

Company results & earnings revision

Belgium

Bekaert^[9]

2005's net earnings to exceed 2004's record level?

Engineering & machinery 18/03/05 **€64.85**

Bekaert posted excellent 2H04 results last Thursday, which led us to revise our forecasts upwards. Our BUY recommendation and €72 price target is maintained.

Bekaert's 2H04's results demonstrated resilience from its gross margin as the company faced a strong rise in raw materials prices. Profitability increased at double-digit rates for all bar one of its divisions, while its Latin American activities generated a record high contribution.

We have revised our forecasts upwards, which has led us to raise our adjusted EPS for 05F to 07F by, respectively, 4.4%, 9.9% and 14.7%. Due to the divestment of the Fencing division, Bekaert's recurrent earnings should remain well below FY04's level. However, due to the corresponding €56m capital gain, FY05F's net earnings could exceed FY04's level.

We consider Bekaert's performance in 2004 as particularly strong considering the rising wire rod prices and the weakened US dollar which the company has had to face. This reassures us regarding Bekaert's long-term strategy and justifies our **BUY** recommendation with a €72 price target, in line with an adjusted PER05F of 12.9x. Bekaert's EV/EBITDA adjusted for the sizeable contribution of Latin American equity affiliates to Bekaert's net result also points to further upside.

Forecasts and ratios

Yr to Dec	Turnover (€m)	Net profit (€m)	Adj EPS (€)	CFPS (€)	Div (€)	Adj PER (x)	EV/EBITDA (x)	Yield (%)
2004	2,173.2	167.6	7.93	9.05	2.00	8.2	5.9	3.1
2005F	1,814.1	177.9	5.57	17.54	2.00	11.6	6.5	3.1
2006F	1,885.2	130.0	5.94	11.49	2.14	10.9	6.2	3.3
2007F	1,953.9	136.1	6.22	11.49	2.29	10.4	6.0	3.5

Source: Company data, ING estimates

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Maintained

Buy

21 March 2005

Target price: 12 month

€72.00

Reuters

BERTt.BR

Key ratios (%)

	2004	2005F
EBITDA margin	14.6	13.2
Operating margin	8.8	7.1
Net debt/equity	47.8	12.0
ROA	13.3	9.5
ROE	19.9	11.9

Performance (%)

	12m	3m	Target
Absolute (%)	45.2	10.1	11.0
BEL 20	2,367.7	2,915.3	
FTSE E300	973.3	1,033.1	
Relative to (%)			
BEL 20	11.3	3.8	
FTSE E300	30.7	5.2	

Share data

No. of shares (m)	21.9
Volume	32,808
Free float (%)	60.0
Market cap (€m)	1,418.5
Enterprise value (€m)	1,561.2
Price/NAV (x)	1.3

Share price performance (rebased)



Source: ING

FY04 results and analysts' meeting: highlights

Record FY04 earnings

Bekaert 2H04's results, issued on 17 March, came in very strong as:

- Gross margin held up very well during 2H04 (22%, vs 20.6% estimated), thereby providing evidence that Bekaert had pricing power and recovered a large part of the sharp rise in raw materials prices (wire rod). We should, however, consider that a €46m revaluation of Bekaert's inventory (already c.€20m during 1H04) aided keeping Bekaert's gross margin close to the 23.2% margin recorded during 1H04.
- The weakening of the US dollar, on the other hand, wiped out €17m of the FY04 EBIT progression.
- Profitability increased YoY in every division at double-digit growth rates, apart from Advanced Materials (due to a €6.3m write-down on the part of the specialised film activity).
- The contribution for its Latin American affiliates was a stunning €53.6m for FY04, thereby rising 67% YoY.

As a result, the company's net result for FY04 was €167.6m (YoY +93.4%).

The dividend increased by only 7%, up to €2.00 gross per share (a €1.875 normal dividend and a symbolic premium dividend of €0.125 as Bekaert celebrated its 125th anniversary this year). We were expecting a higher dividend: €2.00 as a regular dividend in view of the sharp increase in results, alongside an extraordinary dividend of €2.00 following the divestment of the Fencing division.

A good start in 2005...

The outlook provided by management remained vague. "Bekaert made a good start in 2005" and comprised no indication on turnover or order book evolution. Management stated that demand in China is starting to pick up again. For FY05, we should, however, consider the Fencing division as sold and be aware that it accounted for €453m in sales 2004 as well as €52m in EBIT in 2004. Capex for 2005F should remain at the same level as in 2004 (c. €170m) and is likely to be primarily spent in increasing capacity in China, India, Central Europe and Latin America.

Revision of forecasts

We have revised our forecasts for Bekaert, thereby incorporating the underlying trends of the FY04 results. For FY05F, we expect Bekaert's gross margin to slip to 20.7% (as inventory revaluation lifted FY04's margin by 210 basis points to 22.6%). We integrated an average €/US\$ exchange rate of €1.328, which still is 6.4% below FY04's level and which should therefore still impact FY05's EBIT by c. €11m (mainly via translation).

