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Q4 FY07

Result Update

# Bharat Forge

Under Performer

Rs 340

May 23, 2007

## Chinese operations hit bottom line

Company Details		Result Snapshot	
Market Cap:	Rs 75,671m	<p>Bharat Forge's unimpressive results showed net sales, at Rs 5.16bn, growing only 17.7% (against our expected 31.8%) even as traction in exports sputtered. Hence, the leverage on EBITDA was missing, pulling it down sequentially by 188bp to 24.1% and virtually flat yoy. PAT grew 21.2% to Rs 643m against our estimate of Rs 783m.</p> <p>On a consolidated basis, the Chinese operations hit the bottom line hard as PAT slipped 3.7% yoy to Rs 613m even as net sales grew a healthy 47.3% to Rs 11.1bn.</p> <p>The poor outlook in major CV markets, coupled with the deep losses in China, forces us to lower our PAT estimates 19.2% for FY08. At the current market price, the stock is available at a valuation of 28.1x FY08E EPS of Rs 12.1. We downgrade to <b>UNDER PERFORMER</b>.</p>	
52-Week High/Low:	Rs 396 / 221		
Bloomberg Code:	BHFC@IN		
Reuters Code:	BFRG.BO / NS		
Shares O/s:	222m		
Average Volume (3 months):	0.5m		
Price Performance			
(%)	1m	3m	12m
Absolute	4.1	3.4	(2.5)
Relative to Sensex	0.3	0.3	(36.1)

## Q4 FY07 Result Overview

(Rs m)

Y/e March	Q4 FY07	Q4 FY06	YoY Gr. (%)	Q3 FY07	FY06	FY07	YoY Gr. (%)
<b>Net Sales</b>	<b>5,161</b>	<b>4,384</b>	<b>17.7</b>	<b>4,771</b>	<b>15,779</b>	<b>18,644</b>	<b>18.2</b>
Raw Material	2,491	2,260	10.2	2,255	7,598	8,634	13.6
Change in Stock	(59)	(60)	(2.4)	(80)	(295)	(225)	
<i>as % of Net Sales</i>	<i>47.1</i>	<i>50.2</i>		<i>45.6</i>	<i>46.3</i>	<i>45.1</i>	
Personnel Cost	280	209	34.0	278	917	1,077	17.4
<i>as % of Net Sales</i>	<i>5.4</i>	<i>4.8</i>		<i>5.8</i>	<i>5.8</i>	<i>5.8</i>	
Mfgr. Expenses	849	675	25.8	838	2,535	3,223	68,814
<i>as % of Net Sales</i>	<i>16.5</i>	<i>15.4</i>		<i>17.6</i>	<i>16.1</i>	<i>17.3</i>	
Other Expenses	356	247	44.0	242	1,128	1,259	11.7
<i>as % of Net Sales</i>	<i>6.9</i>	<i>5.6</i>		<i>5.1</i>	<i>7.1</i>	<i>6.8</i>	
<b>EBITDA</b>	<b>1,243</b>	<b>1,053</b>	<b>18.1</b>	<b>1,239</b>	<b>3,896</b>	<b>4,676</b>	<b>20.0</b>
<i>EBITDA Margin (%)</i>	<i>24.1</i>	<i>24.0</i>		<i>26.0</i>	<i>24.7</i>	<i>25.1</i>	
Depreciation	267	214	24.6	252	730	998	36.6
<b>EBIT</b>	<b>976</b>	<b>839</b>	<b>16.4</b>	<b>987</b>	<b>3,166</b>	<b>3,678</b>	<b>16.2</b>
Net Interest	234	155	50.9	215	548	821	49.9
Non-Operating Income	222	144	54.1	162	531	809	52.3
<b>PBT</b>	<b>965</b>	<b>828</b>	<b>16.5</b>	<b>933</b>	<b>3,149</b>	<b>3,666</b>	<b>16.4</b>
Tax	322	298	8.1	303	1,079	1,211	12.2
<i>Tax Rate (%)</i>	<i>33.4</i>	<i>36.0</i>		<i>32.5</i>	<i>34.3</i>	<i>33.0</i>	
<b>Adj. Profit after Tax</b>	<b>643</b>	<b>530</b>	<b>21.2</b>	<b>630</b>	<b>2,070</b>	<b>2,454</b>	<b>18.6</b>
Extraordinary Expenses	-	-		-	8	45	
<b>Reported Profit</b>	<b>643</b>	<b>530</b>	<b>21.2</b>	<b>630</b>	<b>2,062</b>	<b>2,410</b>	<b>16.9</b>

(Stock price as on May 22, 2007)



## Result highlights

Bharat Forge reported a 17.7% yoy jump in its Q4 FY07 standalone net sales to Rs 5.16bn, aided by a 30% rise in domestic sales and a mere 4.7% exports growth. Absolute EBITDA grew by only 18.1% yoy and hence expanded the margin by a mere 7bp to 24.1%. However, sequentially it was 188bp down. PAT, at Rs 643m, returned a better (21.2%) growth because the tax rate fell from 36% to 33.4%.

