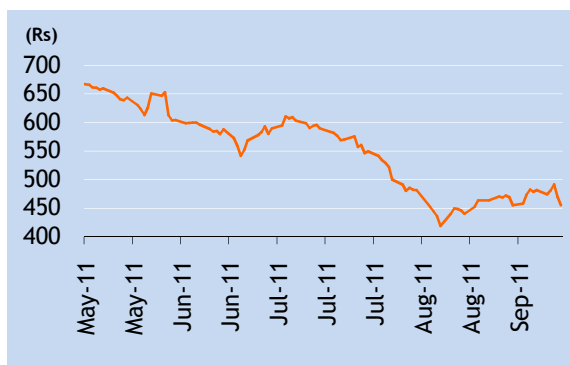


**BUY**

**Poised for Higher Growth**

Recommendation:	
<b>CMP - 449</b>	<b>Target Price :625</b>
<b>Upside:39%</b>	<b>Invest. Horizon:12 mn</b>
<b>Sensex:16051</b>	<b>Market Cap : 1871.94</b>
Basic Detail	
<b>BSE Code/NSE Symbol</b>	500048/BEML
<b>Bloomberg/Reuters</b>	BEML IN/BEML.BO
<b>INDUSTRY</b>	Engineering - Industrial Equipments
<b>Face Value</b>	10.00
<b>BSE 52 Wk High/Low Price</b>	1224.00/413.00
Key Indicators	
<b>Shares Outstanding (Cr.)</b>	4.1644
<b>Market capitalization (Rs Cr)</b>	1893.78
<b>Average 2 wk volume</b>	17.09
<b>Latest Book Value</b>	514.42
<b>TTM EPS</b>	35.49
<b>TTM PE (x)</b>	12.81
<b>Industry PE</b>	17.13
<b>Price/BV (x)</b>	0.88
<b>Dividend Yield %</b>	0.22
<b>EV / EBITDA (TTM)</b>	9.29
<b>Mcap / Sales (TTM)</b>	0.72
Price Performance	



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BEML is a mini-Ratna Public sector company under the Ministry of defense. The company has operation in three core business i.e Mining & construction, Rail & Metro and Defense & Aerospace. The company has global presence in about more than 58 countries and expanding aggressively overseas by stepping up subsidiaries and phased local manufacturing program.

### Infrastructure development-Growth Engine

India is planning to invest ~US\$ 1 trillion in 12<sup>th</sup> Plan compared to US\$14 billion in during 11<sup>th</sup> Plan with Power and Railways gaining top priority. Coal import dependence is set to increase from 19.8% to 22.1% equivalent to 250 mn tonnes in next five years thus creating a need to huge infrastructure build up in rail products. Government has sanctioned development of Western and Eastern Dedicated Freight corridors (DFC) to be completed by 12<sup>th</sup> Plan (FY12-FY17). Recently, Government approved infusion of 18,500 Cr. for 1483 km Delhi-Mumbai Industrial corridor. Public urban transport accounts for less than 25% of total urban transport leading to major constraint in urban cities. In addition to metros, tier II cities like Jaipur, Ludhiana and Kochi has been shortlisted for metro network leading to exponential growth for Rail and Metro business in next two years.

### Defense spending to turn inward

India has tenth largest Defense spend and is expected to increase by 10% CAGR from US\$32 bn in 2011 to US\$42 bn in 2015. The Indian defense is expected to increase the indigenous procurement from 30% currently to target 70% in next five years. According to a study, India is the largest importers of arms between 2006 and 2010 and estimates modernization of the industry at US\$ 80 bn by 2015. In January 2010, Ministry of Defense released India's first ever Defense production policy with a sharp focus on self-reliance in Defense. It enables for increasing capacity for domestic industrial base supporting defense, wider participation from private sector and broadening country's defense R&D base. It encourages private sector and PSUs to work in close coordination with Ministry of Defense to improve indigenous production and giving preference to contracts to products made by Indian industry with immediate effects.

### Outlook and Valuation

We believe with higher indigenization levels in metro business, wage settlement provisions behind us and shifting of focus to high margin business like aerospace and defense, the earning momentum is set to increase. At the CMP, The stock trades at P/E of 8.85x and 7.06x FY12BE and FY13BE respectively. **We put a BUY rating on the stock with a target price of Rs. 625 providing an upside of 39% from the current levels.**

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*M. Mangapati Pallam Raju, Indian Minister of State for Defense said: "We have seen a number of innovative tie-ups and partnership agreements between foreign and Indian companies, both public and private, giving us the confidence to adopt a cautious, calibrated approach in opening up the defense sector. We are now entering a new age of international cooperation in defense."*

Attractiveness of India as a cost efficient, high quality manufacturing and service delivery destination

Example : Engineering Design, Sheet metal work, Specialised forgings

Work coming to India due to regulatory constraints in other parts of the world.