Our divisional forecasts are presented in Figure 2. Due to the divestment of the Fencing division (as from 1/1/2005), FY05's EBIT is estimated to decline 32.5% YoY to €128.7m. We have slightly increased the anticipated contribution of Bekaert's Latin American affiliates (Latin America is likely to become one of the areas where Bekaert will increase its capex). All in all, we expect Bekaert to post a (net current) EPS of

€5.57 in FY05F. If we consider the €56 estimated capital gain on the Fencing disposal, net EPS05F should come in at €8.13.

Fig 1 Bekaert : Revision of forecasts

	2005F	2006F	2007F
Sales: new estimate (€m)	1,814.11	1,885.22	1,953.99
Sales: % of revision	0.3	0.4	0.6
Adj.EPS (€): previous estimate	5.344	5.411	5.433
Adj.EPS (€): new estimate	5.577	5.944	6.222
Adj.EPS: % of revision	4.4	9.9	14.7

Source: ING estimates

*Undemanding
EV/EBITDA multiples if
adjusted for company's
Equity affiliates*

Fig 2 Bekaert: Overview of Divisional Performance and forecasts

Advanced Wire products	2003	2004	2005F	2006F	2007F	2008F
Consolidated sales	1196.22	1500.00	1553.11	1599.55	1644.88	1686.44
EBITDA	206.55	259.00	239.00	250.00	259.33	265.00
as a % of sales	17.3	17.3	15.4	15.6	15.8	15.7
EBIT after non recurring	121.211	185.44	1655	172.55	180.255	184.3699
Equity Affiliates (net)	30.2711	53.5522	48.77	47.55	48.455	42.55
Fencing Europe						
Consol. Sales (=extern)	382.99	453.00	0.00	0.00	0.00	0.00
EBITDA	43.77	67.00	0.00	0.00	0.00	0.00
EBIT after non recurring	25.44	52.00	0.00	0.00	0.00	0.00
Advanced Materials						
EBITDA	13.77	14.88	14.00	16.00	18.22	19.77
as a % of sales	13.4	12.6	10.9	11.5	12.2	12.3
EBIT after non recurring	7.77	9.44	7.77	8.88	10.44	11.33
Advanced coatings						
Consol. Sales (=extern)	111.66	127.00	137.77	151.66	164.77	178.55
EBITDA	11.88	13.00	14.55	16.66	17.88	19.22
as a % of sales	10.6	10.2	10.5	11.0	10.8	10.8
EBIT after non recurring	-2.11	-2.00	-1.00	0.66	1.33	2.22
Bekaert : Group						
Consol. Sales (=extern)	1797.00	2173.00	1814.11	1885.22	1953.99	2020.22
EBITDA	239.11	307.11	239.55	253.22	264.44	271.55
as a % of sales	13.3	14.1	13.2	13.4	13.5	13.4
EBIT after non recurring	111.88	175.44	128.77	137.55	146.11	150.55
as a % of sales	6.2	8.1	7.1	7.3	7.5	7.4
Equity Affiliates (net)	32.00	53.22	49.00	47.88	48.88	42.88

Source: Company data, ING estimates

We believe the positive momentum for Bekaert's shares could continue, backed by these solid FY04 results. If we look at Bekaert's valuation multiples, we would prefer using an EV/EBITDA multiple rather than an adjusted PER, but this valuation multiple completely neglects the major impact of the contribution of the Latin American equity affiliates (32% of FY04's net profit). We restated Bekaert's EBITDA, EBIT and net debt so as to account for the JVs: For 04F, EBITDA comes in €105.5m higher, net debt is increased by €50m. This would lead to an adjusted EV/EBITDA for Bekaert on 2004, 2005F, 2006F and 2007F of, respectively, 4.5x, 4.6x, 4.4x and 4.1x. In terms of EV/EBIT, the adjusted multiples for these four years would come in at 7.1x, 7.6x, 7.3x and 6.8x. We therefore believe that Bekaert still has ample upwards potential, considering that 05F EV/EBITDA and EV/EBIT for Belgian small & Mid caps currently amounts to, respectively, 6.7x and 11.0x. Hence, we maintain our **BUY** rating.

Comments on financials

- The divestment of the Fencing division has a substantial impact on FY05's P&L, as this division accounted for €454m in sales as well as €52m in EBIT in FY04. The Fencing division was sold for an EV of €281.5m, thereby generating a capital gain of €56m.

