

## Engineering &amp; machinery

Belgium

Previously: Hold

## Bekaert

Buy

## Upgrade to BUY after 3Q09 trading update

13/11/09

Previously: €90

Reuters: BEKB.BR

Price: €95.04

12-mth target: €112.00

- **Bekaert's focus on emerging markets and innovative products proved to be crucial to get through the crisis. With the company suggesting the trend is improving, we upgrade our 2009 and 2010 EPS estimates by c. 5.0%. We also increase our TP by 24.0% to €112.0, targeting 13.0x 2010F PER, which still seems cautious versus Benelux cyclicals, which currently trade on 15x 2010F on consensus estimates. We upgrade from HOLD to BUY.**

**Supportive 3Q09 trading update.** As expected, 3Q09 consolidated sales improved 2% QoQ to €619m. The increase was due mainly to higher market demand in Asia Pacific, where sales increased by a higher than anticipated 10% QoQ to €228m. Sales in Latin America were also up 10% QoQ to €87m, as expected, due to the first time consolidation of Prodac and Ideal Alambrec. Sales in North America and EMEA declined more than expected by 13% and 1% respectively QoQ. Bekaert reported very healthy cash flow generation and reduced net debt to €500m, versus €622m at the end of 1H09, and versus our previous estimate of net debt of €567m by year-end 2009.

**Improving outlook.** Bekaert signalled that the trend is gradually improving in automotive, repeated that the crisis is impacting sales in construction and said that the company continued to perform well in the energy and mining sectors. For 4Q09F, sales will continue to be impacted by a c. 35% decline in raw material prices and the negative impact from the strong euro, but Bekaert is guiding for 4Q09 sales in line with previous quarters, driven by strong demand.

**Change in estimates.** We have increased our 2009 and 2010 Adj. EPS estimates by c. 5% to €6.56 and €8.66 respectively, driven by a slight margin increase (geographical split has positive impact on REBIT) and lower net financing charges, after revising down our net debt assumption to €488m at the end of 2009. We regard our 2010 estimates as cautious, since our FY10 sales estimate is equal to 4x 3Q09 sales plus 1.5% (ie, inflation), while our EBIT margin assumptions are close to the level reported in 1H09, excluding the €40m negative FIFO impact on inventories.

**Rating upgrade from HOLD to BUY.** On our new estimates, Bekaert is trading at 11x Adj. PER 2010F, and 12x on consensus estimates. This implies that even on consensus estimates, Bekaert is now trading at a 19% discount to the median valuation for Benelux cyclicals, which trade at 15x (according to Factset). This discount has never been higher in the past 10 years and seems unjustified to us, given Bekaert's focus on (higher-growth) emerging markets (51% of 3Q09 sales) and innovative product portfolio (Bekaert invests c. 3% of sales in R&D). We increase our target multiple from 11x to 13x 2010F Adj. PER (and not 15x, since we consider the latter a peak multiple) and upgrade our target price to €112. We upgrade our rating from HOLD to BUY.

## 12-month forecast returns (%)

Share price	17.8
Dividend	2.9
12m f'cst total return	20.8

## Forecasts and ratios

Yr to Dec (€m)	2008	2009F
Turnover	2,663.0	2,437.8
EBITDA	461.2	346.0
Net profit	174.1	108.5
Adj EPS (€)	11.58	6.56
Adj PER (x)	8.2	14.5
Dividend yield (%)	2.9	2.9
EV/EBITDA (x)	5.6	6.9
Price/NAV (x)	1.7	1.6
ROE (%)	15.6	9.4

## Share data

No. of shares (m)	19.7
Daily turnover (shares)	99,077
Free float (%)	60.9
Enterprise value (€m)	2,404.5
Market cap (€m)	1,875.0

## Share price performance



Source: ING

Filip De Pauw

Brussels (32 2) 547 6097

filip.de.pauw@ing.be

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SEE THE DISCLOSURES APPENDIX FOR IMPORTANT DISCLOSURES AND ANALYST CERTIFICATION

