Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

KEI Industries Ltd

Visible growth trajectory, reasonable valuations

Capital Goods	Sharekhan code: KEI		
Reco/View: Buy ↔	CMP: Rs. 1,214	Price Target: Rs. 1,410 ↑	

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

ESG Disclosure Score NEW

ESG RISK RATING 24.94
Updated Apr 08, 2022

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

Company details

Market cap:	Rs. 10,939 cr
52-week high/low:	Rs. 1,377/690
NSE volume: (No of shares)	2.44 lakh
BSE code:	517569
NSE code:	KEI
Free float: (No of shares)	5.6 cr

Shareholding (%)

Promoters	38.0
FII	26.5
DII	19.5
Others	16.0

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	1.2	1.7	22.7	70.3
Relative to Sensex	-3.0	4.2	24.2	64.9

Sharekhan Research, Bloomberg

Summary

- We retain Buy rating on KEI with a revised PT of Rs. 1,410, factoring in a promising growth outlook and reasonable valuation.
- KEI Industries reported strong numbers for Q1Y2023 helped by low base and registered ~27%/~61% volume/value growth in cables and wires segment. Higher input cost continued to weigh on gross/operating margin which reduced by ~612/~100 bps and came in at ~24.9%/10.2%.
- The management expects a 17-18% revenue CAGR in the next two-three years with 30-35% y-o-y growth in the retail business. It also eyes an operating margin of 10.5-11% and PAT margin of 6.5% in FY23.
- De-bottlenecking in existing capacities and greenfield expansion in cables and wires at ~ Rs. 800 crore investment (first phase by 2024E) would help sustain its high-growth trajectory.

KEI Industries' Q1FY23 standalone performance was above our estimates on all the fronts. Its sales grew by ~54% y-o-y to Rs 1,565 crore. The growth was driven by strong performance of domestic institutional wire and cables business, exports and EHV cables. Total institutional cable sales including export contributed 48.9% in Q1FY23 against 49.46% in Q1FY22. Sales through dealer/distribution market increased by 68.3% Y-y-o-y and contributed ~42% to overall sale as against 38% in Q1FY22. The rise in commodity cost and inflationary pressures weighed on profitability with operating margin declining by ~100bps y-o-y to 10.2% (although above our estimate of 9.9%). Net profit grew by ~55% y-o-y to Rs 104crore (beating our estimate of Rs 87crore) led by strong revenues and lower interest costs. Net debt including acceptances declined and stood at Rs 32 cr (vs Rs 270cr in Q4FY22). The management targets to grow its revenues at 17-18% CAGR (retail to grow at 30-35% p.a.) over the next three years. The company would be undertaking greenfield expansion in the cables segment at an investment of ~Rs. 800 crore (land acquisition to be done in next couple of months- first phase by 2024E) to maintain a high-growth trajectory.

Key positives

- Fall in net debt (including acceptances) to Rs 32 crore (vs Rs 270 crore in Q4FY22) would further reduce interest cost.
- Revenues from dealer/distribution network increased by ~68% y-o-y contributing over 42% to total revenues. Export in institutional cables more than doubled y-o-y to Rs 193 crore.

Key negatives

- OPM remained under pressure on account of the rise in input cost.
- There has been some delay in land acquisition for capacity expansion in LT, HT and EHV cables.
- Decline in commodity prices has led to destocking by the channel partners.

Management Commentary

- The company retained its revenue growth guidance of 17-18% CAGR for the next three years with retail sales growing at 30-35% CAGR.
- The management expects continuous demand generation in the long-term from government infrastructure spend, private industrial capex and real estate. It expects good demand in the coming quarters in both institutional and retail businesses due to the cooling off of commodity prices. It also expects revenue from exports to be around Rs 750cr in FY23.
- The company has cut prices by 8-9% in the last one and a half months following decline in commodity prices.
- The company is undertaking greenfield capacity expansion in LT, HT and EHV with a capex of ~Rs. 800 crore over 3 years. The annual capex is expected to be around Rs 200-250 crore. The company through debottlenecking would improve the capacity utilization of its existing plants including EHV cables.

Revision in estimates – We have maintained our estimates for FY2022-FY2024E

Our Call

Valuation: Retain Buy with a revised PT of Rs. 1,410: KEI's growth outlook is expected to be positive with its diversified user industries, increased focus on retail, high-margin EHV cables business and export sales along with a focused-industry approach as well as utilization-driven capex plans. These are likely to help in sustaining a strong growth trajectory. An uptick in infrastructure spending, likely pick up in private capex and increasing housing demand bodes well for its institutional and retail business. KEI is focusing on brand-building, distribution expansion & increasing B2C sales which shall bear healthy results in the medium to long-term. The stock is currently trading at a P/E of ~19x its FY2024E EPS, thereby leaving further headroom for upside. Hence, we maintain a Buy on the stock with a revised PT of Rs. 1,410.

