

Beat estimates, Improved outlook

- Bharat Forge's (BFL) reported 1Q numbers above estimates. Consolidated revenues declined 50% YoY to Rs11.5b and EBITDA loss stood at Rs.141mn. (vs est. loss Rs 914mn).
- The management highlighted that recovery is encouraging across segments, and guided domestic revenues to be flat YoY in 2Q. However, export numbers expected to be slightly lower due to weakness persist in Oil & Gas segment.
- The company has accelerated the cost reduction measures (saving manpower & energy costs, consolidation of production facilities and digitization) which benefit was visible in Q1FY21; this will continue in next three quarters for FY21.
- Notwithstanding the adverse impact of the covid-19 disruption in the near term, we remain positive on BFL's growth prospects on the back of improving outlook for class 8 trucks, recovery in demand of construction & mining equipment, focus on diversification (improving long term revenue prospects for PVs, Defence and Railways segments) and the cost optimization initiatives. BFL's focus on balance sheet and re-structuring of cost across plants will help tide over the COVID-led disruption.
- As capacity utilization, which is now below 60%, impacted by the slowdown across verticals and geographies, the company has enough bandwidth to expand margins once utilization ramps up. We increase our EPS estimates by 25/34/30% for FY21/22/23E factoring in improving demand recovery across segment and cost control measures. AT CMP, the stock is trading at 28/20x our FY22E/FY23E EPS, versus the historical mean of 29x. We recommend Accumulate the stock, with a TP of Rs 477 (22x FY23E EPS).

Recovery expected from 2Q

Outlook appears encouraging for forthcoming quarters led by cyclical recovery in class 8 trucks order book, recovery in demand of construction & mining equipment, and incremental revenue inflow from segments, including defence and railways. (Cont..)

Q1FY21 Result (Rs Mn)

Particulars	Q1FY21	Q1FY20	YoY (%)	Q4FY20	QoQ (%)
Revenue	11,542	23,279	(50.4)	17,419	(33.7)
Total Expense	11,683	19,174	(39.1)	15,938	(26.7)
EBITDA	(141)	4,104	(103.4)	1,481	(109.5)
Depreciation	1,385	1,382	0.2	1,457	(4.9)
EBIT	(1,527)	2,722	(156.1)	24	(6384.5)
Other Income	450	449	0.2	537	(16.1)
Interest	368	455	(19.2)	462	(20.4)
EBT	(1,444)	2,716	(153.2)	(414)	248.5
Tax	(190)	941	(120.1)	57	(429.8)
RPAT	(1,258)	1,731	(172.7)	(720)	74.9
APAT	(1,258)	1,731	(172.7)	(207)	509.4
			(bps)		(bps)
Gross Margin (%)	52.7	57.3	(463)	54.1	(140)
EBITDA Margin (%)	(1.2)	17.6	NA	8.5	NA
NPM (%)	(10.9)	7.4	NA	(4.1)	NA
Tax Rate (%)	13.1	34.6	NA	(13.9)	NA
EBIT Margin (%)	(13.2)	11.7	NA	0.1	NA

CMP	Rs 435
Target / Upside	Rs 477 / 10%
BSE Sensex	38,354
NSE Nifty	11,308

Scrip Details

Equity / FV	Rs 931mn / Rs 2
Market Cap	Rs 202bn
	US\$ 3bn
52-week High/Low	Rs 534/Rs 208
Avg. Volume (no)	36,51,130
NSE Symbol	BHARATFORG
Bloomberg Code	BHFC IN

Shareholding Pattern Jun'20(%)

Promoters	45.8
MF/Banks/FIs	15.2
FII	21.2
Public / Others	17.8

Valuation (x)

	FY21E	FY22E	FY23E
P/E	71.3	27.7	20.1
EV/EBITDA	24.1	14.2	11.1
ROE (%)	5.4	13.0	16.1
RoACE (%)	4.9	9.8	12.4

Estimates (Rs mn)

	FY21E	FY22E	FY23E
Revenue	67,325	82,494	97,607
EBITDA	9,244	15,614	19,772
PAT	2,839	7,309	10,091
EPS (Rs.)	6.1	15.7	21.7

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Moreover, The PV segment is likely to continue to outpace the underlying industry performance led by expansion of product portfolio, upward shift in value chain and addition of new customers. However, a challenging demand environment in the US Oil & Gas segment weighs on earnings.

The management highlighted that an import ban on 101 defense items is a good step taken by Govt. The company has completed 3-4 sets of trials for artillery guns three-guns are in the advanced stage of testing and one in the final stage. Initially the company to produce 50 artillery guns and may ramp up production to 150 guns in a year.

