

Bekaert (Buy - EUR 78): Further increasing LatAm exposure

Facts

- Bekaert signed a memorandum of understanding with its partners in Ecuador, represented by members of the Kohn family, to establish a holding company covering the businesses in the northern part of Latin America. Bekaert and its Ecuadorean partners will merge their operation in Venezuela (100% owned by Bekaert) in Colombia (87.5% owned by Bekaert and 12.5% by the Partner), in Ecuador (50/50 joint venture between Bekaert and the Partner) and in Peru (39.9% investment held 50/50 by Bekaert and the Partner). Bekaert will become the 80% shareholder in this holding company. Since both parties are bringing in activities, no cash payments are involved.
- The companies in Ecuador and Peru are active in wire products for construction, agricultural fencing, and industrial applications.
- The activities in Ecuador and in Peru generated EUR 140m revenues in 2007 or 6.5% of Bekaert's consolidated revenues. Via equity consolidation these 2 countries contributed EUR 2.9m to equity results last year, implying an ROE of 21.6%

Our View

Bekaert announced a next step in streamlining its LatAm operations. The group creates a holding company that combines wire operations in 4 countries. Although the profitability of these joint ventures was already good, Bekaert expects that fixed costs can be reduced and that synergies can be realized by centralizing SG&A. In addition, investment programs will be better streamlined.

As a result, Bekaert shifts EUR 140m revenues from the equity consolidated joint ventures to the consolidated scope or 5% of the group expected revenues in 2009. The Latin American activities have a higher profitability than Bekaert's consolidated business. Excluding potential synergies and cost cutting, we estimate that the acquisition should add 6% to Bekaert's EBIT in 2009. Since the contribution from the associates will decline and a 20% of the business in Venezuela and Colombia will lead to a minority adjustment, we estimate that the deal is slightly EPS enhancing.

Conclusion

We applaud this transaction from a strategic point of view. Bekaert further increases its exposure to emerging markets where growth for its traditional wire products is significantly higher than in the mature Western markets. Hence, the growth profile of the group further improves. In addition, Bekaert generates above average margins in the faster growing regions.

Despite the difficult macro economic environment, the group's volume growth driven by increasing penetration of its products in emerging markets and by newly launched products that enlarge the group's footprint towards sectors such as submarine and energy transmission, green energy, mining, telecommunication, and the oil and gas industry.

The stock price fell back after the recent market turmoil. Valuation is undemanding. Bekaert is trading at less than 4x EV/EBITDA 2009, which includes a 15% earnings drop compared to 2008.

Forecasts and target price will likely be lowered in coming weeks, impacted by economic environment and the forex movements. Given its strategic and geographical positioning, we believe Bekaert will continue to outperform the market. Buy reiterated.