Key Risks

Volatility in input cost may adversely impact its margin guidance. A part of its revenue is generated from exports and any fluctuations in forex rates could affect the company's financials.

Valuation (Standalone) Rs cr

Particulars	FY21	FY22	FY23E	FY24E
Revenue	4,181	5,727	6,769	8,023
OPM (%)	10.9	10.3	11.0	11.4
Adjusted PAT	270	376	479	586
% y-o-y growth	5.7	39.6	27.2	22.3
Adjusted EPS (Rs.)	30.0	41.8	53.1	65.0
P/E (x)	40.5	29.1	22.9	18.7
P/B (x)	2.0	1.6	1.3	1.1
EV/EBITDA (x)	8.9	7.0	5.2	4.1
RoNW (%)	15.2	17.7	18.5	18.5
RoCE (%)	20.0	22.5	24.1	24.5

Source: Company; Sharekhan estimates

Low base and healthy volumes drive performance

KEI Industries' Q1FY23 standalone performance was above our estimates on all fronts. Its sales grew by ~54% y-o-y to Rs 1,565 crore primarily driven by ~27%/~61% volume/value growth in the cables and wires segment. The growth was a result of strong domestic institutional sales, exports and EHV cables. Total institutional cable sales including export contributed 48.9% in Q1FY23 against 49.46% in Q1FY22. Sales through the dealer/ distribution market increased by 68.3% Y-o-y and contributed ~42% to overall sales as against 38% in Q1FY22. Rise in commodity cost and inflationary pressures weighed on profitability with operating margin declining by ~98bps y-o-y to 10.2% (although above our estimate of 9.9%). Net profit grew by ~55% y-o-y to Rs 104crore (beating our estimate of Rs 87crore) led by strong revenues and lower interest costs. Net debt including acceptances declined and stood at Rs 32 cr (vs Rs 270cr in Q4FY22).

Robust demand outlook

The management remains optimistic about expanding its retail franchise by expanding the dealer and distribution base (currently at 1,800 in numbers) and expects its retail segment to grow by 30-35% y-o-y. It wants to increase its market share in house wires to 8% (currently ~6%), while in cables it has a market share of ~12%. The company expects continuous demand from government infra and private capex and is focused on growing exports too. The company is strategically reducing its exposure to EPC business which is capital intensive and low margin and utilising the funds to channel the retail segment's growth. The company would be expanding LT, HT and EHV capacity over 3-4 years with an investment of ~ Rs 800 crore. The company has acquired land in Baroda, Gujarat for capacity expansion and the first phase should be commercially operational by FY23E.

KEI Q1FY2023 Conference call highlights:

- **Guidance:** The company retained its retail sales target of over a 50% contribution in the next two years. The increasing contribution of the retail segment to total revenues would reduce the pricing gap with its competitors. The company targets to achieve a 17-18% revenue CAGR in the coming years.
- **Sanguine demand environment:** The company expects healthy demand from government infrastructure, private capex and real estate projects. It also expects demand for wires and cables to increase given investments and capacity expansion by companies under PLI scheme. Further, a decline in commodity prices leading to price reduction should spur demand for end products in both institutional and retail businesses.
- **Destocking by channel partners:** The company stated that there has been de-stocking of high-value inventory by channel partners and dealers due to a decline in commodity prices. This may impact sales for a few weeks, although the company expects the channel inventory to start picking up soon. Further, it added that companies with higher retail exposure are likely to be impacted more due to destocking.
- **Expansion:** The company is undertaking greenfield capacity expansion in LT, HT and EHV with a capex of ~Rs. 800crore over 3-4 years. The land cost is expected to be around Rs 50-60 cr. The company plans to achieve additional sales of Rs 4,000-5,000 crore out of the capacity expansion.
- **Capex:** The annual capex is expected to be around Rs 200-250crore p.a. (including spending on a new manufacturing facility at Baroda, Gujarat) over the next two-three years. The capacity utilization in EHV cables is 80-90% currently. However, the company can achieve 20-25% revenue growth in EHV through debottlenecking.
- **North region is the highest contributor to revenue:** Q1FY23 Revenue break up - 35% from North, ~31% from West, 19% from South and 15% from Eastern region.
- **Other highlights:** Order book is at Rs 2,741 crore :- EPC @ Rs. 878 crore, EHV @Rs 353 crore, L1 order of Rs 229 crore in EHV, domestic cables @Rs 1,048 crore, exports @Rs 42 cr.

