

Growth challenges remain, cost delivery encouraging

Bharat Forge (BFL) reported a weak Q1FY21 performance. Standalone revenues fell 68.3% YoY to ₹ 427 crore tracking 70.7% YoY tonnage drop to 17,840 MT. Total India revenues were at ₹ 167.8 crore (down 71.7% YoY; CV down 84.7%, PV down 85.8%, industrial down 51.2%). On the international side, PV revenues de-grew 52.6% while CV revenues fell 78.9%, industrial revenues fell 50.7%. Among geographies, Americas posted 74% revenue fall while the drop was more contained in Europe (down 41%). Standalone EBITDA was at negative ₹ 3 crore, with margin performance likely impacted by inventory adjustment. Reported standalone loss at PAT level was at ₹ 56.3 crore, supported by higher other income. At the consolidated level, the company reported ₹ 1.9 crore as share in loss at subsidiaries/associates, down sharply from loss of ₹ 21.4 crore in the previous quarter.

Defence opportunity may quicken CV de-risking

BFL has over the years worked on reducing dependence on cyclical CV industry, both in its India, global operations. Segmental standalone revenue mix for FY20 was at ~39% CV, ~37% industrial, ~16% PV, ~8% others. Poor volume performance, outlook in key CV markets (India, US) in medium-term puts further impetus on de-risking efforts. With subdued mining & construction activity (sluggish economic activity globally), relatively lower crude oil price levels complicating demand picture on the industrial side, PV domain at present is sole bright spot. The recent government decision to impose import embargo on 101 defence products, however, is expected to aid BFL's diversification drive. Localisation impetus in the company's product suit (artillery guns, armoured vehicles, electronic components, etc) is seen leading to rapid growth in division – albeit from FY22E. We factor in 3.2%, 0.7% domestic, export revenue CAGR in FY20P-22E.

Sharp cost focus expected to pay dividends

Despite soft revenue performance during the quarter (~20% capacity utilisation), BFL nearly managed EBITDA breakeven in standalone and consolidated operations. Its focus on reducing breakeven levels by downsizing costs, enhancing efficiencies while simultaneously controlling capex spends is seen leading to improvement in margin trajectory. BFL expects to continue to post sequential improvement in coming quarters and return to previous margin levels on these cost initiatives. We build 17.4% margins by FY22E on structural cost actions, volume uptick in the next year.

Valuation & Outlook

For BFL, we expect 1%, 13.2%, 35% CAGR for consolidated sales, EBITDA, PAT, respectively, in FY20P-22E. Progress on business de-risking from CV, continued margin delivery and improvement in profitability of European subsidiaries remain key monitorables going ahead. We maintain **HOLD** rating on BFL, valuing it at 30x FY22E EPS of ₹ 13.7 for target price of ₹ 415.

Key Financial Summary

Key Financials	FY18	FY19	FY20P	FY21E	FY22E	CAGR (FY20P-22E)
Net Sales	8,357.7	10,145.7	8,055.8	6,589.5	8,216.6	1.0%
EBITDA	1,723.0	2,055.6	1,114.8	803.1	1,428.2	13.2%
EBITDA Margins (%)	20.6	20.3	13.8	12.2	17.4	
Net Profit	754.0	1,032.6	349.2	162.2	636.9	35.0%
EPS (₹)	16.2	22.2	7.5	3.5	13.7	
P/E	26.9	19.6	58.0	124.8	31.8	
RoNW (%)	17.3	19.1	7.8	3.0	11.1	
RoCE (%)	14.9	15.5	5.8	2.2	7.9	

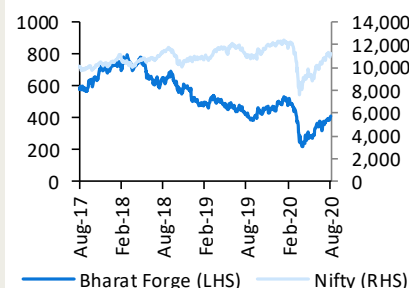
Source: ICICI Direct Research, Company



Particulars

Particular	Amount
Market Capitalization	₹ 20252 Crore
Total Debt (FY 20P)	₹ 4238.2 Crore
Cash and Inv. (FY 20P)	₹ 1641.2 Crore
EV	₹ 22849.3 crore
52 week H/L (₹)	533 / 208
Equity capital	₹ 93.1 Crore
Face value	₹ 2

