

Change in recommendation

Engineering & machinery

Belgium

Previously: Hold

Bekaert^[dg]

Buy

05/11/04

12-month

Reuters: BERTt.BR

Price: €51.65
Target price: €60.00

● **Bekaert's 3Q trading update highlighted – once more – a solid rise in turnover, partly driven by higher selling prices.**

● **As this should lead to reduced pressure on 2H margins, we raise our forecasts, putting Bekaert on low PER multiples. Hence we upgrade our price target from €56 to €60 and our recommendation from Hold to BUY.**

3Q YoY sales growth (21%) continued the impressive pace recorded in 1H (and was even slightly higher, apart from in advanced coatings). As this high organic growth level continued in 3Q (and despite the adverse impact of the weakening US dollar), we expect Bekaert to face solid demand and believe that the lion's share of this 3Q growth stems from Bekaert's decision to increase its selling prices. As this should therefore smoothen the expected pressure on gross margins (due to rising raw material prices), we revise our forecasts.

2004 sales forecast upped by 4%, implying a 9% YoY rise in turnover for 4Q04. We up our gross margin expectation for 2004 by 30bp, but still expect a sizeable drop in gross margin in 2H (-300bp sequentially down to 20.7%, but up YoY from 19.7% in 2H03). We also raise the contribution from Latin American equity affiliates in view of the solid acceleration in turnover growth. All in all, we expect a 2H EBIT margin of 5.3% (9.4% in 1H04), which in turn should lead net 2004 EPS to be 8.8% higher (up to €5.63). We also believe that Bekaert will be able to attain in a more structural way a margin around 7.0-7.5% moving forward. Our forecasts for 2005 and beyond are upped as well, although we do not expect the 2004 EBITA margin (7.8%) to be attained prior to 2008.

Bekaert's outlook statement on 2004 was short: "Bekaert expects double-digit growth in 2004", which is quite logical after an 18.7% turnover rise in the first nine months. We believe this to be a minimum, rather than a precise guidance. Our previous estimate already expected 11.9% YoY sales growth for 2004, which we now up to 16.4% YoY.

We upgrade Bekaert from Hold to BUY as we believe that earnings momentum might further strengthen as: (1) part of our 'gross margin concerns' are offset by the higher turnover growth (and possible increased pricing power); (2) Bekaert's exposure in China is not yet contributing but should sustain long-term potential; and (3) valuation in terms of PER has become low (adjusted 2004F PER of 8.6x). Consequently, we upgrade Bekaert from Hold to **BUY** and set our 12-month target price in line with an adjusted PER 2005F of 10.0x.

Target price based on adj PER

	High	Low	Now	Target
Adj 2005F PER (x)	8.8	7.2	8.6	10.0

Price performance

	12m	3m	Now	Target
Absolute (%)	19.4	1.0	-	16.2
BEL 20	2,172	2,511	2,839	2,550
Rel to BEL 20 (%)	(8.6)	(10.7)		29.3
FTSE E300	927.5	977.5	1,021.1	1,160.0
Rel to FTSE E300 (%)	8.5	(3.3)		2.3

Forecasts (€)

Yr to Dec	2003	2004F	2005F	2006F
Turnover (m)	1,797.0	2,092.3	2,216.3	2,280.1
Net profit (m)	85.2	124.2	124.8	122.9
Adj EPS	4.18	5.94	5.97	5.88
CFPS	11.64	11.05	11.85	11.73
Dividend	1.75	2.00	2.14	2.29
Adj PER (x)	12.4	8.7	8.6	8.8
EV/EBITDA (x)	6.5	5.7	5.6	5.4
Yield (%)	3.4	3.9	4.1	4.4

Share data

No. of shares (m)	22.1	Market cap (€m)	1,140
Volume	25,146	EV (€m)	1,609
Free float (%)	60.0	Price/NAV (x)	1.3

Key ratios (%)

Yr to Dec	2003	2004F	2005F	2006F
EBITDA margin	13.3	13.6	13.1	13.2
Gross margin	20.7	22.3	21.3	21.6
Net debt/equity	50.9	51.5	48.0	45.2
ROACE	8.6	10.7	10.2	9.5
ROE	10.6	15.2	13.9	12.6

Forecasts: ING High/Low 1 year

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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 Asia.

Advanced wire products

This segment is the company's main division (c66% of sales), which groups wire and steel cord activities. Bekaert produces mainly for the automotive and construction sector. 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 c23% 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 (c5% 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 c6% of sales.

Financials

Yr to Dec (€m)	2003	2004F	2005F	2006F
Income statement				
Turnover	1,797.0	2,092.3	2,216.3	2,280.1
EBITDA	239.1	283.9	289.9	300.4
Net financial charges	(43.0)	(32.1)	(34.0)	(33.9)
Adj pre-tax profit	107.8	176.8	172.0	177.6
Amortisation of goodwill	(7.0)	(7.0)	(7.0)	(7.0)
Pre-tax profit	100.9	169.8	165.0	170.6
Taxes	(8.2)	(36.6)	(30.7)	(38.2)
Minorities	(7.5)	(9.0)	(9.5)	(9.5)
Net profit	85.2	124.2	124.8	122.9
Balance sheet				
Total fixed assets and L/T investments	1,153.8	1,281.8	1,373.9	1,458.0
Working capital	302.1	314.0	318.8	326.0
L/T non-interest bearing liabilities	215.2	215.2	215.2	215.2
Enterprise net assets	1,240.6	1,380.5	1,477.5	1,568.8
Group equity	822.3	911.3	998.4	1,080.3
Net debt	418.3	469.2	479.0	488.5
Capital employed	1,240.6	1,380.5	1,477.5	1,568.8
Cash flow				
Operating cash flow	308.0	312.5	326.1	331.0
Cash taxes	(8.2)	(36.6)	(30.7)	(38.2)
Net financial charges (CF)	(43.0)	(32.1)	(34.0)	(33.9)
Gross cash flow	256.9	243.8	261.4	259.0
Capital expenditures (net of disposals)	(209.2)	(210.0)	(183.0)	(180.0)
Free cash flow	47.7	33.8	78.4	79.0

All sources: Company data. ING estimates

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