Results (Standalone) **Rs cr**

Particulars	Q1FY23	Q1FY22	y-o-y (%)	Q4FY22	q-o-q (%)
Revenue	1,565	1,018	53.8	1,792	(12.6)
Operating profit	160	114	40.4	172	(7.1)
Other Income	4	3	27.1	8	(54.9)
Interest	9	11	(19.2)	10	(8.2)
Depreciation	14	14	0.2	14	0.1
PBT	140	91	53.5	156	(10.1)
Tax	36	24	50.5	40	(9.1)
Reported PAT	104	67	54.6	116	(10.5)
Adj. PAT	104	67	54.6	116	(10.5)
Adj.EPS	11.5	7.4	54.6	12.9	(10.5)
Margin			BPS		BPS
OPM (%)	10.2	11.2	(98)	9.6	60
NPM (%)	6.6	6.6	3	6.5	16
Tax rate	25.9	26.4	(53)	25.6	29

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Ample levers offer scope for growth

Domestic demand is improving with unlocking, infrastructure, and construction back in action with labour issues largely resolved, which provides a positive outlook ahead. The wires and cables industry contributes 40%-45% to India's electrical equipment industry. In terms of volumes, the Indian cables & wires industry (including exports) has grown from 6.3 million km in FY2014 to 14.5 million km in FY2018, posting a ~23% CAGR over the period. The industry registered an ~11% CAGR in value terms, from Rs. 34,600 crore in FY2014 to Rs. 52,500 crore in FY2018. The cables & wires industry was expected to register a CAGR of 14.5% from Rs. 52,500 crore in FY2018 to Rs. 1,03,300 crore by FY2023. The government has envisaged a Rs. 111 lakh crore capital expenditure in infrastructure sectors in India from FY2020 to FY2025. Sectors such as energy (24%), roads (18%), urban (17%), and railways (12%) amount to ~71% of the projected infrastructure investments. The continued thrust of the government on infrastructure investment is expected to improve demand for the W&C industry.

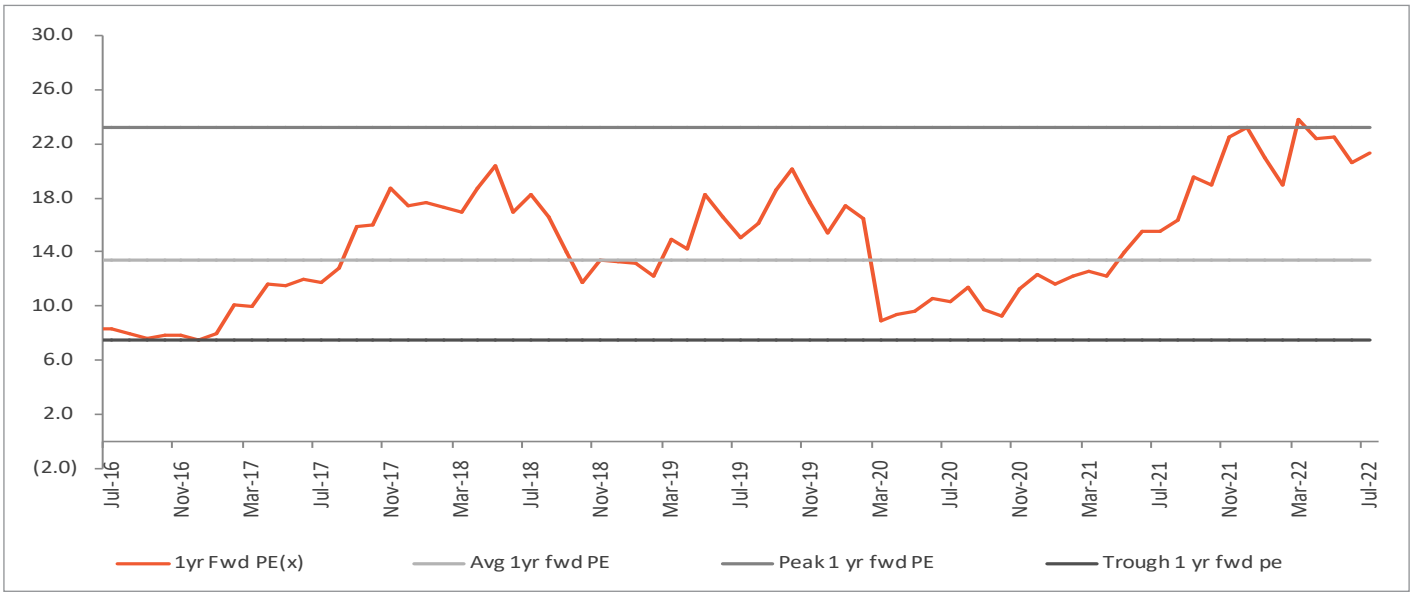
■ Company outlook - High growth to be added by capacity expansion plan

