COMPANY NOTE

Initiating Coverage

India | Industrials | Engineering & Construction

29 January 2018

Jefferies

EQUITY RESEARCH INDIA

KEI (KEII IN)

Holistic India Play; Initiate at Buy

BUY

Price target INR620.00

Price INR400.10^

Key Takeaway

KEI Industries (KEI) is one of the top-four organised players in the Indian cable industry and an EPC player in power T&D. We believe KEI is a play on capex, consumption (housing spend) and engineering exports. We see strong re-rating potential for the stock in the next 12-18 months on 30% earnings CAGR, 23%+ ROE and reducing D:E, besides earnings-linked upside. Initiate at Buy and PT of Rs620 (56% potential upside), valuing it at 22x PE FY20E.

Rising retail and export share in cables: Cables account for 74% of KEI's revenue, with EPC division at 23%. Institutions (ABB, Power Grid, L&T and Siemens, among others) account for 63% of KEI's cable sales, while the remainder is to the housing (retail) segment. Retail and exports have 100-200 bps better margin profile vs the domestic institutional business. As it is more a business to consumer (B2C) business, retail has a better working capital cycle too. We expect the combined share of retail and exports to rise to 51% in FY20E from 45% in FY17. Additionally, fixed overheads from FY17 expansion of EHV cables, which has impacted FY18E margins, should be absorbed in FY19E-20E as utilization improves. This should drive improved B/S and margin profile in FY19E-20E.

GST and industrial capex, additional triggers: We estimate about 35% of the Indian cable market is unorganised. With GST brining companies under the tax net, branded and unbranded goods are seeing the price differential narrow. This could result in market pie itself expanding faster for KEI. 31% of KEI's revenues are domestic institutional sales, where estimates capture the current trough in the cycle. As capex announcements are picking up, this segment could see upside surprise. EPC side (23% of revenues) is covered on current order book contracts for FY17-20E.

ROE, north of 23%: KEI's D:E ratio has been 1.5-2x to support its EPC working capital needs and its 9x overall revenue growth in the past decade. With the rising share of retail and exports in sales, revenue growth stabilising on a larger base at 20% CAGR over FY17-20E and one-third capex being funded from internal accruals, we believe this ratio will trend downwards to below 1x by FY20E.

Valuation/Risks

We believe strong earnings and ROE should drive share price performance. Our PT of Rs620 (potential upside 56%) is based on 22x FY20E PE (premium to its 10-year historical average, as it grows on a sizeable base with stable profitability). Risks: 1) sharp price competition in cables; 2) one-off write-offs in EPC.

INR	Prev.	2017A	Prev.	2018E	Prev.	2019E	Prev.	2020E
Rev. (MM)	--	26,691.0	--	32,977.0	--	39,010.0	--	45,578.0
EBITDA (MM)	--	2,743.0	--	3,119.0	--	3,837.0	--	4,724.0
Net Profit	--	986.0	--	1,250.0	--	1,661.0	--	2,192.0
BV/Share	--	60.90	--	76.00	--	96.20	--	122.90
ROE	--	23.5%	--	23.5%	--	24.8%	--	25.7%
Dividend	--	0.60	--	0.80	--	1.00	--	1.20
EPS								
FY Mar	--	12.70	--	16.10	--	21.30	--	28.20
FY P/E		31.5x		24.9x		18.8x		14.2x

Financial Summary

Net Debt (MM):	INR6,749.0

Market Data

52 Week Range:	INR423.50 - INR133.75
Total Entprs. Value (MM):	NM
Market Cap. (MM):	NM
Shares Out. (MM):	77.8
Float (MM):	37.5
Avg. Daily Vol.:	578,101

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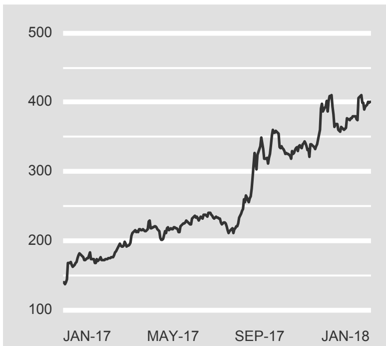
Price Performance



^Prior trading day's closing price unless otherwise noted.

KEI Industries

Buy: INR 620 Price Target

Scenarios

Base Case

- Earnings CAGR of 30% during FY17-20E
- EBITDA margin improves by 91bps over FY18E-20E
- Exports and retail share in revenue improves from 45% in FY17 to 51% in FY20E
- FY20E EPS: Rs28.2; Target Multiple: 22x; PT Rs620

Upside Scenario

- Earnings CAGR of 38% during FY17-20E
- EBITDA margin improves by 105bps over FY18E-20E
- Exports and retail share in revenue improves from 45% in FY17 to 55% in FY20E
- FY20E EPS: Rs33.3; Target Multiple: 24x; PT Rs799

Downside Scenario

- Earnings CAGR of 27% during FY17-20E
- EBITDA margin improves by 84bps over FY18E-20E
- Exports and retail share in revenue improves from 45% in FY17 to 49% in FY20E
- FY20E EPS: Rs25.8; Target Multiple: 20x; PT Rs516

Investment Thesis / Where We Differ

- Rise in the retail and exports share in revenue, which have 100-200 bps better margin profile.
- KEI to gain market share from 11% in FY17 to 15% in FY20E.

Catalysts

- GST implementation to narrow the price differential between branded and unbranded.
- Pick-up in capex cycle

Long Term Analysis

Long Term Financial Model Drivers

LT EBITDA CAGR	**20%**
Organic Revenue Growth	**20%**
Operating Margin Expansion over FY18E-20E	**91bps**

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Table of Content

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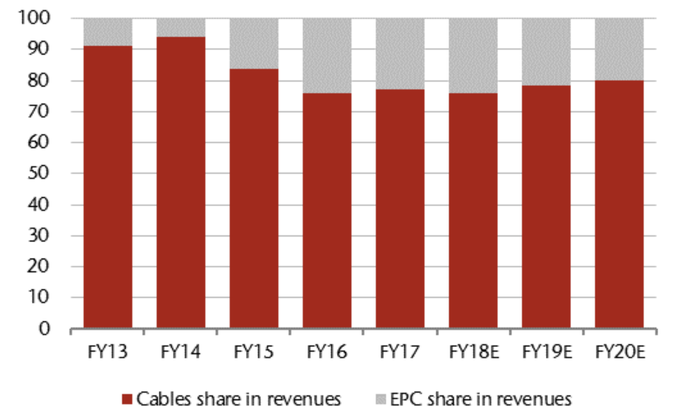
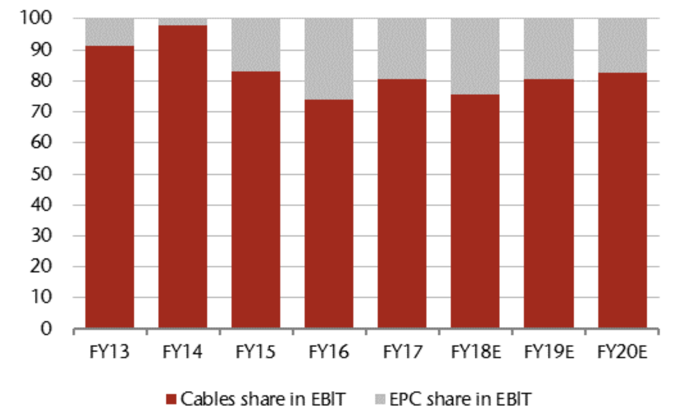
Focus Charts (KEI)

Exhibit 1: Cables to continue to account for a majority of revenue ...



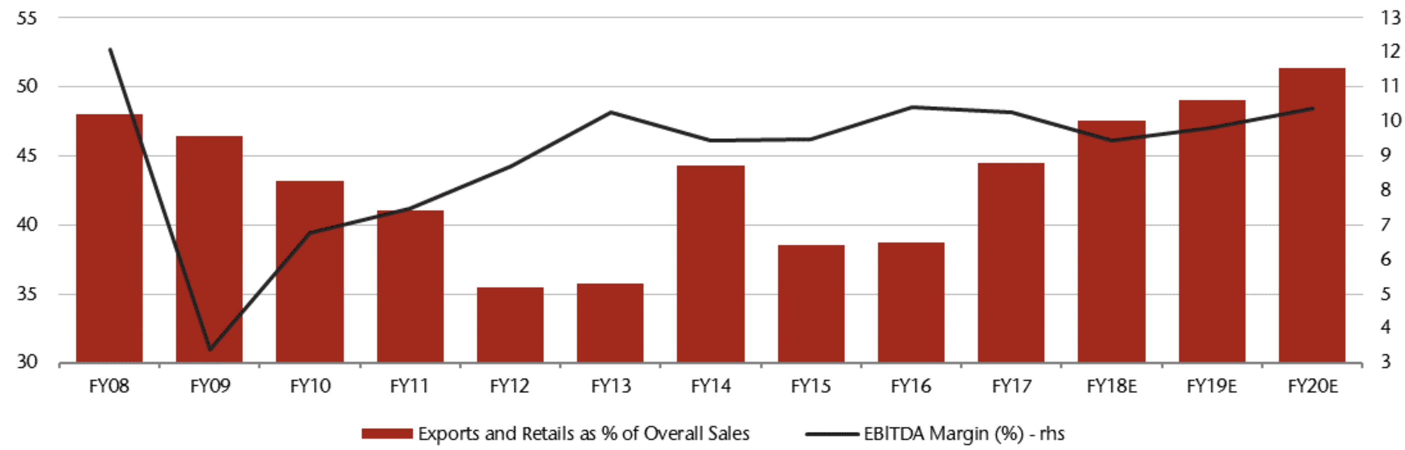
Source: Jefferies estimates, company data