Conference call highlights:

- Demand recovery in domestic's market is encouraging especially in the area of Agriculture, Construction & Mining, Industrial and Passenger car segment. Excluding Oil & gas segment recovery in export is also decent.
- Management expect domestic revenues to be flat as compared to Q2 FY20 due to addition of new customers in Agriculture/ Industrial and Passenger car segment, however export revenue to be lower than Q2FY20 owing to weakness persist in Oil& Gas segment.
- Heavy trucks and PVs in Europe are on the recovery path, visibility for class 8 truck order has improved for current and next year as well.
- April & May month was completely washed out due to lockdown, started production in the month of June, capacity utilization was at 20% in 1Q.
- At present due to weak oil prices financing is not available for drilling activity, However, Management expects if oil prices stabilize near \$42 for a couple of months then drilling activity will pick up.

Defence:

- Import ban on 101 defence item is a good step taken by Govt. and recognizes the capabilities within the country and beneficial for companies like Bhart forge.
- The company has completed 3-4 set of trials for artillery guns three- guns are in advance stage of testing and one in the final stage. Once the last set of trail is completed Bhart forge will get better clarity of timing of the order. Once order is placed, the company can start delivery in 2-3 months and can ramp up significantly over 5-6 months.
- Initially the company to produce 50 artillery guns and may ramp up production to 150 guns in a year.
- In domestic market forging and sale of artillery guns will be done through Bharat forge and for export it will be done through KSSL, however all components and value addition will be done by Bharat forge only.

Aerospace:

- Commercial aerospace manufacturing has reduced significantly, however replacement part demand is on traction. The Company expects revenue of \$85-100mn over the next 2-3 years from aerospace in the area of 1) Commercial Manufacturing; 2) Engine supply and 3) Replacement parts.

International business:

- Expansion in German plant has been commissioned successfully (Aluminum product for Hybrid and Electric Cars) and currently it is in the under trial production phase, it will take 2 years to reach full capacity. 80% of salary is being paid by the government currently, this help to avoid layoff of employees.
- Heavy truck and passenger car segments both are recovering well in Europe.
- In Jan-March, quarter international subsidiaries posted a loss of Rs.360mn and expected to report a cash loss of ~5mn euro in the first half.

Others :

- Nellore plant's commissioning has been done and expects revenue of ~Rs.2bn over 2-3 years.
- Export Non-auto (Ex-Oil&Gas) segment has done well due to higher demand from construction & mining equipment, large diesel engines and power generation equipment. Further, an increase in infrastructure spending in the US will help to improve the segment revenue going forward.

Exhibit 1: Actual vs Dart

Particulars (Rs mn)	Actual	Dart Estimates	VAR (%)	Comments
Revenue	11,542	5,500	110	Better than expected performance across segment(Ex oil& Gas)
EBIDTA	(141)	(914)	-85	Due to efficient cost control measures
EBIDTA Margin (%)	(1.22)	(16.62)	NA	
APAT	(1,258)	(1,931)	NA	

Source: Company, DART

Exhibit 2: Changes in estimates

Rs Mn	FY21E			FY22E		
	New	Previous	Chg (%)	New	Previous	Chg (%)
Revenue	67,325	68,095	(1.1)	82,494	78,519	5.1
EBITDA	9,244	8,762	5.5	15,614	13,432	16.2
EBITDA Margin (%)	13.7	12.9	86.3bps	18.9	17.1	182.1 bps
APAT	2,839	2,275	24.8	7,309	5,458	33.9
EPS (Rs)	6.1	4.9	24.8	15.7	11.7	33.9

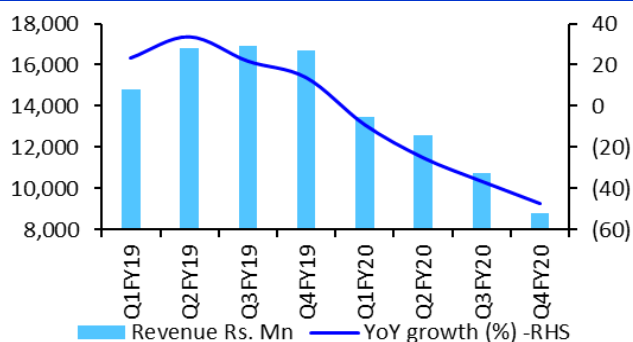
Source: Company, DART

Exhibit 3: Standalone revenue assumption

Segment Rs mn	FY18	FY19	FY20	FY21E	FY22E	FY23E
Commercial Vehicle	23,423	26,860	17,884	13,718	19,576	26,914
YoY growth (%)	31	15	(33)	(23)	43	37
Passenger Vehicle	5,138	7,248	7,310	6,956	8,347	9,430
YoY growth (%)	29	41	1	(5)	20	13
Non-Auto Segment	21,505	26,589	16,811	14,638	17,069	20,252
YoY growth (%)	46	24	(37)	(13)	17	19
Other revenues	3,660	4,497	3,634	3,533	4,062	4,458
YoY growth (%)	(12)	23	(19)	(3)	15	10
Subtotal Standalone	53,725	65,194	45,638	38,845	49,054	61,054
YoY growth (%)	32	21	(30.0)	(14.9)	26.3	24.5

