KBC Securities

Bekaert

20 May 2003

Back to the roots

Engineering & Machinery

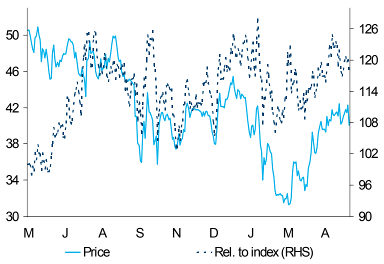
Belgium

Current price € 40.05

Target price € 45.00

Accumulate

Rating unchanged



Source: Thomson Financial Datastream

FY/e 31.12	2002	2003E	2004E	2005E
Sales (€ m)	1,863	1,785	1,888	1,972
EBITDA (€ m)	209	255	267	276
Pre-Tax* (€ m)	42	86	108	119
Adj EPS* (€)	-1.55	4.13	4.78	5.09
EPS (€)	-2.24	3.85	4.28	4.59
DPS (€)	1.68	1.75	1.95	1.90
P/E* (x)	-	9.7	8.4	7.9
Yield (%)	4.2	4.4	4.9	4.7
EV/EBITDA (x)	6.3	4.9	4.7	4.4

Source: KBC Securities **Adjusted for goodwill and exceptionals*

Reuters	BERTt.BR
Bloomberg	BEKB BB

www.bekaert.com

Market Cap	€ 893m
Shares outst.	22.3m
Volume (daily)	€ 0.92m
Free float	60%

Next corporate event

Payment dividend FY02 on 21 May 2003

Performance over	1m	3m	12m
Absolute	1%	9%	-21%
Rel. BEL20	1%	3%	18%
Rel. sector	3%	14%	15%
12-m Hi/Lo	€ 50.90/31.30		

Wouter Vanderhaeghen +32 2 417 29 62

wouter.vanderhaeghen@kbcsecurities.be

Bekaert is an international group with its core competencies in metal transformation and coating technologies.

Bekaert closed 2002 with a net loss of € 49.5m. However, excluding the € 144m non-recurring charges, the group realised an impressive operating improvement. Operating margin, before restructuring, stood at 6.6%, illustrating the improved product mix following an increased weight of the BAM and optimisation measures paying off.

- Sales over the 1Q03 declined by 7.2%, but would have increased by 2.2% at constant exchange rates. Although no precise figures were given in the quarterly update, all units seem to have increased their contribution to the operational and bottom line result. This despite the lower USD, illustrating an impressive improvement of the underlying profitability.
- Despite what seems to be an excellent 1Q (exceeding "internal budget"), Bekaert remained very prudent not disclosing any guidance. However, without major optimisation charges and losses on the solar cells, Bekaert could post a spectacular improvement in results. We count on a 'reported' EPS 03 of € 3.85, up from € -2.24.
- As Bekaert disposed its solar cell interests for $ 6m to ECD, the bulk of the € 84m "impairment" taken in 2002 is lost. The pill has been swallowed but is bitterer than expected. We welcome the new focus on international expansion in the core business and less aggressive growth in the BAM.
- The average of our valuation models used, points towards a theoretical fair value of € 47.6 per share for Bekaert. We have set our price target at € 45, which still leaves some upward potential. However, since the bottom at € 31 in March, much of the trading potential has gone.

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Investment opinion

Bekaert is an international group with its core competencies in metal transformation and coating technologies. Bekaert ranks as the world's largest independent steel wire and steel cord manufacturer. In steel cord, the group holds a worldwide leadership position next to (partially) integrated tyre manufacturers such as Michelin, Bridgestone and Goodyear. Furthermore, it is involved in "advanced materials" such as thin metal fibres, composite materials and sputtered films. The group's main business units are Wire, Fencing, Steel Cord and Advanced Materials.

A more controlled growth of the BAM…

In order to earn a return above its cost of capital and lever the growth potential of its business, Bekaert has followed an ambitious renewal and optimisation process for years. Before the recent management change, this strategy was most visible through a drastic shifting from its lower growth, traditional business (Steel Wire, Bekaert Fencing, Steel Cord) towards its high growth, high margin Advanced Materials (BAM) which were to account for about one third of sales by 2010. However, this strategy was not without any risk as is illustrated by the € 84m "impairment" taken on the solar cell business in 2002 and disposal at $ 6m in 2003.

…together with further optimisation efforts at the traditional business…

As part of Bekaert's ambition to increase the EBIT margins of the traditional business (historical average of about 5%), selective divestments of certain low growth and low margin commodity oriented businesses are not to be excluded. In 2002, Bekaert recorded € 60m of restructuring charges, the majority of which related to the extensive optimisation program at Bekaert Fencing.

…and a geographic expansion of the core business…

In terms of future expansion, Bekaert is now focusing much more on growth regions in the world where it should be able to commercialise its (existing) products as it already does in Europe and North America, without taking extra technological/commercial risks. Eastern Europe and Asia in particular are two regions where the group will expand in the foreseeable future. Anyhow, we find this part of the expansion strategy (apart from the fact that the group will keep growing in Advanced Materials too) credible.

… are to further improve the product mix

While Bekaert's profitability is still too low, with a return on invested capital slightly below the weighted average cost of capital, the strategy pays-off. Although posting a € 49.5m loss, Bekaert observed a spectacular operating improvement in 2002 with the operating result, before restructuring, up 70% to € 123.8m or an operating margin at 6.6% compared to 4.1%. This, in a still very challenging economic environment! These improvements can be explained by the improved product mix with the higher margin BAM, increase in weight (generating 11.3% of 2002 sales), leveraging the overall margins, but also by an improved profitability of the 'traditional' business, which should not be underestimated. On the assumption that the operating margin reaches 10% at the BAM, we estimate the margin of the 'traditional' business to have improved from 3.5% to 6.2% over 2002.

Sales over the 1Q03 declined by 7.2% but would have increased by 2.2% at constant exchange rates. Although no precise figures were given in the quarterly update, all units seem to have increased their contribution to the operational and bottom line result. This, despite the lower US dollar, illustrating an impressive improvement of the underlying profitability. Especially Steel Cord and the equity consolidated activities in Latin America performed very well. Sales of Fencing were flat but due to an improved mix increased their profitability. At the other hand, trading in wire was much weaker.