Exhibit 2: ... and EBIT



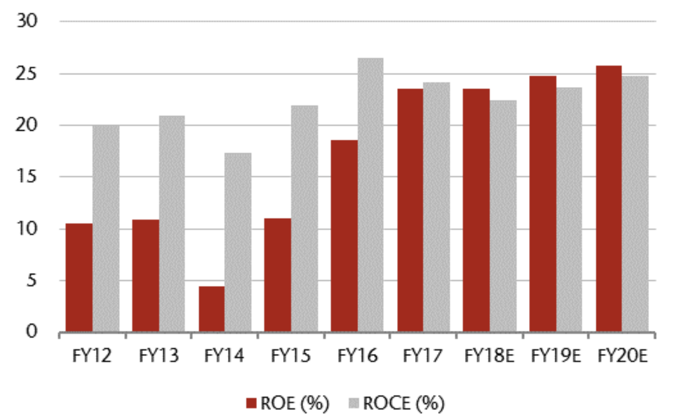
Source: Jefferies estimates, company data

Exhibit 3: Rising share of exports and retail to boost margin upside, as their margin profile is 100-200 bps better



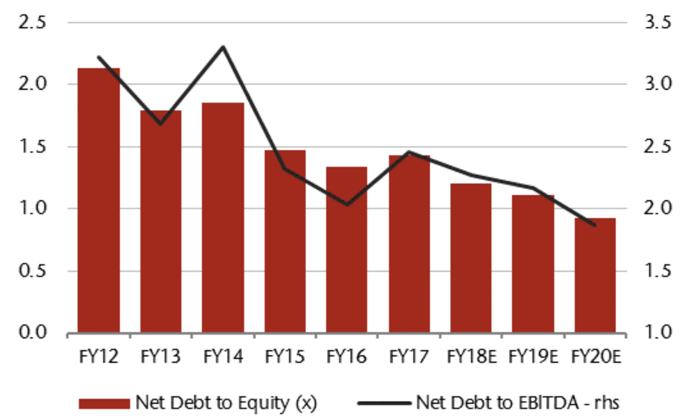
Source: Jefferies estimates, company data

Exhibit 4: ROE to remain above 23% over FY18E-20E



Source: Jefferies estimates, Company data

Exhibit 5: Net debt to equity to be below 1x by FY20E



Source: Jefferies estimates, Company data

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Executive summary

KEI has transformed itself into a mid-sized cables and EPC company in the past decade. From volatility in margins given scale, it has moved to a stable base and is in the right business growth segment. We believe the company is a play on capex, consumption (housing spend) and engineering exports. We believe in the next 12-18 months, it has re-rating potential on the back of 30% earnings CAGR, 23%+ ROEs and reducing D:E stock, besides earnings-linked upside. Initiate at Buy and PT of Rs620 (56% potential upside), valuing it at 22x FY20E.

KEI gaining market share in the cable industry: We estimate that 35% of the cables market in India is unorganised, based on our industry interaction and channel checks. The organised market is fairly concentrated with the top-four players accounting for 78% of this market. KEI is ranked third and has seen its market share rise gradually from 8% in FY09 to 11% in FY17. GST introduction is likely to see share shift from the organised to the unorganised sector. This would be driven by narrowing pricing discount between branded and unbranded products, with unorganised players coming under the tax net. We have factored some rise in KEI's market share in organised moving ahead, with further potential upside from higher market share shift to organised players.

Retail and exports rising share to drive margins: KEI earns 100-200 bps premium in the domestic retail and exports segment vs the domestic institutional sales. We expect the share of margin-accretive segments to move to 51% in FY20E, from 45% in FY17. This is the key driver of our 91bps margins improvement estimate for FY18E-20E.

Valuation – earnings growth momentum to continue: We believe KEI will sustain its 30% earnings CAGR during FY17-20E and ROE will improve as it funds one-third of its expansion from its internal balance sheet. This implies strong returns for the stock in the next 12 months. We initiate coverage with PT of Rs620 (potential upside of 56%), based on 22x FY20E PE (premium to its 10-year historical average, as it grows on a sizeable base with stable profitability).
Risks: 1) sharp price competition in cables; 2) one-off write-offs in EPC.

Exhibit 6: KEI gained market share from 8% in FY09 to 11% in FY17

(Rs mn)	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17
Havells	11,066	10,949	12,318	15,930	16,925	19,264	21,904	24,595	26,756
% market share	*12.0*	*11.8*	*11.0*	*11.6*	*11.3*	*11.9*	*13.0*	*14.5*	*16.4*
Finolex	15,015	17,266	21,864	21,826	24,235	25,100	25,748	25,747	26,708
% market share	*16.3*	*18.6*	*19.6*	*15.9*	*16.1*	*15.5*	*15.3*	*15.1*	*16.3*
KEI	7,376	7,620	9,770	14,213	13,368	12,589	15,636	17,203	17,461
% market share	*8.0*	*8.2*	*8.8*	*10.3*	*8.9*	*7.8*	*9.3*	*10.1*	*10.7*
Diamond Power	6,157	8,755	12,676	17,404	21,264	26,743	24,151	20,824	11,529
% market share	*6.7*	*9.4*	*11.4*	*12.7*	*14.1*	*16.5*	*14.3*	*12.2*	*7.1*
Others Organized	20,310	15,882	15,913	19,985	21,977	21,407	21,960	22,231	23,829
% market share	*22.0*	*17.1*	*14.3*	*14.5*	*14.6*	*13.2*	*13.0*	*13.1*	*14.6*
Others Unorganized	32,267	32,562	39,061	48,116	52,645	56,594	58,907	59,554	57,229
% market share	*35.0*	*35.0*	*35.0*	*35.0*	*35.0*	*35.0*	*35.0*	*35.0*	*35.0*
Overall	**92,192**	**93,033**	**111,602**	**137,474**	**150,413**	**161,698**	**168,306**	**170,154**	**163,511**

Source: Jefferies estimates, company data, Ace Equity

Exhibit 7: Product-wise revenue split; Retail revenue to grow at 25% CAGR over FY17-20E

(Rs mn)	FY12	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Low Tension Cable - Retail	2,751	2,292	2,260	3,020	3,430	3,810	6,193	7,594	9,306
Low Tension Cable - Institutional	7,228	6,816	5,961	6,860	6,480	8,570	5,617	12,106	8,864
High Tension Cable - Institutional	2,193	2,562	2,931	3,300	4,350	3,800	8,913	5,842	12,590
Extra High Voltage Cables - Institutional	1,500	590	590	590	1,330	1,030	1,133	1,246	1,371
House Wire - Retail	2,114	2,665	2,941	3,330	3,780	4,320	4,925	5,614	6,400
Stainless Steel Wire	951	786	937	1,052	949	1,044	1,096	1,151	1,208
EPC	485	882	568	2,170	3,230	4,210	5,100	5,457	5,839
Overall	**17,223**	**16,593**	**16,189**	**20,322**	**23,549**	**26,784**	**32,977**	**39,010**	**45,578**

Source: Jefferies estimates, company data

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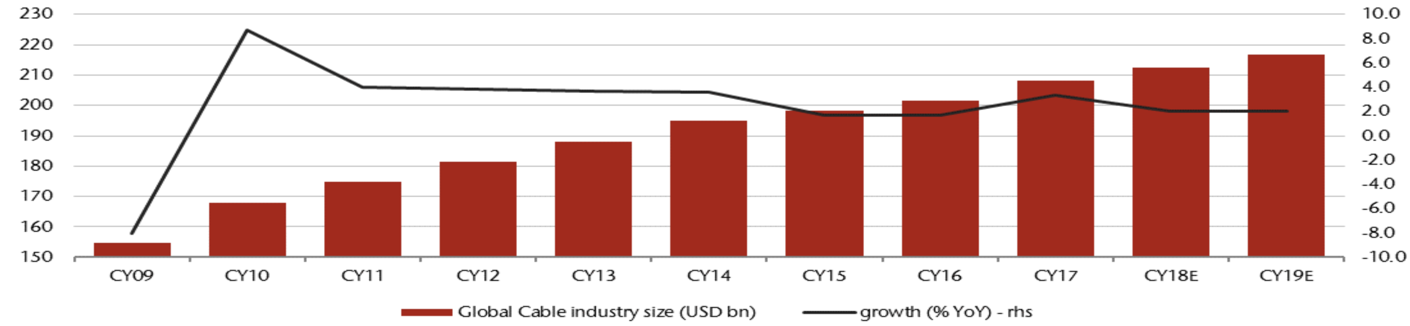
China 27% of global cable demand

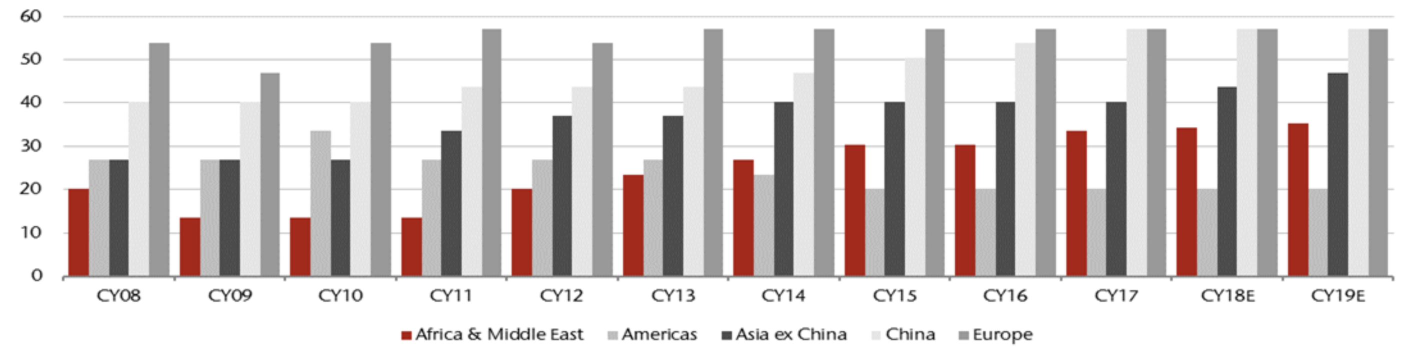
Global cable market stabilises after 2008 Lehman crisis: The global cable market is currently valued at USD208 bn. In 2009, it declined 8% YoY, post the Lehman crisis. CY10 saw a sharp bounce-back and has stabilised in the 2-4% CAGR range since. China remains the dominant consumer at 59% of Asian demand. European demand has been flattish with some negative bias. The interesting trend is that lower production costs has seen manufacturing move to developing economies. KEI, in its 2010 annual report, highlighted that data suggests developed markets accounted for 40% of cable manufacturing in 2001, which dropped to 33% in 2007 and further to 31.5% in 2009. This is despite developed economies accounting for more than 52% of demand in 2009, providing scope for exports from India.