The management remains optimistic about the retail and EHV segments in the longer run. It is focused on expanding its retail franchise through expanding its dealer and distribution base (currently at 1,805 and expects it to increase by 20% y-o-y) and expects its retail segment to contribute more than 45% to revenue by FY2023. The management will also cut down its EPC business and utilise the money to channelise the retail segment's growth. On the high-margin EHV front, which remains a Rs. 2,000 crore market in India, the total capacity is Rs. 1,000-1,100 crore between the company and Universal cables. The company will be undertaking a greenfield Capex of ~Rs.800 crore in LT, HT, and EHV over a three to four-year period. The management expects 17-18% y-o-y revenue growth CAGR in the next two-three years.

■ Valuation - Retain Buy with a revised PT of Rs. 1,410

KEI's growth outlook is expected to be positive with its diversified user industries, increased focus on retail, high-margin EHV cables business and export sales along with a focused-industry approach as well as utilization-driven capex plans. These are likely to help in sustaining a strong growth trajectory. An uptick in infrastructure spending, likely pick up in private capex and increasing housing demand bodes well for its institutional and retail business. KEI is focusing on brand-building, distribution expansion & increasing B2C sales which shall bear healthy results in the medium to long-term. The stock is currently trading at a P/E of ~19x its FY2024E EPS, thereby leaving further headroom for upside. Hence, we maintain a Buy on the stock with a revised PT of Rs. 1,410.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

KEI is among the top three organized players in the Indian W&C industry and an EPC player in the power T&D segment. KEI has a diversified business model with a significant presence in domestic and international markets. The company services retail and institutional customers and caters to both private and public sector clients. Currently, KEI manufactures and markets power cables and addresses cabling requirements of a wide spectrum of sectors such as power, oil refineries, railways, automobiles, cement, steel, real estate, etc. KEI has built its manufacturing facilities in Rajasthan and Silvassa (Dadra and Nagar Haveli). The company is well poised to garner opportunities from power utilities, core infrastructure, and construction projects across the country. The company's prudent foray into the EHV cable for power sector projects has further expanded the opportunity horizon.

Investment theme

Over the years, the company has established its presence in the institutional space by developing the ability to offer various products across locations. KEI has a well-entrenched marketing presence across all states, which increases its ability to deliver products speedily from plants in North and West India. The company has created a presence in building specialized offerings to tap niche segments such as the shipping sector, oil and petroleum plants, etc. The company is now looking at tapping several large realty brands and strengthening its all-India presence by embarking on opening new warehouses across India. The retail segment comprises house wires (HW) and a part of low-tension cables (LT) sold through dealers. Given its growing dealer network and brand-building initiatives (advertising and sponsoring), performance-linked schemes, dealer-electrician meets etc., we expect KEI to increase its retail presence further.

Key Risks

- Volatility in input cost may adversely impact its margin guidance.
- A part of its revenue is generated from exports and any fluctuations in forex rates could affect the company's financials.

Additional Data

Key management personnel

Mr. Anil Gupta	Chairman and Managing Director
Mrs. Akshit Diviaj Gupta	Executive Director
Mrs. Archana Gupta	Non-Executive – Non-Independent Director
Mr. Rajeev Gupta	CFO

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Anil Gupta	12.98
2	Projection Financial & Management Consultants Private Ltd.	8.77
3	Anil Gupta HUF -karta Anil Gupta	5.16
4	Smallcap World Fund, Inc	5.02
5	Shubh Laxmi Motels & Inns Private Ltd.	3.86
6	Soubhagya Agency Private Ltd.	3.47
7	Hdfc Trustee Co. Ltd A/c	2.70
8	Franklin Build India Fund	2.65
9	Invesco India ESG Equity Fund	2.28
10	DSP Value Fund	2.23

Source: Capitaline, Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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