

## Bharat Heavy Electricals Ltd.

15 January 2011

**CMP:**

Rs.2195

**Target Price:**

Rs. 2800

**Investment Period:**

5-8 Month

### Stock Information -

Industry Electric Equipment

Market cap Rs. 109,699 Cr

Face value Rs. 10

Book Value Rs. 325.16

EPS (TTM Basis) Rs. 97.89

52 week H/L Rs. 2694.00/ 2055.00

Dividend

Managing Director B Prasada Rao

Listed At NSE/BSE

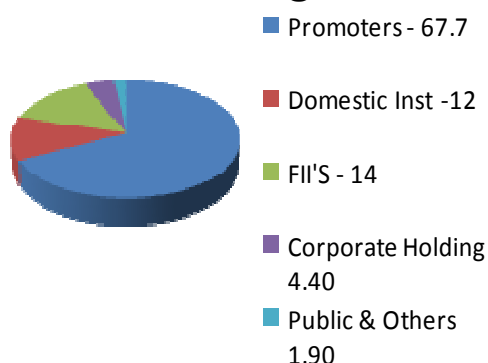
6 Mth. Avg. Vol. (NSE) 485,764.51

6 Mth. Avg. Vol. (BSE) 132,414.53

### BHEL ( Bharat Heavy Electricals Ltd ) - BUY AROUND 21

Bharat Heavy Electricals Ltd (BHEL) is a primarily into manufacturing power generation equipment like turbines and super critical boilers and a leading EPC company. It has emerged as the prime beneficiary of the four-fold increase in the investments in the power sector in India. BHEL, a public sector undertaking, is the largest engineering and manufacturing enterprise in India in the energy-related/infrastructure sector. The company was set up at Bhopal under the name of M/s Heavy electrical (India) Ltd. in collaboration with AEI, UK. Subsequently, three more plants were set up at Hyderabad, Hardwar and Trichy. BHEL manufactures over 180 products under 30 major product groups and caters to sectors like power generation & transmission, industry, transportation, telecommunication, renewable energy, etc. The company has 14 manufacturing divisions, four power sector regional centres, over 100 project sites, eight service centres and 18 regional offices. The company has installed equipment for over 90,000 MW of power generation and has supplied over 2,25,000 MVA transformer capacity and other equipment operating in the transmission & distribution network up to 400 kV (AC & DC). Between Jan. 92 and Feb.92, the government disinvested a portion of its share holding in the company.

### Share Holding



BHEL currently has orders worth Rs154,000 crore on hand, which provides revenue coverage for the next three to four years. It can be believed that the order inflow momentum would continue to remain strong for the company. However, the key challenge for BHEL would be the timely execution of projects. The company is confident of bagging orders for at least five boilers and four turbines as far as the bulk tendering by National Thermal Power Corporation is concerned. The order finalization for the same is expected in January 2011.

The company has already expanded its capacity to 15GW in FY2011. Also, the project to expand the capacity to 20GW by FY2012 is being executed on a fast track. In our view, the stabilization of the new capacity coupled with the de-bottlenecking of the supply chain would aid order execution and sustain robust growth in BHEL's revenues in the coming years.

At the current market price, the stock is trading at 17.6x its FY2012E earnings. The near-term positive trigger in the stock is the order inflow in the power equipment business. We have, therefore, included BHEL amongst our Top Picks.