Example : Some types of surface treatment



**Increasing interest in Indigenous defence and aerospace manufacturing and service delivery**



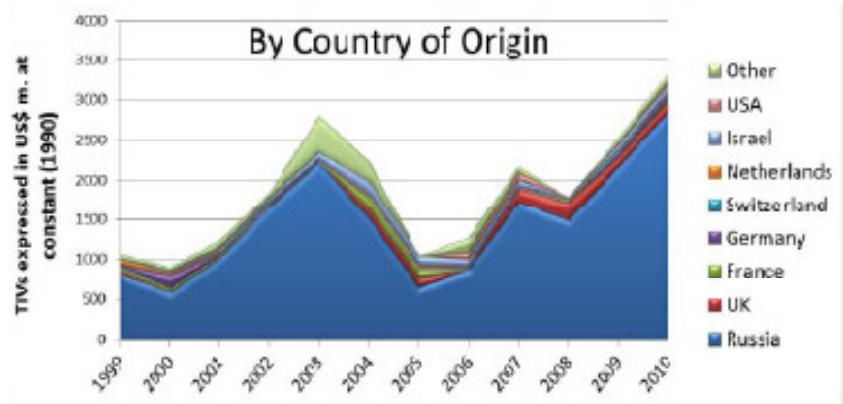
Strong government policy impetus through

Focused offset policy initiative requiring the global defence contractor to invest in the development of indigenous defence and aerospace manufacturing capability

Buy and Make-Indian' and 'Make' Projects which have a minimum stipulation of indigenous content / value add.

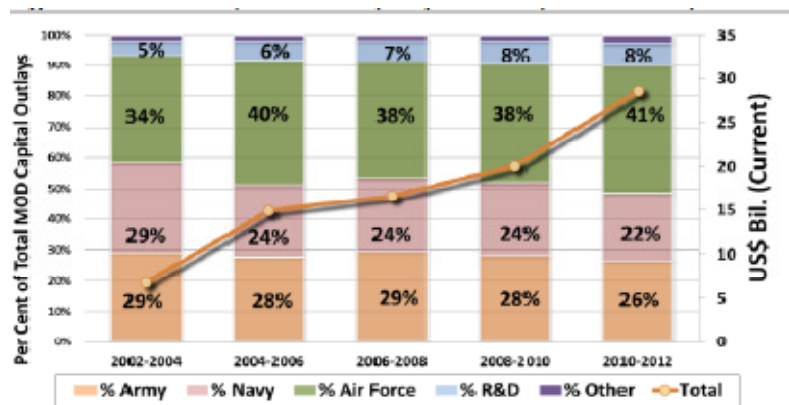
A large homeland security opportunity being driven by significant government initiatives

### India's Arms Imports (1999-2010)



According to a study, India is the largest importers of arms between 2006 and 2010 and estimates modernization of the industry at US\$ 80 bn by 2015. In January 2010, Ministry of Defense released India's first ever Defense production policy with a sharp focus on self-reliance in Defense. It enables for increasing capacity for domestic industrial base supporting defense, wider participation from private sector and broadening country's defense R&D base. It encourages private sector and PSUs to work in close coordination with Ministry of Defense to improve indigenous production and giving preference to contracts to products made by Indian industry with immediate effects.

### MOD Capital Outlays by Service (2002-2012)



MOD has shifted 11% of total expenditure away from army and navy in favor of the air force and R&D in last decade. As a result of 'Offset policy' by GOI whereby any foreign manufacture of aviation sells to govt. owned Indian aviation is required to source up to 30% of sales value in India coupled with up gradation of Indian military aviation provides huge opportunity for the aerospace industry.

## BEML- Poised for Higher Growth

BEML is a mini-Ratna Public sector company under the Ministry of defense. The company has operation in three core business i.e Mining & construction, Rail & Metro and Defense & Aerospace. The company has global presence in about more than 58 countries and expanding aggressively overseas by stepping up subsidiaries and phased local manufacturing program.

