MORNING INSIGHT

kotak Securities

PRIVATE CLIENT RESEARCH

JUNE 13, 2017

Economy News

- Retail inflation hit a record low of 2.18% in May, mainly as food inflation touched a fresh low of -1.05%, partly reflecting the crash in prices of farm items following a good harvest. (Financial Express)
- Industrial output in the country rose by 3.1 per cent in April from a year earlier, mainly due to an increase in electricity generation and mining. (BS)
- Piyush Goyal, Minister of State for Power, Coal, New and Renewable Energy and Mines, said that the Centre is close to finding a solution to tackle the problem of financially stressed assets in the power sector, with focus likely on cases where no significant irregularities are detected or where the promoters are not found to be wilful defaulters. (Indian Express)
- Oil marketing companies (OMCs) maintain that daily petrol and diesel retail price revision will result in better management of inventories. The dealers are set to meet the OMC representatives on Tuesday to put forward their concerns regarding inventory losses which have been ignored. (Financial Express)

Corporate News

- The board of directors of Reliance General Insurance Company Ltd (RGI), a 100 per cent subsidiary of **Reliance Capital**, has approved a proposal to independently list the company on the stock exchanges. (ET)
- Reliance Jio wants lower fees to help telecom sector to thrive. The suggestion was made by Jio in its presentation before a government-appointed inter-ministerial group (IMG) that started meeting different sets of operators to assess the problems in the telecom sector. (Financial express)
- **Tata Motors**-owned Jaguar Land Rover (JLR) has invested $25 million (mn) in Lyft, a US ride-hailing company. The idea is a partnership to include the development and testing of autonomous cars. (BS)
- **Sagar Cement** is expecting around 18 per cent jump in its production to 2.6 million tonnes in FY 2017-18. The company is also targeting an overall market growth of 10 per cent on consolidated basis from its captive market spread between South Maharashtra and Odisha. (ET)
- **PFC Corp** has got the government approval for issuing bonds, redeemable after three year and eligible for exemption from capital gains tax. (ET)
- **Federal Bank** expects loan growth of 18-20% this fiscal. It is confident of being ahead of the curve in handling non-performing assets (NPAs) and achieving credit growth in the coming quarters. Federal Bank's asset quality improved in the fourth quarter of last fiscal with slippages at Rs 2.4 Bn - the lowest in the last seven quarters. (BL)
- **Strides Shasun** has received the US health regulator's nod for Amantadine Hydrochloride tablets, used in the treatment of Parkinson's disease and Shingles to reduce pain. (BL)
- **Axis Bank** has informed the exchanges that it proposes to raise Rs 50 Bn. The bank will issue unsecured redeemable non-convertible subordinated debentures (Basel-III compliant Tier 2 debentures) of face value Rs 10 lakh each for cash at par aggregating to Rs 50 Bn. (BL)

Source: ET = Economic Times, BS = Business Standard, FE = Financial Express, BL = Business Line, ToI: Times of India, BSE = Bombay Stock Exchange

Equity

		% Chg		
	12 Jun 17	1 Day	1 Mth	3 Mths
Indian Indices				
SENSEX Index	31,096	(0.5)	3.0	7.4
NIFTY Index	9,616	(0.5)	2.3	7.6
BANKEX Index	26,547	(1.0)	3.2	12.4
SPBSITIP Index	10,143	0.4	1.2	(3.0)
BSETCG INDEX	17,423	(1.6)	(2.9)	12.9
BSEOIL INDEX	13,755	(0.3)	(3.6)	3.6
CNXMcap Index	17,879	(0.6)	(2.0)	9.7
SPBSSIP Index	15,454	(0.6)	(0.5)	13.6
World Indices				
Dow Jones	21,236	(0.2)	1.6	1.7
Nasdaq	6,175	(0.5)	0.9	5.1
FTSE	7,512	(0.2)	1.0	2.0
NIKKEI	19,909	(0.5)	0.0	1.3
HANGSENG	25,708	(1.2)	2.5	8.2

Value traded (Rs cr)

	12 Jun 17	% Chg - Day
Cash BSE	3,099	0.7
Cash NSE	20,226	(9.4)
Derivatives	-	-

Net inflows (Rs cr)

	9 Jun 17	% Chg	MTD	YTD
FII	(69)	(103.3)	9,957	50,479
Mutual Fund	(9)	(101.0)	10,473	32,452

FII open interest (Rs cr)

