	673390	723932
Gross fixed assets	125932	134932	138932	142932
Less:depreciation	-84349	-94131	-104401	-114971
net fixed assets	41583	40801	34531	27961
add:capital WIP	5000	0	0	0
Total fixed assets	46583	40801	34531	27961
Total investment	4177	4177	4177	4177
Inventory	101017	96031	114388	129373
Debtors	376373	350549	37119	419312
Cash and bank	98127	129089	112218	101312
Loans and advances	34437	29548	35196	39807
current liabilities	343215	341574	357055	395676
Net current assets	268489	265121	277627	296119
other non current assets				0
Total assets	662464	651672	673390	723932

Ray Research & Consulting Pvt Ltd

Cash flow				
Y/E March	FY15	FY16E	FY17E	FY18E
Profit before tax	25172	-7332	21181	29305
Depreciation and amortisation	-10773	-9782	-10270	-10570
Chg in working capital	-9315	34330	-29377	-29398
cash flow from operations	16568	41090	-3880	2085
Capital expenditure	-4006	-4000	-4000	-4000
Cash flow from investing	-4897	-4400	-4400	-4400
Equity raised /repaid	0	0	0	0
debt raised/repaid	-25938	0	0	0
Dividend paid	-4895	-4895	-7343	-7343
Cash flow from financing	-32273	-5727	-8591	-8591
Net chg in cash	-20602	30963	-16871	-10906

Key ratios				
Y/E March	FY15	FY16E	FY17E	FY18E
OPERATIONAL				
FDEPS	7.1	-2.1	6.1	8.4
CEPS	10.2	2.6	10.3	12.7
DPS	2	2	3	3
Dividend payout ratio	34.5	-143	49.5	35.8
Growth				
net sales	-22.5	-8.7	19.1	13.1
EBITDA	-42.3	-127.9	-346.9	43.7
Adj net profit%	-38	-129.5	-388.9	38.4
FDEPS%	-38	-129.5	-388.9	38.4
PERFORMANCE				
ROE%	5.5	-1.6	4.7	6.4
ROCE%	7.9	-2.2	6.9	9.2
EFFICIENCY				
Asset turnover	1.3	1.3	1.7	1.7
Sales/total assets	0.4	0.4	0.5	0.5
working capital /sales	0.6	0.6	0.5	0.5
Receivable days	465	474.5	421.8	421.3
inventory days	133.1	122.2	134.1	136.8
payable days	306.8	294.2	285.8	298.7
Financial stability				
Total debt/equity	0	0	0	0
net debt/equity	-0.3	-0.4	-0.4	-0.3
current ratio	1.8	1.8	1.8	1.7
interest cover	18.6	-43.9	22.3	42.5
Valuation				
PE	16.9	-57.4	19.9	14.4
EV/EBITDA	7.1	-21.4	9.5	7
EV/Net sales	0.7	0.6	0.6	0.5
PB	0.9	1	0.9	0.9
Dividend yield	1.7	1.7	2.5	2.5
free cash flow yield %	4.3	12.6	2.7	0.7