## Supportive 3Q09 trading update

**Fig 1 Bekaert quarterly sales 2009**

	1Q09	2Q09	3Q09	Q3-Q2
EMEA	210	200	198	-1.0%
North America	142	122	106	-13.1%
Latin America	81	79	87	10.1%
Asia Pacific	159	207	228	10.1%
<b>Total</b>	<b>592</b>	<b>608</b>	<b>619</b>	<b>1.8%</b>

Source: Company data

As expected, 3Q09 consolidated sales improved 2% QoQ to €619m. The increase was due mainly to higher market demand in Asia Pacific, where sales increased by a higher than anticipated 10% QoQ to €228m. Sales in Latin America were also up 10% QoQ to €87m, as expected, due to the first time consolidation of Prodac and Ideal Alambrec. Sales in North America and EMEA declined more than expected by 13% and 1% QoQ respectively. Bekaert reported very healthy cash flow generation and reduced net debt to €500m, versus €622m at the end of 1H09, and versus our previous estimate of net debt of €567m by year-end 2009.

## Improving outlook

Bekaert signalled that the trend is gradually improving in automotive, repeated that the crisis is impacting sales in construction and stated that the company continued to perform well in the energy and mining sectors. For 4Q09F, sales will continue to be impacted by a c. 35% decline in raw material prices and the negative impact from the strong euro, but Bekaert is guiding for 4Q09 sales in line with previous quarters, driven by strong demand.

## Changes to estimates

**Fig 2 Changes to key estimates**

(€m)	2009F		% ch	2010F		% ch	2011F		% ch
	old	new		old	new		old	new	
<b>Consolidated sales</b>	2,438.1	2,437.8	0.0	2,499.0	2,513.1	0.6	2,624.0	2,663.9	1.5
<b>REBIT</b>	193.4	201.0	3.9	244.3	244.0	-0.1	265.7	272.0	2.4
REBIT margin (%)	7.9	8.2		9.8	9.7		10.1	10.2	
<b>Non-recurring</b>	(20.0)	(20.0)	0.2	(15.0)	(15.0)	0.0	(15.0)	(15.0)	0.0
<b>EBIT</b>	173.4	181.0	4.4	229.3	229.0	-0.1	250.7	257.0	2.5
EBIT margin (%)	7.1	7.4		9.2	9.1		9.6	9.6	
<b>Net financing charges</b>	(59.0)	(58.3)	-1.2	(53.7)	(45.2)	-15.8	(47.9)	(39.7)	-17.1
<b>Taxes</b>	(31.1)	(32.9)	5.9	(44.8)	(46.7)	4.3	(54.4)	(58.1)	6.8
<b>Share in the JVs</b>	35.4	35.4	0.1	36.8	37.8	2.7	38.6	40.1	3.9
<b>Minorities</b>	(16.7)	(16.7)	-0.1	(19.0)	(19.0)	0.0	(20.0)	(20.0)	0.0
<b>Net profit</b>	102.1	108.5	6.3	148.6	155.9	4.9	167.0	179.3	7.4
<b>EPS (€)</b>	5.18	5.50	6.2	7.53	7.90	4.9	8.46	9.09	7.4
<b>Adj. EPS (€)</b>	6.23	6.56	5.2	8.29	8.66	4.5	9.22	9.85	6.8

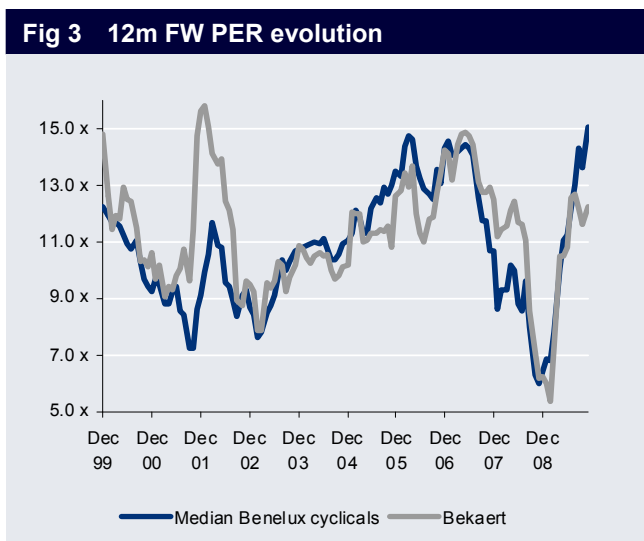
Source: Company data, ING estimates

We have increased our 2009 and 2010 Adj. EPS estimates by c. 5% to €6.56 and €8.66 respectively, driven by a slight margin increase (geographical split has positive impact on REBIT) and lower net financing charges, after revising down our net debt