	9 Jun 17	% Chg
FII Index Futures	23,522	3.8
FII Index Options	66,260	2.8
FII Stock Futures	73,456	(0.0)
FII Stock Options	7,438	3.7

Advances / Declines (BSE)

12 Jun 17	A	B	T	Total	% total
Advances	86	416	44	546	100
Declines	209	727	63	999	183
Unchanged	3	22	15	40	7

Commodity

		% Chg		
	12 Jun 17	1 Day	1 Mth	3 Mths
Crude (US$/BBL)	46.3	0.5	(3.2)	(4.3)
Gold (US$/OZ)	1,267.1	(0.1)	3.2	5.2
Silver (US$/OZ)	17.0	(1.5)	3.0	(0.4)

Debt / forex market

	12 Jun 17	1 Day	1 Mth	3 Mths
10 yr G-Sec yield %	6.5	6.5	6.9	6.9
Re/US$	64.4	64.3	64.3	66.6

Sensex

COMPANY UPDATE

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FIEM INDUSTRIES LTD (FIEM)

PRICE: RS.865 **RECOMMENDATION: BUY**
TARGET PRICE: RS.1,254 **FY19E P/E: 12.4x**

FIEM's performance iS expected to improve in FY18 on the back of expected healthy two wheeler industry growth and strong performance by FIEM's key clients. In the auto business (accounted for 94% of FIEM's FY17 revenues), we expect strong revenue growth over FY17-FY19E. Domestic two wheeler industry has shown initial signs of strong growth in FY18. FIEM's top two clients - Honda Motorcycle India Limited (HMSI) and TVS Motors - have reported robust volume growth in April/May 2017 and that augurs positively for FIEM. LED business (6% of FIEM's FY17 revenues) performance is expected to remain weak in the near to medium term. EBITDA margin is expected to witness gradual improvement in FY18/ FY19. We retain BUY on the stock with unchanged price target of Rs1,254.

Summary table

(Rs mn)	FY17	FY18E	FY19E
Sales	10,174	12,091	14,184
Growth (%)	3.1	18.8	17.3
EBITDA	1,174	1,472	1,776
EBITDA margin (%)	11.5	12.2	12.5
PBT	455	952	1,309
Adjusted Net profit	471	667	916
Adjusted EPS (Rs)	35.8	50.7	69.6
Growth (%)	(25.2)	41.6	37.5
CEPS (Rs)	54.8	82.1	103.0
Book value/share	321.7	362.7	422.6
Dividend/share (Rs)	8.0	8.0	8.0
ROE (%)	13.5	14.8	17.7
ROCE (%)	15.2	17.8	22.2
Net cash (debt)	(1,608)	166	581
Net Work Cap (Days)	20	18	18
VALUATION PARAMETERS			
P/E (x)	24.2	17.1	12.4
P/BV (x)	2.7	2.4	2.0
EV/Sales (x)	1.2	0.9	0.8
EV/EBITDA (x)	10.4	7.6	6.1

Source: Company, Kotak Securities - Private Client Research

Expect healthy volume growth for two wheeler industry over FY17-FY19E

Domestic two wheeler industry volume CAGR has been in mid-single digit in the past five years, lower than past 10 year average volume CAGR of ~10%. In FY1H17, two wheeler demand did show some signs of healthy recovery, but demonetization significantly impacted demand in 2HFY17, thereby impacting full year growth.

We expect the two wheeler demand to grown at a healthy rate in FY18. In April / May 2017 volume growth has been healthy at 10%. We expect volume growth to accelerate in 2HFY18 - partly due to low base. Deferment of demand due to demonetization will also give fillip to growth in FY18.

Rural demand will receive boost from expected good monsoon this year. In the urban areas, strong demand for scooters and premium motorcycle will drive growth.

With ~80% of overall revenue exposed to two wheeler OEM's, FIEM remains a big beneficiary of expected volume growth in the two wheeler segment.

FIEM's customers to outperform industry growth

HMSI and TVSM are FIEM's top two customers - accounting for ~70% of FIEM's auto segment revenues. We expect both - HMSI and TVSM's volume growth in FY18 to be ahead of the industry.

In first two months of FY17, HMSI and TVSM has reported volume growth of 29% and 12% respectively. In FY18, HMSI is aiming for volume growth of 20%. TVSM is also focused on market share gain.

