

Bharat Forge

India Research

MANAGEMENT MEET NOTE

 Bloomberg: BHFC IN
 Reuters: BRFG.BO

BUY

Recently we met the Management of Bharat Forge (BFL). We expect BFL to report 15.4% sales CAGR and 16.6% PAT CAGR over FY18-20E. At CMP of Rs501, BFL stock is quoting at PE of 20.1x FY20 earnings. We upgrade the stock from HOLD to BUY rating with a revised price target of Rs589 (PE of 24x FY20E – 5% discount to its 7 years 12M forward PE). Following are the meeting key take ways:

Export CV Business Outlook (~24% of sales): BFL supplies engine and chassis components for CV applications across North America, EU and Asia. US Class 8 market contributes ~15% to its sales. Management highlighted that this year US Class 8 volumes (YTD 4.9L) have been exceptionally high and likely to be normalized over the next 3-4 months. Past trends suggest that US class 8 market typically bottoms out at ~2.2L and peaks at ~3.5L on yearly basis. Despite near term slowdown in its user market, Management expects BFL to perform better than the underlying market as it anticipates its content per vehicle to improve over the next 2-3 years on account of new product development and supply to its customers.

Export Industrial Business Outlook (~26% of sales): Under this segment, BFL generates ~15% of its overall sales Oil and Gas business. Currently this business is pre-dominantly single product. Recently BFL has added new customer in this segment wherein supply ramp up is expected in FY20. With new customer additions and new product development the Company intends to increase Oil & Gas business contribution from the current levels over the next 3-4 years. Other businesses within the industrial segment are anticipated to grow in line with end markets.

Export PV business (~5% of sales): BFL supplies engine components to passenger vehicles in the export markets. Currently the Company is supplying forged components which will be machined going ahead. This business is expected to maintain its growth momentum.

Domestic CV (~20% of sales): Under this segment, BFL supplies engine and chassis components to Indian MHCV market. Management believes that though MHCV numbers were weak in recent months, FY20 is likely to be a positive growth year on account of pre-buying due to emission norm changes.

Key Financials:

Y/E (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Net sales	43,338	38,647	53,160	63,878	70,738
EBIDTA	13,168	10,726	15,368	18,338	20,379
Margin (%)	30.4	27.8	28.9	28.7	28.8
PAT	7,018	5,471	8,405	10,413	12,115
YoY %	1.8	(22.1)	53.6	23.9	16.3
EPS (Rs)	15.1	11.7	18.0	22.4	26.0
ROCE (%)	15.0	10.8	14.1	15.6	16.3
ROE (%)	19.7	13.9	19.0	20.5	20.0
PE (x)	34.8	44.6	29.0	23.4	20.1

Source: Karvy Stock Broking

Recommendation

CMP:	Rs501
Target Price:	Rs589
Previous Target Price	Rs650
Upside (%)	17.6%

Stock Information

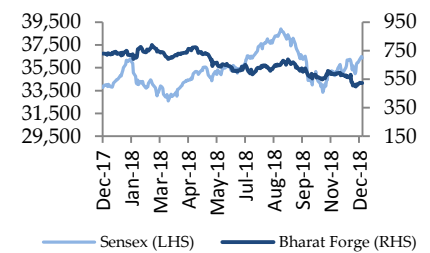
Market Cap. (Rsbn / US\$ mn)	243/3,468
52-week High/Low (Rs)	799.7/488.1
3m ADV (Rsmn / US\$ mn)	890/13
Beta	1.0
Sensex/ Nifty	36,432/10,952
Share outstanding (mn)	466

Stock Performance (%)

	1M	3M	12M	YTD
Absolute	(9.6)	(18.4)	(28.7)	(28.7)
Rel. to Sensex	(12.0)	(16.8)	(33.9)	(33.4)

Performance

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Source: Bloomberg

Earnings Revision

(%)	FY19E	FY20E
Revenue	↓ 1.1	↓ 4.9
EBITDA	↓ 1.1	↓ 4.9
PAT	↓ 4.6	↓ 10.6

Source: Karvy Stock Broking

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Currency Depreciation –Neutral Impact: BFL generates ~55% of its sales from international market. On account of recent rupee depreciation, the Company is not expecting major benefit in the form of new business orders in the near term as its business activities are guided by new product development and long term contracts. Hence management does not anticipate major benefit in terms of new business or margin expansion in the near term. It hedges its receivables based on 12 month forward rolling basis.

