

KEI INDUSTRIES

On a strong growth trajectory

India Equity Research | Consumer Durables

We hosted KEI Industries' management at our recent investors' meet.

Key takeaways

- KEI Industries (KEI) has 3 verticals - Retail (30%), B2B (56%) and Exports (14%).
- **Retail to account for >40% of revenues in 2 years:** a) 50% of retail sales are through channel financing. This entails minimal working capital with LT cables constituting 55-60% of retail sales; b) KEI has 26 stocking points across India; c) India positioning in retail – No.2 in North, No.4 in West after Polycab and Finolex ,No.1 in East and No.5 in South; and d) dealers' spread across India - 35% in North, 25% in West and South each and 15% in East.
- **Project business:** a) Project cost break-up and scope - 10% termination and joining, 20% civil; and 70% cables (EHV cables) and EPC projects (other than EHV cables, cable component is 25-30%); b) mgmnt expects EHV cable (220/400kV) growth potential to improve as T&D capex shifts to states; c) KEI has ongoing EPC projects at 22-24 sites (of these 70% are in Uttar Pradesh).
- **Strong demand for B2B segment:** a) KEI enjoys 12-15% market share in B2B business; b) institutional sales account for 56% of total revenues broken up into - government projects - 10%, industrial - 30% and balance 16% being EPC; c) KEI expects strong demand from sectors like metro, housing, oil & gas, etc.
- **Industry size:** Cable & wires industry size is INR400bn, broken up into – a) housing wires at INR120-140bn; b) EHV cables INR20bn, c) 11-33kV at INR40-50bn; and d) balance being LT and HT cables out of which LT would be more than HT cables.
- **Payment cycle:** 3 months EPC, 2.5 months institutional, retail lower at 1 month.
- **Premium pricing:** As per management, large players like Havells and Finolex enjoy strong brand equity, which aides' premium pricing (5-10% vs. market).
- **Margin profile:** Retail/Exports 11%, institutional 9%, EHV 15% and EPC 12%.

Outlook and valuations: Robust visibility; maintain 'BUY'

KEI has expanded market share/positioning in past 2-3 years in North in cables & wires, while focusing on profitability. High profitable growth in cables & wires, ramp up in distribution and major debt repayment provides financial leverage and renders KEI our preferred pick in the India consumer electrical space (refer [Consumer Durables - Home Run](#)). We maintain 'BUY/SO' with target price of INR322.

Financials

(INR mn)

Year to March	FY16	FY17E	FY18E	FY19E
Revenues	22,929	26,312	31,352	37,536
Rev. growth (%)	13.6	14.8	19.2	19.7
EBITDA	2,423	2,743	3,337	4,043
Adjusted Profit	622	986	1,110	1,464
Adjusted diluted EPS (INR)	8.1	12.8	14.4	18.9
Diluted P/E (x)	32.8	20.7	18.4	13.9
ROAE (%)	18.6	23.5	21.1	22.6

EDELWEISS 4D RATINGS

Absolute Rating	BUY
Rating Relative to Sector	Outperform
Risk Rating Relative to Sector	Low
Sector Relative to Market	Overweight

MARKET DATA (R: KEI.N.BO, B: KEI.I.N)

CMP	: INR 264
Target Price	: INR 322
52-week range (INR)	: 268 / 99
Share in issue (mn)	: 77.8
M cap (INR bn/USD mn)	: 21 / 321
Avg. Daily Vol.BSE/NSE('000)	: 390.2

SHARE HOLDING PATTERN (%)

	Current	Q4FY17	Q3FY17
Promoters *	46.6	46.6	49.0
MF's, FI's & BK's	18.6	18.7	17.7
FII's	4.0	4.3	5.3
Others	30.8	30.4	28.0
* Promoters pledged shares (% of share in issue)	:	NIL	

RELATIVE PERFORMANCE (%)

	Sensex	Stock	Stock over Sensex
1 month	(1.9)	14.3	16.2
3 months	1.2	19.4	18.2
12 months	9.5	123.5	114.0

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Other highlights

400kV cables

- Management stated that testing of cables is mandatory before selling it commercially and Brugg kabel gives technical guarantee that the product can be manufactured.
- EHV cables are mostly imported in India where KEI and Universal are the only suppliers of EHV cables across India.
- There is demand for 400kV in power projects, which are increasing in numbers. With the increase in power cables, power transcos want to enhance voltage levels of single cables instead of laying multiple lines so that more power gets transmitted through a single cable. Also, the companies do not prefer to erect towers anymore and rather prefer to lay lines underground.
- KEI invested ~INR650mn towards upgrading 220kV lines to produce and test 400kV.
- Revenue that can be generated with capacity is ~INR1.5-2bn.
- Management believes it is in for a long haul with benefits flowing only after 1-2 years in FY19 and FY20.
- Capex-to-revenue ratio at 1:4x in the first year and 1:5x in later years.

