



Bharat Forge

STOCK INFO.	BLOOMBERG
BSE Sensex: 17,605	BHFC IN
	REUTERS CODE
S&P CNX: 5,209	BFRG.BO

21 January 2008

Buy

Previous Recommendation: Buy

Rs310

	YEAR	NET SALES	PAT	EPS	CONS.	P/E	CONS.	ROE	ROCE	EV/	EV/	
	END	(RS M)	(RS M)	(RS)	EPS (RS)	(X)	P/E (X)	(%)	(%)	SALES	EBITDA	
Actual Equity Shares (m)	222.7											
Diluted Equity Shares (m)	237.3											
52-Week Range (Rs)	390/254	3/07A	18,644	2,533	10.0	12.0	31.0	25.8	18.2	16.0	3.8	15.0
1,6,12 Rel.Perf.(%)	0/-11/-35	3/08E	22,262	2,323	9.2	11.4	33.8	27.3	17.2	15.2	3.4	14.3
M.Cap. (Rs b)	69.0	3/09E	26,288	3,038	12.0	15.6	25.8	19.8	17.1	16.7	2.7	11.2
M.Cap. (US\$ b)	1.7	3/10E	30,306	3,606	14.2	18.2	21.8	17.0	17.3	17.4	2.2	9.2

- Bharat Forge posted lower than expected numbers (standalone) for 3QFY08. Net sales grew just 16.7% YoY to Rs5.6b, impacted by lower export growth. EBITDA margin shrank 150bp YoY (10bp QoQ) to 24.5%. Adjusted PAT declined 5.1% YoY (1.3% QoQ) to Rs597m.
- Exports for the quarter were Rs2.3b, up just 17.4% YoY as compared to 36.6% growth in 1HFY08. Domestic sales continued to display signs of revival, growing 16.2% YoY after 11.4% growth in 1HFY08. Domestic sales growth has been impacted by the slowdown in the domestic CV industry; the management had indicated that industry volumes would pick up in 2HFY08.
- There was an extraordinary expense of Rs23m due to loss on translation of foreign currency loans.
- Consolidated revenues (excluding China JV) grew 6.1% YoY to Rs10.8b. EBITDA margin declined 20bp YoY (80bp QoQ) to 16.2%. Consolidated PAT declined 5.8% YoY to Rs725m.
- We have revised our estimates to factor in the lower than expected revenue growth in 3QFY08. Our consolidated EPS estimates are now lower by 8.8% for FY08 and by 5.5% for FY09. The stock trades at 19.8x FY09E consolidated EPS of Rs15.6 and 17x FY10E consolidated EPS of Rs18.2. We maintain **Buy**.

QUARTERLY PERFORMANCE

(Rs Million)

Y/E MARCH	FY07				FY08				FY07	FY08E
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE		
Net Sales	4,206	4,507	4,771	5,161	4,969	5,632	5,567	6,094	18,644	22,262
Change (%)	15.7	19.7	19.5	17.7	18.1	25.0	16.7	18.1	18.2	19.4
Total Expenses	3,132	3,330	3,532	3,917	3,956	4,249	4,204	4,599	13,912	17,008
EBITDA	1,073	1,177	1,239	1,243	1,012	1,383	1,364	1,495	4,732	5,254
As % of Sales	25.5	26.1	26.0	24.1	20.4	24.6	24.5	24.5	25.4	23.6
Change (%)	23.3	21.1	25.6	18.1	-5.7	17.5	10.1	20.2	21.9	11.0
Other Income	233	192	162	222	200	144	179	225	809	748
Interest	176	197	215	234	234	273	294	301	821	1,102
Depreciation	229	250	253	267	329	351	353	370	998	1,404
Extraordinary Expenses	101	0	0	22	0	0	23	0	124	23
Extraordinary Income	0	0	0	0	333	109	0	0	0	442
PBT	800	922	933	943	983	1,012	872	1,048	3,598	3,915
Tax	285	301	303	300	335	334	290	352	1,189	1,311
Effective Tax Rate (%)	35.6	32.6	32.5	31.8	34.1	33.0	33.3	33.6	33.0	33.5
PAT	515	622	630	643	648	677	582	696	2,409	2,604
Adj. PAT	616	622	630	665	425	605	597	696	2,533	2,323
Change (%)	29.9	20.1	18.2	25.5	-31.0	-2.8	-5.1	4.7	23.3	-8.3