Exhibit 8: We expect global cable market CAGR of 2% over CY16-19E



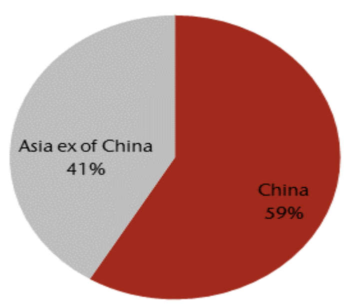
Source: Jefferies estimates, company data, World Bank, IMF

Exhibit 9: Cable market across different regions; Demand in Europe remained flat in last few years (USD bn)



Source: Jefferies estimates, company data, World Bank, IMF

Exhibit 10: China dominant consumer with 59% of Asian demand



Source: Jefferies estimates, company data

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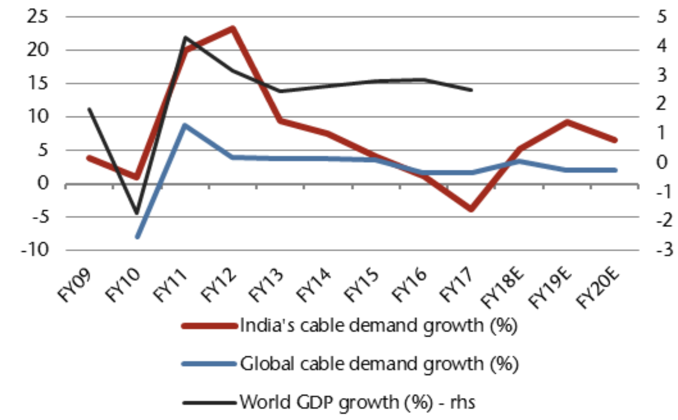
India driven by capex and housing

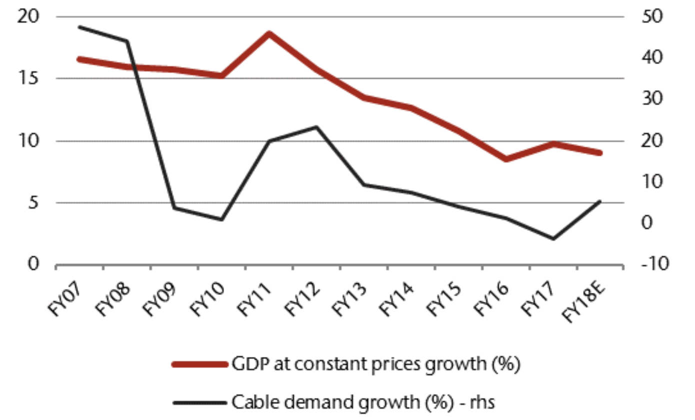
India cables market relatively insulated in Lehman crisis: Globally, GDP growth and cable industry demand growth have seen an efficient correlation. This is also true in India in the context of its demand and GDP growth. However, compared with a decline in global demand, India still saw marginal growth during the Lehman crisis period. India accounts for 1.2% of global cable demand and 3% of Asian demand. It has been among the fastest growing economies in this segment and should rise faster than the global growth in the next three years too.

Exhibit 11: Cable market in India expected to grow at 7% CAGR over FY17-20E, faster than global market



Source: Jefferies estimate, Ace Equity

Exhibit 12: India's annual GDP growth and cable demand growth exhibit an efficient correlation



Source: Jefferies estimate, Ace Equity, CMIE

Underlying drivers strong for 7% CAGR at least: India's cable demand rose at 10% CAGR during FY07-17. Cable demand for a project starts after the project is half completed. On-ground industrial capex is yet to recover, and announcements beginning in FY18E should translate into actual spend only FY20E onwards. Hence, we believe that housing will be more of a driver of cable demand in the next two-three years, and overall CAGR during FY17-20E is likely to be closer to 7% vs 10%+. However, faster recovery in capex could imply upside surprise to our estimates.

Exhibit 13: Industrial demand of cables to grow at 4% while housing demand to grow at 10% CAGR over FY17-20E

	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Industrial size (Rs mn)	55,315	55,820	66,961	82,484	90,248	97,019	100,984	102,093	98,107	97,856	107,888	113,158
Industrial capex (Rs bn)	18,899	16,390	18,825	13,649	10,038	9,665	15,621	15,212	13,877	13,842	15,261	16,006
Implied share of cables (%)	*0.3*	*0.3*	*0.4*	*0.6*	*0.9*	*1.0*	*0.6*	*0.7*	*0.7*	*0.7*	*0.7*	*0.7*
Housing size (Rs mn)	36,877	37,213	44,641	54,990	60,165	64,679	67,322	68,062	65,404	74,122	80,052	87,256
Housing capex (Rs bn)	11,030	12,437	14,424	17,237	18,826	20,282	22,174	22,862	23,091	24,707	26,684	29,085
Implied share of cables (%)	*0.33*	*0.30*	*0.31*	*0.32*	*0.32*	*0.32*	*0.30*	*0.30*	*0.28*	*0.30*	*0.30*	*0.30*
Overall cables market (Rs mn)	92,192	93,033	111,602	137,474	150,413	161,698	168,306	170,154	163,511	171,978	187,939	200,414
Overall capex (Rs bn)	29,929	28,827	33,250	30,886	28,863	29,948	37,795	38,074	36,968	38,549	41,945	45,092
Implied share of cables (%)	*0.3*	*0.3*	*0.3*	*0.4*	*0.5*	*0.5*	*0.4*	*0.4*	*0.4*	*0.4*	*0.4*	*0.4*

Source: Jefferies estimates, company data, CMIE

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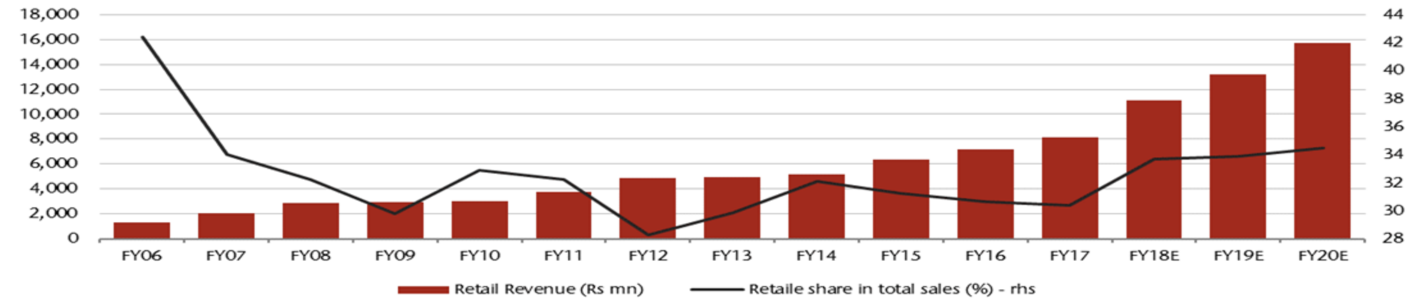
KEI among top-four organised players

Retail focus playing out: Sales to the housing segment are primarily through dealer networks and more reflective of B2C business dynamics vs B2B. Receivables period is normally 30-45 days vs closer to 90 in institutional business. Additionally, industry and management interactions suggest that margins in this segment are 100-200 bps higher than institutional. KEI hired a new CEO specifically for its retail business in FY14. Since then, they have doubled their dealer base across India from 600 to close to 1,200 in FY17. KEI's 9MFY18 retail business has risen at 40% YoY, with its market share rising 1.5-2% every year in the past five years. On this stable base, we expect retail share to rise to at least 34% of revenue by FY20E from 30% in FY17. This contributes to our 91bps margin improvement over FY18E-20E along with exports, which are also higher margins. Any upside surprise in retail would imply margin and revenue upside for our estimates for FY18E-20E.

Exhibit 14: Retail share to rise to 34% of revenues by FY20E from 30% currently



Source: Jefferies estimates, CEA, CERC

Focus on LT and HT cables: Low tension cables (LT – upto 3.3 KV) and High Tension cables (HT – up to 66 KV) are the main segments for KEI in the institutional business, running at close to 90% utilisation. Power generation, T&D and industrial capex are the major drivers for this segment. Extra High Voltage (EHV) cables are primarily used in transmission projects and is the only division running at sub-60% utilisation.