Price chart



Key Highlights

- Q1FY21 standalone revenues fell 68% YoY tracking 71% drop in tonnage to 17,840 MT. BFL posted marginal loss at EBITDA level on negative operating leverage
- Demand challenges continue to weigh, with softness in CV & Industrial segments continuing. However, defence opportunity could improve pace of de-risking from CVs
- Structural cost initiatives seen leading to improved margins, going forward
- Maintain HOLD with revised target price of ₹ 415

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Exhibit 1: Variance Analysis

	Q1FY21	Q1FY21E	Q1FY20	YoY (%)	Q4FY20	QoQ (%)	Comments
Total Operating Income	427	403	1,347	-68.3	881	-51.5	Revenues ahead of estimates tracking lower than anticipates decline in domestic revenues
Raw Material Expenses	184	151	498	-63.0	325	-43.2	
Employee Expenses	114	98	124	-8.1	119	-4.3	Employee costs were down 8% YoY at ₹ 114 crore
Other Expenses	132	141	375	-64.9	327	-59.8	
EBITDA	-3	12	350	-100.8	110	-102.5	Company reported marginal loss at the EBITDA level against our expectation of marginal profit
EBITDA Margin (%)	-0.7	3.1	26.0	-2661 bps	12.5	-1318 bps	
Depreciation	80.8	88.4	88.6	-8.8	84.7	-4.6	
Interest	29.9	32.4	38.8	-22.9	41.5	-27.9	
Other Income	42	13	40	4.6	31	33.3	Other income came in ahead of estimates
PBT	-71.6	-95.5	262.3	-127.3	-78.3	-8.6	
Tax	-15.3	-24.1	88.1	-117.4	-5.0	204.2	
Reported PAT	-56.3	-71.4	174.2	-132.3	-73.3	-23.2	Loss at the PAT level was ahead of estimates tracking higher other income and partially lower depreciation
Key Metrics							
Domestic revenues	154	111	556	-72.3	370	-58.4	Domestic revenues were down 72% YoY to ₹ 154 crore
Export revenues	259	282	753	-65.6	490	-47.1	Export revenues were down 66% YoY to ₹ 259 crore

Source: Company, ICICI Direct Research

Exhibit 2: Change in estimates

(₹ Crore)	FY21E			FY22E			Comments
	Old	New	% Change	Old	New	% Change	
Revenue	5,854	6,590	12.6	7,522	8,217	9.2	Upgrade our estimates factoring in new client wins at the company as well increase in market share across key segments. On CAGR basis, however, revenues are expected to be largely flat over FY20-22E
EBITDA	580	803	38.5	1,156	1,428	23.5	
EBITDA Margin (%)	9.9	12.2	228 bps	15.4	17.4	201 bps	Upgrade margin estimates amid stringent cost control measures being undertaken both in domestic and international operations
PAT	1	162	NM	465	637	37.0	
EPS (₹)	0.0	3.5	NM	10.0	13.7	37.0	Upgrade in sales and margin estimates leads to sharp upward revision in EPS estimates for FY21E & FY22E

Source: Company, ICICI Direct Research

Exhibit 3: Assumptions

(₹ crore)	Current			Earlier		Comments
	FY18	FY19	FY20P	FY21E	FY22E	
Domestic Revenues	2,227	2,627	1,782	1,514	1,898	We expect revenues to decline 18% YoY in FY21E amid muted demand outlook for CV sales both domestically and globally and muted oil & gas sector outlook. Sales, however, are seen growing 25% in FY22E as cyclical downturn ends as well as global economy stabilises post Covid-19 induced disruption. On a CAGR basis, revenues are seen growing at 1% CAGR in FY20-22E
Export revenues	2,971	3,726	2,650	2,171	2,689	
Americas (\$ mn)	296	369	265	199	248	
Europe (Euro mn)	102	125	87	74	89	
Asia Pac (\$ mn)	21	18	14	9	12	
USD/INR	68.0	70.4	70.6	75.1	75.0	
EUR/US\$	1.2	1.1	1.1	1.1	1.1	