Bekaert prudent for 2003: no targets released

Despite the good 1Q and the promising order book (up more than 10% y-o-y), Bekaert remains very prudent for the rest of the year, without giving any outlook. However, in the absence of major optimisation charges and losses at the solar cells and given lower financial charges, we expect Bekaert to turn the € 49.5m loss observed over 2002 into a € 85.3m (3.85 per share) net profit, group share.

In our valuation of Bekaert, we assumed an average sales growth of 2.7%. This can be split into a 2% CAGR for the traditional business (1.4% for wire & fencing and 2.9% for Steel Cord) and 10.2% for the Advanced Materials. At the end of the projected period, BAM accounts for 20.5% of total sales. Due to an improving product mix, following the further increased weight of the higher margin Advanced Materials and Steel Cord business, and optimisations at the Wire and Fencing business, we are counting on an operating margin of 7.4% by 2010. This is based upon a margin of 11% for the BAM and 6.5% for the traditional business.

Price target at € 45

The average of our valuation models used, points towards a theoretical fair value of € 47.6 per share for Bekaert. We have set our price target at € 45, which still leaves some upwards potential. However, since the bottom at € 31 in March, most of the trading potential has gone and we do not see Bekaert substantially outperforming the Belgian market within the coming 12 months. Our target price implies a premium of close to 20% towards the BV, end 2002, and as such illustrates our confidence in Bekaert's strategy, which aims to earn a ROCE throughout the cycle above the WACC.

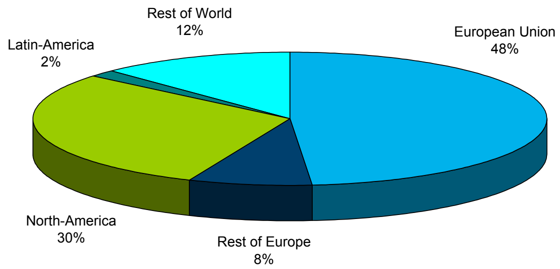
Strengths	Weaknesses
• Leading market positions • Improving product mix and profitability • Technological edge • Strong balance sheet and CF • Determined to innovate and change the business • Ready to restructure or divest if growth and margins unsatisfactory	• ROCE of current mix insufficient to cover WACC • Substantial part (55%) of business derived from lower growth, lower margin business (wire & fencing) • Visibility (no operating segmental information) • Track record in external growth (~Unisolar)
Opportunities	**Threats**
• Enhance margins by upgrading the product mix • Benefit from an economic upswing as early cyclical • Growth opportunities in China and Eastern Europe • New management	• Acquisition risk • Threat of substitution product for steel cord • Pressure on margins • USD exposure

Company description

Core business in metal transformation and coating technologies

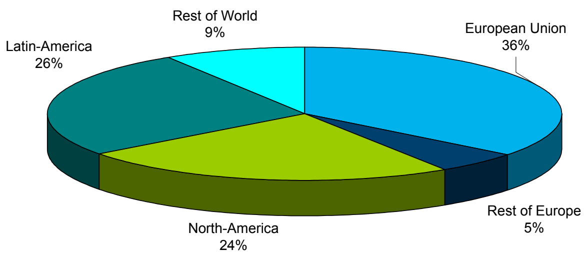
Bekaert produces and markets a wide range of products based on metal transformation and coating technologies. The group's activities are built around four business units: Wire, Fencing, Steel Cord and the Bekaert Advanced Materials (BAM). The group has grown from a small manufacturing and trading company, founded in 1880, into a global player. Starting in Western Europe, the group moved towards North America and Latin America and has been expanding rapidly in Asia in recent years. Much of the group's growth has been built on steel cord for radial tyre reinforcement. Bekaert now has 96 production centres in 29 countries and an extensive network of sales offices and agencies. In 2002, Bekaert generated sales in excess of € 1.8bn. and employed 16,077 people. Adding Bekaert's participating interests (mainly Wire activities in Latin America), 'combined sales' amounted to about € 2.8bn. While the EU accounts for about 50% of the consolidated sales, combined sales better reflects Bekaert's regional exposure with Latin America accounting for 26,3% (vs. only 1.6% of consolidated sales). On a longer-term perspective, Bekaert would like to have a more balanced geographical presence with Europe, Asia, Latin- and North America each accounting for about ¼.

2002 consolidated sales breakdown by region



Source: Bekaert

2002 combined sales breakdown by region



Source: Bekaert

Bekaert aims to earn a ROCE above the WACC over the cycle

Bekaert has committed itself to a process of strategic renewal based on its core competencies. The group is evolving from a volume-driven producer into a manufacturer of higher-margin products offering greater added value. Bekaert's strategy is to focus on selected international market segments with high inherent growth potential and to move closer to the end-user. The aim is to increase shareholder value (earn a ROCE above the WACC over the cycle) and secure sustainable and profitable growth.

Strategy

Determined to innovate and change the business

Over the past years, Bekaert made considerable efforts to improve its growth potential and margins, evolving from a volume-driven manufacturer into a technology-driven business, making products with higher added value and higher margins. Its core competences are metal transformation and a range of coating technologies. Profitable growth is being achieved by shifting the emphasis increasingly towards finished products instead of semi-manufactures (e.g. burners employing fine metal fibres).

In pursuit of its profitability goals, Bekaert also focuses on markets with growth potential, such as renewable energy, clean water, clean air and electronics. Examples include fine metal-fibre filters for removing contaminants from liquids and air (such as particulate filters for diesel engines), special films for computer touch-screens, special films for printed circuits to support further miniaturisation in the electronics industry and products used in seawater desalination by reverse osmosis.

Bekaert is currently engaged in a twin-track renewal process:

- By maintaining existing business in top form through high efficiency and continuous product innovation.
- By developing new markets/business.

Ready to optimise or divest if growth and margins unsatisfactory

Via the first track, Bekaert intends to keep its existing activities in peak condition. As part of the ambition to increase EBIT margins of the traditional business (historical average of about 5%) selective divestments of certain low growth and low margin commodity oriented businesses are not excluded. In addition, optimisation programmes are to lower the break-even point, further optimising cash-flows, which can then serve to finance new applications or expansion in new regions (e.g. growth in Asia and Eastern Europe).