*Strategic alliance with Kamaz Vectra, Russia to develop vehicles for Defense, Para military and police forces and mining equipments*

*MOU with Alenia Aeronautica Italy, a global player in commercial and defense market worldwide. It plans for collaboration in designing, manufacturing and selling basic training aircraft.*

*MOA with UAC, Russia to explore business opportunities in production, sales, marketing and maintenance of civil transport and passenger aircrafts in India*

The company has setup Palakkad complex recently with a total investment of Rs. 260 cr. on a total land bank of 1000 acres of which 375 acres has already been transferred by Karnataka government. This facility is dedicated to defense equipments and rail coaches. Along with this, the company will invest Rs. 455 cr. for aerospace components plant in Bangalore SEZ which would be operational by FY13. The facility will manufacture helicopter gears, jigs for aircraft structure, aerospace components machinery facility and fabrication of structural sub-assemblies for Su-30 aircraft and ground support equipment. The company expects to do achieve a turnover of Rs. 1000 cr. from aerospace and offset business by FY17. In wind energy, it will invest Rs. 100 cr. to setup 18 MW wind power plant in Karnataka. The company envisages spending a total of Rs. 1,000 cr. in next three years.

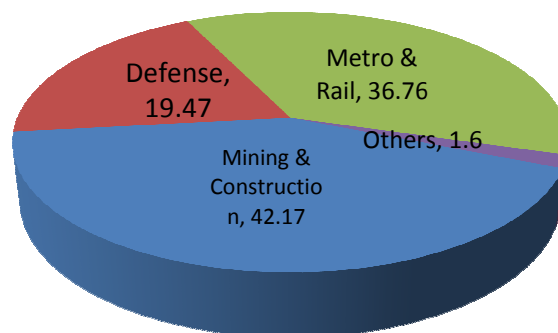
Currently has following four main plants:-

Bangalore	Kolar	Palakkad	Mysore
<ul style="list-style-type: none"> <li>•Railway rolling stock</li> <li>•Metro coaches</li> <li>•Defence equipments</li> <li>•Aggregates</li> </ul>	<ul style="list-style-type: none"> <li>•Heavy earthmoving equipments</li> <li>•Rail Coaches and Wagons</li> </ul>	<ul style="list-style-type: none"> <li>•Defense products</li> <li>•Metro &amp; Rail</li> </ul>	<ul style="list-style-type: none"> <li>•Dumpers</li> <li>•Engines</li> <li>•Aerospace manufacturing (defense use)</li> <li>•Diesel engines (captive)</li> </ul>

For FY12, the management has highlighted for a target for Rs. 4500 crs gross revenue. In Defense segment, BEML is expected to enter the overhaul of the BMP-II and management has highlighted that the government has already nominated BEML. It expects orders worth 4000-5000 heavy mobility vehicles. In addition, BEML has been shortlisted for wheeled caliber gun for which it has tied up with a Slovakian company.

In Metro business, the company has received order from Jaipur metro whereas it is also the L1 (lowest bidder) in Kolkata orders and further orders from Delhi and Hyderabad metro orders with the total business opportunity of Rs. 10,000 cr. The company has indicated earlier that 50% indigenous content as the threshold for metro projects to be profitable. Currently, the company is running on 50% indigenization levels and it plan to take it to 60% in FY12.

### Business wise Order book (FY11)



In mining business, Coal India is planning to expand its mining capacity by 81 m tones involving a total capital outlay of Rs. 59600 cr by FY17 with majority of Rs. 33900 cr. by FY12. This could significantly add to BEML's order book. The company has aggressively taken step to expand internationally opening offices in South Africa, China and Thailand.

### Outlook & Valuation

The company performance was subdued in FY11 due to slower execution and wage provisions for prior years. The company has booked Rs. 124 crore of extra wages on account of wage negotiations in FY11 and has increased the wage bill by Rs. 60 cr p.a. The management expects the productivity to increase by 30% and increasing contribution from high margin product to offset wage inflation going forward. The current Order book stands at Rs. 4712 cr and the company expects further orders worth Rs. 6000 cr. We believe with higher indigenization levels in metro business, wage settlement provisions behind us and shifting of focus to high margin business like aerospace and defense, the earning momentum is set to increase. At the CMP, The stock trades at P/E of 8.85x and 7.06x FY12BE and FY13BE respectively. **We put a BUY rating on the stock with a target price of Rs. 625 providing an upside of 39% from the current levels.**

*The stock has underperformed the sensex by 19.6% and 38.9% on 6 month and 12 month respectively.*

### Peer comparison

Company Name	P/BV		EV/EBITDA		PER(X)	
	FY12E	FY13E	FY12E	FY13E	FY12E	FY13E
BEML	0.8	0.8	9.7	6.4	8.9	7.1
BHEL	3.1	2.6	7.2	6.4	11.6	10.2
Cummins India	5.5	4.6	15.7	13.5	18.6	16.0

## **Risks**

### **Cyclicality in Capital goods**

There has been concern on slowing industrial production and thus capital goods and infrastructure spending recently. We do not rule out further weakening in the sector.

