

BHARAT FORGE LIMITED
Registered Office
Mundhwa, Pune Cantonment, Pune 411 036

CHAIRMAN'S SPEECH

CHAIRMAN'S SPEECH TO THE MEMBERS OF THE
COMPANY
AT THE 47TH ANNUAL GENERAL MEETING
ON WEDNESDAY, 6TH AUGUST 2008

Ladies and Gentlemen,

Introduction:

It is my pleasure to extend a very warm welcome to all of you to your company's 47th Annual General Meeting. I thank you for having spared your valuable time and made it convenient to attend.

The Annual Report containing the Directors' Report and the audited accounts for the year ended 31st March 2008 has been with you for some time and, I am sure, you have had the opportunity to peruse them.

Dividend :

Keeping in view the performance of your company, your Directors have recommended a dividend of 175 % on equity share capital i.e. Rs 3.50 per equity share of Rs 2/-.

Global Economy :

The surge in global commodity prices over the past year has resulted in high inflation in most countries. Inflation has become a

major threat for growth leaving government with virtually no room to leverage monetary policies to lower interest rates. In the short term, we expect moderate growth in developing countries, though relatively robust growth in emerging market economies like China and India could bolster the global economy. The challenge for our government therefore, is to bring down double digit inflation and still maintain the growth momentum.

Indian Economy :

The above 9% growth in GDP in the past three years has created optimism among global investors about the Indian economy. The uppermost question however is, “how vulnerable is the Indian economy to oil shocks and the alarming rise in input prices?” These have already reflected in a marked slow down in the industrial sector. If government had pushed labour and capital market reforms more aggressively in the past 2-3 years, perhaps industry would have become more resilient. Now the challenge is to build our competitiveness in the global market where volatility in commodity prices has become a fact of life. Will we be able to rise to the challenge? I am optimistic and believe that Indian entrepreneurs have the capability to convert this phase of global slowdown into an opportunity, take major strides in enhancing their competitiveness and build unassailable advantage that would contribute in consolidating the gains of the past few years.

Political developments in the last fortnight have provided the government an opportunity to push ahead with some key reforms that had been stalled for the past four years. The government has set a challenging 9.1% growth target for 2008-09. I personally believe that in spite of difficult market conditions in the global economy this could still be achieved.

Manufacturing Industry :

A recent ranking by revenues of Indian private sector companies has four manufacturing companies in the top five. What is relevant is that Indian manufacturing companies are succeeding not because of a tariff-protected large domestic market but on account of

consistently good export performance and a widening global manufacturing footprint that they have built through overseas acquisitions. Your Company is a notable example. For the past several years, exports have consistently accounted for over 40% of our Company's sales and this year 74% of our consolidated revenues are from sales outside India.

Our performance and that of other leading Indian manufacturing companies clearly reflects Indian industry's growing confidence to transform into global players. Indian companies have the processes, linkages and management capabilities to make a success of their international acquisitions, most of which are in developed countries. The challenge is to manage these in a downturn. I am confident that we can leverage the synergies of our international acquisitions and export competitiveness to further consolidate our global footprint.

Auto Component Industry :

The auto component industry in India has grown at a compounded annual growth rate of 27.2% between 2002-03 & 2007-08. It has attained a turnover level of \$18 billion in 2007-08, which includes \$3.6 billion exports and \$4.9 billion imports. This phase of growth has also seen a surge in investments from \$2.7 billion in 2003 to \$5.4 billion in 2007. We expect fresh foreign investments of \$5 billion in the industry in the next five years.

One of the major threats for the Indian auto component industry is the alarming increase in unfairly priced imports from China. In some cases, the landed cost of Chinese components are said to be cheaper than the raw material cost of the same component when manufactured in India. Auto component imports from China have rapidly grown in the past two years from less than 1.5% of all component imports to almost 10% in 2007-08. This is at a time when input costs for domestic industry have escalated phenomenally. Significantly, not all component manufacturers have been able to recover these cost increases from their customers. This has led to a squeeze on margins and profitability of companies. Fortunately for your company, we have strong and durable

relationships with all our customers, both domestic and international. Our contracts with them have pass through clauses which enable us to recover steel price increases. Transparency coupled with mutual trust and confidence with customers has therefore, enabled us to minimize the impact of higher input costs on performance. I would like to take this opportunity to thank all our customers for their kind understanding and co-operation in this regard.

