

Earnings and target price revision

Engineering & machinery

Belgium

Bekaert^[dg]

Maintained

Hold

05/08/04

12 month

Reuters: BERTt.BR

Price: €51.15

Target price: €56.00

- **Bekaert's impressive 1H04 results have led us to raise our forecasts substantially.**
- **We believe the Bekaert shares have additional upside potential, although earnings momentum should gradually fade. We therefore maintain our HOLD recommendation and raise our 12-month price target from €48 to €56.**

Highlights of Bekaert's 1H04 results were: 1) high organic sales growth (+19% YoY), due for the most part to volume growth; 2) massive gross margin expansion (187 basis points) despite higher raw material prices, driven by the revaluation of inventories (c.€20m) following FIFO; 3) strong top- and bottom-line results at the Fencing division; 4) weak growth in China; and 5) a still strong order book, despite a slowdown in the ordering of, eg, wire products (although not steel cord), linked partly to early ordering in 1H04 so as to avoid announced price increases. All in all, Bekaert's 1H04 results were definitely strong (with the EBIT margin peaking at 9.3%), but we believe the 1H04 performance is unlikely to be repeated in the short run.

We have reviewed our forecasts following the massive rise in 1H04 earnings (+80.2% YoY) and incorporating the likelihood that raw material prices will now have an adverse impact on gross margins moving forward (2H04F and 2005F), with the positive FIFO impact already included in the 1H04 results. We expect the gross margin to fall to 19.9% in 2H04F (from 23.7% in 1H04 and 20.1% in 2H03). Moreover, we expect order intake to slow down in 2H04 (due to the early ordering in 1H04), but estimate that there should still be a YoY increase, partly aided by the strengthening US\$. We have also increased the forecast tax rate for 2004F to 28% (vs a 30.7% rate in 1H04). The table below summarises the main items of our forecast revisions, which lift our 2004F EPS by 33.9% (to €5.17) and EPS in 2005F and beyond by double digits.

Bekaert: Overview of forecast revisions

	2004F	2005F	2006F	2007F
Sales (change in %)	+4.2	+4.5	+3.6	+4.3
Gross margin (change in basis points)	58	-156	-125	-117
Net EPS, previous (€)	3.86	4.13	4.28	4.35
Net EPS, new (€)	5.17	4.69	4.75	4.77
Net EPS revisions in %	+33.9	+13.6	+11.0	+9.7

Source : ING estimates

We maintain our Hold recommendation on Bekaert as we believe the market had already anticipated the good news, earnings momentum should gradually fade, and €56 (our new target price in line with a 2005F PER of 12x) should prove a tough technical share price level (five-year high) to exceed.

Target price based on PER, 2005F

	High	Low	Now	Target
PER (x)	11.1	8.5	10.9	11.9

Price performance

	12m	3m	Now	Target
Absolute (%)	21.5	6.8	-	9.5
BEL 20	2,031.2	2,458.8	2,511.4	2,550.0
Rel to BEL 20 (%)	-1.7	4.5	-	7.8
FTSE E300	872.4	1,008.5	977.5	1,160.0
Rel to FTSE E300 (%)	8.4	10.2	-	-7.7

Forecasts (€)

Yr to Dec	2003	2004F	2005F	2006F
Turnover (m)	1,797.0	2,011.5	2,081.9	2,145.5
Net profit (m)	85.2	114.2	103.6	104.8
Adj EPS	4.18	5.49	5.01	5.07
CFPS	11.64	11.22	11.58	11.25
Dividend	1.75	1.87	2.00	2.14
Adj PER (x)	12.2	9.3	10.2	10.1
EV/EBITDA (x)	6.5	5.8	6.0	5.7
Yield (%)	3.4	3.7	3.9	4.2

Share data (€)

No. of shares (m)	22.1	Market cap (m)	1,128.9
Volume	32,500	Ent'prise val (m)	1,591.9
Free float (%)	60.0	Price/NAV (x)	1.3