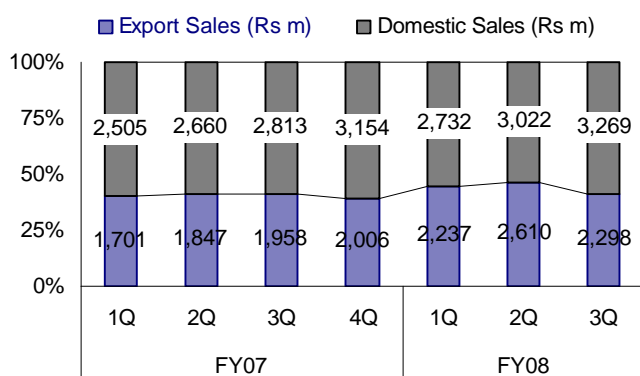
E: MOST Estimates

Export growth slows down

In 3QFY08, Bharat Forge's standalone net sales grew 16.7% YoY to Rs5.6b. Sales growth was impacted by lower than expected export growth. Exports for the quarter were Rs2.3b, up just 17.4% YoY as compared to 36.6% growth in 1HFY08.

Domestic sales continued to display signs of revival, growing 16.2% YoY after 11.4% growth in 1HFY08. Domestic sales growth has been impacted by the slowdown in the domestic CV industry; the management had indicated that industry volumes would pick up in 2HFY08.

REVENUE BREAK-UP



Source: Company/Motilal Oswal Securities

Bharat Forge is aggressively moving into the non-automotive space, for which it is incurring a capex of Rs3.5b. The non-automotive segments being tapped are aerospace, oil & gas exploration, energy, railways & locomotive, marine activities, infrastructure, solar, wind, thermal power equipment, etc. By FY08-end or early FY09, Bharat Forge expects to make a foray into the capital goods business. Entry into the non-automotive space would further de-risk the company's business model and this segment is expected to contribute up to 40% of global revenues by FY11 (17% in FY07 and 25% in FY09E). Bharat Forge is looking to gain a market share of 30% in large marine engineering contracts.

EBITDA margin flat, sequentially

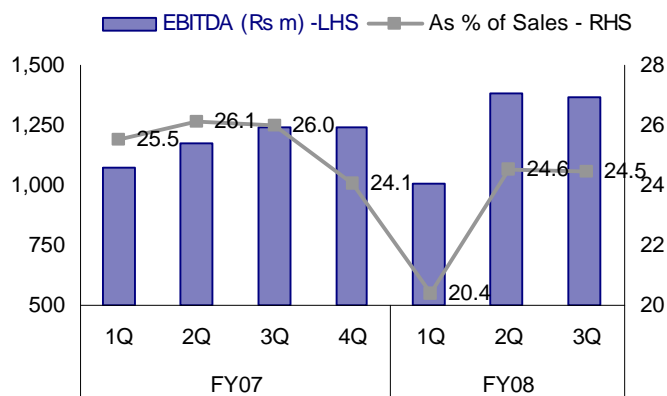
EBITDA margin shrank 10bp QoQ and 150bp YoY to 24.5%. The YoY margin decline has been mainly due to significantly

higher other expenditure (24.3% of net sales v/s 22.6%) and high staff expenses (6.8% of net sales v/s 5.8%). However, RM/Sales declined 120bp YoY (44.4% v/s 45.6%).

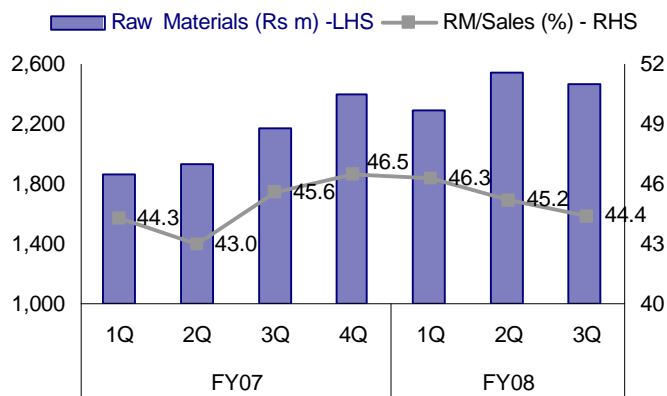
To compensate the loss occurring due to rupee appreciation and to improve its margins, Bharat Forge plans to deepen its natural hedge, is trying to connect its input costs to the dollar, increasing raw-material imports, increasing productivity, considering higher prices, and focusing more on the domestic market and euro-based revenues as compared to dollar-based revenues.

There was an extraordinary expense of Rs23m due to loss on translation of foreign currency loans. This resulted in the company reporting PAT of Rs582m, while the adj. PAT was Rs597m.