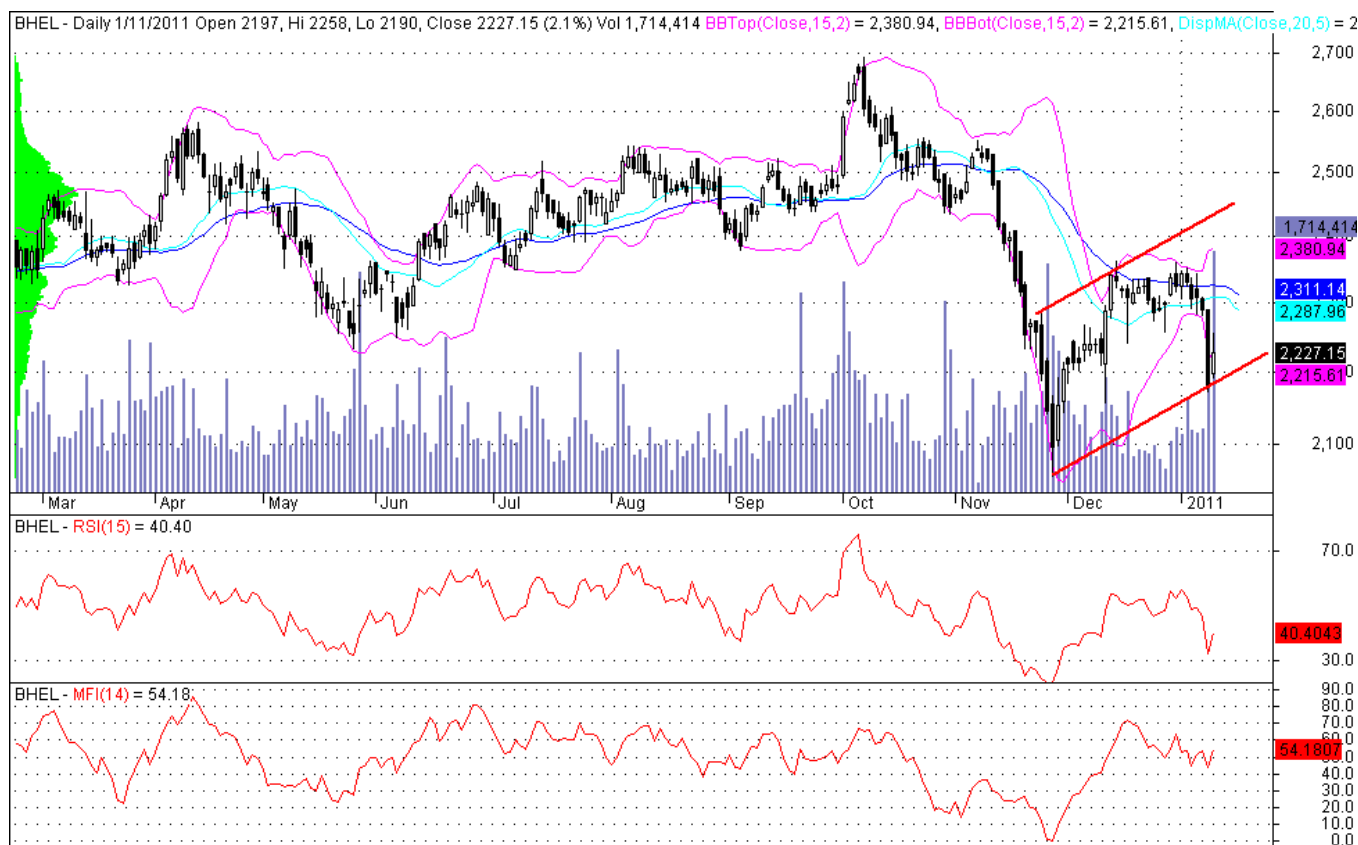
BHEL is also a fundamentally strong company for a long term investment purpose. This is one of those stocks which should always be kept in the portfolio.

## Bharat Heavy Electricals Ltd.

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### Bharat Heavy Electricals to announce Q3 results

The board meeting of Bharat Heavy Electricals (BHEL) will be held on 21 January 2011 to consider and take on record the unaudited financial results for the quarter ended 31 December 2010 (Q3).



### Price and moving averages:

BHEL has closed below its Short time moving average. Short time moving average is currently above mid-time, AND below long time moving averages. The relationship between price and moving averages is: neutral in short-term, and neutral in mid-long term. Bollinger Bands: BHEL has closed Bollinger Bands are narrower than normal. RSI and MFI indicating an upside momentum.