Rationalizing internal costs and improving operational efficiencies can to an extent contribute in sustaining performance. However, when external factors such as a strong currency, higher interest rates, unfairly priced imports etc., come into play, industry needs government's proactive intervention. In all fairness, government has always supported our industry, however the threat from unfairly priced imports can be neutralized only if our anti-dumping and safeguards mechanisms are re-enforced to make them more responsive to industry's needs. The process of receiving, processing, hearing and deciding petitions needs a re-look so that it is speeded up to provide quick relief to domestic industry.

Power situation :

I would like to express anguish about the alarming power situation in Pune and Maharashtra. Perhaps for the first time ever, Pune is experiencing power cuts of over 6 hours every day. The situation in rural Maharashtra is much worse. Common citizens have been hit the hardest while industries are also bearing the brunt. It is distressing that a State which prides itself of being the most industrialized in the country is in this situation. Members will recall that till a few years ago Maharashtra was power surplus and exported power to neighboring States. While the late arrival of this year's monsoon, the financial and technical problems at Dabhol and the maintenance shut downs by some of the other power plants would have contributed to the 5000 MW shortfall in the State, clearly a time has come for the Government of Maharashtra to take immediate steps to radically enhance generation capacities in the State. If this is not done urgently Maharashtra runs the risk of loosing large investments to other States. As a company that was

born, nurtured and has grown in Maharashtra, we would like our State to remain the premier investment destination for Indian and foreign investors. I am confident that our government, with whatever support it needs from industry, will rise to the occasion and take urgent remedial actions.

New business development :

Your company sees tremendous opportunities in infrastructure and particularly in the capital goods sector. We signed a Memorandum of Understanding (MoU) with NTPC Ltd. that envisages setting up a joint venture company to manufacture large forgings and castings for high value, critical components such as rotor shafts, components for turbo generators and other capital goods, which currently constitute strategic bottlenecks from a national capacity building point of view causing slow down in execution of several large projects. We would like to contribute our experience in metal forming, metallurgical and related technologies to fill much needed gaps in the country's critical sectors. I am pleased to inform that the JV Company under the name 'BF-NTPC Energy Systems Limited' has since been incorporated.

We are also exploring opportunities to manufacture power equipment that would add about 5000 MW of indigenous capacity in this critical sector of the country's economy. Your company's vision is to contribute our strengths and capabilities to make our country self sufficient in power in the next 5-7 years.

As a Member of the US-India CEO's forum, I have in the past two years had opportunity to participate in meetings with our US counterparts to jointly identify areas of mutual co-operation between the two countries. This was part of the composite dialogue process that was initiated by President Bush and Prime Minister Manmohan Singh. Besides various other areas, co-operation in civilian use of nuclear energy had also been identified as a potential area for co-operation between both sides. For energy starved economy like ours, co-operation in this field is clearly an imperative.

Subject to the treaty between the countries being signed later this year, Bharat Forge visualizes several opportunities that could arise for us from this co-operation. As part of our business development activities, we propose to examine and aggressively pursue opportunities in areas that are relevant to our business.

Performance in 2007-08 :

2007-08 has been a challenging year for your Company. Notable among these challenges were currency appreciation, significant slowdown in key markets, increasing fuel prices and increasing steel prices. Our performance must therefore be viewed in light of these challenges. I believe we have responded well. The strategies that we have followed in the past 10 years have resulted in significant de-risking of our business and have contributed towards your company successfully addressing all these challenges. This has enabled us to report a stable performance.