Exhibit 15: Product-wise revenue split; Share of LT and HT cables combined will rise to 67% of revenues

(In Rs mn)	**FY12**	**FY13**	**FY14**	**FY15**	**FY16**	**FY17**	**FY18E**	**FY19E**	**FY20E**
Low Tension Cable - Retail	2,751	2,292	2,260	3,020	3,430	3,810	6,193	7,594	9,306
Low Tension Cable - Institutional	7,228	6,816	5,961	6,860	6,480	8,570	5,617	12,106	8,864
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Stainless Steel Wire	951	786	937	1,052	949	1,044	1,096	1,151	1,208
EPC	485	882	568	2,170	3,230	4,210	5,100	5,457	5,839
Overall	**17,223**	**16,593**	**16,189**	**20,322**	**23,549**	**26,784**	**32,977**	**39,010**	**45,578**

Source: Jefferies estimates, company data

Exhibit 16: Segmental revenues as reported by management

	FY12	**FY13**	**FY14**	**FY15**	**FY16**	**FY17**	**FY18E**	**FY19E**	**FY20E**
Cables	**15,463**	**14,340**	**14,565**	**17,110**	**19,113**	**21,254**	**25,863**	**31,700**	**38,068**
% of sales	*89.8*	*86.4*	*88.5*	*78.8*	*72.3*	*73.6*	*72.9*	*75.6*	*77.7*
Stainless steel wire	**951**	**786**	**937**	**1,052**	**949**	**1,044**	**1,096**	**1,151**	**1,208**
% of sales	*5.5*	*4.7*	*5.7*	*4.8*	*3.6*	*3.6*	*3.1*	*2.7*	*2.5*
Turnkey projects	**808**	**1,469**	**947**	**3,567**	**6,391**	**6,585**	**8,500**	**9,095**	**9,732**
% of sales	*4.7*	*8.9*	*5.8*	*16.4*	*24.2*	*22.8*	*24.0*	*21.7*	*19.9*
Unallocated	0	-3	0	-5	0	0	0	0	0
Overall	**17,223**	**16,593**	**16,449**	**21,724**	**26,453**	**28,883**	**35,459**	**41,946**	**49,008**
Less: inter-segment revenue	0	0	260	1,402	2,904	2,099	2,482	2,936	3,431
% of overall	*0.0*	*0.0*	*1.6*	*6.5*	*11.0*	*7.3*	*7.0*	*7.0*	*7.0*
Sales	**17,223**	**16,593**	**16,189**	**20,322**	**23,549**	**26,784**	**32,977**	**39,010**	**45,578**

Source: Jefferies estimates, company data

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GST could add to opportunity

KEI gradually gaining share in domestic market: We estimate that 35% of the cables market in India is unorganised, based on our industry interaction and channel checks. The organised market is fairly concentrated with the top-four players accounting for 78%. KEI is ranked third and has seen its market share rise gradually from 8% in FY09 to 11% in FY17. We have factored a further rise of 4.5% over FY17-20E. KEI's advertising campaign, particularly in retail, roping in a popular actor and also sponsorships for the Indian cricket league (IPL) is yielding results in retail as well as for the overall market share of the company.

Exhibit 17: KEI gained market share from 8% in FY09 to 11% in FY17 and expected to further gain 4.5% over FY17-20E

(in Rs mn)	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17
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% market share	*12.0*	*11.8*	*11.0*	*11.6*	*11.3*	*11.9*	*13.0*	*14.5*	*16.4*
Finolex	15,015	17,266	21,864	21,826	24,235	25,100	25,748	25,747	26,708
% market share	*16.3*	*18.6*	*19.6*	*15.9*	*16.1*	*15.5*	*15.3*	*15.1*	*16.3*
KEI	7,376	7,620	9,770	14,213	13,368	12,589	15,636	17,203	17,461
% market share	*8.0*	*8.2*	*8.8*	*10.3*	*8.9*	*7.8*	*9.3*	*10.1*	*10.7*
Diamond Power	6,157	8,755	12,676	17,404	21,264	26,743	24,151	20,824	11,529
% market share	*6.7*	*9.4*	*11.4*	*12.7*	*14.1*	*16.5*	*14.3*	*12.2*	*7.1*
Others Organized	20,310	15,882	15,913	19,985	21,977	21,407	21,960	22,231	23,829
% market share	*22.0*	*17.1*	*14.3*	*14.5*	*14.6*	*13.2*	*13.0*	*13.1*	*14.6*
Others Unorganized	32,267	32,562	39,061	48,116	52,645	56,594	58,907	59,554	57,229
% market share	*35.0*	*35.0*	*35.0*	*35.0*	*35.0*	*35.0*	*35.0*	*35.0*	*35.0*
Overall	**92,192**	**93,033**	**111,602**	**137,474**	**150,413**	**161,698**	**168,306**	**170,154**	**163,511**

Source: Jefferies estimates, company data, Ace Equity

Shift from unorganised to organised adds to upside potential: GST introduction has put unorganised players in a tight spot as they are now a part of the tax net. The biggest selling point for the unorganised players was the 15-20% pricing discount vs organised players. GST implementation since 1 July 2017 means that every vendor has a GST registration number and their sales are monitored by the income tax department. This makes it harder to evade taxes and evasion is possible only if the entire value chain does not have a GST number. However, on larger scale industry sizes, this is difficult. Hence, as unorganised players start paying taxes and the discount with branded organised players narrows, there could be a shift in market share with time.

Exhibit 18: At least 9% differential due to tax evasion

	Compliant manufacturer	Non-compliant manufacturer*
Number of cables (mn)	100	100
Cost per cable	50	50
Profit margin (10%)	5	5
Ex-factory selling price	55	55
Ex-factory sales (mn)	5,500	5,500
Excise duty on cables (5%)	688	344
State VAT on cables (5%)	248	124
Overall sales	6,435	5,968
Additional benefit from corporate tax evasion (Rs mn)	0	85
Sales price per cable	64	59

* assuming non-compliant manufacturer only reports 50% of its sales

Source: Jefferies estimates, company data

Currently, GST rates for cables and wires is 18% and our industry checks suggest there is already a demand rise for branded products of organised players, as unorganised players have seen some escalation in prices.

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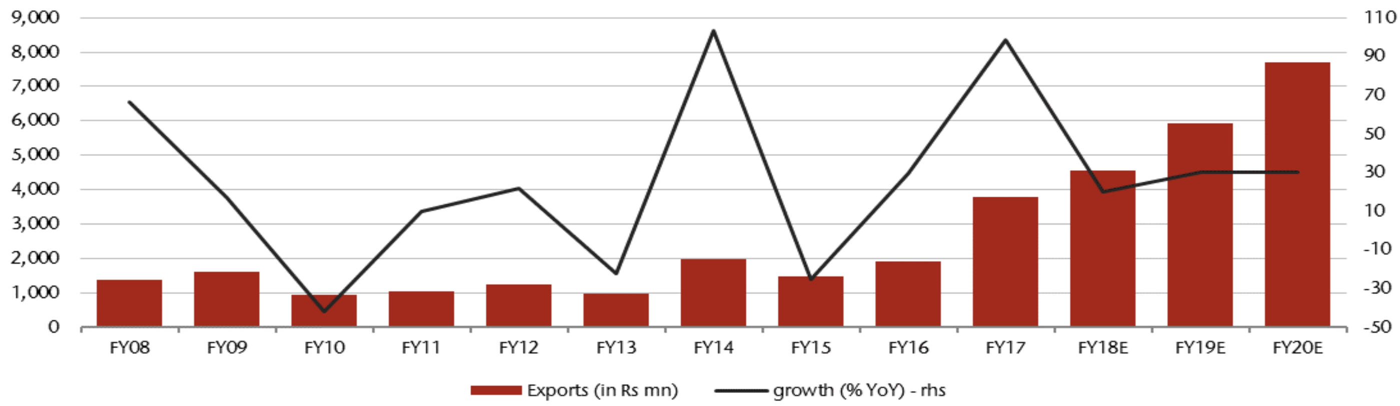
Exports thriving on focused long-term strategy

Foray in FY06 paying off: We are strong believers in the India engineering exports theme being driven by FY14-16 currency depreciation, better patent protection laws and perceived quality of Indian products relative especially to China. Additionally, sizeable home market base helps gain scale efficiencies. KEI formulated its export strategy 2006 onwards and has seen a 16% CAGR during FY07-17. The company started off in 21 countries and currently has its footprint across 45 countries. Australia is a key contributor for its revenue visibility in exports over the next 12-24 months. Based on existing backlog, we expect exports to see 27% CAGR during FY17-20E. Interestingly, management indicated that export margins also tend to be 100-200 bps better than domestic institutional sales, adding to margin cushion.

Exhibit 19: Exports to grow at a 27% CAGR over FY17-20E



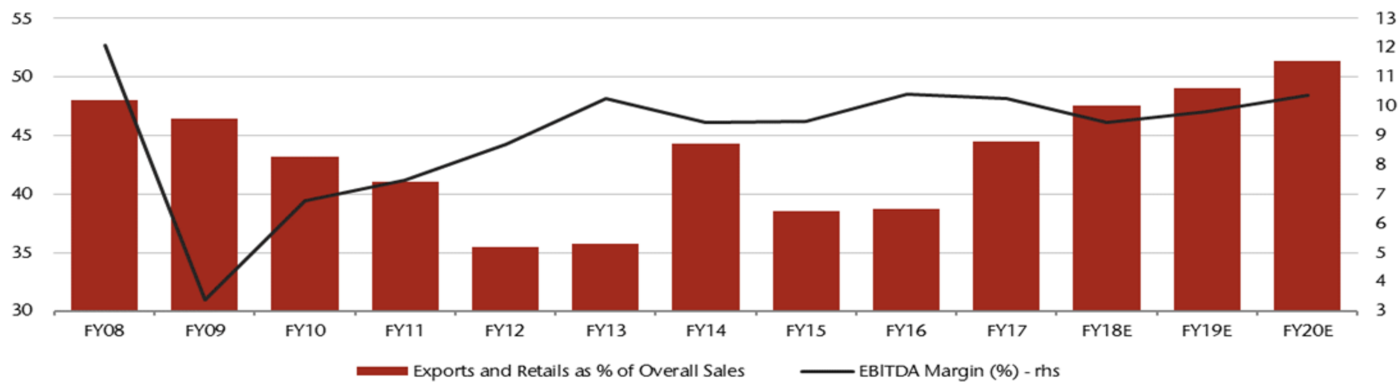
Source: Jefferies estimates, Company data

Exhibit 20: Extensive international footprint across 45 countries with 5 international offices

International Offices	Products sold
Dubai	Instrumentation Cables
Abu Dhabi	Instrumentation Cables
Singapore	Hi Tension Cables
Nigeria	Instrumentation Cables
Australia	Hi Tension Cables

Source: Jefferies estimates, company data

Exhibit 21: Rising share of exports and retail to boost margin upside as they have 100-200 bps better margin profile