Even other smaller customers for FIEM, like Suzuki Motorcycle, Royal Enfield and India Yamaha have reported better than industry growth in the first two months of FY17.

We thereby expect FIEM's revenue growth in the auto segment to remain robust and ahead of industry growth.

LED business to stay weak in the near to medium term

FIEM's LED business has been weak in the past two quarters - impacted by steep fall in LED prices. Given significantly low prices, FIEM has in recent times, refrained from participating in ESSL contacts.

In the near term, we expect LED revenues for FIEM to remain low as LED prices will likely take some time to improve from existing low levels.

LED sales for the company, in the near to medium term, will come from non-government institutional orders, IPIS (integrated passenger information system) and retail sales (JV with Su-Kam Power Systems).

FIEM has also signed an MOU with M/S VKL Holding Co. SPC (in Bahrain) to look into various possibilities related to manufacturing and marketing LED bulbs in Bahrain and GCC member countries. This arrangement is at nascent stage and will take time to contribute towards revenues.

4QFY17 was a weak quarter; expect gradual improvement going forward

FIEM reported weak 4QFY17 results. Company's performance during the quarter was impacted by weak performance in the LED segment. Lower LED prices on government contract and Rs23mn after sales return impacted FIEM's LED segment performance. In the auto segment, performance was relatively better as the two wheeler industry was continued to recover from demonetization impact. EBITDA margin was impacted by low margins from LED business (on falling LED prices). Company also reported one-time exceptional loss of Rs142mn related to discontinuation of comprehensive maintenance contract by ESSL.

In FY18, we expect gradual improvement in company's performance. In 1HFY18, growth in the auto segment is expected to be positive, but LED segment revenues are likely to stay under pressure. Further, the company is expected to book Rs31mn as after sales return in FY18.

In 2HFY18, we expect YoY growth to improve substantially - partly due to expected robust demand in two wheeler segment and low base. In the LED segment too, we expect gradual improvement in performance (QoQ) for the company.

Valuation

We recommend BUY on FIEM Industries Ltd with a price target of Rs.1,254

At the CMP of Rs865, the stock trades at a PE of 17.1x on FY18E and 12.4x on FY19E earnings.

We retain **BUY** on the stock with unchanged price target of Rs1,254. We value the stock at stock at 18x FY19E earnings.

SECTOR UPDATE

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SECTOR UPDATE: STEEL

Exports continue to remain strong

As per JPC provisional data, domestic steel demand grew by a mere 1.1% YoY in the month of May 2017 to 7.49T and for YTDFY18 the steel demand grew by 4.2% YoY to 13.79MT. In a subdued domestic demand environment, steel producers continued to maintain supply by focusing on export markets. Domestic steel prices continued to remain higher, compared to global prices, due to anti-dumping duty. However, weakness in global steel prices continues to be key headwind for the steel exports from India, as margins get impacted. We believe that, given the weak domestic demand, the steel prices in the domestic market are not sustainable and hence, steel producers have revised prices downwards in 1QFY18. Secondly, with GST roll out round the corner, dealers would be more focused on inventory liquidation, which would also put pressure on steel prices. With monsoon round the corner and 2QFY18 seasonally a weak quarter, we believe steel demand would be under pressure and so would be the prices. Going ahead, we believe that, subdued demand and risk of fall in international steel prices will restrict further hike in steel prices in the domestic market. We believe that, the current valuation of steel companies factor in the majority of the positive development and hence we continue to maintain our cautious stance on the ferrous space.

Steel exports continue to surge

Production during the month grew by 7.1% YoY to 9.07MT (up 7.5% MoM). For YTDFY18 steel production stood at 17.55MT (up 6.7% YoY). Imports during the year declined by 11.4% YoY to 1.06MT. For the month of May 2017, imports stood at 558KT (up 10.7% MoM). Exports during the month grew 69.5% YoY to 641KT. Increase in exports during Apr-May 2017 was on account of higher global steel prices. However, with the weakness in steel prices globally, we believe exports volume will get capped at current levels. Steel prices globally fell in the month of May 2017, largely attributed to the fall in raw material prices and oversupply. Steel imports accounted for 7.5% of domestic steel demand.

Inventory liquidation to restrict steel prices

For YTDFY18, domestic steel production has grown 6.7% YoY to 17.55MT. But due to muted demand, it resulted in a 3.76MT increase in domestic inventory during the year, which is equivalent to 15 days' domestic sales. Given the GST roll out, we expect inventory in the system to come down, as dealer would be focusing on reducing higher inventory levels in the near term.