Retail

- Margin at 10.5-11% for exports which is the same for retail.
- Management expects retail revenue to touch INR10bn in FY18 and INR12.5bn in FY19 with 10-15% growth in dealers.
- Dealer distribution across India– 35% in North, 25% West and South each and 15% in East.
- LT accounts for 55-60% of retail sales.
- Current utilization for LT cables is 80% and will rise to ~90% by end of the year. Therefore, KEI is undergoing small expansion at Bhiwadi (existing land) for LT cables by investing INR400bn and will start production by April 2018 which will have capacity to produce cables worth another INR3-4bn.
- KEI has recruited marketing personnel in retail as it targets retail to account for 40% of total revenues in next 2 years from current ~30% of revenues.
- Management indicated margins are improving by 10% every year which could increase dealer incentives.
- Exports
 - Stood at INR 3.9bn last year which management expects to grow by 15% in FY 18 and breach INR4bn in FY18.
 - KEI exports to the Middle East, Kuwait and Oman and this time it will mainly be to Australia.
 - The company took 4 years to get approvals in the Middle East.
 - It supplies mainly to utilities and contractors who are involved in utilities, wind and solar projects.

- Management expects exports business to grow only to an extent as the product is bulky and involves freight and logistics cost to ship it to customers outside India. With revenue growing they expect exports to grow, but only till they constitute 15% of revenues.
- KEI executed a project for the Singapore government for INR100mn.
- Export of SSW is INR300bn.

EPC

- KEI's scope in EPC involves digging, trenching, stretching and joining the cables and termination of cables. Around 10% is termination and joining, 20% civil and 70% cables, in case of EHV cables. In EPC projects (other than EHV cables), the cable component is 25-30%.
- The company executes many turnkey projects of 32kV, 66kV, 132 kV up to 600kV.
- There are 3 types of EPC projects in Power industry – Power Generation, Power Transmission (transmits bulk power from generating station and offloads it to the distribution company's network) and Power Distribution (creates a system and delivers power to the user be it industry, commercial complex or residential complex).
- Out of this, KEI is in 2 types of EPC projects –
 - Power Transmission – KEI provides EHV cables in substations and the GIS, which is utilized in transmission apart from civil activities which involves cables ranging from 33-400kV.
 - Power Distribution – the range of cables is limited to 1-33kV, but industry wants to upgrade power levels to 66kV. KEI's scope entails supplying and laying cables, which involves projects from IPDS and Deendayal Yojana which are related to discoms and the main objective is to lower ATNC losses. Competition is higher in this area of EPC projects.
- KEI fetches operating margin of 12% in EPC in cables other than EHV cables and in case of EHV cables it is 15%.
- Management plans to cap revenues at INR9bn this year and INR10bn next year, out of which INR3bn will be from cables. Management stated they have hired manpower and want to stabilize the manpower base. Another reason for capping revenues is that retention money should have a cycle and they do not block too much of their money there.
- The company does not subcontract any of its EPC projects as the risk increases and execution time too extends.
- Currently, KEI has ongoing EPC projects at 22-24 sites and of these 70% are in the state of Uttar Pradesh.

Institutional

- Management stated they have supplied cables to all projects that Engineers India has executed in the oil and gas space in past 20 years.
- Segment margins were 13%, but now it is ~9% and has scope to regain previous levels going forward.

- Sale to government projects is mere 10%, industrial 30% and balance is EPC.

Industry size: Cable & wires market size INR400bn, broken up into -

- Housing wires INR120-140bn
- EHV cables ~INR20bn
- 11-33kV INR40-50bn
- Balance is LT and HT cables out of which LT would be more than HT cables.

Debt

- Management believes debt peaked as of March'17.
- Debt, as on June'17' included buyer credit at INR 6.84bn.
- KEI targets repayment of INR500-600mn every year with complete repayment of debt in next 3 years.

Other comments

- KEI has invested ~INR1.30bn for EHV.
- The company expects margin expansion by 200bps in next 2 years.
- WC cycle is 3 months and retail receivables are 1 month.
- Pricing differential - Havells is 10% higher and Finolex is 5% higher than KEI.
- Management is looking at acquisitions in LT switchgears.

