

4Q07 trading update

Engineering & machinery

Belgium

Maintained

Bekaert

Buy

Earnings revision & preview 2H07 results

25/02/08

Maintained

Reuters: BEKB.BR

Price: €90.05

12-mth target: €108.00

- We have fine-tuned our forecasts following Bekaert's 4Q07 trading update and the on-site Investor day last week.
- Our EPS forecasts are raised for 2007F and beyond. We expect Bekaert to record a solid YoY improvement in 2H07F EBIT, which should, however, only lead to limited EPS growth if taxation in 2H07F returns to a normalised level. BUY recommendation and €108 target price maintained.

Bekaert posted strong 4Q07 sales (YoY +16% up to €585m), driven by strong organic growth of c.11%, a 7.9% increase due to changes in consolidation parameters, but held back by a c.3% negative impact due to currency exchange rates.

We fine-tune our forecasts for Bekaert, incorporating among other factors Bekaert's buyout in Beksa, the ongoing share buybacks (it has bought back 161,000 shares in 2008 so far) and Bekaert's higher capex plans for 2008F. The table below summarises our EPS revisions. Note that our EPS forecast for 2007F appears to be in line with JCF consensus, ie, to be c.3% lower for EPS 2008F and c.7% below JCF consensus for EPS 2009F.

Bekaert: Earnings revision

	2007F	2008F	2009F
New EPS (€)	7.04	7.20	7.55
Previous EPS (€)	6.84	7.17	7.08
Revision (in %)	3.1%	0.3%	6.7%

Source: ING estimates

We reiterate our BUY recommendation and our €108 target price (5% below our DCF value) on the company. Bekaert shares trade at a c.6% discount to the median for Belgian small & mid caps in terms of PER, adj. EV/EBIT and adj. EV/EBITDA 2007-09F (adjusted for the sizeable contribution of the Latin American equity affiliates), which is understandable in view of the cyclical nature of its business.

On the other hand, and from a longer-term perspective, we believe Bekaert's shares hold potential, in view of Bekaert's sound long-term strategy of building up, ahead of its competitors, a worldwide platform in growth areas such as China, Latin America, Central Europe, India and Russia, while also continuously streamlining its operations in mature markets. Besides this first-mover advantage, we believe Bekaert will remain a leading worldwide player thanks to its other fundamental strengths, ie, strong worldwide market shares, leading technology, focus on quality and a geographically well balanced manufacturing platform.

12-month forecast returns (%)

Share price	19.9
Dividend	3.0
12m f'cst total return	22.9

Forecasts and ratios

Yr to Dec (€m)	2006	2007F
Turnover	2,009.6	2,174.0
EBITDA	262.2	293.9
Net profit	142.3	139.7
Adj EPS (€)	6.80	7.04
Adj PER (x)	13.3	12.8
Dividend yield (%)	2.8	3.0
EV/EBITDA (x)	8.8	8.0
Price/NAV (x)	1.8	1.7
ROE (%)	13.2	13.2

Share data

No. of shares (m)	19.7
Daily turnover (shares)	39,646
Free float (%)	53.7
Enterprise value (€m)	2,409.8
Market cap (€m)	1,771.3

Share price performance



Source: ING

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4Q07 trading update

Bekaert's 4Q07 sales increased 16% to €585m, driven by strong organic growth of c.11%, a 7.9% increase due to changes in consolidation parameters but held back by a c.3% negative impact due to currency exchange rates.

At (sub) divisional level, the 4Q07's sales evolution highlighted:

- the decelerating YoY growth of steel cord in China (+c.25% YoY), which is logical as 4Q06 was a tough comparison basis.
- accelerating growth at its Latin American JVs (c.24% in 4Q07)
- much better-than-expected sales at wire North America (c.+4%) and for building products (c.+12%)

We consider Bekaert's 4Q07 sales as strong and we were in particular positively surprised by the resilience of sales in building products and of its US activities, certainly when considering the YoY c.12% weakening of the USD (compared to the Euro) in 4Q07.

Feedback from Bekaert's Investor Day

Bekaert organised an Investor's day on 22 February, during which it gave a strategic update and additional background information on its operations (eg, product development and capex).