Source: ICICI Direct Research

Conference Call Highlights

Demand and management guidance/outlook

- The company operated at ~20% capacity utilisation in Q1FY21. However, it is witnessing green shoots of demand in every domestic segment ex-CV (agri, PV, industrial) and expects positive growth in these spaces (driven by festive uptick and some changes in consumer behaviour) to lead to flattish YoY revenue performance in Q2FY21E. Overall Q2FY21E revenues, however, would be lower than last year courtesy decline in exports
- International operations ex-oil & gas are expected to be flattish YoY in Q2FY21E, with CV leading the way – especially in Europe
- Net orders on the US Class 8 truck side have trended positively for the past two months. The company is witnessing some traction towards increased demand. Stability of Brent crude oil prices at present levels would improve drilling activity
- Client-side inventory destocking phase in various segments is largely over
- Operations at overseas subsidiaries will continue to be impacted by Covid in the next quarter (consolidated with a quarter's lag)

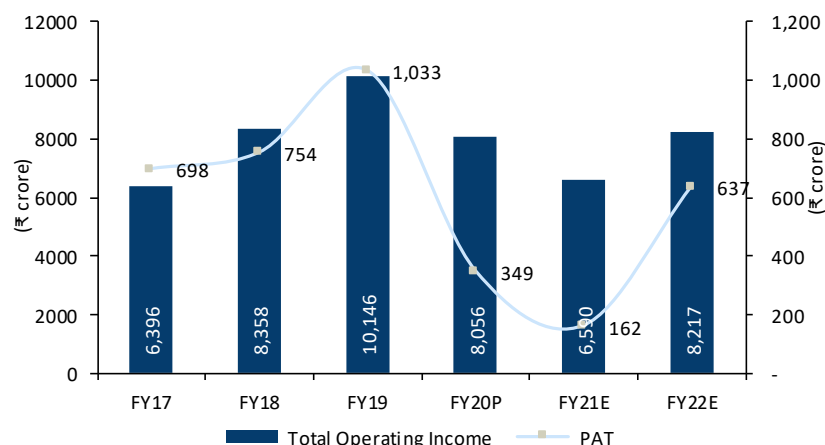
Defence opportunity

- **BFL has developed four programmes in artillery guns, which are currently in advanced trial stages. It would produce and supply these guns for domestic as well as global buyers**
- Guns made, sold for India would be captured in BFL while those for other markets would contain components, systems produced by BFL
- **BFL has the capacity to produce 50/100-150 fully finished artillery guns in the first & second year, respectively. Broad realisation is at ~₹ 12-15 crore/gun**
- Once approved, the company is capable of starting defence deliveries within two months of order placement
- The company is not looking at entering products other than those already on books (artillery guns, armoured and special vehicles, electronics, etc)
- **Incremental defence capex for existing products would total ~₹ 100 crore over the next two years**
- **Earlier guidance on doubling ₹ 500 crore defence revenues (FY19; for small systems and components) by FY23E stands. Revenues from future large orders on account of recent defence related announcements would be over and above this**
- On a longer-term basis, the company views defence as having the potential to grow into a significant division like non-auto business