Source: Jefferies estimates, Company data

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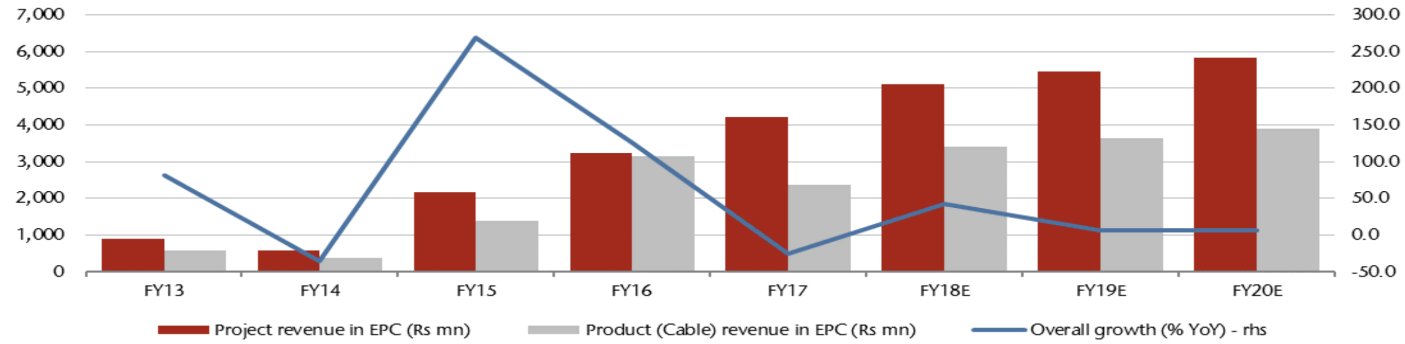
EPC to be steady on current base

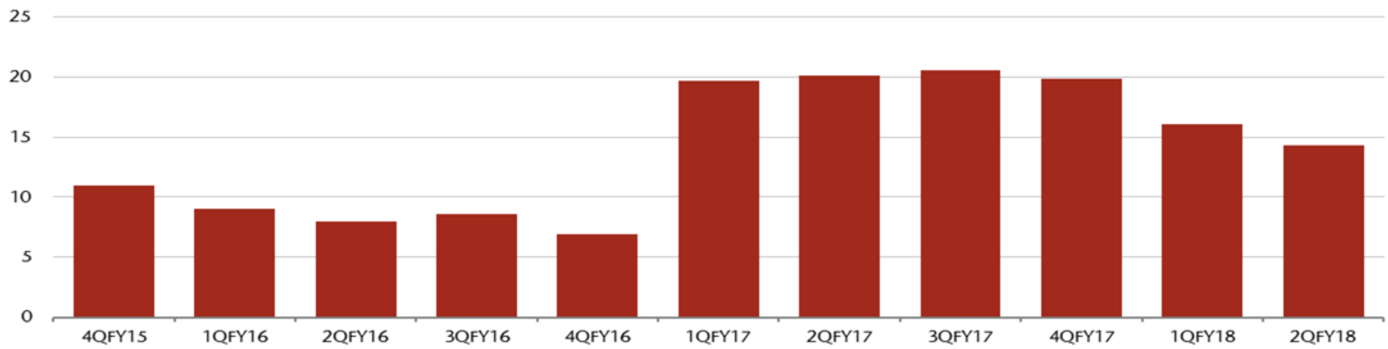
Extension of cables business: KEI entered the EPC segment in FY12 and has been bagging projects primarily under the Deen Dayal Upadhyaya Gram Jyoti Yojana and Integrated Power Development Scheme. These projects are primarily T&D-linked EPC and 40% of project size requires cables. Hence, KEI forayed into this field. Existing order book of Rs14 bn provides sufficient visibility for FY18E-20E EPC financials. This has contributed to higher working capital, resulting in D:E of 1.5x in FY17. However, going forward, revenue from this segment should stabilise, helping absolute debt levels to stay constant, despite our capex expectation of Rs3 bn during FY18E-20E. Effectively, D:E ratio should improve to 0.9x in FY20E, from 1.5x in FY17.

Exhibit 22: ~40% of EPC revenue is contributed by products (cables)



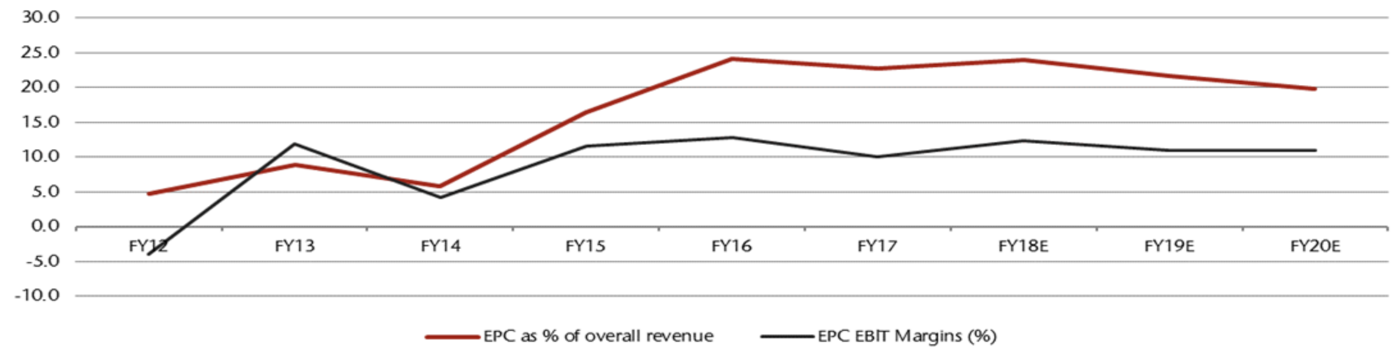
Source: Jefferies estimates, Company data

Exhibit 23: Majority of order book comprises orders from Uttar Pradesh (Rs bn)



Source: Jefferies, Company data

Exhibit 24: EPC margins to remain in double digits



Source: Jefferies estimates, Company data

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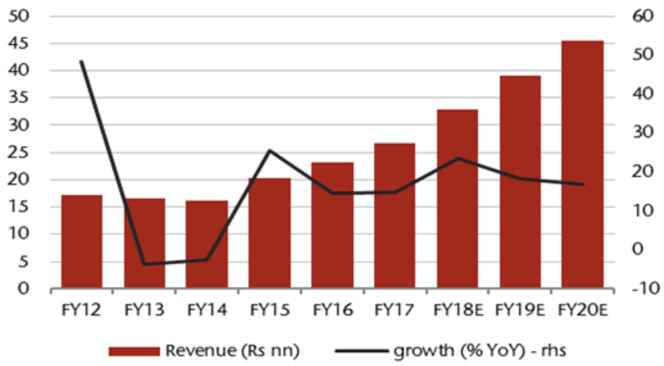
Asset sweating drives financials

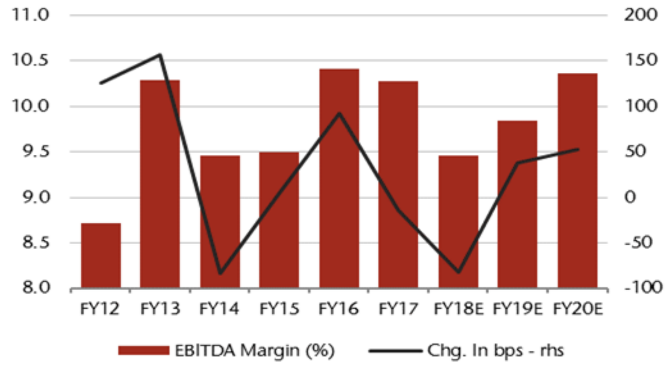
Anticipate Rs3 bn capex across segments except EHV: KEI has seen a sharp ROE improvement in the past 10 years, as it has gained scale which has led to margin stability and focussed asset sweating. Currently, all its capacities, except EHV, are running at 90%+ utilisation. EHV capacity addition has hurt FY18E margins, which should improve as utilisation of that segment picks up in FY19E-20E. We have factored Rs2.3 bn capex during FY19E-20E to expand existing facilities and cater to growth beyond FY20E.

Exhibit 25: Revenue to grow at 20% CAGR over FY17-20E



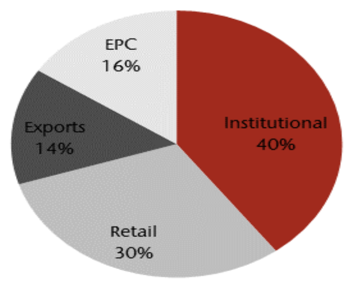
Source: Jefferies estimates, Company data

Exhibit 26: EBITDA margin to improve by 91bps over FY18E-20E



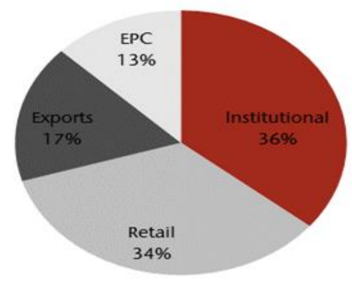
Source: Jefferies estimates, Company data

Exhibit 27: Exports and retail combined share to rise from 44% in FY17…



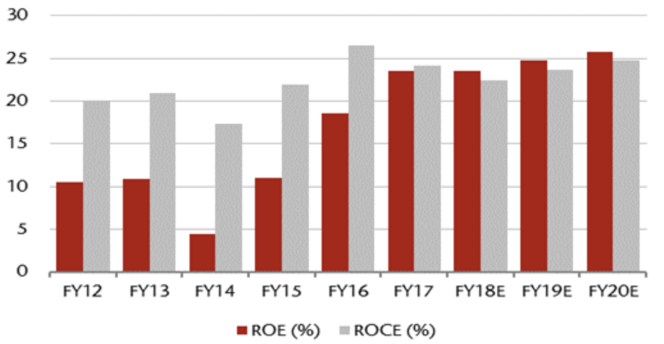
Source: Jefferies estimates, Company data

