Portfolio 001

With rising NPAs banks have now tightened its lending process (credit score threshold raised, etc.) while many poorly managed NBFCs have been bleeding on the D-street. Real Estate, SME and lower-rated corporate/commercial lending segments have witnessed drying-up of sources for fresh liquidity and refinancing. To revive the Indian economy the government has been taking various steps, on the other hand RBI has reduced interest rate for the fifth time in consecutive meet.

Notably, the major step that government has taken to boost the economy is reducing corporate tax cut. This has refuelled the confidence amongst the investor community across the globe. This will also help in boosting new investment in the country.

The factors that are helping the Indian Incs are stable and low crude oil prices along with lower prices of other key raw material like metal. The country has witnessed good amount of rainfall which is likely to spur the rural demand.

With taking consideration the overall economic situation and outlook for the foreseeable future we have shortlisted the following stocks for our Super 60 :

Company Name	Porfolio Weight	Sector	Portfolio Type	Price
Polycab India Ltd.	9%	Wire/Cables	Large Cap	565.3
Asian Paints Ltd.	9%	Paint	Large Cap	1504.5
PI Industries Ltd.	9%	Agrochemicals	Large Cap	1115.8
Bharat Electronics Ltd.	9%	Defence	Large Cap	98.7
Dabur India Ltd	9%	FMCG	Large Cap	425.0
Tata Global Beverages Ltd.	9%	FMCG	Large Cap	259.1
Dixon Technologies (India) Ltd.	9%	Consumer Electronic	Mid Cap	1995.8
KEI Industries Ltd.	9%	Wire/Cables	Mid Cap	440.6
Mahanagar Gas Ltd.	9%	Gas	Mid Cap	795.9
PSP Projects Ltd.	9%	Construction	Mid Cap	483.3
Ahluwalia Contracts	5%	Construction	Small Cap	290.0
Cupid Ltd.	5%	Personal Product	Small Cap	121.9

Bharat Electronics (BEL)

Bharat Electronics (BEL) is a government undertaking Navratna company which mainly caters to defence requirement. The company is manufacturer and supplier of strategic electronic products primarily to defence services. It produces a wide range of state-of-the-art equipment in fields such as Defence Communication, Radars, Naval Systems, C4I Systems, Weapon Systems, Homeland Security, Telecom & Broadcast Systems, Electronic Warfare, Tank Electronics etc. The company is also involved in the production of Electronic Voting Machines, Tablet PC, solar-powered traffic signal systems and Access Control Systems. Apart from the defence business, the company has ventured into opportunities in non-defence areas like Homeland Security, Smart City, Space Electronics, Network & Cyber Security, Railways, Weather Radars, VVPAT, etc. It also provides services like contract manufacturing and design manufacturing. In the term of segment wise break up, the company's 68 per cent revenue was from defence business in FY19 and the rest was from non-defence business.

Robust orders in hand

At present the company has strong order book of around Rs. 57,600 crore which translate to book-to-bill of almost 4.7x on FY19 revenue, giving healthy revenue visibility for next 4-5 years. The company's two major orders include LRSAM (long-range surface-to-air missile) worth Rs. 15,000 crore and Akash worth Rs. 5360 crore. The Akash order is likely to get complete in three years starting FY21E. On the other hand, LRSAM is expected to get complete by FY26E. Further, the company has given an order inflow guidance in the range of Rs. 13,000-15,000 crore in FY20E. The company has strong orders in pipeline which consist coastal surveillance order worth Rs. 2500 crore, naval project worth Rs. 2500-3000 crore, smart city and homeland security order worth Rs. 1000 crore. The management expects revenue growth of around 8-10 per cent in FY20E.