Others

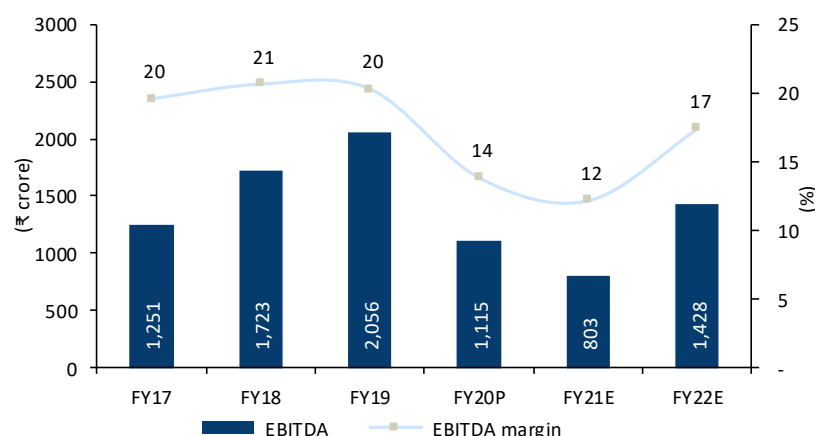
- BFL continues to focus on driving efficiencies and reducing costs. These efforts are set to continue, going forward, and result in further sequential improvement. **It expects margins to go back to previous levels despite reduced sales on account of cost initiatives (staff, travel, marketing, etc)**
- German PV-related expansion is complete (cost €60 million). The plant has been commissioned, with full capacity ramp up likely to take two years. The facility would almost double existing Europe capacity
- BFL expects to clock US\$80-90 million revenues from aerospace division in the next three years

Financial story in charts

Exhibit 4: Top line trend


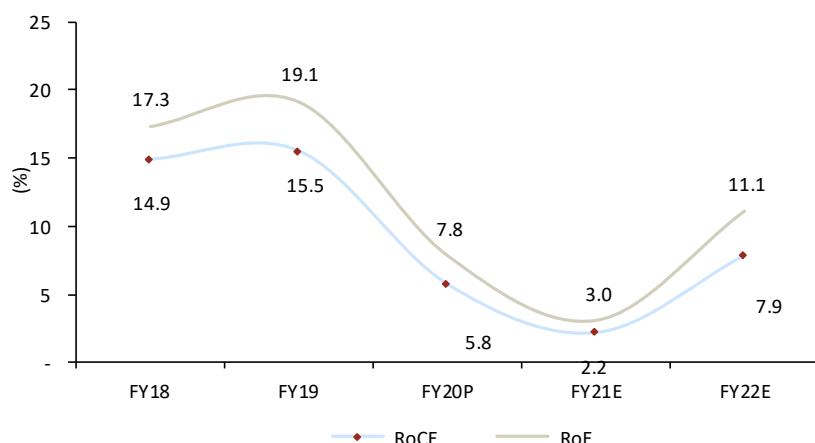
Source: Company, ICICI Direct Research

We expect consolidated sales to grow at 1% CAGR over FY20P-22E to ₹ 8,217 crore amid pressures on CV and oil & gas space. Growth in PAT is expected to be higher as cost initiatives feed into margin improvement at both standalone and consolidated levels

Exhibit 5: EBITDA and EBITDA margin trend


Source: Company, ICICI Direct Research

Margins seen growing to 17% levels by FY22E, aided by structural cost related initiatives and shift in product mix towards aluminium. This would, however, be on the back of a dip during FY21E amid expected negative operating leverage

Exhibit 6: Trend in return ratios


Source: Company, ICICI Direct Research

Return ratios are seen dipping substantially during FY21E before recovering towards 8% mark in the following year backed by rise in margins

Exhibit 7: Segment-wise revenue mix at BFL (standalone)

India Revenues (Segmental Bifurcation)										
Particulars	% Share	Q1FY21 ₹ crore	Q1FY20 ₹ crore	YoY %	Q4FY20 ₹ crore	QoQ %	% Share	FY20 ₹ crore	FY19 ₹ crore	YoY %
Commercial Vehicles	19.7	33.0	215.9	(84.7)	98.3	(66.4)	27.1	518.2	1,094.8	(52.7)
Industrial	60.8	102.0	209.0	(51.2)	177.3	(42.5)	42.1	805.8	1,013.3	(20.5)
Passenger Vehicles	4.5	7.6	53.5	(85.8)	54.2	(86.0)	11.8	226.3	237.3	(4.6)
Others	15.0	25.2	115.3	(78.1)	61.8	(59.2)	19.0	363.4	448.8	(19.0)
Total	100.0	167.8	593.7	(71.7)	391.6	(57.2)	100.0	1,913.7	2,794.2	(31.5)