Exhibit 28: … to 51% in FY20E



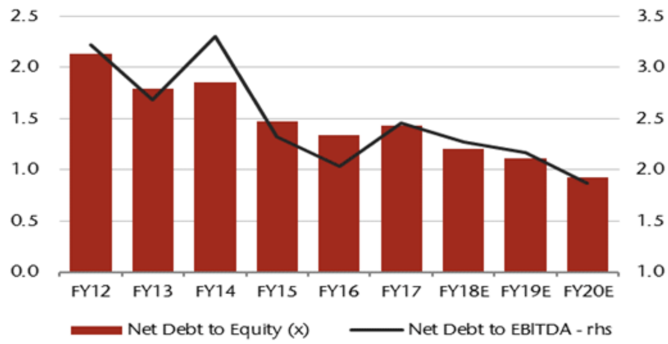
Source: Jefferies estimates, Company data

Exhibit 29: ROE to remain above 23% over FY18E-20E



Source: Jefferies estimates, Company data

Exhibit 30: Net debt to equity to be below 1x by FY20E



Source: Jefferies estimates, Company data

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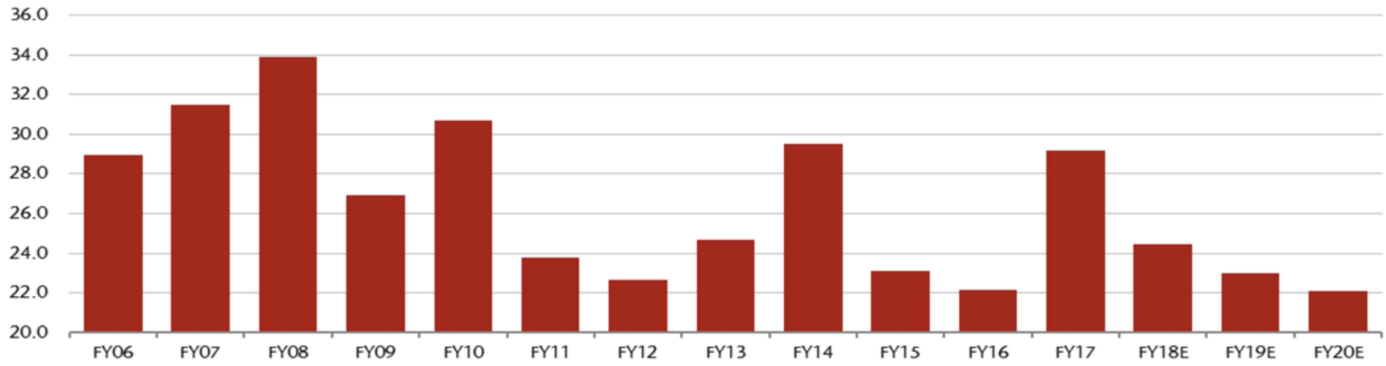
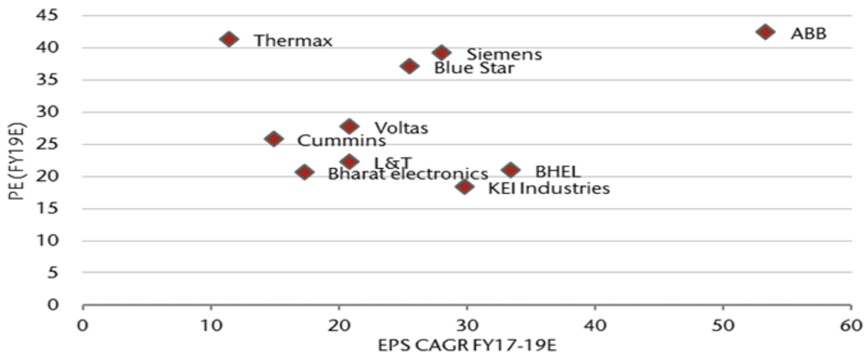
Exhibit 31: Working capital as a % of sales to ease off over FY18E-20E



Source: Jefferies estimates, Company data

Favourable comparison with peers on valuations but debt reduction needed to bridge gap: KEI has debt, unlike its peers, and hence we expect it to trade at some discount till it starts actual debt repayment. We estimate D:E ratio to reduce, given only some debt increase and rising net worth from profit. However, we believe KEI will take at least two-three years to pare down absolute debt, as it is still in an expansion phase. Within our coverage universe also, KEI is best placed in context of valuations and earnings growth.

Exhibit 32: KEI favourably placed among our coverage universe



Source: Jefferies estimates, company data

Exhibit 33: Comparative financials

Company	Revenue Growth (%)		EBITDA Margin (%)		EBITDA Margin chg. (bps)		PAT Growth (%)		ROE (%)		Net debt to equity (x)	
Indian Players	**FY16**	**FY17**	**FY16**	**FY17**	**FY16**	**FY17**	**FY16**	**FY17**	**FY16**	**FY17**	**FY16**	**FY17**
FINOLEX	0.59	8.33	13.87	14.03	3.17	0.16	25.27	26.93	17	18	(0.4)	(0.4)
HAVELLS	2.99	22.07	13.99	12.51	0.65	(1.48)	53.14	(24.30)	27	17	(0.4)	(0.5)
DIAMOND POWER	(16.12)	(90.54)	(2.43)	(340.38)	(6.57)	(337.95)	132.72	195.05	(37)	(124)	3.4	2.4
KEI	14.51	14.77	10.42	10.28	0.92	(0.14)	96.59	58.57	19	23	1.3	1.4

DIAMOND POWER (DIPI IN, Rs20, NC); HAVELLS (HAVI IN, Rs583, NC); FINOLEX (FNXC IN, Rs735, NC);
Source: Jefferies, company data, NC data Bloomberg

Exhibit 34: Comparative valuation

			P/E			P/B			ROE			Net Debt to Equity (x)		
Company	**CMP (loc. curr.)**	**MCap ($ m)**	**2018E**	**2019E**	**2020E**	**2018E**	**2019E**	**2020E**	**2018E**	**2019E**	**2020E**	**2018E**	**2019E**	**2020E**
FINOLEX	735	1,745	28.9	25.4	23.3	5.1	4.4	3.7	18.4	17.9	17.6	-0.3	-0.4	-0.5
HAVELLS	583	5,656	52.5	42.0	34.8	10.0	8.8	7.8	19.8	21.9	23.4	-0.2	-0.3	-0.5
KEI	398	476	24.8	18.6	14.1	5.2	4.1	3.2	23.5	24.8	25.7	1.2	1.1	0.9

HAVELLS (HAVI IN, Rs583, NC); FINOLEX (FNXC IN, Rs735, NC)
Source: Jefferies estimates, company data; NC data Bloomberg

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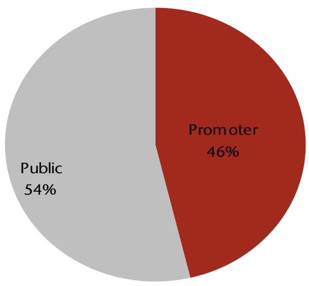
Shareholding Pattern



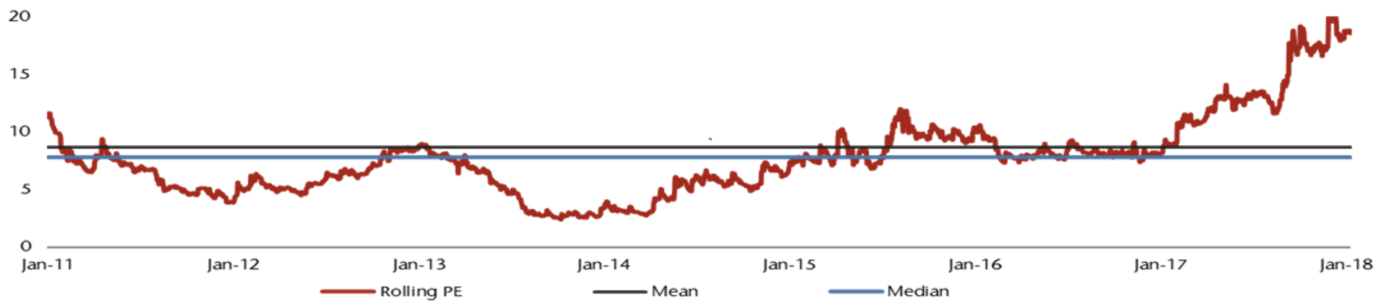
Source: Jefferies, BSE

Valuation – blend of growth and ROE

30% earnings CAGR, 23%+ ROEs, steady utility: KEI has transformed into a mid-sized cables and EPC company in the past decade. From volatility in margins given scale, it has moved to stable base and is in the right business growth segments. The company is a play on housing, capex and also engineering exports in India, which adds to its appeal. We believe it will sustain its 30% earnings CAGR during FY17-20E and ROEs will improve as it funds one/third of its expansion from its internal B/S.

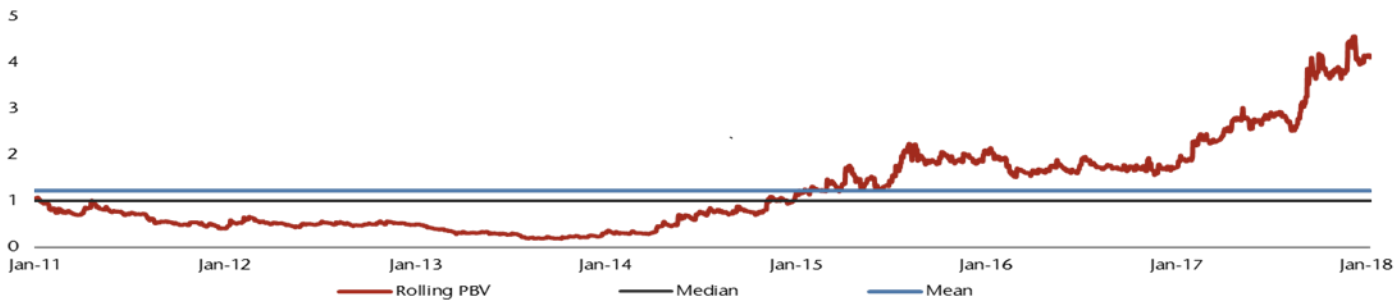
Our PT of Rs620 is based on a PE multiple of 22x PE FY20E, which might appear rich in context of its history (158% premium to historical average). However, particularly for KEI, historical valuations do not reflect the size and scale of the company currently and our target multiple is at a discount to peers. Additionally, our target multiple indicates a PE similar to its existing FY18E multiples currently with our assumption being strong earnings growth linked upside vs additional re-rating. However, we are confident that as it delivers on its expectations, scope for upside PE surprise also remains.