EBITDA MARGIN FLAT SEQUENTIALLY BUT DOWN 150BP YOY

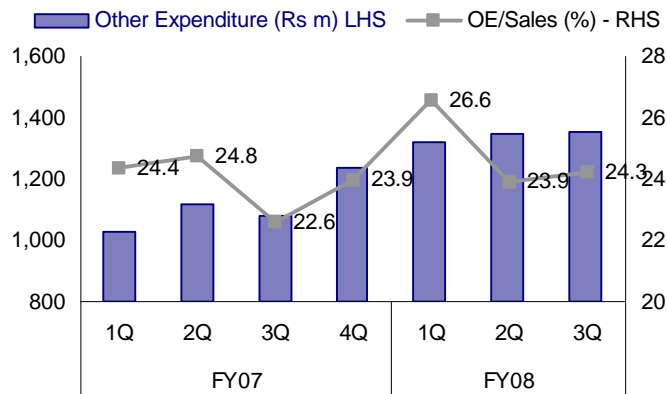


RM/SALES WAS LOWER

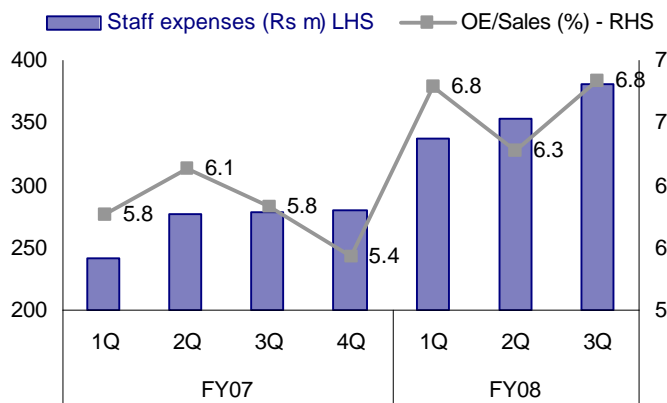


Source: Company/Motilal Oswal Securities

OTHER EXPENDITURE INCREASED SIGNIFICANTLY...



... AS DID STAFF EXPENSES



Source: Company/Motilal Oswal Securities

Consolidated results

Consolidated revenues (excluding China JV) grew 6.1% YoY to Rs10.8b. EBITDA margin declined 20bp YoY (80bp QoQ) to 16.2%. Consolidated adjusted PAT declined 5.8% YoY to Rs725m.

CONSOLIDATED QUARTERLY PERFORMANCE (RS M)

	FY07				FY08		
	1Q	2Q	3Q	4Q	1Q	2Q	3Q
Net Sales	9,878	9,709	10,174	11,098	10,614	10,452	10,800
Gr. (%)	54.8	41.4	8.2	16.6	7.5	7.7	6.1
EBITDA	1,591	1,607	1,670	1,726	1,466	1,776	1,750
Gr. (%)	28.6	23.7	21.0	13.6	-7.8	10.5	4.8
Margin (%)	16.1	16.6	16.4	15.6	13.8	17.0	16.2
Rep. PAT	781	742	770	800	804	791	710
Adj. PAT	848	742	770	815	581	719	725
Gr. (%)	36.6	21.4	22.7	18.5	-31.5	-3.2	-5.8

Source: Motilal Oswal Securities

Valuation and view

We remain positive on Bharat Forge's dual shore model and the management's global vision. Its recent initiatives like the global technology center, its acquisitions and the JV with FAW, China, make Bharat Forge a world leader in its class. However, the company's performance in FY08 has been negatively impacted on account of the slowdown in domestic auto sales, slowdown in the US CV market, and appreciation of the rupee leading to lower export realization. With a recovery expected in CV volumes in the near term and strong passenger car sales growth to sustain, increase in non-automotive revenues 4QFY09 onwards, and implementation of strategies to counter rupee appreciation, we remain positive on the company's long-term prospects.

We have revised our estimates to factor in the lower than expected revenue growth in 3QFY08. Our consolidated EPS estimates are now lower by 8.8% for FY08 and by 5.5% for FY09. The stock trades at 19.8x FY09E consolidated EPS of Rs15.6 and 17x FY10E consolidated EPS of Rs18.2. We maintain **Buy**.

Bharat Forge: an investment profile

Company description

Bharat Forge is one of the top forgings players globally. Primarily focused on automobile forgings, it is now diversifying into non-automotive forgings to broaden its product mix. The company also has substantial geographic distribution of sales and production facilities; its nine manufacturing plants are spread across six countries.