International Revenues (Segmental Bifurcation)										
Particulars	% Share	Q1FY21 ₹ crore	Q1FY20 ₹ crore	YoY %	Q4FY20 ₹ crore	QoQ %	% Share	FY20 ₹ crore	FY19 ₹ crore	YoY %
Commercial Vehicles	31.7	82.2	389.3	(78.9)	238.8	(65.6)	47.9	1,270.2	1,591.2	(20.2)
Industrial	46.2	119.8	242.9	(50.7)	140.3	(14.6)	33.0	875.3	1,647.1	(46.9)
Passenger Vehicles	22.1	57.2	120.6	(52.6)	110.5	(48.2)	19.0	504.7	487.5	3.5
Total	100.0	259.2	752.8	(65.6)	489.6	(47.1)	100.0	2,650.2	3,725.8	(28.9)

International Revenues (Geographical Bifurcation)										
Particulars	% Share	Q1FY21 ₹ crore	Q1FY20 ₹ crore	YoY %	Q4FY20 ₹ crore	QoQ %	% Share	FY20 ₹ crore	FY19 ₹ crore	YoY %
Americas	53.7	139.3	530.2	(73.7)	339.6	(59.0)	70.5	1,867.3	2,602.2	(28.2)
Europe	42.0	108.9	185.4	(41.3)	142.6	(23.6)	25.8	684.2	991.2	(31.0)
Rest of World	4.2	11.0	37.2	(70.4)	7.4	48.6	3.7	98.7	132.4	(25.5)
Total	100.0	259.2	752.8	(65.6)	489.6	(47.1)	100.0	2,650.2	3,725.8	(28.9)

Source: Company, ICICI Direct Research

Exhibit 8: Key valuation metrics

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY18	8,358	30.7	16.2	8.1	26.9	13.2	17.3	14.9
FY19	10,146	21.4	22.2	37.0	19.6	11.3	19.1	15.5
FY20P	8,056	-20.6	7.5	-66.2	58.0	20.5	7.8	5.8
FY21E	6,590	-18.2	3.5	-53.5	NA	27.7	3.0	2.2
FY22E	8,217	24.7	13.7	NA	31.8	28.4	11.8	11.1

Source: Bloomberg, ICICI Direct Research

Exhibit 9: Shareholding pattern

(in %)	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20
Promoter	45.8	45.8	45.8	45.8	45.8
FII	18.9	19.2	20.5	20.7	22.1
DII	13.5	13.9	15.2	15.7	15.1
Others	21.8	21.1	18.5	17.8	17.0

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 10: Profit and loss statement ₹ crore				
(Year-end March)	FY19	FY20P	FY21E	FY22E
Total operating Income	10145.7	8055.8	6589.5	8216.6
Growth (%)	21.4	-20.6	-18.2	24.7
Raw Material Expenses	4,214.3	3,576.4	2,833.5	3,615.3
Employee Expenses	1,246.3	1,195.5	1,120.2	1,191.4
Other expenses	2,629.5	2,169.1	1,832.7	1,981.7
Total Operating Expenditure	8,090.2	6,941.1	5,786.4	6,788.4
EBITDA	2,055.6	1,114.8	803.1	1,428.2
Growth (%)	19.3	-45.8	-28.0	77.8
Depreciation	520.8	547.7	593.1	657.3
Interest	127.2	171.3	155.5	147.5
Other Income	202.8	187.9	203.2	218.0
PBT	1,610.4	583.6	257.7	841.3
Others	-11	-43	-39	-19
Total Tax	566.4	112.5	56.7	185.1
PAT	1,032.6	349.2	162.2	636.9
Growth (%)	37.0	-66.2	-53.5	292.5
EPS (₹)	22.2	7.5	3.5	13.7