Bekaert is buying out minorities in JV in emerging markets. In September 2007, Bekaert raised its stake in Vicson (Venezuela) to 100%. On 18 February 2007, Bekaert announced its intention to gain full ownership in the Turkish steel cord and Dramix manufacturer, Beksa (€60m annual sales, the remaining 50% stake is to be bought for c.€40m). Beksa was accounted for in Bekaert's accounts via minorities. As such, obtaining full ownership will not have an impact on Bekaert's top line moving forward. It is Bekaert's clear intention to further increase investments in such types of growth markets (ahead of the market growth so as to capture, or retain, its market share), which combined, account for more than half of Bekaert sales.

Bekaert invested c.€200m in 2007. Capex for 2008F will be of the same order of magnitude. Future investments will be directed to China (increasing capacity in steel cord from 250,000 tonnes pa to 300,000 tonnes pa by the end of 2008F (the Chinese steel cord market is growing by c.100,000 tonnes pa, and is currently estimated at 600,000 tonnes pa), Indonesia (€22m capex in 2008F, in galvanizing and concrete reinforcing products, this country can also become a substitute for exporting into the Asian region), Russia (€97m to be spread over five years, tire cord and bead wire), Turkey (through Beksa) and India (€33m). The latter represents a major long-term opportunity in steel cord, but this market is developing slower-than-expected in the wire products sector due to a lack of road infrastructure growth.

Due to this expansion plan, sales in Asia (mainly China) should exceed Bekaert's US exposure by the end of 2008F. Bekaert continues to streamline its capacities in the US and Western Europe. As Bekaert's clients are delocalising, Bekaert's growth in the Asian or LAM region should therefore more than offset the declining trend in Western European and the US markets.

Bekaert invests c.€60m annually in R&D to retain its technological leadership and to expand (and renew) its product portfolio. Several developments and projects were shown during our visit to Bekaert's Technology Centre in Deerlijk. Some examples being: steel-reinforced thermoplastic bumper beams (going into production in 2010) offering weight reduction, steel-reinforced strips for strengthening flexible high pressure pipes,

Focus remains fully oriented to growth markets

High capex level for 2007F and 2008F

Aligning capacities to its client's location

R&D to maintain competitive edge

biodegradable coatings, metal foam-based products used infiltration (eg. diesel particles filtration).

We consider Bekaert's investments as being regionally well allocated, so as to help sustain growth thanks to the exposure to emerging markets, but also as fitting well with Bekaert's core expertise in metal transformation and coatings.

Preview 2H07 results

Bekaert will publish 2H07 results on 14 March 2008, prior to the market opening.

The table below summarises our (slightly upward) revised forecasts for 2H07F.

Fig 1 Bekaert: Preview 2H07F results

	2H07F	YoY (%)	2H06
Sales (€m)	1108.9	10.9	1000.2
EBIT (€m)	87.4	32.4	66.0
as % of sales (%)	7.9		6.6
Equity affiliates (net) (€m)	21.9	-5.5	23.2
Taxes (€m)	-17.2	565.5	-2.6
Net profit (group share)	67.1	0.3	66.9
as % of sales (%)	6.0		6.7
Net EPS (€)	3.38	5.9	3.19

Source: Company data, ING estimates

We expect the company to record a slightly further YOY expanding gross margin, driven by good volumes sold (better capacity usage) and the continuing increase of the proportion of sales stemming from emerging markets, which should lead to a better product mix.

In line with 1H07, we expect the profit contribution from Bekaert's Latin American equity affiliates to declined YoY (-5.5% YoY), due to intensified price competition, albeit less pronounced as during 1H07 (-15.5% YoY).

Nomalised taxation in 2H07F would wipe out large part of YoY EBIT gain

At the EBIT level, we therefore anticipate on a major YoY increase in Bekaert's results (+32.4%), expanding Bekaert's EBIT margin by 128bp, up to 7.9%. At the bottom-line level, we believe the YoY advancement should be limited (+0.3%), as 2H06 benefited of an extremely low taxation rate (c.5%), whereas we anticipate on a (for Bekaert more normalised) 25.5% taxation rate for 2H07F. The company's had an active share buyback programme throughout 2007F (buying in 1.16m shares or 5.5% of the outstanding capital), which should result in lifting 2H07F EPS 5.9% higher, to €3.38.