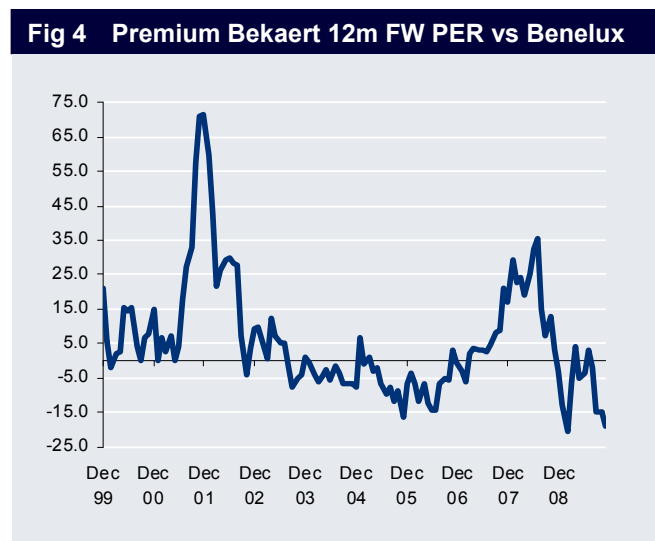
assumption to €488m at the end of 2009. We regard our 2010 estimates as cautious, since our FY10 sales estimates are equal to 4x 3Q09 sales plus 1.5% (ie, inflation), while our EBIT margin assumptions are close to the margins reported in 1H09, excluding the €40m negative FIFO impact on inventories.

### Valuation

On our new estimates, Bekaert is trading at 11x Adj. PER 2011F, and 12x on consensus estimates. This implies that even on consensus estimates, Bekaert is now trading at a 19% discount to the median valuation for Benelux cyclicals, which trade at 15x (according to Factset). This discount has never been higher in the past 10 years and seems unjustified to us, given Bekaert's focus on (higher-growth) emerging markets (51% of 3Q09 sales) and innovative product portfolio (Bekaert invests c. 3% of sales in R&D). We increase our target multiple from 11x to 13x 2010F Adj. PER (and not 15x, since we consider the latter a peak multiple) and upgrade our target price to €112. We upgrade our rating from HOLD to BUY.



Source: Factset



Source: Factset

## Company profile

### Overview

Bekaert is an international group, headquartered in Belgium. Core competencies are advanced metal transformation, advanced materials and coatings. This unique combination is the company's key strength. Bekaert's basic raw material is wire rod steel wire about the thickness of a finger, which it converts by mechanical deformation and heat treatment into wires that can be as fine as one-50th of the thickness of a human hair. These wires are then turned into cable and cord, woven or knitted into cloth, or processed into ultra-fine filters and fibres, for a wide range of industrial applications in virtually all sectors of the economy but mainly in the automotive (31% of sales), infrastructure (23%) and utilities (16%) sectors.

### Key numbers

Bekaert recorded 2008 combined sales (ie, sales of consolidated companies +100% of sales of joint ventures and associates after intercompany elimination) of €4.0bn and a net result of €174.1m. The company employs c.23,000 people and is organised into three business segments: advanced wire products (98.5% of REBIT); advanced materials; and advanced coatings.

### Geographical breakdown of combined sales (2008)

Latin America 38%, Europe 27%, Asia 19%, US 15%, ROW 1%.

### Risks

**Raw material price risk:** during 2008, Bekaert was able to pass on higher raw material prices. We would not rule out the possibility of Bekaert facing difficulties if raw material prices increase during the economic downturn. That said, raw material prices and the economy tend to move in the same direction.