New management focuses less on aggressive expansion of the BAM …

The second track addresses to the development of new regions and brand-new activities, both in-house and by acquisition. Until recently, this strategy existed mainly from shifting from its lower growth, traditional business towards its high growth, high margin, Advanced Materials (BAM). The most visible examples include United Solar Systems in 2000 and Bekaert Speciality Films in 2001. However, the painful exit from the solar cell business illustrates that this was not without any risk.

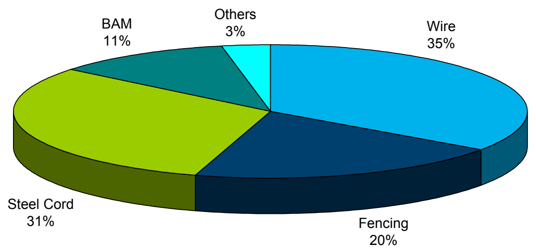
… and more on growth in Asia and Eastern Europe

In terms of future expansion, the new management is now focusing much more on growth regions in the world where Bekaert should be able to commercialise its (existing) products as it already does in Europe and North America. Eastern Europe and Asia in particular are two regions where the group will expand in the foreseeable future. Over the period 2003-05, Bekaert will invest € 180m – € 200m in China to keep up with the growth of the Chinese steel cord market.

Sharp criteria

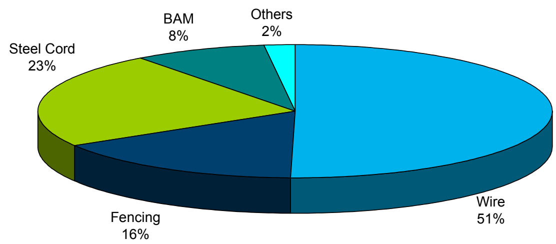
Bekaert has set some sharp criteria: the growth of the addressed markets must be in excess of 10% and allow for a leadership position. The applications targeted by these new activities must also be compatible with Bekaert's core competencies, hence based on metal transformation and coating technologies. With regard to the profitability, the businesses must observe high margins with EBITDA margins in excess of 20% and EBIT margins above 15%.

2002 consolidated sales by activity



Source: Bekaert

2002 combined sales by activity



Source: Bekaert

An analysis of the 2002 sales per activity illustrated the high growth BAM increasing its weight, accounting for 11.3% and 8.4% of the consolidated and combined sales, compared to respectively 8.6% and 6.6% in 2001. The vast bulk remains the low (no) growth Wire and Fencing business generating respectively 34.6% and 20.0% of the consolidated sales and 50.2% and 16.2% of the combined sales. Bekaert's cash cow, the Steel Cord business, accounted for 31.1% of the consolidated sales. With respect to its exposure, Bekaert's most important markets are the automotive (steel cord) and building (Dramix, fencing, window coatings, etc.) markets.

Wire

Most important business in terms of sales

The Wire business accounts for respectively 34.6% and 50.2% of the consolidated and combined 2002 sales. With the exception of high carbon specialties, most sectors were affected by the economic downturn. Especially 'Cable Solutions' had a weak 2002 due to the persistent crisis in telecommunication. Consolidated sales remained stable at € 674m, while combined sales decreased by 2.2% to € 1,457m. The business can be split up between global and regional businesses.

Global businesses:

These activities can be split in four business units:

- **Cable solutions**
  Solutions for the protection and support of power transmission and telecommunications cables used in niche markets. The product range includes reinforcement of optical-fibre cables and armouring wire for undersea cables. The exposure is mainly to the telecom and energy markets.

- **High-carbon specialities**
  Products for selected segments around the world, chiefly in the automotive and offshore oil production sectors. The products include industrial spring wire, flexible hose reinforcement wire, plastic-coated specialities, textile machine wire and profiled wire.

- **Low-carbon specialities**
  Products for global clients, offering individual customer service and process technology, including bookbinding wire, weaving wire, champagne cork wire and various types of lacquered and nylon coated wire. As a consequence of the poor profitability (loss making), Bekaert decided in April 2002 to stop all production and sales of the preformed staple wire in Europe.

- **Building products**
  Products for use in the building industry. The product range includes steel fibres for concrete reinforcement (Dramix) and road reinforcement products.

Regional business:

The other wire products (with mostly lower (no) growth and margins) are handled by the regional businesses for Europe, North America, Latin America and Asia. It mostly concerns commodity products like galvanised wire. As part of Bekaert's strategy to increase the growth and margins of the traditional business, selective divestments are not to be excluded.

Bekaert Fencing

Bekaert Fencing, the former 'Merchant Products Europe', generated respectively 20.0% and 16.2% of the consolidated and combined 2002 sales. The business unit designs, develops, produces and markets woven and welded mesh products for:

- the garden and agricultural markets,
- security fencing systems,
- products for industrial applications and
- material handling systems (50/50 JV).

The product range includes complete garden and industrial fencing systems, posts and gates and other products such as glass reinforcement mesh. While the garden market observes almost no growth and the agricultural market even is in decline, growth of the professional fencing systems and security systems can be estimated at about 5% a year.

Optimisation plan to structural increase cash-flow by € 15m

Proving determined to increase the overall margins, Bekaert announced in July 2002 an extensive optimisation program for the Merchant Products, which have been rationalised and set up as a separate legal entity. The plan resulted in the closure of 3 out of the 14 production units and a headcount reduction of approximately 20% (about 455 persons) of the BU's workforce. The one-off cost amounted to € 34m, of which € 8m fixed assets write-offs. Bekaert estimates the structural optimisation of cash flow at € 15m.

Bekaert mentions the performance of the Handling division as unsatisfactory, being on top of the agenda. As such, a disposal or a rationalisation programme for the handling systems JV is not to be excluded in the near future.

Steel Cord

The second most important unit in terms of sales is the steel cord business, generating respectively 31.1% and 23.3% of 2002 consolidated and combined sales. The BU develops, produces and markets steel cord products for polymer reinforcement worldwide. Tyre cord and bead wire (estimated to generate more than 85% of the steel cord sales) are used for reinforcement of truck and car tyres. The product range also includes high-pressure hose reinforcement wire, conveyor belt cord, woven steel cord, fine cord for transmission belts and sawing wire.

