Flash

Bekaert

18 March 2003

Future looks brighter

Engineering & Machinery			
Belgium			
Performance over	**1m**	**3m**	**12m**
Absolute	-5%	-5%	-23%
Rel. BEL20	-1%	10%	20%
Rel. sector	-2%	5%	17%
12-m- Hi/Lo			€ 50.90/31.30
Reuters			BERTt.BR
Bloomberg			BEKB BB
Market Cap			€ 802.8m
Next corporate event			
General Assembly 03 on 14 May 2003			

Current price € 36.00 — **Buy**

Target price € 45.00 — Rating unchanged

FY/e 31.12	2002	2003E	2004E	2005E
Sales (€m)	1,863	1,950	1,974	1,999
EBITDA (€m)	209	234	257	262
Pre-Tax* (€m)	42	101	114	121
Adj EPS* (€)	-1.13	4.37	4.83	5.09
EPS (€)	-2.24	3.68	4.13	4.37
DPS (€)	1.68	1.75	1.95	2.05
P/E* (x)	-	8.2	7.4	7.1
Yield (%)	4.7	4.9	5.4	5.7
EV/EBITDA (x)	5.9	4.5	3.9	3.7

Source: KBC Securities **Adjusted for goodwill and exceptionals*

Bekaert published FY02 results last week. These were disappointing but in line with what the group already had announced on 10-Feb-02. The consolidated net loss of the group amounted to € 49.5m as expected (down from € 47.8m last year). We have upgraded the stock to Buy because the underlying trend in the business is more positive than the loss - because of exceptional charges - suggests. We regard the sharp drop in the share price (+/- 22% year-to-date) following the announcement of the € 84m impairment charge on Uni-Solar, as excessive. Operating margins improved when excluding exceptional items (better product mix following the divesture of volume driven businesses, focus on efficiency and return) while the strategy to expand in Eastern Europe and China is (more) credible. Results FY03 will improve significantly if the current trend persists. A strong balance sheet, high dividend yield, low Price-to-Book ratio, market leadership in several of the product lines… deserves a Buy rating given the current price levels and despite the geopolitical uncertainties.

FY02

In the first place the FY02 results published last week were disappointing. The group booked a € -49.5m net loss (versus a net profit of € 47.8m last year which was also far from excellent). The poor result however was in line with what Bekaert had announced on 10-Feb-03:

Bekaert FY02 results

	1H01	2001	1H2002	2002	2003E
Sales	931	1796	986	1863	1950
Growth	-1.0%	+2.3%	+5.9%	+3.8%	+4.6%
EBITDA	120.2	207.5	101.5	225.8	233.9
Margin	12.9%	11.5%	10.3%	13.8%	12.0%
Operating result	53.4	59.5	20.8	64.2	121.5
Margin	5.7%	3.3%	2.1%	3.4%	6.2%
Financial result	-14.1	-30.4	-14.9	-32.9	-31.9
Other	-7.8	5.4	-5.8	-100.6	0
Taxes	-7.4	4.6	-1	7.4	-25.2
Equity consolidated	7.6	16.6	13.9	23.1	23.1
Net profit group share	30.8	47.8	9.4	-49.5	89.7
Per share data					
EPS	1.38	2.15	0.43	-2.24	4.37
CFPS	4.46	9.02	4.16	9.14	8.56

Source: Bekaert, KBC Securities

For comparative reasons, we have included the figures as published by the group in the table above. Our 2003 estimates are on a current basis before GW and exceptional items. It is possible that we will be making some more adjustments once the annual report FY02 becomes available (18 April 2003 on www.bekaert.com).

- **Sales** increased by 3.8% to €1,863m. Steel wire (-0.1%), Steel cord (+1.4%) and Fencing (+0.7%) remained approximately flat. "Advanced Materials" posted a 34.4% increase in Sales to € 220m (consolidated). This was mainly the result of Bekaert Specialty Films, acquired in Apr-01 and consolidated for no more than 6 months last year. Without $ effect, sales would have increased by 5.9% according to the group.
  The European Union (48.7%) and North America (29.7%) remain the most important regions for Bekaert. Rest of Europe (7.7%) and Rest of World (12.3%) are less important. However, they will be gaining more importance. The group will namely focus - as announced at Bekaert's analyst day in Dec-03 - on growth regions (Eastern Europe, Asia, China in particular) where Bekaert intends to broaden its presence in the years to come.

Sales per business unit

	1H01	2001	1H2002	2002a	2003e
Wire	306	675	344	674	668
Steel cord	310	597	305	605	605
Fencing	212	388	215	392	394
BAM	65	164	111	220	231
Others	13	87	11	58	52
Intersegment sales	n.a.	-113	n.a.	-84	
Total	906 (°)	1796	986	1863	1950

Source: Bekaert, KBC Securities

(°) €25m difference with other releases because of IAS adjustments

- **Operating margins**: the FY02 results were affected by a number of one-off costs related among others to the impairment charge on Uni-Solar (€ 84m). Bekaert mentions € 144m of non-recurring provisions to cover restructurings, closures and impairments. Excluding these from the "Results from operations" yields an EBIT margin of 6.6% compared to 3.4% before exceptional charges:

