Indiabulls

BHARAT FORGE LIMITED RESEARCH

EQUITY RESEARCH — **October 15, 2007**

Results Review

Share Data

Market Cap	Rs. 64.4 bn
Price	Rs. 289.30
BSE Sensex	19,058.67
Reuters	BFRG.BO
Bloomberg	BHFC IN
Avg. Volume (52 Week)	0.2 mn
52-Week High/Low	Rs. 396/254
Shares Outstanding	222.7 mn

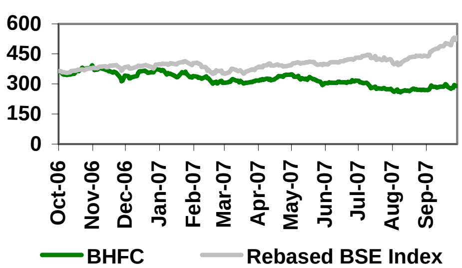
Valuation Ratios (Consolidated)

Year to 31 March	2008E	2009E
EPS (Rs.)	14.1	17.3
+/- (%)	4.2%	22.7%
PER (x)	20.5x	16.7x
EV/ Sales (x)	1.5x	1.3x
EV/ EBITDA (x)	10.6x	8.7x

Shareholding Pattern (%)

Promoters	39
FIIs	18
Institutions	14
Public & Others	29

Relative Performance



Bharat Forge Limited — Buy

Strong rupee and auto slowdown ruled the quarter

Q1 FY'08 was a tough quarter for Bharat Forge Limited (BFL), both due to rapid and significant appreciation in the value of Indian Rupee and risked US business helped the Company to maintain the overall US revenue and improving the same marginally, the growth during the quarter was primarily driven by two fold growth in revenues in the European markets. Net sales of the standalone entity grew by 18.1% yoy on the back of Exports showing substantial growth of 31.5% yoy and domestic operations growing by 9.4% yoy. The growth in Exports of BFL was primarily driven by serial production of several medium and heavy-duty programs in Europe, significant growth in the US passenger car engine component and re-commencement of business with Chinese OEM. Despite remarkable growth in Exports which contributed around 42% of total revenues in the gross revenue of BFL, EBITDA declined by 0.5% yoy while on a consolidated basis EBITDA decreased 7.8% yoy. The consolidated net profit for the first quarter was flat at Rs. 804 mn. The Company's profitability could have been significantly better but for the sudden and rapid drop in the off take in the domestic market and slowdown in the US heavy truck market on the back of change in the emission norms.

Taking in view the performance of the Company in the first quarter of FY08E and expected strengthening of rupee we have downgraded our earning estimates for FY08E and FY09E. However, we continue to hold a positive outlook on the future prospects of BFL and maintain our Buy rating on the stock.

Key Figures (Consolidated)

Quarterly Data	1Q'07	4Q'07	1Q'08	YoY%	QoQ%
(Figures in Rs. mn, except per share data)					
Net Sales	9,878	11,098	10,614	7.5%	(4.4%)
EBITDA	1,591	1,726	1,466	(7.8%)	(15.1%)
Net Profit	804	800	804	0.1%	0.5%
Margins(%)					
EBITDA	16.1%	15.6%	13.8%		
NPM	7.9%	7.1%	7.2%		
Per Share Data (Rs.)					
Adjusted EPS	3.6	3.6	3.6	0.3%	0.1%

Result Highlights

Strong rupee impacted the sales growth

Significant appreciation in the value of Indian Rupee against major currencies of USD, Euro and GBP, lower off-take in the Indian auto market along with slowdown in the US heavy truck market lead to slower growth of revenues during the first quarter of FY08. Consolidated net sales for the quarter witnessed sluggish growth of 7.5% yoy to Rs. 10.6 bn as compared to Rs. 9.9 bn in the corresponding period last year. On standalone basis, net sales increased 18.1% yoy driven by robust growth of 31.5% yoy in Exports and 9.4% yoy growth in domestic sales. Excise duty as a percentage of sales increased 30 bps yoy leading to reduction in net sales.