Company Description

KEI was established in 1968 as a partnership firm Krishna Electrical Industries with prime business of manufacturing house wiring rubber cables. It was converted into a public limited company with the corporate name KEI Industries in December 1992. In 1996, KEI acquired Matchless, a company under same management, which manufactured stainless steel wires. KEI has, over the years, invested in building flexible manufacturing facilities and expanded capacities. The company manufactures and supplies power and other industrial cables. The company operates through 3 segments—cables, stainless steel wires and turnkey projects. It also focuses on EPC business.

Investment Theme

Government's infra push: Potent demand catalyst - Housing For All & improving power availability, in our view, will be key drivers of the domestic cables & wires industry. With the government sharpening focus on power generation, transmission and distribution, demand for cables as part of T&D equipment is expected to expand significantly. KEI's expertise in EPC projects and excellent track record has rendered it the preferred candidate for such projects.

Huge scope to leverage cables business with forward integration in EPC - In EPC, KEI has the advantage of manufacturing (in house) EHV, HV and LT cables, which account for product pull-through of 30%, leading to superior margins. Also, technological collaboration with Switzerland-based Brugg Kabel AG has helped the company gain faster entry in the EHV cable market with designs and process back up—services sought by end users.

Key Risks

Cyclical nature of business - KEI's products are used primarily by power utilities, infrastructure, real estate and industrial segments. Any slowdown in these sectors can significantly impact demand for KEI's products.

High competition - A majority of KEI's products are highly competitive in nature and face strong threat from other players.

Raw material price fluctuation - Excessive volatility in prices of key raw materials—copper and aluminium—can severely impact profitability. Although KEI tries to recover rise in raw material prices either through hike in selling price of products or via hedging, there is no assurance that it can do so successfully or at all in the future.

Currency fluctuation - With exports being a key contributor to the company's revenue, excessive volatility in currency rates can significantly impact profitability. KEI also imports raw material and extreme currency fluctuations can adversely affect costs of the same, in turn denting profitability.

Financial Statements

Key Assumptions

Year to March	FY16	FY17	FY18E	FY19E
Macro				
GDP(Y-o-Y %)	7.2	6.5	7.1	7.7
Inflation (Avg)	4.9	4.5	4.0	4.5
Repo rate (exit rate)	6.8	6.3	5.8	5.8
USD/INR (Avg)	65.0	67.5	66.0	66.0
Company				
Capacity Utilisations (%)				
Cables	75.0	77.0	82.0	85.5
Stainless steel wires	90.0	84.0	87.0	89.7
Winding Housing & Flexible Wires	79.0	50.0	58.0	64.5
Realisation (INR)				
Cables (INR mn/km)	33.3	25.1	27.6	31.0
Stainless steel wires (INR '000/kg)	23.7	20.6	22.9	25.7
Winding Hsg & Flex. Wires (INR mn/km)	1.3	1.3	1.3	1.5
Order Intake for Turnkey Projects (INR bn)	6.5	17.0	15.0	14.0
Depreciation	5.4	5.1	5.1	5.2
Tax rate (%)	34.8	26.3	32.5	33.5

Income statement

(INR mn)

Year to March	FY16	FY17	FY18E	FY19E
Income from operations	22,929	26,312	31,352	37,536
Materials costs	16,743	18,855	22,588	27,037
Employee costs	828	1,109	1,257	1,464
Other mfg expenses	2,935	3,604	4,170	4,992
Total operating expenses	20,506	23,569	28,015	33,493
EBITDA	2,423	2,743	3,337	4,043
Depreciation	253	280	343	371
EBIT	2,170	2,463	2,993	3,672
Add: Other income	53.48	104.06	40.79	71.81
Less: Interest Expense	1,270	1,229	1,389	1,542
Profit Before Tax	953	1,338	1,645	2,201
Less: Provision for Tax	331	351	535	737
Reported Profit	622	986	1,110	1,464
Adjusted Profit	622	986	1,110	1,464
Shares o /s (mn)	77	77	77	77
Diluted shares o/s (mn)	77	77	77	77
Adjusted Diluted EPS	8.1	12.8	14.4	18.9
Adjusted Cash EPS	11.3	16.4	18.8	23.7
Dividend per share (DPS)	0.5	0.6	0.7	0.9
Dividend Payout Ratio(%)	6.2	4.7	5.0	5.0

Common size metrics

Year to March	FY16	FY17	FY18E	FY19E
Operating expenses	89.4	89.6	89.4	89.2
EBITDA margins	10.6	10.4	10.6	10.8
Net Profit margins	2.7	3.7	3.5	3.9