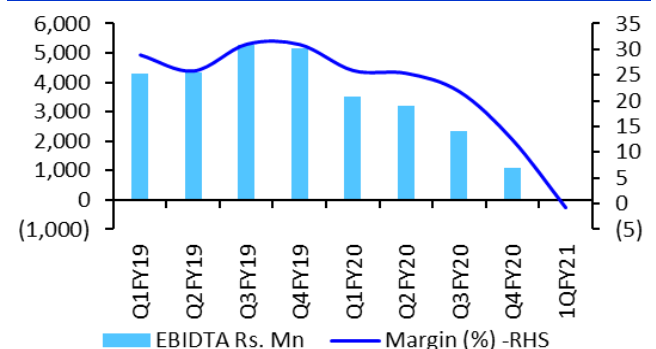
Source: DART, Company

Exhibit 4: (Std.) Revenue declined due to lockdown



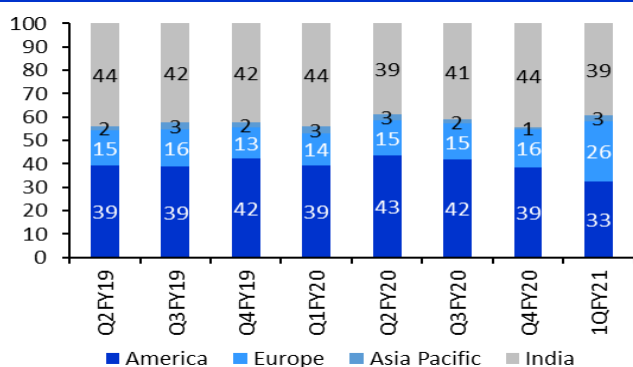
Source: DART, Company

Exhibit 5: (Std.) EBIDTA turned negative



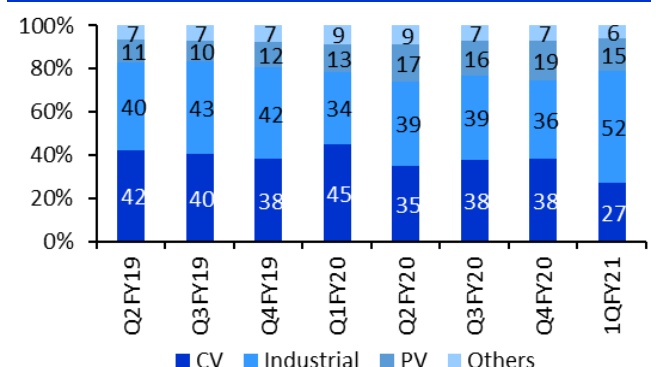
Source: DART, Company

Exhibit 6: Geography mix (%)



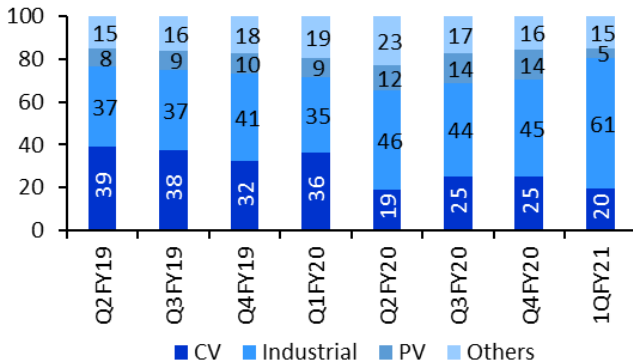
Source: DART, Company

Exhibit 7: Segment mix (%)



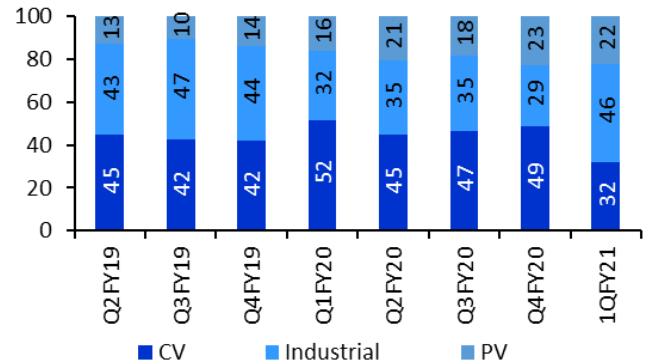
Source: DART, Company

Exhibit 8: India: CV revenue under pressure (%)