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Tyre cord

Largest independent tyre cord manufacturer

Bekaert is the world's largest independent tyre cord (used for reinforcement of radial tyres) producer with a market share of around 20% (est. production of about 260,000 tons). The biggest competition in this segment comes from the tyre manufacturers themselves, which integrated (to a certain extent) steel cord production in their production chain. The market is currently estimated at 1.2 m tons with integrated tyre manufacturers accounting for about 40% of this volume. Bekaert could gain market share as integrated producers push the integration back by concentrating on their core business and outsourcing the production of steel cord. Note that in down cycle periods, the independent producer is most vulnerable as integrated players tend to fall back as much as possible on their own production capacity.

Although a cyclical business, depending on the global economic environment (automotive), cyclicity is somehow 'softened' as the replacement market roughly represents about 70-80% of demand for steel cord for the car and truck segments. With radial penetration of tyres saturated in the industrial countries, Bekaert will have to focus on developing countries where the increase in new highways and roads are expected to boost tire radialisation. For the next years, Bekaert expects its steel cord sales to grow with about 2-3% p.a.

Aggressive expansion in China

It is clear that growth will have to come from new markets. It is in this context that Bekaert started new steel cord plants in India and Slovakia. In China, Bekaert is currently present through 2 JV's (90% Bekaert) with an estimated capacity of about 45,000 tons, or more than 40% of the market. Since 1997, the Chinese steel cord market increased on average by 25% per year and is expected to double in the coming 3 to 4 years. Bekaert targets at least to consolidate this market share by keeping up with the market growth and even expanding its market share to 50%. Over 2003-05, Bekaert will invest about € 180-200m in China bringing its capacity in steel cord at about 100,000 tons. By 2005, the capacity at the two existing plants will have increased to 80-90,000 tons and, in addition, a third plant will come on stream with an initial capacity of 10,000 tons. In Latin America, the group holds with an annual production of about 30,000 tons more than 40% of a market, which is expected to grow by about 5% p.a. for the next years.

Double-digit operating margin?

Bekaert does not yet supply operating segmental information for commercial reasons. This could be explained by the realisation of much higher margins in this concentrated niche market, in comparison with its steel wire and fencing activities. We estimate the 6.6% operating margin -before restructuring-, observed over 2002, to be build up as follows: a 10% margin for the BAM and 6.2% for the 'traditional' business (11% for steel cord and 3.3% for wire & fencing).

Bekaert Advanced Material (BAM)

Advanced Materials: "new" activities with higher growth profile and margins in Bekaert's core competencies

After consolidation of BSF (Specialty Films), the BAM now accounts for 11.3% of Bekaert's consolidated sales. The business unit develops, manufactures and markets innovative industrial products that combine Bekaert's core skills with new technologies. These products are used in such areas as filtration, electromagnetic screening, electrostatic dissipation, flexible electrical circuit boards, theft prevention, seawater desalination, energy saving and health care. Many are designed to meet the growing demands imposed by environmental protection and health and safety standards or to fulfil the requirements of growth sectors such as telecommunications, information technology and clean energy.

BAM can be divided into three sub-units: Metal Transformation, Coating Technologies and Composites:

Metal transformation

- **Bekaert Fibre Technologies**
  Manufactures fine fibres in a range of metal alloys, mainly stainless steel, and products incorporating metal fibres in various forms.
- **Bekaert Combustion Technology**
  Products mainly based on metal fibre technology and metal fibre media for environmental friendly gas burners.

Coating technologies

- **Bekaert Advanced Coatings**
  Coatings applied to various materials by vacuum techniques or thermal spraying, including diamond-like coatings.
- **Bekaert Specialised Films**
  Coatings applied by sputtering or by a wet-coating process whereby a plastic film is coated with a liquid chemical.

Composites

Glass-fibre reinforced plastic products employing various technologies for a wide range of applications in the transport and other sectors, in corrosive environments and in seawater desalination.

Metal transformation

Bekaert Fibre Technologies (BFT) develops, manufactures and markets very thin metal fibres and metal fibre based products. BFT is today the largest manufacturer of metal fibres in the world with production facilities in Belgium, Japan and the USA. These metal fibres are up to 60 times thinner than human hair and are available in various alloys. By using the metallic and fibre-like nature of metal fibres, unique products have been and are being developed. The most important applications are Porous Media, Filter Elements, Conductive Plastics, Heat-Resistant and Electro-Conductive Textiles, Airbag and Burner Pads:

- Porous Media: production of non-woven, sintered metal fibre filter media used in a wide variety of industries, from polymer to automotive and aerospace.
- Filter Elements: innovative filter solutions and elements.
- Textiles: a range of metal fibre fabrics to withstand extreme temperatures and metal fibre products blended with synthetic fibres for the production of anti-static and electrically conductive textiles.
- Conductive Plastics: stainless steel fibre grains for conductive plastics to protect against Electro-Magnetic Interference and Electrostatic Discharge.
- Airbags: a specially designed filter strip used in automotive airbag systems.

Recent merger of 'Acotech' and 'Furigas'

Bekaert Combustion Technology consists of two main brands: 'Acotech' for high temperature-resistant metal fibres and 'Furigas' for complete gasburner heads. In 2003, 'Acotech', the former 50/50 JV between Bekaert and Shell, and 'Furigas' merged into BCT after which Shell exchanged its 50% stake in 'Acotech' for 25% in BCT. After a modest increase in 2001, BCT increased its sales by 10% in 2002 to € 24m.

Coating Based Technologies

Bekaert Advanced Coatings (Bekaert VDS, Bekaert Dynomics & Sincaco) includes all activities of Bekaert related to thermal spraying and vacuum coating. It is one of the main centres of growth within the BAM witnessing 30% growth in 2002 and exists of three companies:

- Bekaert **VDS** is an innovative provider of thermal sprayed coatings and is involved in the development and production of rotating sputter targets and related sputter hardware. The company also provides highly specialised sputtered thin film on flexible substrates. Applications are e.g. industrial coatings to improve resistance or medical coatings on hip implants.