Growth ratios (%)

Year to March	FY16	FY17	FY18E	FY19E
Revenues	13.6	14.8	19.2	19.7
EBITDA	34.7	13.2	21.6	21.2
Adjusted Profit	96.6	58.6	12.6	31.8

Balance sheet		(INR mn)			
As on 31st March	FY16	FY17	FY18E	FY19E	
Share capital	154	156	156	156	
Shareholders' funds	3,666	4,735	5,778	7,155	
Short term borrowings	2,490	4,898	5,048	5,198	
Long term borrowings	1,881	1,641	1,641	1,641	
Total Borrowings	4,371	6,540	6,690	6,840	
Long Term Liabilities	40	51	51	51	
Sources of funds	8,440	11,752	12,946	14,472	
Gross Block	4,995	6,082	6,732	7,132	
Net Block	3,279	4,086	4,392	4,421	
Capital work in progress	293	-	-	-	
Non current investments	31	31	31	31	
Cash and Equivalents	59	369	480	598	
Inventories	4,225	4,990	5,728	6,871	
Sundry Debtors	5,674	7,392	8,675	10,387	
Loans & Advances	865	945	992	1,042	
Other Current Assets	744	297	297	297	
Current Assets (ex cash)	11,508	13,624	15,693	18,596	
Sundry creditors	6,319	6,305	7,598	9,122	
Provisions	411	53	53	53	
Total Current Liab	6,730	6,358	7,650	9,175	
Net Curr Assets-ex cash	4,777	7,266	8,042	9,421	
Net Deferred tax	362	427	427	427	
Uses of funds	8,440	11,752	12,946	14,472	
BVPS (INR)	47.4	61.3	74.8	92.6	

Free cash flow		(INR mn)			
Year to March	FY16	FY17	FY18E	FY19E	
Reported Profit	622	986	1,110	1,464	
Add: Depreciation	253	280	343	371	
Interest (Net of Tax)	828	906	938	1,026	
Others	656	453	411	445	
Less: Changes in WC	509	2,588	777	1,379	
Operating cash flow	1,850	38	2,025	1,927	
Less: Capex	977	624	650	400	
Free Cash Flow	873	(585)	1,375	1,527	

Peer comparison valuation

Name	Market cap (USD mn)	Diluted P/E (X)		P/B (X)		ROAE (%)	
		FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
KEI Industries	321	18.4	13.9	3.5	2.9	21.1	22.6
Finolex Cables	1,315	24.5	20.1	3.9	3.4	17.0	17.9
Havells India	4,814	41.5	33.2	8.3	7.3	21.3	23.5
Median	-	24.5	20.1	3.9	3.4	21.1	22.6
AVERAGE	-	28.1	22.4	5.2	4.5	19.8	21.4

Source: Edelweiss research

Cash flow metrics		FY16	FY17	FY18E	FY19E
Year to March					
Operating cash flow		1,850	38	2,025	1,927
Investing cash flow		(975)	(617)	(609)	(328)
Financing cash flow		(866)	890	(1,306)	(1,480)
Net cash Flow		9	311	111	118
Capex		(977)	(624)	(650)	(400)
Dividend paid		-	56	67	89

Profitability and efficiency ratios

Year to March	FY16	FY17	FY18E	FY19E
ROAE (%)	18.6	23.5	21.1	22.6
ROACE (%)	28.1	24.5	24.3	26.8
Inventory Days	94	89	87	85
Debtors Days	83	91	94	93
Payable Days	137	122	112	113
Cash Conversion Cycle	40	58	68	65
Current Ratio	1.7	2.1	2.1	2.0
Gross Debt/EBITDA	1.8	2.4	2.0	1.7
Gross Debt/Equity	1.2	1.4	1.2	1.0
Adjusted Debt/Equity	1.2	1.4	1.2	1.0

Operating ratios

Year to March	FY16	FY17	FY18E	FY19E
Total Asset Turnover	3.0	2.6	2.5	2.7
Fixed Asset Turnover	7.3	7.1	7.4	8.5
Equity Turnover	6.3	5.6	5.4	5.2

Valuation parameters

Year to March	FY16	FY17	FY18E	FY19E
Adj. Diluted EPS (INR)	8.1	12.8	14.4	18.9
Y-o-Y growth (%)	96.7	58.6	12.6	31.8
Adjusted Cash EPS (INR)	11.3	16.4	18.8	23.7
Diluted P/E (x)	32.8	20.7	18.4	13.9
P/B (x)	5.6	4.3	3.5	2.9
EV / Sales (x)	1.0	1.0	0.8	0.7
EV / EBITDA (x)	10.2	9.7	8.0	6.6