There were five major challenges that we had to face. Notably all these were due to external factors over which we, as a company, had no control.

1. The severe slowdown in the largest automotive market in the world – USA that recorded a staggering 40% decline in production of medium and heavy commercial vehicles.
2. The Indian automobile industry also witnessed substantially slower growth. Production of commercial vehicles, your company's largest customer segment, grew by less than 5%. In spite of this, we were able to increase our domestic sales by 11%.
3. The rupee appreciated by more than 11% against the US dollar in 2007-08. That affected the realisations of our exports. Members are aware that exports account for over 40% of our sales. In spite of this, we could achieve a 28% export growth in rupee terms.

4. Oil prices remained volatile throughout the year and spiked to \$147 per barrel last month. The unprecedented rise in oil prices raised our production costs. At the same time, subdued vehicle demand meant lower than anticipated off take of your company's products by customers.
5. Steel prices continued to rise phenomenally. Fortunately for your Company we could recover these increases from customers.

The economic environment throughout 2007-08 was therefore extremely difficult. What is heartening is the fact that in spite of this your Company could turn in a stable performance. This reflects the inherent resilience in our business model. Since the Annual Report has been with Members for some time, with your permission, I will only highlight some of the key aspects of our performance. These include:

- On a consolidated basis, net sales grew by over 11% to Rs.4,652 crores in 2007-08. Total revenue increased to Rs.4,752 crores.
- Your Company now has the world's largest forging capacity of over 700,000 tonnes per annum. This includes our on-going expansions at Mundhwa and Baramati.
- We have a global manufacturing presence with 12 manufacturing facilities spread across India, China, Europe and USA.
- Our strategy to further de-risk our business by building a strong presence in the non-automotive sector is under implementation. Our new facilities at Baramati and Mundhwa are reflective of this. Heavy Forge Division (HFD) II by which name our Mundhwa facility is known, will be inaugurated on Friday, 8th August 2008 by Shri Ajit Pawar, Hon'ble Minister for Water Resources, Govt of Maharashtra and Guardian Minister for Pune district. This is a Rs.150

crore plant in which we will manufacture components for power generation, wind energy, oil & gas and various other capital goods industries.

- Profit before depreciation, interest, taxes and amortization (PBDIT) on a consolidated basis grew by 8% to Rs.804 crores. Your Company thus, had a PBDIT margin of almost 17% of total revenue – which was a reasonably good performance considering that 2007-08 was such a difficult year.
- Despite significant increase in depreciation, interest and taxes, your Company earned post-tax net profit of Rs.302 crores, which was marginally more than last year's profit.

There were five factors that contributed to your Company being able to record moderate growth in spite of difficult market conditions.

1. We could build scale and created an environment to share best practices across the organization through flexible product lines. We now have the capability to manufacture large volumes of forged and value-added machined products. We have further been able to enhance growth in rated capacities by sharing best-in-class shop floor practices within our group companies which have resulted in increases in productivity and throughput.
2. A diversified product portfolio combined with a global footprint was another advantage that we could leverage. In 2000-01, supplying chassis components for commercial vehicles in India constituted the overwhelming bulk of our business. Today this product segment accounts for only a third of our business; and the domestic market accounts for only a quarter of our sales. Our product mix is now well diversified; commercial vehicle chassis is 35%, passenger vehicle parts is 22%, diesel engine parts is 25%, and the non-automotive business is 18%. Our geographical footprint is

equally diversified. Europe accounts for 49% of our business, India 26%, North America 17% and Asia Pacific 8%. Diversification has not only de-risked our business, but also created greater opportunities for dual shoring.

Our immediate target is to rapidly scale up our non-automotive business so that by 2011-12 it comprises about 40% of our total sales. This is an important element of our de-risking strategy that is now under implementation.