Exhibit 35: Trading above historical average on PE ...



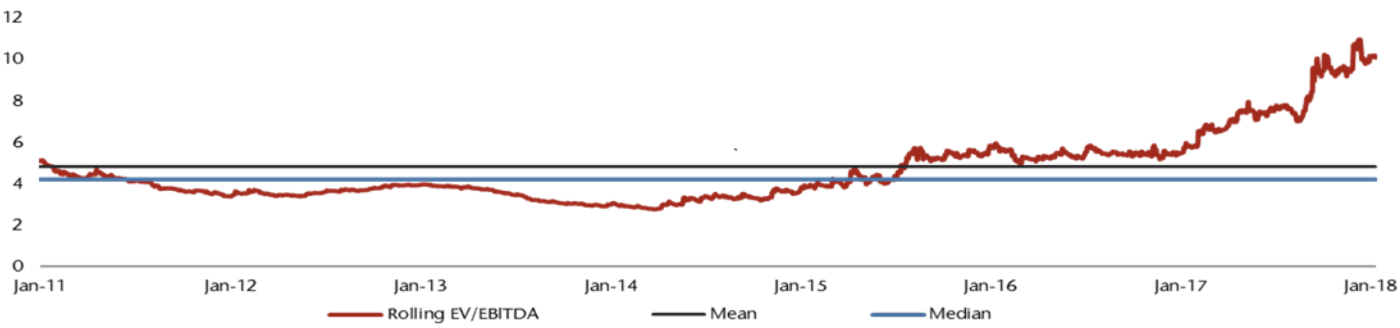
Source: Jefferies estimates, company data

Exhibit 36: ... on PB



Source: Jefferies estimates, company data

Exhibit 37: ... and on EV/EBITDA basis



Source: Jefferies estimates, company data

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Key risks

We believe downside risks to our estimates and price target are:

- **Sharp pricing competition in cables:** Currently, all organised players have maintained pricing and not really seen aggressive competition. In case there is a change in stance by one of the top-four players, it could signal margin compression going ahead.
- **One-off write-offs in EPC division:** EPC is a project business, unlike cables, and tends to have more volatility in revenue and margin booking. Any one-off losses there could lead to downside to our earnings expectations.

Management

Mr. Anil Gupta, Chairman-cum-Managing Director
Mr. Anil Gupta is a recognized and an accomplished expert in the Indian cable and wire industry. He became a part of the KEI group in 1979 as a partner in the erstwhile Krishna Electrical Industries. He soon rose to become its Chairman cum- Managing Director.

Mrs. Archana Gupta, Director
Mrs. Gupta has played a pivotal role in transforming Stainless Steel Wires Division at KEI Industries Limited. Mrs. Gupta heads planning, organising and optimizing resources for this division of KEI Industries Limited. Mrs. Gupta has been instrumental in the expansion of this division.

Mr. Rajeev Gupta, Executive Director (Finance) & CFO
Mr. Rajeev Gupta is B.Com. (Hons.) and a Chartered Accountant. Mr. Gupta has about 24 years' experience in Corporate Finance and currently heads the Finance & Accounts Department of KEI Industries Limited

Mr. Akshit Diviaj Gupta, Director
Mr. Akshit Diviaj Gupta has BBA degree in Management and Honorary Graduate Fellowship, and has an entrepreneurial background.

Mr. Pawan Bholusaria, Director
Mr. Pawan Bholusaria is a fellow Member of The Institute of Chartered Accountants of India. Mr. Bholusaria is a practicing Chartered Accountant.

Mr. K.G. Somani, Director
Mr. K.G. Somani is a fellow member of the Institute of Chartered Accountants of India. Mr. Somani is a practicing Chartered Accountant and is also the former president of The Institute of Chartered Accountants of India. Mr. Somani has been on the Board of Directors of many other Private/Public companies.

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Exhibit 38: Income statement

Rs mn	FY15	FY16	FY17	FY18E	FY19E	FY20E
Income from operations	**20,310**	**23,256**	**26,691**	**32,977**	**39,010**	**45,578**
Cost of materials consumed	15,133	15,682	18,687	23,084	27,307	31,904
as a % of sales	75	67	70	70	70	70
Purchases of stock in trade	31	10	16	17	19	20
as a % of sales	0	0	0	0	0	0
Increase/decrease in inventory	-395	455	-427	0	0	0
as a % of sales	-2	2	-2	0	0	0
Employee cost	621	828	1,109	1,220	1,342	1,477
as a % of sales	3	4	4	4	3	3
Subcontractor expense for turnkey	0	596	579	660	780	912
as a % of sales	0	3	2	2	2	2
Other expenses	2,991	3,262	3,983	4,877	5,724	6,541
as a % of sales	15	14	15	15	15	14
Total Expenditure	18,381	20,833	23,948	29,859	35,172	40,854
EBITDA	**1,929**	**2,423**	**2,743**	**3,119**	**3,837**	**4,724**
Other non-operational income	24	53	104	150	125	120
Interest income/expense	1,204	1,270	1,229	1,100	1,150	1,190
Depreciation & amortisation	246	253	280	330	370	430
Miscellaneous exp. Written off	0	0	0	0	0	0
Extraordinary income/expense	26	0	0	0	0	0
PBT	**529**	**953**	**1,338**	**1,839**	**2,442**	**3,224**
Tax	186	331	351	588	782	1,032
Tax rate%	35	35	26	32	32	32
PAT (Reported)	**342**	**622**	**986**	**1,250**	**1,661**	**2,192**
PAT (Adjusted)	**316**	**622**	**986**	**1,250**	**1,661**	**2,192**

Source: Jefferies estimates, company data

Exhibit 39: Balance sheet

Rs mn	FY15	FY16	FY17	FY18E	FY19E	FY20E
Share Capital	154	154	156	156	156	156
Reserves & surplus	2,884	3,512	4,579	5,756	7,326	9,409
Networth	**3,039**	**3,666**	**4,735**	**5,912**	**7,482**	**9,565**
Preference capital	0	0	0	0	0	0
Total loan funds	**4,520**	**4,972**	**7,118**	**7,618**	**8,418**	**9,118**
Amt. recd. Und. Long term infra	0	0	0	0	0	0
Deferred tax	235	362	427	464	513	577
Sources of funds	**7,794**	**9,001**	**12,280**	**13,994**	**16,413**	**19,260**
Fixed assets	4,451	4,995	6,044	6,644	7,944	8,944
Less: Depreciation/amortisation	1,470	1,716	1,990	2,320	2,690	3,120
CWIP	44	484	44	44	44	44
Net block	**3,025**	**3,763**	**4,098**	**4,368**	**5,298**	**5,868**
Investments	31	31	31	1,031	2,031	3,031
Liquid Investments	0	0	0	0	0	0
Current Assets	**10,361**	**10,835**	**13,981**	**15,579**	**17,559**	**20,513**
Inventories	4,403	4,225	4,989	5,692	6,626	7,492
Sundry debtors	5,041	5,951	7,683	8,312	9,619	11,238
Cash & bank balance	47	58	370	525	114	283
Loans and advances	870	602	939	1,050	1,200	1,500
Other current assets	0	0	0	0	0	0
Current liabilities & provisions	**5,623**	**5,628**	**5,830**	**6,984**	**8,475**	**10,152**
Advances from customers	225	173	440	660	780	912
Other Liabilities	5,399	5,455	5,390	6,324	7,695	9,240
Provision for tax	0	0	0	0	0	0
Provision for dividend	0	0	0	0	0	0
Net current assets	4,738	5,207	8,151	8,596	9,084	10,361
Miscellaneous Expenditure	0	0	0	0	0	0
Intangibles	0	0	0	0	0	0
Application of funds	**7,794**	**9,001**	**12,280**	**13,994**	**16,413**	**19,260**

Source: Jefferies estimates, company data

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Exhibit 40: Cash flow Statement

Rs mn	**FY15**	**FY16**	**FY17**	**FY18E**	**FY19E**	**FY20E**
PBIT	1,733	2,223	2,567	2,939	3,592	4,414
Add: depreciation	246	253	280	330	370	430
Less other income	-24	-53	-104	-150	-125	-120
Working capital changes	85	-458	-2,632	-288	-900	-1,109
Less: tax	-111	-204	-287	-552	-733	-967
Others	51	92	214	0	0	0
Net cash from operations (a)	1,979	1,852	38	2,279	2,205	2,648
Change in fixed assets	-136	-984	-608	-600	-1,300	-1,000
Change in investments	0	0	0	-1,000	-1,000	-1,000
Add: other income	24	53	104	150	125	120
Others	-54	-45	-113	0	0	0
Cash flow from inv. (b)	-166	-975	-617	-1,450	-2,175	-1,880
Proceeds from issue of equity	63	63	63	0	0	0
Change in borrowings	-584	452	2,146	500	800	700
Dividends paid + dividend tax	-35	-43	-53	-73	-91	-109
Interest paid	-1,204	-1,270	-1,229	-1,100	-1,150	-1,190
Others	-52	-68	-36	0	0	0
Financial cash flow (c)	-1,811	-866	891	-673	-441	-599
Net inc/dec in cash (a+b+c)	1	11	312	156	-411	169
Add: opening cash balance	46	47	58	370	525	114
Closing cash balance	47	58	370	525	114	283

Source: Jefferies estimates, company data

Exhibit 41: Key ratios

	FY15	**FY16**	**FY17**	**FY18E**	**FY19E**	**FY20E**
Diluted EPS (Rs)	4.1	8.0	12.7	16.1	21.3	28.2
BVPS (Rs)	39.1	47.1	60.9	76.0	96.2	122.9
Dividend per share	0.40	0.50	0.60	0.80	1.00	1.20
Dividend payout	11.0	7.0	5.3	5.8	5.5	5.0
Valuation (x)						
Diluted PE	97.8	49.8	31.4	24.8	18.6	14.1
Diluted EV/EBITDA	18.4	14.8	13.7	12.2	10.2	8.4
Diluted PSR	1.5	1.3	1.2	0.9	0.8	0.7
PBV	10.2	8.4	6.5	5.2	4.1	3.2
Profitability Ratios						
ROCE %	21.9	26.5	24.1	22.4	23.6	24.7
ROE%	11.0	18.6	23.5	23.5	24.8	25.7
Turnover Ratios						
Inventory in days	76	68	63	63	62	60
Debtor days	86	86	93	92	90	90
Creditors turnover	86	85	74	70	72	74
Wkg. Capital cycle	76	69	82	85	80	76

Source: Jefferies estimates, company data

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Company Description

KEI Industries (KEI) is among the top 4 organised players in the Indian cables industry and an EPC player in power T&D.