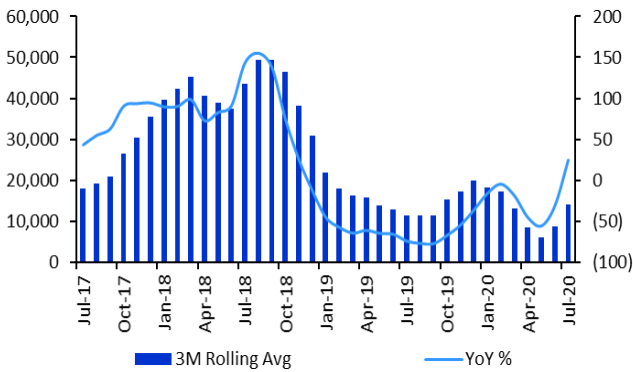
Source: DART, Company

Exhibit 9: International business performance (%)



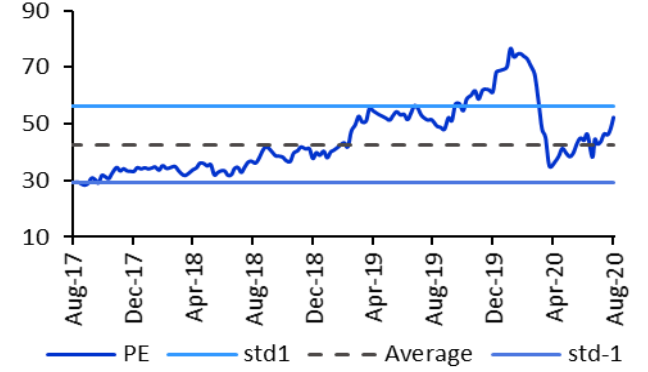
Source: DART, Company

Exhibit 10: Class 8 truck net order rebound sharply



Source: DART, Company

Exhibit 11: 1 yr fw/PE band



Source: DART, Company

Profit and Loss Account (Conso.)

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
Revenue	80,558	67,325	82,494	97,607
Total Expense	69,411	58,081	66,881	77,834
COGS	35,765	30,715	35,615	41,433
Employees Cost	11,955	10,022	11,312	12,923
Other expenses	21,691	17,345	19,953	23,478
EBIDTA	11,147	9,244	15,614	19,772
Depreciation	5,477	5,759	6,275	6,877
EBIT	5,670	3,485	9,338	12,896
Interest	1,713	1,528	1,504	1,513
Other Income	1,879	1,973	2,071	2,175
Exc. / E.O. items	(789)	0	0	0
EBT	5,046	3,930	9,905	13,557
Tax	1,125	990	2,496	3,416
RPAT	3,498	2,839	7,309	10,091
Minority Interest	(6)	1	0	0
Profit/Loss share of associates	(429)	(100)	(100)	(50)
APAT	4,287	2,839	7,309	10,091

Balance Sheet (Conso.)

(Rs Mn)	FY20A	FY21E	FY22E	FY23E
Sources of Funds				
Equity Capital	931	931	931	931
Minority Interest	320	320	320	320
Reserves & Surplus	51,266	52,475	57,689	65,451
Net Worth	52,197	53,406	58,620	66,383
Total Debt	38,784	36,284	32,785	29,287
Net Deferred Tax Liability	506	506	506	506
Total Capital Employed	91,807	90,516	92,230	96,495

Applications of Funds

Net Block	38,659	37,458	37,254	37,449
CWIP	11,427	11,427	11,427	11,427
Investments	7,410	7,410	7,410	7,410
Current Assets, Loans & Advances	57,619	54,812	59,492	66,867
Inventories	17,347	13,885	15,612	18,163
Receivables	14,939	14,756	18,081	21,393
Cash and Bank Balances	16,412	15,521	13,081	12,117
Loans and Advances	557	613	674	742
Other Current Assets	8,364	10,036	12,044	14,453
Less: Current Liabilities & Provisions	23,307	20,591	23,352	26,658
Payables	10,309	9,425	10,928	12,714
Other Current Liabilities	12,997	11,166	12,424	13,944
sub total				
Net Current Assets	34,312	34,221	36,140	40,209
Total Assets	91,807	90,515	92,230	96,495