Income statement (€m)

Yr to Dec	2004	2005F	2006F	2007F
Turnover	2,173.2	1,814.1	1,885.2	1,953.9
Total operating revenues	2,173.2	1,814.1	1,885.2	1,953.9
Costs of goods sold	(1,682.4)	(1,438.9)	(1,489.8)	(1,540.1)
Staff costs	(142.8)	(124.7)	(131.2)	(137.4)
Other operating costs	(31.3)	(11.0)	(11.0)	(12.0)
Depreciation	(125.9)	(110.8)	(115.7)	(118.4)
Amortisation of goodwill	(5.8)	0.0	0.0	0.0
Total operating costs	(305.7)	(246.5)	(257.9)	(267.7)
EBIT before exceptionals	185.1	128.7	137.5	146.1
EBITA	190.9	128.7	137.5	146.1
Operating profit	190.9	128.7	137.5	146.1
EBITDA	316.7	239.5	253.2	264.4
Income from associates (net)	53.6	49.0	47.8	48.8
Net interest income	(26.6)	(14.6)	(5.4)	(6.6)
Investment income	(4.0)	(4.0)	(5.3)	(5.4)
Net financial charges	(30.6)	(18.7)	(10.7)	(12.0)
Adj pre-tax profit	213.8	159.0	174.6	182.8
Exceptionals & GW	(5.8)	0.0	0.0	0.0
Pre-tax profit	208.1	159.0	174.6	182.8
Taxes	(28.1)	(28.6)	(36.1)	(38.2)
Extraordinary items (net)	0.0	56.0	0.0	0.0
Group profit	180.0	186.4	138.5	144.6
Minorities	(12.4)	(8.5)	(8.5)	(8.5)
Net profit	167.6	177.9	130.0	136.1
Net attributable profit	167.6	177.9	130.0	136.1
Adj net attributable profit	173.4	121.9	130.0	136.1
Net attributable profit from ordinary ops	167.6	121.9	130.0	136.1
Dividend on ordinary shares	(43.7)	(43.7)	(46.8)	(50.1)
Retained earnings	123.9	134.2	83.2	86.0

Source: Company data, ING estimates

Cash flow (€m)

Yr to Dec	2004	2005F	2006F	2007F
EBITDA (CF)	316.7	295.5	253.2	264.4
Change in working capital	(113.7)	86.5	(2.9)	(11.5)
Operating cash flow (pre-tax)	256.6	431.0	298.1	301.6
Cash taxes	(28.1)	(28.6)	(36.1)	(38.2)
Operating cash flow (after-tax)	228.5	402.4	262.0	263.4
Net financial charges	(30.6)	(18.7)	(10.7)	(12.0)
Capital expenditure (net of disposals)	(271.3)	(65.0)	(180.0)	(160.0)
Free cash flow	(73.3)	318.8	71.3	91.4

Source: Company data, ING estimates

Balance sheet (€m)

Yr to Dec	2004	2005F	2006F	2007F
Cash & cash equivalents	102.5	46.0	48.3	50.7
Inventories	419.3	326.5	329.9	341.9
Trade receivables	385.2	317.5	329.9	341.9
Other current operating assets	59.4	32.7	33.9	35.2
Total current assets	966.4	722.7	742.0	769.8
Goodwill	76.0	76.0	76.0	76.0
Other intangible assets	42.4	42.4	42.4	42.4
Tangible fixed assets	791.6	745.8	810.1	851.8
L/T investments	312.9	361.9	409.7	458.5
Total fixed assets and L/T investments	1,222.9	1,226.1	1,338.2	1,428.6
Total assets	2,189.3	1,948.8	2,080.3	2,198.4
S/T debt	314.4	59.9	82.5	89.0
S/T hybrid debt	0.0	0.0	0.0	0.0
Other current liabilities	202.5	188.9	197.6	206.4
L/T debt	246.7	128.7	128.7	128.7
L/T hybrid debt	0.0	0.0	0.0	0.0
L/T non-interest-bearing liabilities	216.4	162.4	162.4	162.4
Total liabilities	1,230.8	757.7	797.5	821.1
Minority interests (equity)	48.8	57.3	65.8	74.3
Shareholders equity	909.7	1,133.8	1,217.0	1,303.0
Total liabilities & group equity	2,189.3	1,948.8	2,080.3	2,198.4
Ratios (%)				
EBITDA margin	14.6	13.2	13.4	13.5
Operating margin	8.8	7.1	7.3	7.5
EBITDA growth	32.5	(24.4)	5.7	4.4
Operating profit growth	60.7	(32.6)	6.8	6.2
Adj tax rate	17.5	26.0	28.5	28.5
ROE	19.9	11.9	11.1	10.8
ROACE	13.3	9.5	9.2	9.1
Net debt/equity	47.8	12.0	12.7	12.1
Valuation (x)				
EV/turnover	0.9	0.9	0.8	0.8
EV/EBITDA	5.9	6.5	6.2	6.0
Adj PER	8.2	11.6	10.9	10.4
Price/NAV	1.6	1.3	1.2	1.1
P/FCFPS	(19.3)	4.5	19.9	15.5
Adj PEG	0.1	(0.4)	1.7	2.2
Dividend yield (%)	3.1	3.1	3.3	3.5

Source: Company data, ING estimates

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.70% of sales), which regroups 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 c.20% of sales, comprises end products and was divested at the beginning of 2005. It designs, develops, produces and markets woven and welded mesh products for 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.5% of sales.

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