Capacity Expansion and New plant: Currently BFL's forging capacity stands at ~410,000 MT and it is operating at ~85% utilization. It can add further capacity at its Baramati facility. The company is setting up a new facility at Nellore, Andhra Pradesh known as Centre for Light weighting for applications across Autos and Industrials. This plant is expected to be operational in Q1FY20. Full impact of this is likely to be seen in FY21.

Defence and Aerospace: In the near term, BFL is witnessing slow ramp-up in its domestic defence orders and international aerospace business. However management remains highly optimistic about the growth prospects in both these segments in the medium term.

Earning revision downwards: To factor in recent slackness in US class 8 market and Indian MHCV market and slow ramp up in defence and aerospace division, we have revised our sales and PAT estimates downwards by 1.1%/4.9% and 4.6%/10.6% for FY19 and FY20 respectively. We anticipate BFL's sales momentum to remain soft over the next two quarters and pick-up is expected post Q4FY19. We expect BFL to report 15.4% volume, 15.4% sales and 16.6% PAT CAGR over FY18-20E.

Upgrade to BUY: At CMP of Rs501, BFL stock is quoting at PE of 20.4x FY20 earnings. We upgrade the stock from HOLD to BUY rating with a revised price target of Rs589 (PE of 24x FY20E – 5% discount to its 7 years 12M forward PE).

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Exhibit 1: Revision in Estimates

Old (Rs Mn)	FY19E	FY20E
Sales	64,559	74,375
EBITDA	18,534	21,426
Margins (%)	28.7%	28.8%
PAT	10,541	12,798
EPS (Rs)	22.6	27.5
Volumes (Nos)	2,98,341	3,40,297
New Estimates (Rs Mn)	FY19E	FY20E
Sales	63,878	70,738
EBITDA	18,338	20,379
Margins (%)	28.7%	28.8%
PAT	10,051	11,435
EPS (Rs)	21.6	24.6
Volumes (Nos)	2,98,149	3,30,169
Variance (%)	FY19E	FY20E
Sales	-1.1%	-4.9%
EBITDA	-1.1%	-4.9%
Margins (bps)	0.00-	0.00
PAT	-4.6%	-10.6%
EPS	-4.6%	-10.6%
Volumes	-0.1%	-3.0%

Source : Karvy Stock Broking

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Financials

Exhibit 2: Income Statement

Y/E Mar (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Net Sales	43,338	38,647	53,160	63,878	70,738
YoY (%)	(4.7)	(10.8)	37.6	20.2	10.7
Raw Material Cost	14,894	13,205	18,870	22,802	25,181
Employee Cost	3,725	3,759	4,359	5,238	5,800
SGA cost	11,551	10,956	14,563	17,499	19,378
Total expenses	30,170	27,921	37,792	45,539	50,359
EBIDTA	13,168	10,726	15,368	18,338	20,379
Margins (%)	30.4	27.8	28.9	28.7	28.8
Depreciation	3,085	2,949	3,068	3,486	3,753
EBIT	10,084	7,777	12,300	14,852	16,625
Interest	905	728	848	951	853
Other Income	1,123	995	1,187	1,212	1,423
PBT	10,302	8,045	12,639	15,114	17,196
(-) Tax	3,284	2,574	4,234	5,063	5,760
Tax/ PBT	31.9	32.0	33.5	33.5	33.5
PAT	7,018	5,471	8,405	10,051	11,435
YoY (%)	1.8	(22.1)	53.6	19.6	13.8