Additional Data

Directors Data

Mr. Anil Gupta	Chairman & Managing Director	Mr. Rajeev Gupta	Executive Director (Finance) & CFO
Mr. K.G. Somani	Non-Executive & Independent Director	Mr. Pawan Bholusaria	Non-Executive & Independent Director
Mr. Vijay Bhushan	Non-Executive & Independent Director	Mr. Vikram Bhartia	Non-Executive & Independent Director
Mrs. Archana Gupta	Non-Executive Director	Mr. Akshit Diviaj Gupta	Mr. Akshit Diviaj Gupta

Auditors - M/s. Pawan Shubham & Co. Chartered Accountants

**as per last annual report*

Holding – Top10

	Perc. Holding		Perc. Holding
Gupta anil rai	23.56	Projection fin & mgm	10.15
Templeton asset mgmt	6.62	Subhlaxmi motels & i	4.47
Soubhgaya agency It	4.02	Hsbc global inv maur	3.4
Mirae asset global i	2.83	Hsbc	2.37
L&t investment manag	2.09	Kei cables pvt ltd	2.02

**in last one year*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
17 Feb 2017	Anil Gupta	Sell	1900000	172.34
16 Dec 2016	Hsbc Global Investment Fundsasia Ex Japan Equity Smallercompanies	Buy	3451330	120.35
16 Dec 2016	Cophall Mauritius Investment Ltd	Sell	3451330	120.35

**in last one year*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
02 Mar 2017	PAWAN KUMAR AGGARWAL	Sell	80000.00
02 Mar 2017	LALIT SHARMA	Sell	30000.00
20 Feb 2017	ANIL GUPTA	Sell	1900000.00

**in last one year*

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Bajaj Electricals	HOLD	SP	M	Crompton Greaves Consumer Electrical	BUY	SO	L
Finolex Cables	BUY	SO	L	Havells India	BUY	SO	L
KEI Industries	BUY	SO	L	Symphony	BUY	SO	L
V Guard Industries	HOLD	SP	L	Voltas	BUY	SO	L
Whirlpool of India	BUY	SO	M				

ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return

Aditya Narain

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Coverage group(s) of stocks by primary analyst(s): Consumer Durables

Bajaj Electricals, Crompton Greaves Consumer Electrical, Finolex Cables, Havells India, KEI Industries, Symphony, V Guard Industries, Voltas, Whirlpool of India

Recent Research

Date	Company	Title	Price (INR)	Recos
07-Sep-17	Symphony	Growth confidence reinstated; <i>Result Update</i>	1,305	Buy
30-Aug-17	KEI Industries	Solid operational start; <i>Result Update</i>	260	Buy
11-Aug-17	Symphony	Temporary setback dents Q1; prospects sanguine; <i>Result Update</i>	1,205	Buy

Distribution of Ratings / Market Cap

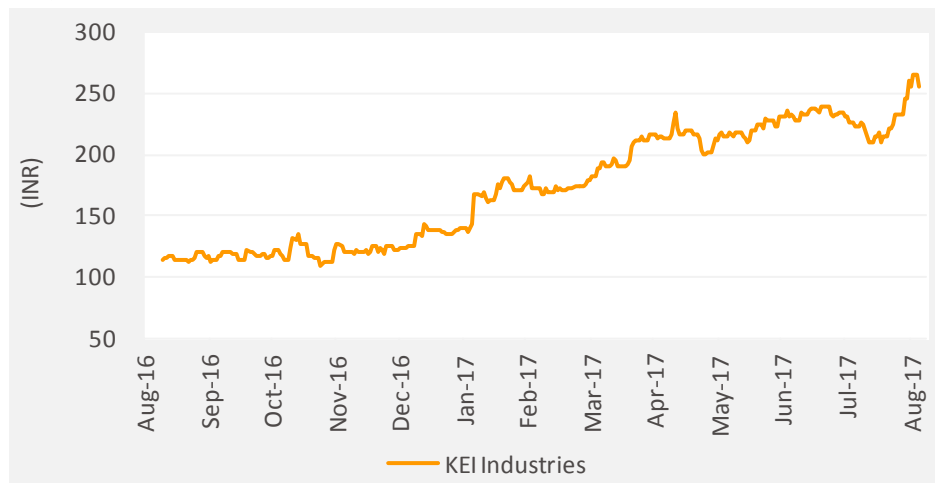
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart



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