- Bekaert **Dymonics** develops and manufactures Diamond-like Carbon and Diamond-like Nanocomposite Coatings. The variety of industrial applications is huge ranging from sliding machine components, several types of moulds, punches for powder pressing, etc. In July 2002, Bekaert announced to have acquired the remaining 20% in Bekaert Dynomics from the VITO (Flemish Institute for Technological Research) for an undisclosed sum. For the period 2000-2004 Bekaert targeted overall, organic growth at 50% and 30% respectively for Dymonics with a minimum operating margin of 15%. According to Bekaert, 2002 sales would have exceeded € 10m, one year ahead of the business plan.

- **Sinvaco** is an engineering company specialised in vacuum know-how and processing, offering advanced vacuum coating equipment. The company worked closely together with Bekaert ECD for the development of equipment to produce solar cells and is the in-house supplier of equipment to Bekaert Dynomics. Sinvaco also supplies sputtering equipment to the glass industry.

Acquisition of BSF in 2001 for $122m

Bekaert Specialty Films (BSF): In June 2001, Bekaert acquired all the assets of the Specialty Films Inc. (SFI), a division of Material Sciences Corporation (MSC), for $ 122m in cash. The deal also included MSC's share in Innovative Specialty Films (ISF), the 50/50 JV established in 1998 between MSC/SFI and Bekaert and the extensive distribution network (17 centres targeting mainly the professional installer market). As well as the industrial sputtered film produced by the former ISF, BSF also manufactures and distributes Window films, which are applied by specialised installers to vehicle glass and windows in residential properties and commercial and public buildings. Solar control films help to save energy while reflecting the UV radiation, which fades furnishings. Safety films contain the fragments if the window is shattered by explosion, vandalism or storm.

SFI and ISF realised respectively $ 58.3m and $ 17.4m in 2000 with a profit before taxes of respectively $ 9.8m and $ 1.6m. BSF's (n° 2 position) world market share is estimated at around 20% and has an operating margin of about 15%. The market observed a historical growth rate of 15 to 20%. BSF is fully consolidated since 2002 (6 months in 2001). The business seems to have slowed down in 2002, although Bekaert still mentioned double-digit growth.

Composites

Bekaert Composites designs, produces and markets glass fibre reinforced composite products (profiles and pressure vessels) focussed on 4 segments: transportation (refrigeration trucks, trailers, trains, busses, public transport infrastructure), industry (construction elements for corrosion sensitive applications), building (radar-transparent fences) and filtration (high pressure vessels for reverse osmosis, e.g. water desalination). The BU has two production processes: pultrusion and filament winding.

Recent exit from solar cell business:

Exit from solar cell business: a bitter pill

One of the most visible illustrations of Bekaert's renewal process was the investment made in the solar cell business in 2000. The € 84m "impairment" booked in 2002 and the bitter exit in 2003 at $ 6m illustrates that the strategy of aggressively reinvesting cash flows from the traditional business into the high growth, high margin Advanced Materials (BAM) was not without any risk…

In 2000, Bekaert (60%) and United Solar Systems (40%) set up the joint venture Bekaert ECD Solar Systems. Bekaert also took 19% in United Solar, controlled for 81% by Energy Conversion Devices (ECD), with the option to increase the stake to 55% (for an additional $ 12m), by January 2004 at the latest. United Solar developed and manufactured flexible solar cells for the "Unisolar" brand of photovoltaic panels and systems and Bekaert ECD assembled and sold these photovoltaic panels and systems through its worldwide network. United Solar had a production plant with a yearly solar cell production of 5MW and the cash brought in by Bekaert has been used to expand production with a new plant with an annual production of 30MW, which came on stream in April 2002. The project cost for Bekaert amounted to $ 72m (JV funding, new plant and 19% in United Solar).

The solar cell business made a negative equity contribution of € 2.4m, € 6.1m and € 8m in 2000-02. In 2002, Bekaert announced that it would take longer for the business to break even (in 2000, Bekaert hoped for 2003) and that they would search for a third partner for additional financing. Finally, Bekaert took a € 84m impairment in 2002, setting the value of the solar cell activities at 0. At that time, it was already clear that Bekaert was no longer prepared to further invest in the business and that an exit was near.

On 14 May 2003, Bekaert announced to have disposed of its 19% interest in Unisolar (+ call option) and 60% in Bekaert ECD Solar Systems to ECD (Energy Conversion Devices) for $ 6m. In addition, ECD will take over Bekaert's guaranties with respect to liabilities of the joint ventures amounting to approximately $ 25m. Bekaert maintains the rights to technologies outside the field of photovoltaics and rights limited to build sputtering machines outside the field of triple-junction photovoltaics. The pill has been swallowed but is bitterer than anticipated. Nevertheless, we regard the fact that the situation has cleared up as being positive.

Earnings review

2002: Impressive operating improvement but distorted by € 144m non-recurring elements

Bekaert's FY02 results gave a mixed picture: Due to optimisation measures (€ 60m) and a € 84m impairment charge on the solar cell business, the group booked a € -49.5m net loss (versus a net profit of € 47.8m last year, which was also far from excellent). However, before restructuring, the EBIT margin improved to an impressive (for Bekaert) 6.6%!

Bekaert FY02 results

	1H01	2001	1H02	2002	2003e
Sales	931	1,796	986	1,863	1,785
Growth	*-1.0%*	*+2.3%*	*+5.9%*	*+3.8%*	*-4.2%*
EBITDA	120.2	207.5	101.5	225.8	256.0
Margin	*12.9%*	*11.5%*	*10.3%*	*12.1%*	*14.3%*
Operating result	53.4	59.5	20.8	64.2	106.1
Margin	*5.7%*	*3.3%*	*2.1%*	*3.4%*	*5.9%*
Financial result	-14.1	-30.4	-14.9	-32.9	-27.0
Other	-7.8	5.4	-5.8	-100.6	+5.2
Taxes	-7.4	4.6	-1	7.4	-16.8
Equity consolidated	7.6	16.6	13.9	23.1	29.1
Net profit group share	30.8	47.8	9.4	-49.5	85.3
EPS	1.38	2.15	0.43	-2.24	3.85

Source: Bekaert, KBC Securities

Sales increased by 3.8% to € 1,863m. Steel wire (-0.1%), Steel cord (+1.4%) and Fencing (+0.7%) remained approximately flat while "Advanced Materials" posted a 34.4% increase in Sales to € 220m (consolidated). This was mainly the result of Bekaert Specialty Films, acquired in Apr-01 and only consolidated for 6 months in 2001. Without a dollar effect, sales would have increased by 5.9%.