Key investment arguments

- ✎ Bharat Forge's addressable market opportunity stands at US\$10b per year; it is well placed to aggressively increase its global market share.
- ✎ The company is broadening its revenue base by focusing on the non-automotive sector. Within the automotive sector as well, it derives revenues from various segments - PVs and CVs. Hence, Bharat Forge is not overly dependant on any one segment for its revenues.
- ✎ Bharat Forge's China JV with FAW will help tap the tremendous potential offered by China.
- ✎ Forgings and casting by the mere nature of the manufacturing process are popular outsourcing items.

Key investment risks

- ✎ Slowdown in the domestic auto sector and in the US CV market have resulted in lower revenues in FY08.

COMPARATIVE VALUATIONS

		BHARAT FORGE	AMTEK AUTO
P/E (x)	FY08E	27.3	12.0
	FY09E	19.8	10.2
EPS Gr (%)	FY08E	-5.3	25.0
	FY09E	37.5	17.7
RoE (%)	FY08E	17.2	18.4
	FY09E	17.1	17.8
EV/EBITDA (x)	FY08E	14.3	8.3
	FY09E	11.2	7.0

SHAREHOLDING PATTERN (%)

	DEC.07	SEP.07	DEC.06
Promoter	40.6	40.2	36.0
Domestic Inst	15.6	14.9	12.1
Foreign	15.2	17.0	22.8
Others	28.6	27.9	29.1

Recent developments

- ✎ Bharat Forge has signed an MoU with the Maharashtra State Government to jointly develop a multi-product Special Economic Zone (SEZ) near Pune. This SEZ is expected to attract investments of Rs250b and will be set up through an SPV where the company will hold 74% stake.

Valuation and view

- ✎ The stock trades at 19.8x FY09E consolidated EPS of Rs15.6 and 17x FY10E consolidated EPS of Rs18.2. Given the bright prospects, high growth visibility and clear road map for future growth, we maintain **Buy** with a target price of Rs375.

Sector view

- ✎ Auto ancillary sector is witnessing strong demand from global OEMs attempting to offshore components and reduce costs.
- ✎ Forgings and casting due to environmental and health norms have been witnessing the strongest demand from global players.
- ✎ We maintain an overweight stance on the sector.

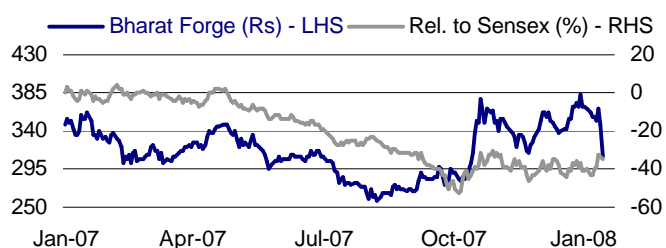
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY08	11.4	14.6	-22.1
FY09	15.6	17.8	-12.4

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
310	375	21.0	Buy

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT		(Rs Million)				
Y/E MARCH	2006	2007	2008E	2009E	2010E	
Net Sales	15,779	18,644	22,262	26,288	30,306	
Change (%)	29.4	18.2	19.4	18.1	15.3	
Expenditure	11,898	13,912	17,008	19,874	22,881	
EBITDA	3,881	4,732	5,254	6,414	7,425	
Change (%)	18.5	21.9	11.0	22.1	15.8	
% of Net Sales	24.6	25.4	23.6	24.4	24.5	
Depreciation	730	998	1,404	1,510	1,592	
Interest & Finance Charge	548	821	1,102	1,044	1,056	
Other Income	531	809	748	673	606	
Non-recurring Expense	0	0	0	0	0	
Exceptional Expenses	-15	124	23	0	0	
Non-recurring Income	0	0	442	0	0	
PBT	3,149	3,598	3,915	4,534	5,383	
Tax	1,079	1,189	1,311	1,496	1,776	
Effective Rate (%)	34.3	33.0	33.5	33.0	33.0	
PAT	2,070	2,409	2,604	3,038	3,606	
Change (%)	28.0	16.4	8.1	16.7	18.7	
% of Net Sales	13.1	12.9	11.7	11.6	11.9	
Adj. PAT	2,055	2,533	2,323	3,038	3,606	
Change (%)	27.1	23.3	-8.3	30.8	18.7	