E – Estimates

Important Ratios

Particulars	FY20A	FY21E	FY22E	FY23E
(A) Margins (%)				
Gross Profit Margin	55.6	54.4	56.8	57.6
EBIDTA Margin	13.8	13.7	18.9	20.3
EBIT Margin	7.0	5.2	11.3	13.2
Tax rate	22.3	25.2	25.2	25.2
Net Profit Margin	4.3	4.2	8.9	10.3
(B) As Percentage of Net Sales (%)				
COGS	44.4	45.6	43.2	42.4
Employee	14.8	14.9	13.7	13.2
Other	26.9	25.8	24.2	24.1
(C) Measure of Financial Status				
Gross Debt / Equity	0.7	0.7	0.6	0.4
Interest Coverage	3.3	2.3	6.2	8.5
Inventory days	79	75	69	68
Debtors days	68	80	80	80
Average Cost of Debt	4.5	4.1	4.4	4.9
Payable days	47	51	48	48
Working Capital days	155	186	160	150
FA T/O	2.1	1.8	2.2	2.6
(D) Measures of Investment				
AEPS (Rs)	9.2	6.1	15.7	21.7
CEPS (Rs)	21.0	18.5	29.2	36.4
DPS (Rs)	2.0	3.5	4.5	5.0
Dividend Payout (%)	21.7	57.4	28.7	23.1
BVPS (Rs)	112.1	114.7	125.9	142.6
RoANW (%)	6.6	5.4	13.0	16.1
RoACE (%)	6.9	4.9	9.8	12.4
RoAIC (%)	7.2	4.6	12.1	15.8
(E) Valuation Ratios				
CMP (Rs)	435	435	435	435
P/E	47.2	71.3	27.7	20.1
Mcap (Rs Mn)	2,02,458	2,02,458	2,02,458	2,02,458
MCap/ Sales	2.5	3.0	2.5	2.1
EV	2,24,830	2,23,221	2,22,162	2,19,628
EV/Sales	2.8	3.3	2.7	2.3
EV/EBITDA	20.2	24.1	14.2	11.1
P/BV	3.9	3.8	3.5	3.0
Dividend Yield (%)	0.5	0.8	1.0	1.2
(F) Growth Rate (%)				
Revenue	(20.6)	(16.4)	22.5	18.3
EBITDA	(45.8)	(17.1)	68.9	26.6
EBIT	(63.1)	(38.5)	167.9	38.1
PBT	(68.7)	(22.1)	152.0	36.9
APAT	(58.5)	(33.8)	157.5	38.1
EPS	(58.5)	(33.8)	157.5	38.1
Cash Flow				
(Rs Mn)	FY20A	FY21E	FY22E	FY23E
CFO	16,008	7,354	8,658	11,273
CFI	(11,322)	(2,097)	(5,000)	(5,897)
CFF	(3,814)	(6,233)	(7,099)	(7,340)
FCFF	6,437	4,284	2,587	4,201
Opening Cash	10,965	16,412	15,521	13,081
Closing Cash	16,412	15,521	13,081	12,117

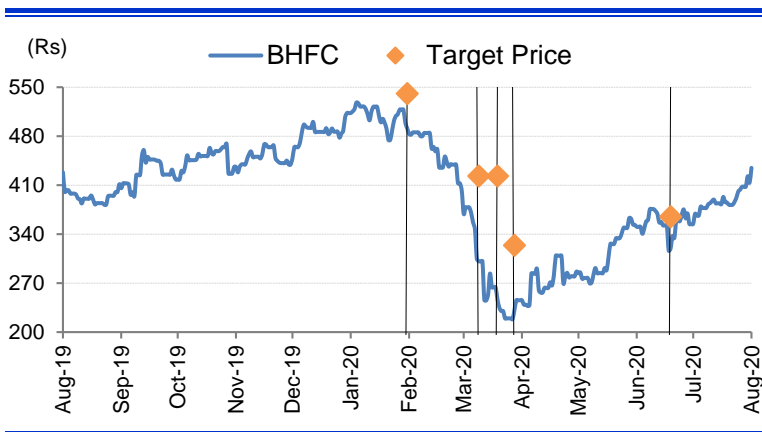
E – Estimates

DART RATING MATRIX

Total Return Expectation (12 Months)

Buy	> 20%
Accumulate	10 to 20%
Reduce	0 to 10%
Sell	< 0%

Rating and Target Price History



Month	Rating	TP (Rs.)	Price (Rs.)
Feb-20	Accumulate	541	491
Mar-20	Buy	423	301
Mar-20	Buy	423	246
Apr-20	Buy	324	232
Jun-20	Accumulate	365	319

**Price as on recommendation date*

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