The European Union (48.7%) and North America (29.7%) remain the most important regions for Bekaert. Rest of Europe (7.7%) and Rest of World (12.3%) are less important but are to become more important as the group will focus on growth regions in the world (Eastern Europe, Asia) where the group intends to broaden its presence in the next couple of years.

Sales per business unit

	1H01	2001	1H02	2002	2003e
Wire	306	675	344	674	602
Steel cord	310	597	305	605	593
Bekaert Fencing	212	388	215	392	388
BAM	65	164	111	220	229
Others	13	87	11	58	-27
Intersegment sales	n.a.	-113	n.a.	-84	
Total	**906**	**1,796**	**986**	**1,863**	**1,785**

Source: Bekaert, KBC Securities

Operating margins: the FY02 results were affected by a number of one-off costs related amongst others to the impairment charge on the solar cell business (€ 84m). Bekaert mentions € 144m of non-recurring provisions to cover restructurings, closures and impairments. Excluding these from the "Results from operations", this yields an EBIT margin of 6.6% compared to 3.4% after exceptional charges. That makes it possible to assess future cash flow potential from a longer term perspective:

Bekaert FY02 results

	1H01	2001	1H02	2002	2003E
Sales	931	1,796	986	1,863	1,785
Growth			*+5.9%*	*+3.7%*	*-4.2%*
Results operations	53.4	59.5	20.8	64.2	106.1
Margin	*5.7%*	*3.3%*	*2.1%*	*3.4%*	*5.9%*
Normalised EBIT	n.a.	73.6	n.a.	123.8	111.1
Margin		***4.1%***		***6.6%***	***6.2%***

Source: Bekaert, KBC Securities

Anyway, a second look at the 'disappointing' 2002 results points towards an impressive rebound of the underlying business in 2002. Bekaert never did better than the 6.6% EBIT margin "before restructurings" posted last year (except in 1994 but that is a long way back), considering a very challenging economic environment! The improvements are to be explained by the higher margin BAM, increasing in weight (generating 11.3% of 2002 sales), leveraging the overall margins, but also by an improved profitability of the 'traditional' business, which should not be underestimated.

The share in the result of the joint ventures and associates (mainly Wire activities in Latin America) increased significantly from € 16.6m to € 23.1m. The solar cell and handling business' made a negative contribution of respectively € 8m and € 2.5m.

Net financial debt decreased significantly by € 127.5m to € 444.6m or a gearing of 50.7%. The shareholder's equity amounted to € 878.5m or € 37.6 per share at the end of 2002.

Outlook

Trading update:

At the AGM, Bekaert also gave a trading update for the first quarter. Although no precise figures were given, the overall picture was rather positive. Of course, sales were impacted by a decline in US dollar of 18% y-o-y. Sales decreased by 7.2% in euro, but would have increased by 2% at constant exchange rates. Sales of the Wire business decreased by 16%, of which about 8% due to the lower US dollar and roughly 5% on discontinued activities, leaving an organic decline of about 3%. Sales of the Fencing business (the former Merchant Products Europe) remained stable (no US dollar effect) while a very high activity level in Steelcord could limit the decline in sales to 2.2%. Sales of the BAM were at the same level as the previous year but would have observed an 8-9% rise at constant exchange rates.

… despite a "good" 1Q and "firm" order book, prudence for the full year

All units seem to have increased their contribution to the operational and bottom line figures, despite the lower US dollar, illustrating an impressive improvement of the underlying profitability. Consolidated profit increased "substantially" and overall order book is "good" - "substantially" and "good" might be interpreted as above 10%. The contribution of equity-consolidated companies (mainly Wire business in Latam) increased "sharply". Despite what seems to be an excellent 1Q (exceeding "internal budget"), Bekaert remained very prudent not disclosing any guidance. Despite a strong 1Q and good hopes for the 2Q03, the uncertainties surrounding the US dollar and the outlook for the current strong holders (steel cord and Latam) bode for some prudence.

We count on a € 3.85 'reported' EPS

Despite the very low visibility and prudent outlook given by Bekaert, we remain cautiously optimistic as concerns 2003. Despite lower sales due to the weak US dollar, the improved profitability together with the absence of major optimisation charges should boost the 2003 earnings. We count on a € 3.85 'reported' EPS, compared to the € -2.24 observed over 2002. Our assumptions can be summarised as follows:

- A 4.2% decline in sales to € 1,785m. Based upon a 7% decline in the wire & fencing business, while the steel cord and advanced materials limit the impact of the weaker US dollar to a 2% decline and 4% increase in sales.
- Without major optimisation measures (we only assume € 5m in 2003), a recovery in the operating result from € 64.2 to 106.1m. Before restructuring, we count on an operating margin at 6.2% compared to 6.6% in 2002.
- Compared to the € 100.6m non-recurring charges in 2002, mainly the € 84m "impairment" on the solar business, a € 5.22m "capital gain" on the disposal of the solar business to ECD. Against the lower net financial debt, we assume an improvement in financial result from € -32.9m to € -27m.
- A tax rate of 20% leading to € 16.8m of taxes, compared to the 'positive' fiscal result of € 7.4m in 2002.

- An increase in the net contribution (after goodwill) of joint ventures and associates from € 19.0m to € 25.0m. This is probably much too prudent as: the solar cell business made a negative contribution of € 8m in 2002 but will not be consolidated in 2003, the Handling JV made a negative contribution of € 2.5m in 2002 but turned positive in the 1Q - and especially the very strong performance of the Wire business in Latin America. As such, our € 25m includes a very comfortable buffer against a potential disappointing 2H03.

Bottom line, this scenario leads us to a € 85.3 m net profit, group share, compared to the € -49.5m in 2002.

Valuation

Scenario based upon a 2.7% average sales growth and normalisation in 2010 at a 7.4% operating margin

For our valuation of Bekaert, we made LT assumptions over 2003-10. After 2003, we assume an average sales growth of 2.7%. This can be split into a 2% CAGR for the traditional business (1.4% for Wire & Fencing and 2.9% for Steel Cord) and 10.2% for the Advanced Materials. At the end of the projected period, BAM accounts for 20.5% of total sales. Due to an improving product mix, following further increased weight of the higher margin Advanced Materials and Steel Cord business, and optimisations at the Wire and Fencing business, we count on an operating margin of 7.4% by 2010 (versus 6.6% in 2002). This is based upon a margin of 11% for the BAM and 6.5% for the traditional business. Despite normalising at a margin substantially above the historical - through the cycle - margin of about 5% for Bekaert, we regard this scenario very conservative.