Another growth engine

The company has been focusing now more on non-defence segment which would aid margin going forward. As on FY19 the company's overall non-defence business contributed around 32 per cent to overall revenue. Due to inclusion of AMC in the most of its large projects has resulted to higher service income (10 per cent of FY19 revenue). Rising complexity of new products gives headroom for services revenue throughout the product lifecycle. The company targets to take this service revenue to 25 per cent of overall revenue in the coming 4-5 years which is expected to aid margin as this service business commands high margin. Besides, the company is focusing on other non-defence segment like Railways, Civil Aviation, Li-ion Batteries, Homeland Security, Space Electronics, Solar etc. Going forward, the focus on non-defence business would not just aid in revenue growth but will act as a cushion for the margin going forward.

R&D spend, to keep growth engine running

BEL spends around 9 per cent of sales (FY19) on R&D for developing new products. Company has incurred R&D majorly on the segments like Radars, military communication, Naval systems, missile systems, Electronic warfare, avionics, Electro optics, Tank electronics. Going ahead, R&D spend is likely to rise to 12 per cent of sales through which new product development is likely to gain further momentum. In FY19, enhancing focus on R&D has helped the company to achieve 89 per cent of overall sales from indigenous products.

Looking at the capex front, the company has planned capex worth Rs. 3000 crore for next 3-4 years. The focus of this capex would be majorly on modernization of its facilities followed by capacity expansion. The capex plan includes setting up a missile/defence systems integration complex, Electro optical device manufacturing facility, Electronic warfare test range and ten product support centres across India.

Growing emphasis on exports

On the export front, export order book stood at USD162.24 million as on July 1, 2019. Major products exported includes Naval Equipments, Smart City Business, Real Time Information System etc. The company is also exploring civil market in developing & third world Countries with product like smart cities, solar power generation, etc. Company has achieved an export sale of US$ 21.6 Million during 2018-19.

The decline in export sale by 15 per cent yoy was mainly due to the non-establishment of Letter of Credit by customer for various Naval Systems and Land Based Systems and Solutions. Going ahead, company expects order inflows to pick up from various countries once the LC issue will get resolved. Further, it is looking for development of new markets through strategic alliance with Indian platform and Foreign OEM's.

Well poised to post healthy margin

Ministry of Defence in its new pricing circular has lowered the maximum PBT margin on new contracts awarded on nomination basis to 7.5 per cent from 12.5 per cent earlier. However, earlier the margin was based on the value-added product and used to ignore the cost and risk associated with the order. The new pricing policy is more detailed and scientific in nature and covers all the cost associated with the order. Further, new policy allows pass through of royalty, R&D, programme management and prototype cost which in earlier policy were not taken into consideration. The company is looking to counter the margin pressure through various initiative like lowering direct costs and faster execution, slower growth in employee costs post wage bill settlement. Also, rising share of non-defence and service business is expected help company to post healthy margin going forward. Overall, the management has guided EBITDA margin in the range of 18-20 per cent.

Financial performance

Looking at the recently concluded quarter Q1FY20, the standalone revenue came in at Rs. 2042 crore as against Rs. 2077.84 crore in the corresponding quarter last year. The EBITDA for the quarter grew by 12.1 per cent yoy to Rs. 348.11 crore as against Rs. 310.49 crore in the corresponding quarter last year, with a corresponding margin expansion of 179 bps. EBITDA margin for the quarter stood at 16.6 per cent. The PAT for the quarter came in at Rs. 204.73 crore as against Rs. 179.73 crore in the corresponding quarter last year, yoy increase of 13.9 per cent.

Valuation and outlook

The company's strong order book gives robust revenue visibility over the next 4-5 years. Also, the company has strong orders in pipeline. Also, increasing share of non-defence and service business is expected to aid in both revenue growth and margin improvement. Notably, company's emphasis on R&D spends likely to add in new product development, in turn fuelling future revenue growth. In terms of return ratios, the company has strong ROE and ROCE of 21.5 per cent and 30.5 per cent respectively. In terms valuations, the stock of BEL is available at P/E multiple of 14.22 on TTM earnings which looks attractive as compared to five-year median P/E of 22.04x.