**Exchange rate risk:** Bekaert has important sales and production facilities outside Europe and therefore has a natural currency hedge. Still, the company faces translation risk, which is not hedged.

**The need to streamline operations:** since 2002, Bekaert has been constantly downsizing operations in mature markets and investing in emerging markets. The company is expected to continue to do so for the foreseeable future. As the latter entails restructuring charges, we expect the company to report €15m in non-recurring charges on an annual basis.

## Financials

Yr to Dec (€m)	2008	2009F	2010F	2011F
<b>Income statement</b>				
Turnover	2,663.0	2,437.8	2,513.1	2,663.9
EBITDA	461.2	346.0	389.0	417.0
Net financial charges	(49.2)	(58.3)	(45.2)	(39.7)
Operating exceptionals	0.0	0.0	0.0	0.0
Adj pre-tax profit	301.1	178.1	236.6	272.4
Corporate exceptionals	(83.8)	(20.0)	(15.0)	(15.0)
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	217.3	158.1	221.6	257.4
Taxes	(25.5)	(32.9)	(46.7)	(58.1)
Extraordinary items (net)	0.0	0.0	0.0	0.0
Minorities	(17.7)	(16.7)	(19.0)	(20.0)
Preference dividend	0.0	0.0	0.0	0.0
Net profit	174.1	108.5	155.9	179.3
<b>Balance sheet</b>				
Total fixed assets and L/T investments	1,534.0	1,549.0	1,564.0	1,579.0
Working capital	739.9	609.5	653.4	692.6
L/T non-interest-bearing liabilities	445.1	445.1	445.1	445.1
Enterprise net assets	1,828.8	1,713.4	1,772.3	1,826.5
Group equity	1,172.3	1,225.6	1,322.3	1,438.5
Net debt	656.5	487.8	450.0	387.0
Capital employed	1,828.8	1,713.4	1,772.3	1,825.5
<b>Cash flow</b>				
Operating cash flow	312.8	476.5	345.1	377.8
Cash taxes	(25.5)	(32.9)	(46.7)	(58.1)
Net financial charges (CF)	(49.2)	(58.3)	(45.2)	(39.7)
Gross cash flow	238.0	385.2	253.1	280.0
Capital expenditures (net of disposals)	(295.2)	(160.0)	(160.0)	(160.0)
Free cash flow	(57.2)	225.2	93.1	120.0
<b>Ratios (%)</b>				
EBITDA margin	17.3	14.2	15.5	15.7
Operating margin	11.0	8.2	9.7	10.2
Net debt/equity	56.0	39.8	34.0	26.9
ROACE	15.3	9.8	11.6	12.5
ROE	15.6	9.4	12.7	13.4
<b>Growth (%)</b>				
Turnover	22.5	(8.5)	3.1	6.0
EBITDA	50.7	(25.0)	12.4	7.2
Net profit	13.9	(37.7)	43.7	15.0
<b>Valuation</b>				
EV/EBITDA (x)	5.6	6.9	6.1	5.5
Adj EPS	11.58	6.56	8.66	9.85
Adj PER (x)	8.2	14.5	11.0	9.6
Price/NAV (x)	1.7	1.6	1.5	1.3
DPS	2.80	2.80	3.00	3.20
Dividend yield (%)	2.9	2.9	3.2	3.4

Source: Company data, ING estimates

# Disclosures Appendix

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Buy	39%	32%
Hold	46%	34%
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	<b>100%</b>	

\* Percentage of companies in each rating category that are Investment Banking clients of ING Financial Markets LLC or an affiliate.

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Total return: forecast share price appreciation to target price plus forecast annual dividend. Price volatility and our preference for not changing recommendations too frequently means forecast returns may fall outside of the above ranges at times.

**PRICE & RATINGS HISTORY TO 04/11/09: BEKAERT (BEKB.BR)**



B = Buy; H = Hold; S = Sell; NR = Not Rated; R = Restricted

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 Where ING coverage is longer than three years, chart shows recommendation current at start of the share price history

Source: ING

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