Two fold increase in European revenues while US revenues remained relatively flat

Despite taking a hit of Rs. 187 mn due to rupee appreciation against all the major currencies, exports rose sharply during the quarter due to doubling of revenues from the European markets. European markets achieved 98.9% yoy growth on the back of commencement of serial production for two medium & heavy duty engine components programs as well as growth in non-automotive sales for applications such as Agri equipment, oil and gas segments. While European markets excelled, US markets witnessed a massive slowdown in the Commercial Vehicle segment. The US Commercial Vehicle segment registered a 28% yoy decline in revenues. However, this fall was offset by the significant growth in the Passenger Vehicle and Non-Automotive segment. As a result, the overall US revenues showed a marginal growth of 4.3% yoy to Rs. 1.2 bn.

Geographical Revenue Distribution of BFL

Rs. mn

Geographies	Q1'08	Q1'07	Q4'07	YOY%	QOQ%
India*	2,732	2,505	3,154	9.1%	(13.4%)
USA	1,223	1,173	1,221	4.3%	0.2%
Europe	933	469	725	98.9%	28.7%
Asia Pacific	81	59	61	37.3%	32.8%
Total	4,969	4,206	5,161	18.1%	(3.7%)

**Excluding other income*

EBITDA dipped 420 bps yoy

Currency	Avg. 1Q'08	Avg. 1Q'07	YOY%
USD-INR	40.85	45.25	(9.7%)
EURO-INR	56.34	58.22	(3.2%)
GBP-INR	83.28	84.27	(1.2%)

Consolidated EBITDA for the quarter dipped by a steep 7.8% yoy and 15.1% qoq. However, on standalone basis the decline was restricted to 0.5% yoy. Owing to strengthening of rupee against US Dollar by 9.7% yoy, Euro by 3.2% yoy and GBP by 1.2% yoy along with rising cost pressures EBITDA margins compressed by a sharp 380 bps yoy. Due to spiralling prices of steel and other components raw material cost for the quarter rose to 46.3% from 44.6% in the corresponding period last year. Manufacturing expenses rose by 110 bps yoy while staff cost increased by 100 bps yoy. Other expenditures for Q1'08 were more or less flat at 8.5%.

Despite net gain of Rs. 333 mn relating to foreign exchange difference, net profit remained flat

Consolidated net profit was flat at Rs. 804 mn despite a net gain of Rs. 333 mn relating to exchange difference on foreign currency borrowings and bank deposits during the quarter. Consolidated net profit margin declined 70 bps yoy on account of higher interest and depreciation cost. Interest cost increased by 30 bps yoy owing to higher interest rates prevailing in India and increased working capital requirement; depreciation increased by 70 bps yoy due to completion of capacity expansion program with a total capital outlay of around Rs. 7 bn.

Key Events

Issue of Foreign Currency Convertible Bonds

The Company had issued 0.5% Foreign Currency Convertible Bonds (FCCB) due 2010 in two tranches, each having varied rights and obligations, aggregating to USD 60 mn each, convertible at an initial price of Rs. 336.11 and Rs. 384.12 per share of Rs.2/- each respectively.

The Company had further issued Zero Coupon Foreign Currency Convertible Bonds (FCCB) in two tranches amounting to USD 40 mn and USD 39.9 mn due 2012 and 2013 respectively.

Key Risks

Appreciating rupee a major cause for concern

Strengthening of Indian rupee against major global currencies

Strengthening of Indian rupee against major global currencies pose a significant risk to the performance of Bharat Forge as well as our rating as it drives major portion of its revenue from various global markets.

Sluggishness in the auto industry

Continuation of the slowdown in the Indian auto industry as well as US markets which is expected to pick up sales from the thrid quarter of FY08E and early 2008 respectively, pose a risk to our rating.

Spiralling steel prices

Spiralling global steel prices as well as other components used in the auto industry continue to pose a risk to our rating. The first quarter of FY08E witnessed a significant increase in raw material prices by 210 bps yoy.

Outlook

Growth affected due to short term localized reasons

Despite not so exciting quarter for Bharat Forge Limited we continue to hold a positive outlook on its long term growth. The demand drivers in the short term are affected more due to localized reasons such as sudden increase in the interest rates in India as well as change in emission norms in the US. The macro economic factors both in India and US continue to be strong. The volumes are likely to pick up in the US truck market from early 2008 while in the Indian auto market from third quarter of FY08E.