Source: Company, ICICI Direct Research

Exhibit 11: Cash flow statement ₹ crore				
(Year-end March)	FY19	FY20P	FY21E	FY22E
Profit after Tax	1032.6	349.2	162.2	636.9
Add: Depreciation	520.8	547.7	593.1	657.3
(Inc)/dec in Current Assets	-630.3	893.3	527.7	-683.8
Inc/(dec) in CL and Provisions	135.4	-50.7	-345.8	337.8
CF from operating activities	1185.7	1910.8	1092.7	1095.7
(Inc)/dec in Investments	-156.3	-525.8	-250.0	-150.0
(Inc)/dec in Fixed Assets	-1097.7	-1101.3	-200.0	-200.0
Others	-70.4	275.3	-47.9	-165.1
CF from investing activities	-1324.4	-1351.8	-497.9	-515.1
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	262.3	306.0	-350.0	-200.0
Dividend paid & dividend tax	-280.2	-196.1	-93.1	-209.5
Inc/(dec) in Sec. premium	0.0	0.0	0.0	0.0
Others	328.0	-569.3	-155.5	-147.5
CF from financing activities	310.1	-459.3	-598.6	-557.0
Net Cash flow	171.4	99.7	-3.8	23.6
Opening Cash	304.0	475.4	575.1	571.3
Closing Cash	475.4	575.1	571.3	594.9

Source: Company, ICICI Direct Research

Exhibit 12: Balance Sheet ₹ crore				
(Year-end March)	FY19	FY20P	FY21E	FY22E
Liabilities				
Equity Capital	93.1	93.1	93.1	93.1
Reserve and Surplus	5,312.7	5,158.6	5,227.7	5,655.0
Total Shareholders funds	5,405.9	5,251.7	5,320.8	5,748.2
Total Debt	4,022.8	4,238.2	3,888.2	3,688.2
Deferred Tax Liability	270.2	131.1	131.1	131.1
Minority Interest / Others	178.8	228.1	228.1	228.1
Total Liabilities	9,877.7	9,849.0	9,568.2	9,795.5
Assets				
Gross Block	8,636.8	9,426.1	10,076.1	10,526.1
Less: Acc Depreciation	5,047.4	5,595.1	6,188.1	6,845.5
Net Block	3,589.4	3,831.0	3,888.0	3,680.6
Capital WIP	830.7	1,142.7	692.7	442.7
Total Fixed Assets	4,420.1	4,973.7	4,580.6	4,123.3
Investments	1,558.8	1,655.2	2,005.2	2,255.2
Inventory	1,844.7	1,734.7	1,444.3	1,800.9
Debtors	2,147.8	1,493.8	1,263.7	1,575.8
Loans and Advances	2.8	5.2	4.2	5.3
Other Current Assets	527.9	396.1	389.9	404.1
Cash	475.4	575.1	571.3	594.9
Total Current Assets	4,998.6	4,205.0	3,673.5	4,380.9
Creditors	1,366.4	1,030.9	812.4	1,013.0
Provisions	72.6	98.5	77.6	96.8
Other Current Liabilities	325.5	584.3	478.0	596.0
Total Current Liabilities	1,764.5	1,713.8	1,368.0	1,705.8
Net Current Assets	3,234.1	2,491.2	2,305.5	2,675.1
Other non-current assets	664.7	728.9	676.8	741.8
Application of Funds	9,877.7	9,849.0	9,568.2	9,795.5

