

October 24, 2009

Rating	Accumulate
Price	Rs272
Target Price	Rs312
Implied Upside	14.7%
Sensex	16,811

(Prices as on October 23, 2009)

Trading Data

Market Cap. (Rs bn)	60.6
Shares o/s (m)	223.0
Free Float	56.0%
3M Avg. Daily Vol ('000)	418.3
3M Avg. Daily Value (Rs m)	101.0

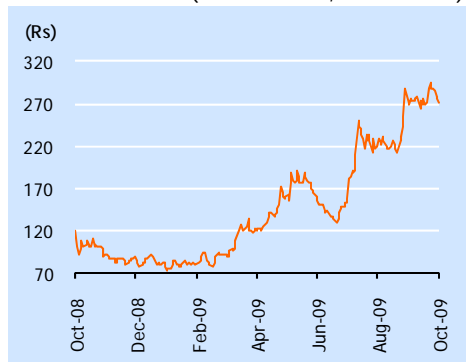
Major Shareholders

Promoters	44.0%
Foreign	11.7%
Domestic Inst.	17.5%
Public & Others	26.8%

Stock Performance

(%)	1M	6M	12M
Absolute	(1.3)	120.4	165.5
Relative	(2.0)	72.0	72.3

Price Performance (RIC: BFRG.BO, BB: BHFC IN)



Source: Bloomberg

■ **Sequential recovery in topline:** Bharat Forge (BFL) reported a sharp 36.7% YoY de-growth in its topline to Rs4.3bn, on account of a 22.2% YoY decline in the domestic revenues at Rs2.9bn. The company also witnessed a slowdown in their exports; exports declined by a 56.3% YoY at Rs1.5bn. However, the silver lining was that the domestic revenues grew by 30.0% and overall revenues grew by 19.2% on a sequential basis. The improvement on the domestic business can be attributed to the consistent MoM improvement in the production schedules of the commercial vehicle (CV) manufacturers. On a sequential basis, the margins improved by 310bps to 24.0%, mainly on account of a pick up in volumes and lower raw material cost. The company reported a forex loss of Rs30m in the current quarter compared to a loss of Rs875m in Q2FY09. Due to lower forex loss this quarter, the reported PBT was higher by 138% YoY. Adjusted for the exceptional item (forex), the company reported 69.8% YoY decline in the adjusted PAT at Rs298m. On a sequential basis, the Adj. PAT grew by 88% because of better operating leverage.

■ **Capacity utilization set to improve with signs of recovery in the CV segment:** In Q1FY10, BFL produced around 22,000 MT which improved in Q2FY10. The company expects improvement in subsequent quarters due to a pick up in the CV segment. Currently, the capacity utilization for the standalone business stands at 30%. With CV players reporting a consistent MoM improvement in the volume numbers, the capacity utilization could reach 50% in FY11E.

■ **Outlook & Valuation:** With signs of recovery visible, one can 'Accumulate' the stock on dips as the restructuring of the subsidiaries will soon be completed and operating leverage will be visible in FY11E. At the peak of the cycle, BFL has traded at a 20x to 30x 1 Yr fwd PE multiple (at a premium to its peers) on account of its sheer size and diversified revenue mix. Assigning a multiple of 25x on FY11E EPS of Rs12.5, we arrive at a target price of Rs312 on the stock, an upside of 14.7% from the current levels.

Key financials (Y/e March)	FY08	FY09	FY10E	FY11E
Revenue (Rs m)	46,523	47,740	35,249	46,973
Growth (%)	11.3	2.6	(26.2)	33.3
EBITDA (Rs m)	7,045	5,565	4,227	7,795
Reported PAT (Rs m)	3,014	583	140	2,998
Adjusted PAT (Rs m)	2,803	1,918	619	2,998
EPS (Rs)	11.7	8.0	2.6	12.5
Growth (%)	(3.5)	(31.6)	(67.7)	384.6
Net DPS (Rs)	3.5	1.0	1.0	1.0

Source: Company Data; PL Research

Profitability & valuation	FY08	FY09	FY10E	FY11E
EBITDA margin (%)	15.1	11.7	12.0	16.6
RoE (%)	19.2	11.6	3.7	16.4
RoCE (%)	11.1	7.2	3.6	9.4
EV / sales (x)	1.5	1.6	2.3	1.7
EV / EBITDA (x)	10.1	14.0	19.0	10.3
PE (x)	23.3	34.1	105.7	21.8
P / BV (x)	3.7	3.7	3.6	3.1
Net dividend yield (%)	1.3	0.4	0.4	0.4