Moreover, with early signs of recommencement of demand from China, BFL's FAW JV is expected to breakeven by FY08E and start contributing to the bottom line by FY09E. In the first quarter of 2007, the China's Commercial Vehicle market grew by 33% yoy and 14% on a sequential basis. China market is witnessing strong growth and the inventory build up is getting progressively corrected. The situation is expected to improve further as the inventory correction gets completed.

The Company's de-risked business model along with strong global footprint will keep the Company in good stead. The benefits of de-risked business model can be seen from the growth in the US Passenger Vehicle and Non-Automotive segment which countered off the slowdown in the US Commercial Vehicle segment. BFL recently commenced the installation of its non-automotive manufacturing facility at Pune and Baramati. The installation of the capacity is progressing as per schedule and BFL expects to commence commercial production between March to September 2008 in a phased manner.

Better times awaiting BFL

BFL, being one of the lowest cost manufacturers and the second largest forging manufacturer in the world, is expected to be among the major beneficiaries in the upcoming better times in the auto industry. Considering the performance of the Company in the first quarter of FY08E, we expect the net sales to grow at a CAGR of 10.2% over FY07-09E. At the current price of Rs. 289.30 the stock is trading at 20.5x FY08E and 16.7x FY09E earnings estimates. We maintain our Buy rating with the target price of Rs. 370.

Key Figures (Consolidated)

Year to March	FY05	FY06	FY07	FY08E	FY09E	CAGR (%)
(Figures in Rs. mn, except per share data)						(FY07-09E)
Net Sales	19,934	30,189	41,783	47,451	55,965	10.2%
EBITDA	4,240	5,235	6,494	6,912	8,432	9.1%
Net Profit	2,015	2,510	3,008	3,136	3,847	8.5%
Margins(%)						
EBITDA	21.3%	17.3%	15.5%	14.6%	15.1%	
NPM	10.1%	8.3%	7.2%	6.6%	6.9%	
Per Share Data (Rs.)						
Adjusted EPS	9.3	11.6	13.5	14.1	17.3	8.5%
PER (x)	29.6x	38.4x	21.4x	20.5x	16.7x	

Disclaimer

This report is not for public distribution and is only for private circulation and use. The Report should not be reproduced or redistributed to any other person or person(s) in any form. No action is solicited on the basis of the contents of this report.

This material is for the general information of the authorized recipient, and we are not soliciting any action based upon it. This report is not to be considered as an offer to sell or the solicitation of an offer to buy any stock or derivative in any jurisdiction where such an offer or solicitation would be illegal. It is for the general information of clients of Indiabulls Securities Limited. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or needs of individual clients. You are advised to independently evaluate the investments and strategies discussed herein and also seek the advice of your financial adviser.

Past performance is not a guide for future performance. The value of, and income from investments may vary because of changes in the macro and micro economic conditions. Past performance is not necessarily a guide to future performance.

This report is based upon information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon as such. Any opinions expressed here in reflect judgments at this date and are subject to change without notice. Indiabulls Securities Limited (ISL) and any/all of its group companies or directors or employees reserves its right to suspend the publication of this Report and are not under any obligation to tell you when opinions or information in this report change. In addition, ISL has no obligation to continue to publish reports on all the stocks currently under its coverage or to notify you in the event it terminates its coverage. Neither Indiabulls Securities Limited nor any of its affiliates, associates, directors or employees shall in any way be responsible for any loss or damage that may arise to any person from any error in the information contained in this report.

The analyst for this report certifies that all of the views expressed in this report accurately reflect his or her personal views about the subject stock and no part of his or her compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this report. No part of this material may be duplicated in any form and/or redistributed without Indiabulls Securities Limited prior written consent.

The information given herein should be treated as only factor, while making investment decision. The report does not provide individually tailor-made investment advice. Indiabulls Securities Limited recommends that investors independently evaluate particular investments and strategies, and encourages investors to seek the advice of a financial adviser. Indiabulls Securities Limited shall not be responsible for any transaction conducted based on the information given in this report, which is in violation of rules and regulations of National Stock Exchange or Bombay Stock Exchange.