### Profit & Loss (Rs. in Crores)

Particulars	Mar-10	Mar-09	Mar-08	Mar-07	Mar-06	Mar-05
<b>INCOME :</b>						
Sales Turnover	34,602.47	28,491.34	21,726.57	19,016.18	14,740.59	10,559.43
<b>Excise Duty</b>	1,394.32	1,901.20	2,240.30	1,695.44	1,298.01	1,042.94
<b>Net Sales</b>	33,208.15	26,590.14	19,486.27	17,320.74	13,442.58	9,516.49
Other Income	1,206.85	1,051.10	1,119.20	546.84	346.60	434.24

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Stock Adjustments	786.65	1,151.54	827.26	181.19	386.01	539.77
<b>Total Income</b>	35,201.65	28,792.78	21,432.73	18,048.77	14,175.19	10,490.50
<b>EXPENDITURE :</b>						
Raw Materials	17,174.47	15,087.76	10,030.99	8,183.59	6,829.17	4,872.66
Power & Fuel Cost	337.99	341.82	273.07	259.08	229.01	220.54
Employee Cost	6,447.25	2,982.90	2,611.01	2,368.14	1,877.82	1,649.82
Other Manufacturing Expenses	3,538.42	2,644.65	1,896.29	1,914.97	1,384.85	1,057.59
Selling and Administration Expenses	1,158.36	982.88	778.91	690.98	553.17	467.92
Miscellaneous Expenses	-536.86	1,539.11	1,079.51	579.70	432.20	340.12
<b>Less: Pre-operative Expenses Capitalised</b>	0.00	0.00	0.00	0.00	0.00	0.00
<b>Total Expenditure</b>	28,119.63	23,579.12	16,669.78	13,996.46	11,306.22	8,608.65
<b>Operating Profit</b>	7,082.02	5,213.66	4,762.95	4,052.31	2,868.97	1,881.85
Interest	33.50	30.71	35.42	43.33	58.75	81.41
<b>Gross Profit</b>	7,048.52	5,182.95	4,727.53	4,008.98	2,810.22	1,800.44
Depreciation	458.01	334.27	297.21	272.97	245.93	218.87
<b>Profit Before Tax</b>	6,590.51	4,848.68	4,430.32	3,736.01	2,564.29	1,581.57
Tax	1,971.42	2,172.28	1,946.65	1,435.24	1,022.57	647.93
Fringe Benefit tax	-4.62	40.56	27.10	49.00	18.00	0.00
Deferred Tax	313.07	-502.37	-402.77	-162.93	-155.44	-19.76
<b>Reported Net Profit</b>	4,310.64	3,138.21	2,859.34	2,414.70	1,679.16	953.40
Extraordinary Items	0.20	4.48	0.97	0.71	1.99	-9.88
<b>Adjusted Net Profit</b>	4,310.44	3,133.73	2,858.37	2,413.99	1,677.17	963.28
Adjst. below Net Profit	0.00	0.00	0.00	0.00	0.00	0.00
P & L Balance brought forward	595.46	429.69	442.72	219.06	237.64	103.45
Statutory Appropriations	0.00	0.00	0.00	0.00	0.00	0.00
Appropriations	4,330.71	2,972.44	2,872.37	2,191.04	1,697.74	819.21
P & L Balance carried down	575.39	595.46	429.69	442.72	219.06	237.64
Dividend	1,140.58	832.18	746.52	599.66	354.90	195.81
Preference Dividend	0.00	0.00	0.00	0.00	0.00	0.00
Equity Dividend %	233.00	170.00	152.50	245.00	145.00	80.00
Earnings Per Share-Unit Curr	84.15	61.22	55.82	94.86	66.57	37.86
Earnings Per Share(Adj)-Unit Curr	84.15	61.22	55.82	47.43	33.29	18.93
Book Value-Unit Curr	325.16	264.32	220.10	359.06	298.31	246.24

### Key ratios

	Mar-10	Mar-09	Mar-08
P/E (x)	28.35	24.57	36.84
P/BV (x)	7.34	5.69	9.34
RONW (%)	29.9	26.5	29.2
ROCE (%)	45.5	40.7	45.2
EV/ EVBIDTA (x)	15.12	12.17	19.40
Dividend Yield (%)	1.0	1.0	1.0
APATM(%)	12.5	11.0	13.2



## Bharat Heavy Electricals Ltd.

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### NEWS & UPDATE

#### BHEL emerges as lowest bidder for Rajasthan Rajya Vidyut project: report

The two projects, being set up at Chhabra and Suratgarh in Rajasthan, are of 1,320 MW each and RRVUNL had floated a tender through international competitive bidding (ICB) route.