Source: Company, Karvy Stock Broking

Exhibit 3: Balance sheet

Y/E Mar (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Equity Capital	931	931	931	931	931
Reserves	35,473	41,388	45,212	54,053	64,113
Net worth	36,405	42,319	46,143	54,985	65,044
Loans	14,614	16,980	20,764	17,264	13,764
Def Tax Liability	1807	2772	2545	2545	2545
Total Liabilities	52,826	62,072	69,451	74,793	81,353
Gross Block	45,728	52,153	56,764	60,764	65,764
Acc. Depreciation	24,054	28,420	31,488	34,974	38,727
Net block	21,673	23,733	25,276	25,790	27,037
CWIP	2,721	3,743	3,024	3,024	3,024
Investments	14,298	17,721	21,854	21,854	21,854
Inventories	5,254	4,265	5,381	9,342	10,454
Debtors	5,765	13,799	18,142	19,191	21,252
Cash	3,747	2,782	1,877	2,922	5,849
Other Current Assets	4040	10431	7869	9455	10470
Loans and Advances	5,676	296	238	286	316
Current Assets	24,482	31,573	33,505	41,195	48,341
Current Liabilities	9,503	13,947	13,436	16,141	17,875
Provisions	846	751	773	928	1,028
Net Current Assets	14,134	16,875	19,297	24,125	29,438
Total Assets	52,826	62,072	69,451	74,793	81,353

Source: Company, Karvy Stock Broking

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Exhibit 4: Cash Flow Statement

Y/E Mar (Rs mn)	FY16	FY17	FY18	FY19E	FY20E
Net profit	6,976	5,851	7,073	10,051	11,435
Depreciation	3,085	2,949	3,068	3,486	3,753
Deferred tax	153	(26)	72	0	0
Change in working cap	4,141	(3,706)	(3,327)	(3,783)	(2,386)
Cash from Operations	14,354	5,067	6,885	9,755	12,803
Capex	(6,241)	(5,039)	(4,192)	(4,000)	(5,000)
Investments	(3,261)	(3,423)	(4,133)	0	0
Cash from Investments	(9,502)	(8,462)	(8,324)	(4,000)	(5,000)
Free Cash Flow	8,113	28	2,693	5,755	7,803
Dividend	(3,222)	(841)	(851)	(1,209)	(1,376)
Fresh equity	(1,891)	905	(2,398)	0	0
Debt	(1,910)	2,366	3,784	(3,500)	(3,500)
Cash from Financing	(7,024)	2,430	534	(4,709)	(4,876)
Net change in cash	(2,171)	(965)	(905)	1,045	2,927
Opening cash	5,918	3,747	2,782	1,877	2,922
Closing cash	3,747	2,782	1,877	2,922	5,849

Source: Company, Karvy Stock Broking

Exhibit 5: Ratios

Key Ratios	FY16	FY17	FY18	FY19E	FY20E
EPS (Rs)	15.1	11.7	18.0	21.6	24.6
Book Value (Rs)	78.2	90.9	99.1	118.1	139.7
DPS (Rs)	5.7	1.5	1.5	2.2	2.5
P/E (x)	34.8	44.6	29.0	23.3	20.4
EV/EBDITA (x)	19.4	24.1	17.1	13.5	11.9
P/B (x)	6.7	5.8	5.3	4.3	3.6
Div Yield (%)	1.1%	0.3%	0.3%	0.4%	0.5%
ROCE (%)	15.0%	10.8%	14.1%	15.3%	15.7%
ROE (%)	19.7%	13.9%	19.0%	19.9%	19.1%
Debt-Equity (x)	0.4	0.4	0.4	0.3	0.2
Current Ratio (x)	2.4	2.1	2.4	2.4	2.6
Gross Asset Turnover (x)	1.0	0.8	1.0	1.1	1.1
Working Capital Days	105	116	108	110	116
W/C % of sales (%)	24%	36%	33%	33%	33%

Source: Company, Karvy Stock Broking

Stock Ratings	Absolute Returns
Buy	> 15%
Hold	5-15%
Sell	< 5%

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Disclosures Appendix

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