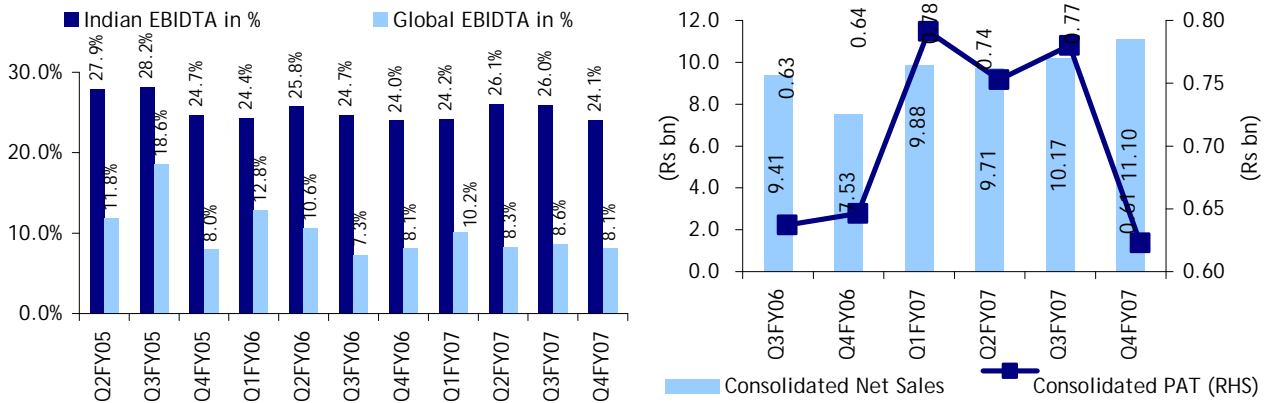
On a consolidated basis, the Chinese operations (JV with FAW) helped boost net sales, which went up by 47.3% to Rs 11.1bn. However, with the capacity utilisation rate at only 38%, the operations were unprofitable. The PAT therefore fell 3.7% yoy to Rs 613m.

For the year, consolidated net sales grew 38.4% to Rs 41.78bn while PAT rose 16% to Rs 2.9bn.

### Consolidated PAT hit by China JV

The Chinese JV, operating at 38% capacity utilisation, was consolidated in the results in Q4 FY07, thereby resulting in the sharp fall in net profit. For the nine months that this JV was operational, it reported net sales of Rs 1.6bn and a Rs 0.23bn loss. The share of BFL in the losses amounted to Rs 0.16bn. These were not entirely unanticipated but, in any case, are yet worrisome. All the more so because the operational losses were Rs 70m and the capacity ramp-up might not entirely erase the operational losses for at least a year.

### Global subsidiaries' net sales bear the brunt of China JV



Source: Company Data, PL Research

### Capacity augmentation is in need of orders

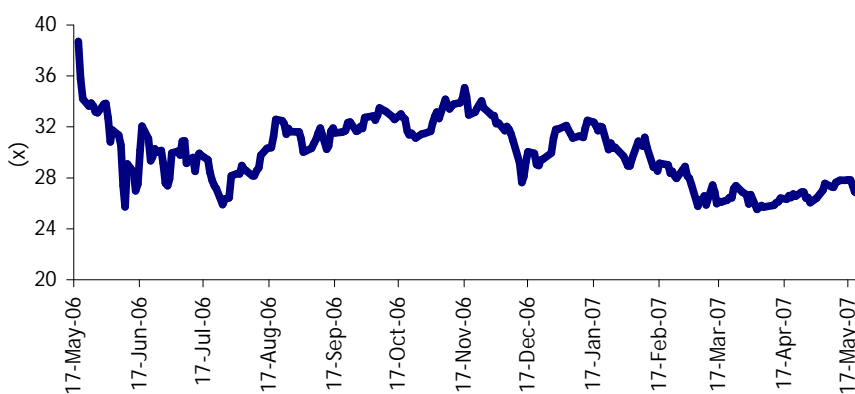
The entire capacity augmentation in India was nearly over by end-Sep.'06, by when BFL had spent Rs 6.69bn of the Rs 6.76bn expended during all of FY07. The enhanced capacity apparently remains under-utilised as its global business was deeply affected by the cyclical downturn. In the post-Q2-FY07-results analyst meet, BFL had revealed that it was in the process of finalising four large orders (each of \$50m) with marquee global customers. Three of them have now been bagged; two of these are in the non-auto segment, for which the company is setting up capacity at a new greenfield site in Baramati at a cost of Rs 3.5bn.



## Valuations

The (standalone) one-year forward rolling P/E chart reveals that the stock traded close to the 25x band for most of the last quarter. The company is attempting to secure orders for its new capacity and has to contend with a cyclical downturn in the US and China. The appreciating rupee too does not help matters on the margin front. With a significant downward revision in earnings and the deep losses in China, we believe that Bharat Forge has limited growth potential next year. At the current market price, the stock is available at a valuation of 28.1x FY08E EPS of Rs 12.1. We downgrade to **UNDER PERFORMER**.

### One-year forward rolling PE - Valuation correction in the offing



Source: Company Data, PL Research

## Key Figures

Y/e March		FY06	FY07E	FY08E	FY09E
Revenue	(Rs m)	15,779	18,644	22,388	30,944
EBITDA	(Rs m)	3,896	4,676	5,608	9,026
Margin	(%)	24.7	25.1	25.0	25.4
PAT	(Rs m)	2,070	2,454	2,907	4,199
EPS	(Rs)	8.6	10.2	12.1	17.5
PER	(x)	39.4	33.3	28.1	19.4
EV / E	(x)	19.5	18.3	15.3	10.4
EV / Sales	(x)	4.8	4.6	3.8	2.6
RoCE	(%)	15.2	12.2	11.8	31.1
RoE	(%)	26.3	18.4	17.6	46.7

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