Key ratios

Yr to Dec	2003	2004F	2005F	2006F
EBITDA margin (%)	13.3	13.6	12.8	13.2
Gross margin (%)	20.7	22.0	20.5	21.0
Net debt/equity (%)	50.9	51.2	49.1	47.6
ROACE (%)	8.6	10.1	9.0	8.6
ROE (%)	10.6	14.0	11.8	11.2

Forecasts: ING High/Low 1 year

Luc Struelens

+32 2 547 3678

luc.struelens@ing.be

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SPARK - single page action research

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Company profile

Bekaert produces and markets a wide range of products based on metal-forming and coating technologies. Incorporated in 1880, Bekaert has evolved from a small manufacturing and trading company into a global group. Bekaert initiated its internationalisation in the 1920s, first in Western Europe, then in Latin America and, since the 1970s, in North America and the Far East.

Advanced Wire Products

This segment is the company's main division (c.66% of sales), grouping together Wire and Steel Cord activities. Bekaert produces mainly for the Automotive and construction sectors. Its product range includes industrial spring wire, flexible hose reinforcement wire, plastic-coated specialities and champagne cork wire. Bekaert's steel cord activities are mainly linked to tyre reinforcement (Tyre cord and bead wire).

Fencing systems Europe

This division, accounting for c.23% of sales, comprises end products. It designs, develops, produces and markets woven and welded mesh products for the garden and agricultural markets, professional and security fencing systems, half-products for industrial applications and products for handling and display.

Advanced materials

This division (c.5% of sales) is focused on specific innovative industrial products in less cyclical markets (fibre technologies and combustion technologies).

Advanced Coatings

Bekaert is specialised in sputtering, a high-end process in which a coating is deposited on a substrate under vacuum. Applications include diamond-like coatings (eg, used in DVD production) and specialised window films (for solar control and safety enhancement). This activity represents c.6% of sales.

Financials

Yr to Dec (€m)	2003	2004F	2005F	2006F
Income statement				
Turnover	1,797.0	2,011.5	2,081.9	2,145.5
EBITDA	239.1	273.2	265.9	282.5
Net financial charges	(43.0)	(32.1)	(33.6)	(33.8)
Operating exceptionals	0.0	0.0	0.0	0.0
Adj pre-tax profit	107.8	163.8	143.4	152.5
Corporate exceptionals	0.0	0.0	0.0	0.0
Profit/loss on sale of tangible fixed assets	0.0	0.0	0.0	0.0
Amortisation of goodwill	(7.0)	(7.0)	(7.0)	(7.0)
Pre-tax profit	100.9	156.8	136.4	145.5
Taxes	(8.2)	(33.6)	(23.3)	(31.2)
Extraordinary items (net)	0.0	0.0	0.0	0.0
Minorities	(7.5)	(9.0)	(9.5)	(9.5)
Preference dividend	0.0	0.0	0.0	0.0
Net profit	85.2	114.2	103.6	104.8
Balance sheet				
Total fixed assets and L/T investments	1,153.8	1,279.5	1,366.6	1,443.4
Working capital	302.1	303.0	299.7	307.1
L/T non-interest-bearing liabilities	215.2	215.2	215.2	215.2
Enterprise net assets	1,240.6	1,367.2	1,451.0	1,535.2
Group equity	822.3	904.2	973.1	1,040.2
Net debt	418.3	463.0	477.9	495.1
Capital employed	1,240.6	1,367.2	1,451.0	1,535.2
Cash flow				
Operating cash flow	308.0	313.3	312.5	313.2
Cash taxes	(8.2)	(33.6)	(23.3)	(31.2)
Net financial charges (CF)	(43.0)	(32.1)	(33.6)	(33.8)
Gross cash flow	256.9	247.6	255.5	248.2
Capital expenditures (net of disposals)	(209.2)	(210.0)	(183.0)	(180.0)
Free cash flow	47.7	37.6	72.5	68.2

All sources: Company data, ING estimates

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