Source: Company Data; PL Research

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Q2FY10 Result Overview (Standalone)

(Rs m)

Y/e March	Q2FY10	Q2FY09	YoY gr. (%)	Q1FY10	H1FY10	H1FY09	YoY gr. (%)
Net Sales	4,276	6,756	(36.7)	3,586	7,862	13,129	(40.1)
Expenditure							
Net Raw material	1,885	3,210	(41.3)	1,626	3,512	6,174	(43.1)
<i>as % of net sales</i>	<i>44.1</i>	<i>47.5</i>		<i>45.3</i>	<i>44.7</i>	<i>47.0</i>	
Personnel Cost	357	383	(6.8)	359	716	766	(6.5)
<i>as % of net sales</i>	<i>8.3</i>	<i>5.7</i>		<i>10.0</i>	<i>9.1</i>	<i>5.8</i>	
Mfgr. Expenses	673	1,101	(38.8)	553	1,226	2,124	(42.3)
<i>as % of net sales</i>	<i>15.7</i>	<i>16.3</i>		<i>15.4</i>	<i>15.6</i>	<i>16.2</i>	
Other Expenses	336	485	(30.6)	299	636	929	(31.6)
<i>as % of net sales</i>	<i>7.9</i>	<i>7.2</i>		<i>8.3</i>	<i>8.1</i>	<i>7.1</i>	
Total Expenditure	3,252	5,178	(37.2)	2,838	6,089	9,992	(39.1)
EBITDA	1,024	1,577	(35.1)	749	1,773	3,137	(43.5)
<i>EBITDA margin (%)</i>	<i>24.0</i>	<i>23.3</i>		<i>20.9</i>	<i>22.6</i>	<i>23.9</i>	
Depreciation	408	389	5.0	384	792	766	3.4
EBIT	616	1,188	(48.2)	365	981	2,371	(58.6)
Net interest	246	236	4.2	254	499	431	15.8
PBT	400	180	122.4	15	415	595	(30.2)
Total tax	132	67	95.8	5	137	216	(36.6)
<i>Total Tax rate %</i>	<i>33</i>	<i>37</i>		<i>33.6</i>	<i>33</i>	<i>36</i>	
Adj. Profit after tax	298	988	(69.8)	158	457	1,947	(76.5)
Extraordinary Expenses	30	875		149	179	1,568	
Reported Profit	268	113	138.3	10	278	378	(26.5)



Key takeaways from management interaction

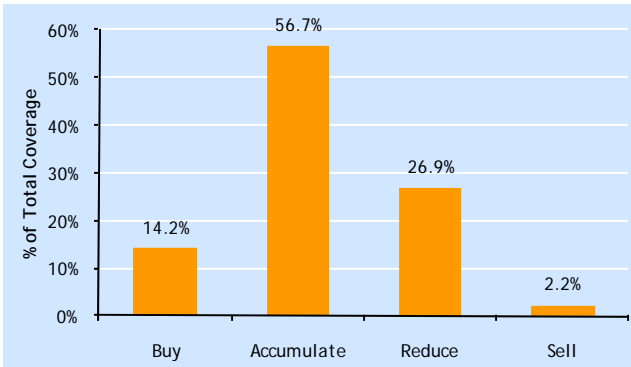
- **New non-auto facilities operating at 20% utilization:** The facilities at the Baramati plant and the open die forge facility in Pune have commenced operations. These plants have an annual forging capacity of 125,000 tpa and will cater mainly to the sectors such as windmills, crankshafts for marine engines and forged components for oil & gas sector. The non-auto segment enjoys an EBITDA margin of 25%+
- **Fund raising of upto US\$150m on cards to fund investments in non-auto segment:** BFL have entered into JVs with Alstom, Areva and NTPC to cater to the requirements of heavy forgings in the power as well as the power equipment sector. The details of the investments would be finalized in the next few months. However, the company has indicated that the investments can be higher which would compel them to raise upto US\$150m through equity/equity-linked instruments, resulting in an equity dilution of ~10-12%.

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Rating Distribution of Research Coverage



PL's Recommendation Nomenclature

BUY	: Over 15% Outperformance to Sensex over 12-months	Accumulate	: Outperformance to Sensex over 12-months
Reduce	: Underperformance to Sensex over 12-months	Sell	: Over 15% underperformance to Sensex over 12-months
Trading Buy	: Over 10% absolute upside in 1-month	Trading Sell	: Over 10% absolute decline in 1-month
Not Rated (NR)	: No specific call on the stock	Under Review (UR)	: Rating likely to change shortly

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