For our valuation of Bekaert, under this scenario, we used three models (DCF, EVA & DDM):

DCF model

Year		**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**
Market risk free	5.0%								
Market risk premium	4.0%								
LT growth	0.5%								
WACC		8.0%	8.0%	8.0%	8.1%	8.1%	8.1%	8.1%	8.1%
NOPLAT		109.9	120.5	126.8	129.8	132.3	137.9	143.4	153.6
+ depreciation		147.9	146.5	145.7	145.0	144.3	143.6	142.8	138.4
- Investment		-145.0	-160.0	-145.0	-140.0	-140.0	-140.0	-140.0	-138.4
- Investment in working capital		18.5	-18.6	-15.9	-12.0	-10.4	-10.5	-5.1	-15.2
Free cash flow		**131.4**	**88.3**	**111.7**	**122.8**	**126.2**	**130.9**	**141.2**	**138.4**
Discount factor		0.95	0.88	0.82	0.75	0.70	0.65	0.60	0.55
PV of FCF		125.2	78.0	91.2	92.6	88.1	84.5	84.3	76.5
Cumulative PV of FCF	720.4								
+ PV of terminal value	1,013.1								
Entreprise value	**1,733.5**								
- Value of debt	-444.6								
- Provisions	-183.4								
- Minorities	-44.3								
Theoretical value of equity	**1,061.1**								
Idem per share	**47.97**								

Source: KBC Securities

DCF points to € 48 per share

A DCF valuation under this scenario points to a theoretical fair value of € 1,061m or € 48.0 per share. After 2010, a perpetual growth rate of 0.5% has been applied.

EVA™ model

Year		2003	2004	2005	2006	2007	2008	2009	2010
Market risk free	5.0%								
Market risk premium	4.0%								
LT growth	0.5%								
RoCE		6.7%	7.8%	8.0%	8.0%	8.1%	8.3%	8.5%	8.9%
WACC		8.0%	8.0%	8.0%	8.1%	8.1%	8.1%	8.1%	8.1%
Spread		-1.4%	-0.1%	0.0%	-0.1%	0.0%	0.2%	0.4%	0.9%
Capital Employed (year start)		1,651.4	1,535.8	1,584.5	1,617.0	1,642.3	1,667.4	1,694.4	1,717.3
Economic profit		-22.3	-1.7	0.1	-1.0	-0.5	3.0	6.4	14.7
NOPLAT		109.9	120.5	126.8	129.8	132.3	137.9	143.4	153.6
Capital charges		-132.2	-122.2	-126.8	-130.8	-132.8	-134.8	-137.0	-138.9
Economic profit		-22.3	-1.7	0.1	-1.0	-0.5	3.0	6.4	14.7
Discount factor		0.95	0.88	0.82	0.75	0.70	0.65	0.60	0.55
Actualized economic profit		-21.2	-1.5	0.1	-0.7	-0.3	2.0	3.8	8.1
Cumulative PV of EP	-9.8								
+ PV of terminal value	84.2								
+ Capital Employed	1,651.4								
Value of operations	**1,725.7**								
- Value of debt & Provisions	-628.0								
- Minorities	-44.3								
Theoretical value of equity	**1,053.4**								
Idem per share	**47.62**								

Source: KBC Securities

EVA™ brings us to € 47.6…

An EVA™ valuation of Bekaert, under our assumptions, points to a theoretical value of € 1,053m or € 47.6 per share. At our normalisation year, Bekaert earns a positive spread of 0.9% above its cost of capital.

… as does the DDM.

We also applied a discounted dividend valuation on Bekaert, using a required rate of return of 9.2%, based upon a risk free rate of 5%, a risk premium of 4% and beta of 1.05. The model brings us to a theoretical fair price of € 47.6 per share.

Price target at € 45 per share

The average of the three applied methods brings us to a theoretical fair price of € 47.7 per share. We have set our price target at € 45, which equals to between 10.6 and 9.7 times the EPS 03-04. The BV, end 2002, amounted to € 37.6 which implies a premium of close to 20% for our target towards the BV, which is not undemanding as Bekaert's ROCE is still flirting with the WACC. As such, our target price implies our confidence in Bekaert's LT strategy.

Financial data

INCOME STATEMENT (€ m)	2000	2001	2002	2003E	2004E	2005E
Sales	1,756.3	1,795.9	1,863.5	1,784.7	1,887.7	1,971.9
Other revenue	22.1	22.1	19.6	18.8	19.9	20.8
Personnel costs	489.0	502.3	503.3	486.9	515.1	538.0
Other operating costs	1,020.9	1,102.0	1,151.5	1,061.6	1,125.9	1,178.5
EBITDA	246.4	191.7	208.7	255.0	266.7	276.2
Depreciation and amortisation	-125.3	-124.5	-133.3	-136.8	-135.4	-134.6
Goodwill amortisation	-3.0	-5.0	-11.1	-7.0	-7.0	-7.0
EBIT	115.7	59.5	64.2	106.1	124.3	134.5
Net interest	-31.0	-33.8	-32.9	-27.0	-23.8	-23.0
Other financial result	4.7	3.4	0.0	0.0	0.0	0.0
Associates before tax	0.0	0.0	0.0	0.0	0.0	0.0
Exceptional results	0.0	0.0	-100.6	5.0	0.0	0.0
Pre-tax profit declared	89.3	29.1	-69.3	84.1	100.5	111.6
Taxes	-22.7	4.6	7.4	-16.8	-24.1	-29.0
Associates after tax	33.7	16.6	19.1	25.0	26.0	27.3
Minority interests	5.3	3.5	6.7	7.0	7.8	8.3
Net attributable profit	94.9	46.7	-49.5	85.3	94.6	101.5
Retained earnings	57.5	9.5	-86.7	46.6	53.7	59.5
Net current result before goodwill	104.3	53.0	-34.4	91.4	105.7	112.6
Net current result after goodwill	101.3	48.0	-49.5	85.3	94.6	101.5
Current cash flow	216.8	166.1	131.2	245.3	258.2	264.4