Source: Company, ICICI Direct Research

Exhibit 13: Key ratios				
(Year-end March)	FY19	FY20P	FY21E	FY22E
Per share data (₹)				
EPS	22.2	7.5	3.5	13.7
Cash EPS	33.4	19.3	16.2	27.8
BV	116.1	112.8	114.3	123.5
DPS	5.0	3.5	2.0	4.5
Cash Per Share	21.8	35.3	40.5	44.3
Operating Ratios				
EBITDA Margin (%)	20.3	13.8	12.2	17.4
PBT / Net sales (%)	15.1	7.0	3.2	9.4
PAT Margin (%)	10.2	4.3	2.5	7.8
Inventory days	66.4	78.6	80.0	80.0
Debtor days	77.3	67.7	70.0	70.0
Creditor days	49.2	46.7	45.0	45.0
Return Ratios (%)				
RoCE	15.5	5.8	2.2	7.9
RoE	19.1	7.8	3.0	11.1
RoIC	20.9	9.0	3.3	11.8
Valuation Ratios (x)				
P/E	19.6	49.3	124.8	31.8
EV / EBITDA	11.3	20.5	27.7	15.3
EV / Net Sales	2.3	2.8	3.4	2.7
Market Cap / Sales	2.0	2.5	3.1	2.5
Price to Book Value	3.7	3.9	3.8	3.5
Solvency Ratios				
Debt/EBITDA	2.0	3.8	4.8	2.6
Debt / Equity	0.7	0.8	0.7	0.6
Current Ratio	2.6	2.1	2.3	2.2
Quick Ratio	1.5	1.1	1.2	1.2

Source: Company, ICICI Direct Research

Exhibit 14: ICICI Direct coverage universe (Auto & Auto Ancillary)

Sector / Company	CMP	TP	Rating	M Cap	EPS (₹)			P/E (x)			EV/EBITDA (x)			RoCE (%)			RoE (%)		
	(₹)	(₹)		(₹ Cr)	FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY22E	FY20	FY21E	FY22E
Apollo Tyre (APOTYR)	130	120	Hold	7,437	8.3	4.9	8.9	15.6	26.5	14.6	7.0	6.1	5.1	4.7	4.7	6.6	4.8	2.5	4.9
Ashok Leyland (ASHLEY)	54	58	Hold	15,806	0.8	0.1	2.1	66.2	807.8	26.3	15.2	21.7	10.9	5.6	2.2	8.6	4.7	0.3	8.0
Bajaj Auto (BAAUTO)	3,025	3,210	Hold	87,534	176.2	136.9	173.5	17.2	22.1	17.4	13.8	16.7	12.3	23.8	23.3	26.6	25.6	17.9	20.2
Bharat Forge (BHAFOR)	435	415	Hold	20,252	7.5	3.5	13.7	58.0	124.8	31.8	20.5	27.7	15.3	5.8	2.2	7.9	7.8	3.0	11.1
Eicher Motors (EICMOT)	22,105	18,070	Hold	60,258	670.4	495.4	690.9	33.0	44.6	32.0	25.8	32.4	23.0	22.5	15.9	19.1	18.3	12.2	14.9
Escorts (ESCORT)	1,118	1,300	Buy	13,704	39.6	46.1	54.5	28.2	24.2	20.5	18.9	15.9	13.3	18.9	15.0	15.2	14.2	11.2	11.8
Exide Industries (EXIIND)	168	180	Buy	14,280	9.7	6.3	8.9	11.8	18.0	12.9	10.3	12.8	9.9	15.7	10.3	13.5	13.4	8.2	10.7
Hero Moto (HERHON)	2,774	2,500	Hold	55,397	181.9	109.8	147.6	15.2	25.3	18.8	12.5	16.5	12.0	26.5	18.7	23.2	22.7	14.5	17.9
M&M (MAHMAH)	635	700	Buy	78,943	10.7	27.9	38.2	59.3	22.8	16.6	13.0	13.4	10.1	12.9	10.8	13.8	6.4	9.2	11.6
Maruti Suzuki (MARUTI)	6,730	5,300	Reduce	2,03,300	187.1	124.9	203.4	36.0	53.9	33.1	23.1	31.6	19.4	7.4	3.5	8.2	11.7	7.4	11.1
Minda Industries (MININD)	292	320	Buy	7,656	5.9	2.8	9.6	49.4	103.4	30.3	13.7	15.5	10.6	10.6	6.6	12.7	10.3	5.1	13.6
Tata Motors (TATMOT)	125	115	Hold	45,688	-32.8	-24.6	7.4	NM	NM	16.8	4.9	5.1	3.4	1.4	1.1	6.8	-18.7	-16.5	4.8

Source: Bloomberg, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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