Fall in raw material prices augur well for the industry

The Iron ore price, both 62% and 58% grade fell, yet again by 19% and 12% MoM to US$56/tonne and US$42/tonne respectively. Iron ore inventory at Chinese port is at a record high in last five years at 127 mt. Going ahead, we believe that, a sharp fall in iron ore prices recently, coupled with increasing supply from global miners, would continue to keep iron ore prices under pressure. Miners such as Rio Tinto, BHP, to name a few would continue to remain profitable below US$50/tonne as well, due to low cost of operations. On the other hand, Coking coal prices, as expected, fell down post subsiding of the cyclone Debbie in Australia and stood at US$149.5 (-39% MoM). Fall in raw material prices in the recent past and rising supply led to fall in global steel prices. Besides this, subdued fixed asset investment will keep the steel demand under pressure.

Outlook

We are of the view that the fall in raw material prices bodes well for the industry, but for the steel prices to sustain over the medium to long term, steel demand needs to improve. However, in the near term, we are of the view that weak demand and fall in raw material prices would keep steel prices under check. An execution of India first policy, will give a big boost to domestic steel demand, as it has ejected Chinese companies from pipeline project, worth Rs30 bn built by GAIL India. Besides these, as per steel ministry all tenders from central and state governments as well as state firms, where the project is worth more than Rs500 mn, preference will be given to domestic companies unless the quality or quantity is not locally available, or if there is a 15% value addition in India. The steps are in the right direction, to revive domestic demand over the medium to long term. As in FY17, for FY18 also we expect growth in steel companies to be largely led by volume and sustainability of the steel prices would be the key thing to watch out. For 1QFY18, we expect EBITDA margin of domestic steel producers to decline sequentially, due to lag impact of coking coal cost.

However, over the long run, improvement in the demand and reduction in the global oversupply are the key for the prices to sustain. As we believe that current valuations factor in the majority of the positive developments, we continue to maintain our cautious stance on the steel sector.

Monthly Steel Data*

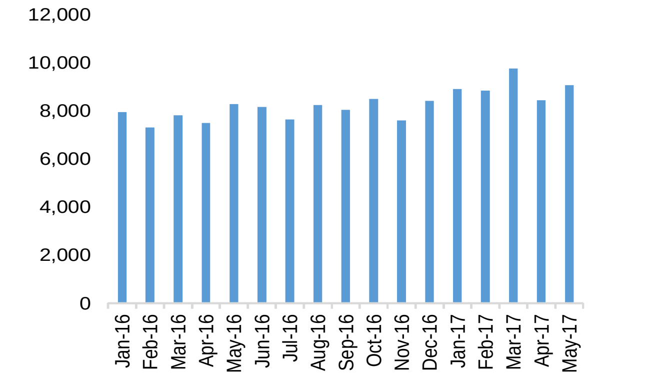
('000 T)	May-17	May-16	% YoY	Apr-17	% MoM
PProduction	9,066	8,468	7.1	8,430	7.5
Imports	558	545		504	
Exports	641	378		747	
Real Consumption	7,491	7,409	1.1	6,015	24.5

Year to Date

('000 T)	FY18	FY17	% YoY
Production	17,546	16,438	6.7
Imports	1,062	1,199	(11.4)
Exports	1,387	688	101.6
Real Consumption	13,785	13,235	4.2

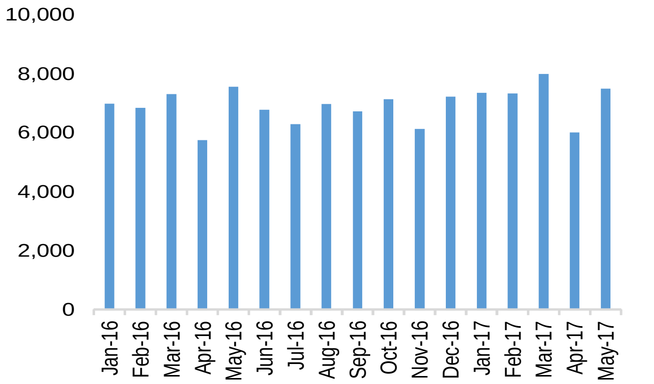
Source: JPC

Monthly Production Trend ('000 tonnes)