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Investment Recommendation Record

(Article 3(1)e and Article 7 of MAR)

Recommendation Published	, 16:52 ET. January 28, 2018
Recommendation Distributed	, 17:00 ET. January 28, 2018

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Buy - Describes securities that we expect to provide a total return (price appreciation plus yield) of 15% or more within a 12-month period.

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Underperform - Describes securities that we expect to provide a total return (price appreciation plus yield) of minus 10% or less within a 12-month period.

The expected total return (price appreciation plus yield) for Buy rated securities with an average security price consistently below $10 is 20% or more within a 12-month period as these companies are typically more volatile than the overall stock market. For Hold rated securities with an average security price consistently below $10, the expected total return (price appreciation plus yield) is plus or minus 20% within a 12-month period. For Underperform rated securities with an average security price consistently below $10, the expected total return (price appreciation plus yield) is minus 20% or less within a 12-month period.

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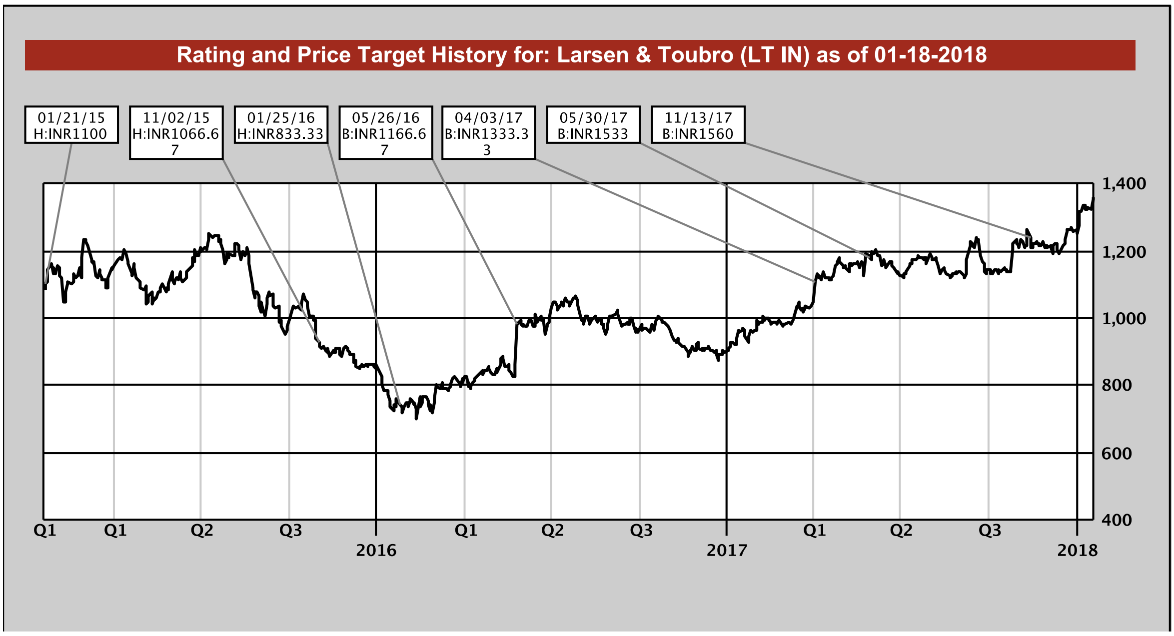
Other Companies Mentioned in This Report

- ABB Limited (ABB IN: INR1,659.30, BUY)
- KEI Industries Ltd (KEII IN: INR400.10, BUY)
- Larsen & Toubro (LT IN: INR1,416.50, BUY)
- Power Grid Corporation of India Limited (PWGR IN: INR194.30, HOLD)
- Siemens Limited (SIEM IN: INR1,296.10, HOLD)



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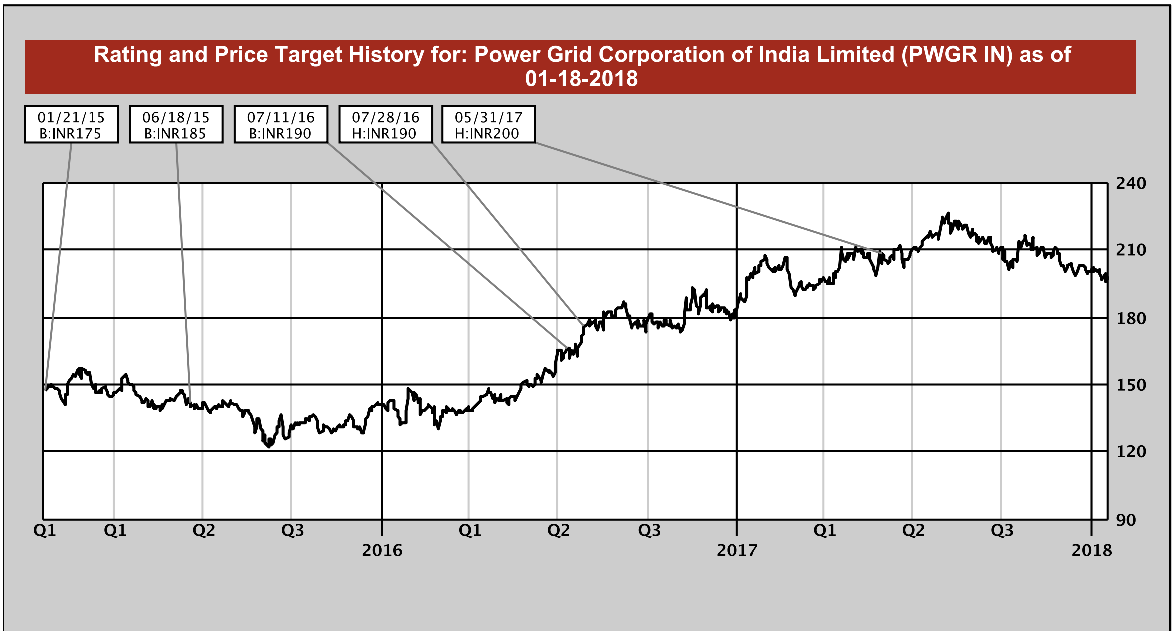

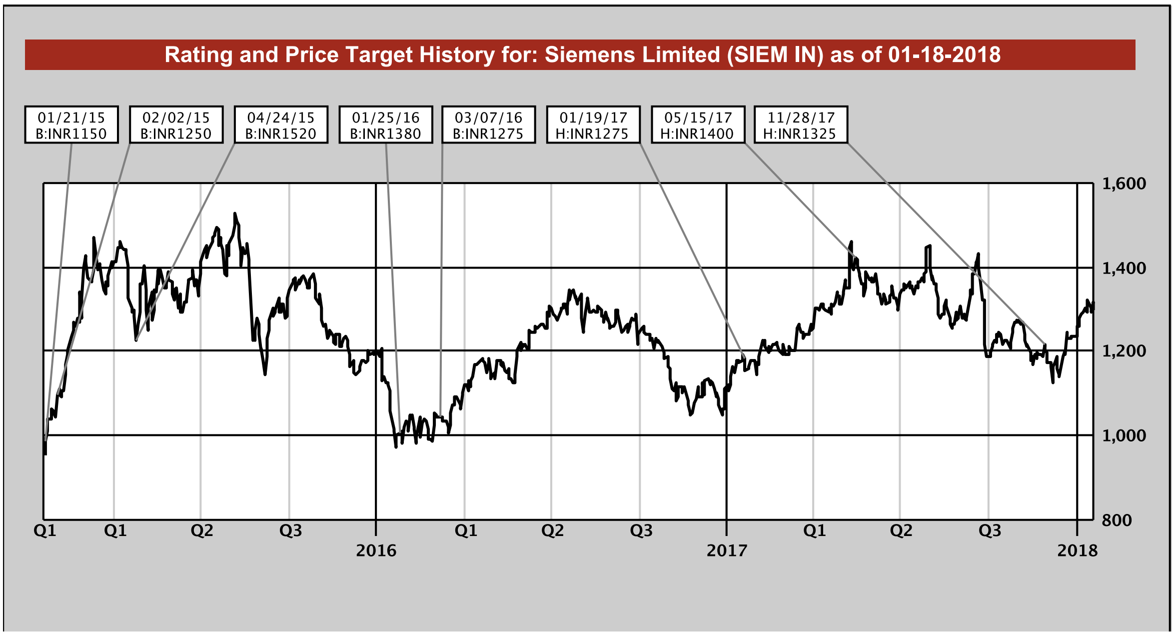

Notes: Each box in the Rating and Price Target History chart above represents actions over the past three years in which an analyst initiated on a company, made a change to a rating or price target of a company or discontinued coverage of a company.

Legend:

I: Initiating Coverage

D: Dropped Coverage

B: Buy

H: Hold

UP: Underperform

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Distribution of Ratings

Rating	Count	Percent	IB Serv./Past 12 Mos.		JIL Mkt Serv./Past 12 Mos.	
			Count	Percent	Count	Percent
BUY	1100	53.22%	342	31.09%	66	6.00%
HOLD	822	39.77%	161	19.59%	23	2.80%
UNDERPERFORM	145	7.01%	20	13.79%	3	2.07%

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