### **Government spending a key monitorable**

Since last six months, there has been slowdown in government spending due to various bureaucracy hurdles. Spending would be monitored since the majority of orders for company depend on Government spending.

### Income Statement

Year End	FY08	FY09	FY10	FY11
Net Sales	2540.1	2797.2	2838.2	2630.4
Employee Cost	450.2	573.8	559.9	687.2
Total Expenditure	2244.2	2442.8	2554.6	2557.7
Operating Profit (Excl OI)	295.9	354.4	283.7	72.7
Operating Profit	391.2	456.4	411.6	287.3
Interest	23.2	39.3	56.4	68.0
Depreciation	18.0	27.6	32.7	34.4
Profit Before Tax	350.1	389.5	322.5	184.9
Provision for Tax	123.1	119.4	97.9	37.1
Profit After Tax	227.0	270.2	224.6	147.7
Extra items	0.0	0.0	0.0	0.0
Earnings Per Share	54.5	64.9	53.9	35.5

### Cash Flow Abstract

Year End	FY08	FY09	FY10	FY11
C/F from Operations	-476.3	-411.4	100.9	-155.9
C/F from investing	-57.5	-39.6	-36.0	-162.2
C/F from Financing	707.1	193.3	238.8	-200.8
Inc./Dec. in Cash	173.3	-257.6	303.7	-518.9
Opening Cash	347.8	521.1	263.5	567.2

### Balance Sheet Abstract

Year End	FY08	FY09	FY10	FY11
Shareholder's Funds	1709.4	1920.1	2043.3	2142.4
Total Debts	304.1	569.1	915.9	823.4
Total Liabilities	2013.7	2489.5	2959.5	2966.1
Gross Block	687.2	756.4	815.0	962.0
Net Block	213.8	258.5	285.7	400.9
Investments	5.4	5.4	5.4	5.4
Sundry Debtors	1496.6	1545.1	1360.7	1287.5
Cash and Bank	521.1	263.5	567.2	48.3
Current Liabilities	1307.7	1134.6	895.4	993.6
Net Current Assets	1752.6	2192.3	2601.8	2435.6
Other Assets	0.0	0.0	0.0	0.0
Total Assets	2013.7	2489.5	2959.5	2966.1

### Growth

Year End	FY08	FY09	FY10	FY11
Net Sales Growth (%)	4.77	10.12	1.47	-7.32
EPS Growth (%)	-2.72	18.99	-16.89	-34.16
<b>Profitability</b>				
PBIDTM (%)	14.21	15.47	13.75	9.99
PATM (%)	8.25	9.15	7.50	5.14
ROE (%)	16.74	14.98	11.36	7.06
ROCE (%)	24.54	19.15	13.93	8.54
<b>Balance Sheet</b>				
Sales(x)/Working Capital	1.57	1.35	1.15	1.18
Total Debt/Equity(x)	0.18	0.30	0.45	0.38
<b>Valuation</b>				
Adjusted PE (x)	18.17	5.88	19.52	19.32
Price / Book Value(x)	2.43	0.83	2.15	1.33
EV/Net Sales(x)	1.54	0.68	1.67	1.38
EV/EBITDA(x)	9.99	4.15	11.49	12.64

### Standalone Quarterly Financials

Date End	Sep-10	Dec-10	Mar-11	Jun-11
Net Sales	509.27	658.18	936.07	553.91
Operating Profit	35.82	87.24	114.10	36.80
PBIDTM%	6.41	12.65	11.68	6.26
Depreciation	7.69	8.06	9.59	9.81
Interest	14.73	14.30	17.60	15.39
PBT	13.40	68.71	83.08	21.39
Tax	-1.34	18.34	12.83	5.52
Profit after tax	14.74	50.37	70.25	15.87
Extraordinary Items	0.00	0.00	0.00	0.00
Net Profit (After EI & MI)	14.74	50.37	70.25	15.87

### Major Shareholders (%)

Date End	Sep-10	Dec-10	Mar-11	Jun-11
Promoters	54.03	54.03	54.03	54.03
Foreign	15.43	16.20	12.85	12.78
Domestic Inst.	22.83	21.89	23.26	23.48
Public & Others	7.72	7.88	9.85	9.71

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