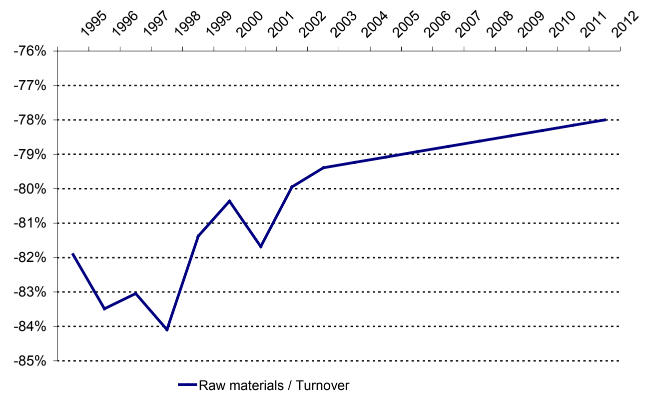
Bekaert FY02 results

	1H01	2001	1H02	2002	2003E
Sales	931	1796	986	1863	1950
Growth			+5.9%	+3.7%	+4.6%
Results operations	53.4	59.5	20.8	64.2	n.a.
Margin	5.7%	3.3%	2.1%	3.4%	n.a.
Normalised EBIT	n.a.	73.6	n.a.	123.0	121.5
Margin		**4.1%**		**6.6%**	6.2%

Source: Bekaert, KBC Securities

The positive trend is in particular reflected by the evolution in the gross margin ("Sales" minus "Costs of goods sold"), which is steadily improving since 1997/1998 (excluding the dip in 2001 following a deterioration in activity levels):

Bekaert gross margin



Source: KBC Securities

The gross margin improvement also involves an EBIT-margin improvement. Bekaert never did better than last year's 6.6% EBIT margin "before restructurings" (except in 1994 but that is a long time ago). The graph (and not taking into account that the group moved to IFRS accountancy standard in 2002) also shows that we have taken into account a gradual improvement of the gross margin in our business model. Cost of goods sold will amount to 78.0% of sales by 2012 in our model (vs. 79.9% in FY02). The improvement is far from aggressive in our view and in line with the gradual improvement witnessed since 1997/1998.

Outlook

Of course Bekaert did not want to comment on the outlook given the uncertainties in the market today. The message was that the order book in Steel Wire and Fencing was slightly down but that Steel Cord and BAM did reasonably well. Nevertheless, if Bekaert is able to avoid exceptional losses this year, earnings should recover significantly. It is also worth mentioning that Bekaert is still looking for a solution for its solar energy project set up in collaboration with ECD. Both parties are looking for a 3rd partner to join the project. It is still possible that Bekaert will book a capital gain on Uni-Solar in the future (book value now zero).
In terms of future expansion, Bekaert now focuses much more on growth regions in the world to commercialise its (existing) products as it already does in Europe and North America without taking extra technological risks. Eastern Europe and China in particular are two regions where the group will expand in the foreseeable future.

We have adjusted our earnings outlook for this year considering prudent estimates. We have taken into account among others a 6.2% EBIT-margin (compared to 6.6% last year). We assumed a flat result from the equity stakes (€ 23.1m) although Bekaert will not have to book losses on Uni-Solar again (€ 8m in FY02). All in all our adjustments (couple of percentage points) are minor as we have already taken into account an earnings recovery. We now take into account a € 89.7m net profit part of the group vs. € 87.6m before.

Valuation

Last week we upgraded the stock to Buy mainly as a result of two things:

- Underlying trend is far more positive than the € -49.5m net loss suggests (as described above);
- The share price dropped 22% this year which we find excessive given the following positive elements with regard to Bekaert's pricing:
    - The value of the solar energy business in our model amounted to € 3.5/share; the € 10 price drop was thus not in line with the impairment charge of € 84m announced on 10-Feb-03;
    - Price-to-Book amounts to approximately 0.80x (perhaps an all time low for Bekaert);
    - The group keeps its € 1.68 gross dividend flat over FY02 (€1.68/€36=4.67% yield) on the back of among others a strong cash flow generation;

- Gearing is low (42%) which makes it easy for the group to attract financial means to support further growth. In our view, there is sufficient room to attract at least € 100-150m without jeopardising the financial solidity of the group;
- Price/Earnings amounts to approximately 8.2x, which is low. Price/Cash Flow amounts to 3.7x. The only point of discussion could be the fact that most Belgian industrials have fallen low and trade at very attractive multiples. Indeed from a Belgian perspective, one could argue that Bekaert is not particularly cheap but looking at market cap, international airs, liquidity (€ 1.14m traded each day)… we feel that Bekaert should trade at higher multiples.

Belgian industry

	Market cap	P/E03	P/E04	EV/EBITDA03	EV/EBITDA04
Bekaert	774	8.3	7.1	4.8	4.5
Umicore	766	9.1	6.8	4.2	3.6
RCA	49	9.1	7.9	4.7	4.4
VPK	188	8.2	7.5	3.3	2.9
Recticel	239	9.5	8.2	5.1	4.7
Resilux	104	15.6	10.3	6.1	4.9
Solvay	4,602	9.5	8.3	4.2	3.8
Tessenderlo	714	8.7	7.3	4.1	3.5
Picanol	122	4.3	3.6	1.6	0.9

Source: JCF Finance

Based on all this we decided last week to upgrade Bekaert. We have kept a price target of € 45 per share which still leaves a 25% upside potential.

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