BHEL is reportedly understood to have emerged as the lowest bidder for Rs. 122bn Rajasthan Rajya Vidyut Utpadan Nigam projects for providing engineering, procurement and construction (EPC) services.

According to reports, the two projects, being set up at Chhabra and Suratgarh in Rajasthan, are of 1,320 MW each and RRVUNL had floated a tender through international competitive bidding (ICB) route. Despite stiff competition from foreign companies, this is the second time that BHEL has emerged successful in the tender floated through ICB route.

Recently, it won the EPC contract for first 700-MW supercritical unit at Bellary Power Project in Karnataka from Karnataka Power Corporation Ltd (KPCL). EPC work on the two super-critical thermal power plants will start as soon as the company gets the contract officially and would take about 36 to 48 months to complete the project, adds report.

#### Rs350bn order inflow during the first nine months

BHEL bagged orders worth Rs350bn during the first nine months of this fiscal, thus indicating an outstanding order book position of Rs1.3trn. This order book provides strong earnings visibility for the next ~3 years. This robust order inflow during 9M FY10 translates into order inflow of ~Rs143bn during Q3 FY10. It won orders for the supply of 11.7GW during the first nine months, higher than our estimate. Majority of these orders are from the private sector, indicating its strong presence despite Chinese competition.

#### Expansion to aid execution

BHEL is scheduled to expand its installed capacity to 15GW from 10GW. It further plans to expand this to 20GW by FY12. We believe this expansion will help the company to overcome execution delays and thus achieve 25% revenue CAGR over FY09-12. Post this expansion the company will be well equipped to capitalize on future growth opportunities.

#### Easing commodity prices will positively impact margin

In order to overcome supply chain issues, BHEL stocks its key raw materials for a period of four-six months. During FY10 steel prices corrected by ~35% over the corresponding period. This coupled with improving average realizations (due to more supercritical orders) will positively impact margins. This is already visible in the Q2 FY10 results where margins expanded by 375bps.

#### Better execution and margin improvement will aid 30% earnings CAGR, upgrade to BUY

With the ordering for the XI plan expected to commence soon we believe BHEL is best placed to take advantage of this opportunity. BHEL's dominance in the sector is seen from the Rs350bn robust order inflow during the first nine months of this fiscal. Expanded capacity will improve its execution cycle. This coupled with better margins will aid 30% earnings CAGR. With an improving margin environment we expect BHEL's cash position to also improve, thus remain as a net debt free company. We factor in FY12 earnings and upgrade the stock to BUY with a target price of Rs2,803/share.

### Valuation summary

Y/e 31 Mar (Rs m)	FY09	FY10E	FY11E	FY12E
Revenues	267,268	324,975	408,682	530,071
yoy growth (%)	35.5	21.6	25.8	29.7
Operating profit	42,190	57,112	74,359	97,358
OPM (%)	15.8	17.6	18.2	18.4
Pre-exceptional PAT	30,492	41,493	52,718	67,936
Reported PAT	31,382	41,493	52,718	67,936



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yoy growth (%)	9.8	32.2	27.1	28.9
EPS (Rs)	62.3	84.8	107.7	138.8
P/E (x)	39.1	28.7	22.6	17.5
Price/Book (x)	9.2	7.6	6.3	5.1
EV/EBITDA (x)	25.8	18.9	14.3	10.8
Debt/Equity (x)	0.0	0.0	0.0	0.0
RoE (%)	25.7	29.0	30.4	32.0
RoCE (%)	40.6	44.7	46.8	49.3

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