BALANCE SHEET		(Rs Million)				
Y/E MARCH	2006	2007	2008E	2009E	2010E	
Equity Capital	445	445	445	445	445	
Reserves	11,097	12,723	14,589	17,214	20,333	
Net Worth	11,641	13,267	15,133	17,758	20,877	
Deferred Tax	967	1,128	1,390	1,689	2,045	
Loans	9,925	14,016	13,777	13,923	14,083	
Capital Employed	22,532	28,411	30,301	33,370	37,005	
Gross Fixed Assets	12,653	17,344	28,937	30,617	32,425	
Less: Depreciation	4,901	5,826	7,313	8,824	10,419	
Net Fixed Assets	7,752	11,518	21,625	21,793	22,007	
Capital WIP	3,707	2,748	400	400	400	
Investments	4,440	4,507	2,817	2,254	1,803	
Curr.Assets, L & Ad	15,352	18,490	15,185	19,616	24,488	
Inventory	2,543	3,028	3,587	4,236	4,884	
Sundry Debtors	1,886	2,540	2,660	3,141	3,621	
Cash & Bank Balances	5,054	7,363	4,558	8,745	13,153	
Loans & Advances	4,957	4,723	3,543	2,657	1,993	
Current Liab. & Prov	8,732	8,855	9,728	10,694	11,695	
Creditors	2,347	2,774	3,312	3,911	4,508	
Other Liabilities	288	504	529	555	583	
Acceptances	2,480	2,480	2,480	2,480	2,480	
Net Current Assets	6,620	9,635	5,457	8,922	12,793	
Miscellaneous Expendit	13	2	2	2	2	
Application of Fund	22,532	28,411	30,301	33,370	37,005	

E: MOST Estimates; Standalone

RATIOS		(Rs Million)				
Y/E MARCH	2006	2007	2008E	2009E	2010E	
Basic (Rs)						
Diluted EPS	8.1	10.0	9.2	12.0	14.2	
Diluted EPS Cons.	9.9	12.0	11.4	15.6	18.2	
Cash EPS	12.6	15.3	18.0	20.5	23.4	
Book Value per Share	52.4	59.7	68.1	79.9	93.9	
DPS	3.4	3.5	2.6	3.1	3.7	
Payout %	41.4	36.3	25.1	26.5	26.5	
Valuation (x)						
P/E (Diluted)		31.0	33.8	25.8	21.8	
P/E Consolidated (Diluted)		25.8	27.3	19.8	17.0	
Cash P/E		20.2	17.2	15.1	13.3	
EV/EBITDA		15.0	14.3	11.2	9.2	
EV/Sales		3.8	3.4	2.7	2.2	
Price to Book Value		5.2	4.6	3.9	3.3	
Dividend Yield (%)		1.1	0.8	1.0	1.2	
Profitability Ratios (%)						
RoE	17.8	18.2	17.2	17.1	17.3	
RoCE	16.3	16.0	15.2	16.7	17.4	
Leverage Ratio						
Debt/Equity (x)	0.9	1.1	0.9	0.8	0.7	

CASH FLOW STATEMENT		(Rs Million)				
Y/E MARCH	2006	2007	2008E	2009E	2010E	
OP/(Loss) before Tax	3,151	3,734	3,850	4,905	5,833	
Interest/Div. Received	531	809	748	673	606	
Depreciation & Amort.	730	998	1,404	1,510	1,592	
Direct Taxes Paid	-924	-1,027	-1,049	-1,197	-1,421	
(Inc)/Dec in Wkg. Capita	-861	-696	1,374	722	537	
CF from Op. Activit	2,627	3,817	6,327	6,613	7,147	
(Inc)/Dec in FA+CWIP	-4,156	-3,805	-9,162	-1,678	-1,806	
(Pur)/Sale of Invest.	-4,057	-67	1,690	563	451	
CF from Inv. Activit	-8,213	-3,872	-7,472	-1,114	-1,356	
Inc./(Dec) in Networth	6,003	91	-84	391	467	
Inc/(Dec) in Debt	5,746	4,092	-239	146	160	
Interest Paid	-548	-821	-1,102	-1,044	-1,056	
Dividends Paid	-857	-875	-653	-803	-954	
CF from Fin. Activit	10,344	2,487	-2,079	-1,311	-1,383	
Inc/(Dec) in Cash	4,773	2,309	-2,805	4,187	4,408	
Add: Beginning Balance	281	5,054	7,363	4,558	8,745	
Closing Balance	5,054	7,363	4,558	8,745	13,153	



For more copies or other information, contact

Institutional: Navin Agarwal. **Retail:** Manish Shah

Phone: (91-22) 39825500 Fax: (91-22) 22885038. E-mail: inquire@motiloswal.com

Motilal Oswal Securities Ltd, 3rd Floor, Hoechst House, Nariman Point, Mumbai 400 021

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Bharat Forge

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|---|----|
| 1. Analyst ownership of the stock | No |
| 2. Group/Directors ownership of the stock | No |
| 3. Broking relationship with company covered | No |
| 4. Investment Banking relationship with company covered | No |

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