BALANCE SHEET (€ m)	2000	2001	2002	2003E	2004E	2005E
Goodwill	47.8	118.0	72.2	65.2	58.2	51.2
Other intangible assets	27.3	60.7	55.0	45.8	47.2	48.0
Tangible assets	841.2	910.0	777.6	805.2	838.6	860.4
Associates	261.4	276.2	204.6	204.6	204.6	204.6
Other financial assets	51.6	51.1	54.6	54.6	54.6	54.6
Inventories	351.0	342.7	311.8	296.3	313.4	327.3
Trade debtors	424.0	434.9	390.5	374.8	396.4	414.1
Other current assets	13.4	16.6	13.2	16.1	17.0	17.7
Cash and equivalents	76.3	74.4	73.8	81.0	82.8	87.9
Short-term liabilities (excl debt)	295.2	283.8	375.2	365.3	386.4	402.9
Provisions for pensions and other	140.8	138.8	129.5	129.5	129.5	129.5
Long-term liabilities (excl debt)	150.8	134.1	53.9	53.9	53.9	53.9
Financial debt	427.3	664.0	518.4	467.6	457.3	429.0
Minorities	48.9	42.5	44.3	48.6	53.5	58.9
Shareholder's equity	1,031.2	1,021.4	831.9	878.5	932.2	991.7
Restated net financial debt	350.9	589.7	444.6	386.7	374.5	341.1
Capital employed (restated)	1,375.1	1,493.3	1,694.0	1,538.6	1,560.2	1,600.8
Restated net financial debt / Equity	32%	55%	51%	42%	38%	32%
Restated net financial debt / Equity ex GW	34%	62%	55%	45%	40%	34%

CASH FLOW STATEMENT (€ m)	2000	2001	2002	2003E	2004E	2005E
EBITDA	246.4	191.7	208.7	255.0	266.7	276.2
Change in working capital	-132.9	-17.2	56.4	18.5	-18.6	-15.9
Change in provisions	80.2	2.5	-7.1	0.0	0.0	0.0
Other non-cash items	0.0	0.0	-133.4	13.1	13.4	13.9
Gross operating cash flow	193.8	177.0	124.6	286.6	261.5	274.2
Net interest paid	-31.0	-33.8	-32.9	-27.0	-23.8	-23.0
Tax paid	-25.3	-11.6	7.4	-16.8	-24.1	-29.0
Net operating cash flow	137.5	131.6	99.1	242.7	213.6	222.2
Capital expenditure	-118.2	-317.4	-74.6	-145.0	-160.0	-145.0
Free cash flow	19.2	-185.8	24.5	97.7	53.6	77.2
Disposals	0.0	0.0	0.0	0.0	0.0	0.0
Acquisitions	-47.6	-12.3	0.0	0.0	0.0	0.0
Dividends	-37.5	-37.2	-37.2	-37.2	-38.7	-40.9
FX and others	-29.8	-6.9	140.2	-2.6	-2.7	-2.9
New equity	0.0	0.0	0.0	0.0	0.0	0.0
Change in net debt	-95.6	-242.1	127.5	-58.0	-12.2	-33.4

PER SHARE DATA (€)	2000	2001	2002	2003E	2004E	2005E
EBITDA per share	11.0	8.6	9.4	11.5	12.1	12.5
EBIT per share	5.16	2.67	2.90	4.80	5.62	6.08
Published EPS	4.57	2.15	-2.24	3.85	4.28	4.59
Current EPS before GW (diluted)	4.66	2.38	-1.55	4.13	4.78	5.09
Current EPS after GW (diluted)	4.52	2.16	-2.24	3.85	4.28	4.59
Current cash flow per share	9.7	7.5	5.9	11.1	11.7	12.0
Gross operating cash flow per share	8.7	8.0	5.6	13.0	11.8	12.4
Free cash flow per share	0.86	-8.35	1.11	4.42	2.42	3.49
Net dividend	1.26	1.26	1.26	1.31	1.39	1.43
NBV per share	46.2	46.1	37.6	39.7	42.1	44.8
PERFORMANCE CRITERIA	**2000**	**2001**	**2002**	**2003E**	**2004E**	**2005E**
EBITDA margin	14.0%	10.7%	11.2%	14.3%	14.1%	14.0%
EBIT margin	6.6%	3.3%	3.4%	5.9%	6.6%	6.8%
EPS annual growth	23%	-49%	-	-	16%	7%
CFPS annual growth	13%	-23%	-21%	87%	5%	2%
Pay-out ratio	39%	80%	-75%	45%	43%	41%
EPS CAGR 3y historic	16%	0%	-	-4%	26%	-
CFPS CAGR 3y historic	6%	-1%	-12%	5%	16%	26%
Return on invested capital	6.7%	4.8%	3.9%	5.9%	6.4%	6.5%
Return on equity	10.9%	5.2%	-3.7%	10.7%	11.7%	11.7%
VALUATION DATA*	**2000**	**2001**	**2002**	**2003E**	**2004E**	**2005E**
Financial year high (€)	56.70	49.95	-	77.03	57.30	56.70
Financial year low (€)	44.20	29.94	-	41.89	34.98	44.20
Reference market capitalisation (€ m)	957	871	-	942	942	942
Enterprise value (€ m)	1,236	1,365	-	1,303	1,295	1,267
PER high (x)	12.2	21.0	-	18.6	12.0	11.1
PER low (x)	9.5	12.6	-	10.1	7.3	8.7
PER reference (x)	10.9	17.1	-	9.7	8.4	7.9
P/CF (x)	5.2	5.4	-	3.6	3.4	3.4
P/Bookvalue (x)	1.1	0.9	-	1.0	1.0	0.9
Gross dividend yield (%)	3.3	4.1	-	4.4	4.9	4.7
EV/EBITDA (x)	5.0	7.1	-	5.1	4.9	4.6

Source: KBC Securities *Historic valuation data are based on historic prices

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Brussels	London	New York	Paris
+32 2 417 44 04	+44 20 7283 9666	+1 212 489 20 40	+33 1 53 05 32 00