We expect Bekaert's outlook statement at the FY07 results announcement to remain (vague and) unchanged. At the company's 4Q07 trading update publication, management expected 'continued growth of its activities in 2008' and that 'Bekaert will closely monitor the rising wire rod prices and the effects of any potential economic correction'. It is clear to us, that going forward, Bekaert will continue to face the key challenge of increasing steel (and wire rod) prices (as well as energy prices) and the consequent management of recovering these raw material costs in its selling prices, as there is uncertainty on the demand side in the current economic environment. However, steep price increases are often easier to recover than moderate, but steady, increases.

Company profile

Overview

Bekaert produces and markets a range of products based on metal-forming and coating technologies. Incorporated in 1880, it has evolved from a small manufacturing and trading company into a global group. Internationalisation began in the 1920s in Western Europe, then in Latin America and, since the 1970s, in North America and Asia. In January 2005, it divested its European fencing systems operations.

Advanced wire products

This is the company's main division (c.83% of 2006 sales), grouping together the 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).

Advanced materials

This division (c.7% of 2006 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 2006 sales.

Geographical breakdown of combined sales (2006)

Europe 32%, Latin America 35%, US 18%, Asia 13%, ROW 2%.

Risks

Bekaert's business model is sensitive to economic cycles (at a global level), to US\$ weakness (compared with the euro) and could suffer from raw material (wire rod) price increases when the economic climate weakens, as this would lower the company's pricing power.

Financials

Yr to Dec (€m)	2006	2007F	2008F	2009F
Income statement				
Turnover	2,009.6	2,174.0	2,339.6	2,460.6
EBITDA	262.2	293.9	317.8	332.5
Net financial charges	(31.7)	(36.5)	(34.3)	(33.6)
Operating exceptionals	0.0	0.0	0.0	0.0
Adj pre-tax profit	165.2	182.7	187.9	199.1
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	0.0	0.0	0.0	0.0
Pre-tax profit	165.2	182.7	187.9	199.1
Taxes	(18.1)	(32.1)	(36.5)	(40.4)
Extraordinary items (net)	0.0	0.0	0.0	0.0
Minorities	(4.8)	(10.9)	(9.8)	(10.1)
Preference dividend	0.0	0.0	0.0	0.0
Net profit	142.3	139.7	141.6	148.6
Balance sheet				
Total fixed assets and L/T investments	1,302.6	1,437.9	1,552.2	1,607.4
Working capital	409.4	424.2	454.1	472.2
L/T non-interest-bearing liabilities	175.6	175.6	175.6	175.6
Enterprise net assets	1,536.4	1,686.5	1,830.6	1,904.0
Group equity	1,121.3	1,107.3	1,192.1	1,295.7
Net debt	415.0	579.1	638.6	608.3
Capital employed	1,536.4	1,686.5	1,830.6	1,904.0
Cash flow				
Operating cash flow	312.6	323.2	326.6	352.1
Cash taxes	(18.1)	(32.1)	(36.5)	(40.4)
Net financial charges (CF)	(31.7)	(36.5)	(34.3)	(33.6)
Gross cash flow	262.8	254.6	255.8	278.1
Capital expenditures (net of disposals)	(252.6)	(210.0)	(210.0)	(155.0)
Free cash flow	10.2	44.6	45.8	123.1
Ratios (%)				
EBITDA margin	13.0	13.5	13.6	13.5
Operating margin	7.3	8.0	7.9	7.8
Net debt/equity	37.0	52.3	53.6	46.9
ROACE	9.6	9.3	8.5	8.5
ROE	13.2	13.2	13.0	12.7
Growth (%)				
Turnover	5.0	8.2	7.6	5.2
EBITDA	1.8	12.1	8.1	4.6
Net profit	4.9	(1.9)	1.3	4.9
Valuation				
EV/EBITDA (x)	8.8	8.0	7.6	7.2
Adj EPS	6.80	7.04	7.20	7.55
Adj PER (x)	13.3	12.8	12.5	11.9
Price/NAV (x)	1.8	1.7	1.6	1.5
DPS	2.50	2.70	2.70	2.80
Dividend yield (%)	2.8	3.0	3.0	3.1

Source: Company data, ING estimates

Disclosures Appendix

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PRICE & RATINGS HISTORY TO 04/02/08: BEKAERT (BEKB.BR)



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