3. We have a strong base of marquee customers. Almost every major OEM in Europe and North America is our customer. We have also migrated from being just a supplier of components to a preferred development partner of our customers. We are now in a position to collaborate with them from the design stage to joint development of prototypes to commercial production and delivery of finished ready-to-use products. These are significantly deeper relationships that can withstand downturns and are much beyond the traditional superficial, transaction-by-transaction, buyer-seller arrangements.
4. We have always given concerted attention to costs and productivity. Nothing takes our eyes and attention away from the basics of manufacturing excellence. I can assure you that however large we are, we will always be concerned about productivity, throughputs and costs. It is part of our DNA.
5. Finally, we now have a well-defined strategy to diversify into key non-automotive businesses. This includes forgings for conventional and non-conventional energy, power, aerospace, Oil and gas exploration, infrastructure metals and mining, and rail and marine. We have embarked on a Rs.500 crore investment plan for creating specialized capacities at Mundhwa, Baramati & Satara. Implementation of these capacities is progressing according to schedule.

As I said earlier, we expect the non-automotive business to become a major growth driver for your company in the next 2-3 years.

Human Resource Development & Corporate Social Responsibility:

I am proud of the capability and dedication of my colleagues at Bharat Forge and its subsidiaries. This year has made me even more proud because despite severely adverse conditions, our employees were able to produce satisfactory results. Perhaps these results do not reflect the efforts that have gone in. I can assure Members that from this year the continued efforts of all our employees will help in building a strong platform to achieve consistently improved performance in the years to come. I therefore, urge my colleagues to continue the good work.

In my last years Speech to Members, I had spoken about our various HR initiatives. To recollect, these include:

1. The 3 year part time Engineering programme leading to a BE in Mechanical Engineering from BITS, Pilani.
2. The M.Sc. programme in Manufacturing Engineering Management that is conducted by the University of Warwick, UK.
3. Take-over of the Government ITI at Khed for 5 years under an MoU that we have signed with Government of Maharashtra. We have now introduced six new courses that are relevant to the emerging needs of manufacturing companies.
4. Commencement of various vocational courses in basic trades at ITI Khed and ITI Narayangaon, Pune for the benefit of rural youth.

I am glad to report excellent progress on all these initiatives. The first two programmes are administered on our campus for the

benefit of our employees. Our work at Khed and Narayangaon is aimed at building and uplifting capacities of people in rural areas and thus contribute towards the creation of an inclusive society. We are committed to further strengthen our HR initiatives to touch the lives of many more people.

Kalyani Group's association with Pratham Pune Education Foundation, an NGO that I had promoted in the year 2000 continues. We are proud to be financially supporting an initiative which is engaged in providing primary education to young and underprivileged children belonging to disadvantaged sections of the local community. I would like to re-iterate our support to this worthy cause.

Corporate Governance :

I would like to re-iterate your company's strong commitment to good corporate governance. We continuously strive to improve the quality of our disclosures by benchmarking against best practices. The contents of our Annual Report over the past few years have been very exhaustive in terms of information about the company and its working.

Besides, I personally interact with groups of business analysts and the media. These interactions are useful in communicating with the external environment and in providing a better understanding about our company's goals, priorities and working. Information about our company is available on company's official website www.bharatforge.com. I suggest that Members should access the website regularly in order to be fully apprised about developments at Bharat Forge.

Acknowledgements :

I would like to take this opportunity to thank all our valued customers, domestic and international, for their unstinted support. They are a source of great encouragement and motivation for us and I am confident that we will benefit from their continued support.

I would like to express my sincere thanks to the Government of India, the Government of Maharashtra, Financial Institutions and Banks for their sustained encouragement and support to your company. I would also like to thank our collaborators for all their help and assistance.

I sincerely appreciate the contributions of all our employees which have resulted in your company's stable performance in difficult times. I request them to carry on the good work and help us realize the Company's goals and objectives.

Conclusion :

Finally, I convey my personal gratitude for the confidence that you have reposed in your company's Board of Directors. I sincerely hope that you will continue to extend your whole-hearted support to us so that we, along with the management team, and all employees will further accelerate the growth and progress of your company.

Thank you !
6th August, 2008