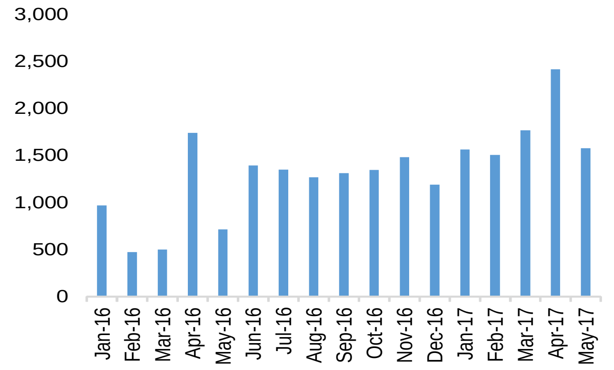
Source: JPC Data

Monthly Consumption Trend ('000 tonnes)



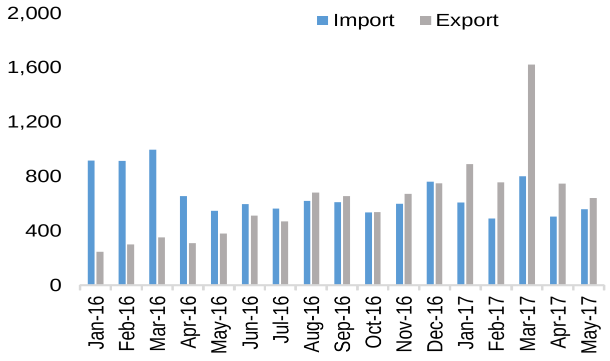
Source: JPC Data

Increase/Decrease in Inventory ('000 tonnes)



Source: JPC Data

Monthly Export-Import Trend ('000 tonnes)



Source: JPC Data

Bulk deals

Trade details of bulk deals

Date	Scrip name	Name of client	Buy/ Sell	Quantity of shares	Avg. price (Rs)
12-Jun	ATISHAY	BALRAM CHAINRAI	B	490,000	129.74
12-Jun	EQUITAS	RIMCO INDIA LIMITED	B	5,000,000	168.99
12-Jun	EQUITAS	CREATION INVEST EQUITAS HOLD LLC	S	5,000,000	169
12-Jun	MEERA	MACRO COMMODEAL PRIVATE LIMITED	S	114,000	36
12-Jun	MEERA	MIKER FINANCIAL CONSULTANTS P LTD	B	117,000	35.96
12-Jun	RAIREKMOH	EXIM SCRIPS CONSULTANTS PVT LTD	S	80,000	90.5
12-Jun	SINCLAIR	XANDER INVESTMENT HOLDING X LTD	S	319,234	326.39
12-Jun	SINCLAIR	ADITYA DEORAH	B	28,000	315
12-Jun	SINCLAIR	OUSEPH VAREEDVELIYATH	B	33,000	333.45
12-Jun	SUYOG	LTS INVESTMENT FUND LTD	S	63,200	390
12-Jun	VISHALBL	HEM INSURANCE BROKERS LIMITED	S	30,000	30.3
12-Jun	WELENT	INSIGHT SOLUTIONS LIMITED - DR	S	4,300,000	90.1
12-Jun	WELENT	PANNA LAL C KOTHARI HUF	B	800,000	90.05

Source: BSE

Gainers & Losers

Nifty Gainers & Losers

	Price (Rs)	chg (%)	Index points	Volume (mn)
Gainers				
TECH MAHINDR	397.3	2.7	(0.0)	2.89
INFOSYS LTD	963.9	1.6	(0.0)	4.3
SUN PHARMA	532.6	1.5	(0.0)	7.63
Losers				
BANK OF BARO	168.05	(3.3)	(0.0)	10.78
TATA MOTORS	283.15	(2.7)	(0.0)	1.2
LARSEN & TOU	1736.6	(2.3)	(0.0)	2.71

Source: Bloomberg

RATING SCALE

Definitions of ratings

BUY	–	We expect the stock to deliver more than 12% returns over the next 9 months
ACCUMULATE	–	We expect the stock to deliver 5% - 12% returns over the next 9 months
REDUCE	–	We expect the stock to deliver 0% - 5% returns over the next 9 months
SELL	–	We expect the stock to deliver negative returns over the next 9 months
NR	–	**Not Rated.** Kotak Securities is not assigning any rating or price target to the stock. The report has been prepared for information purposes only.
RS	–	**Rating Suspended.** Kotak Securities has suspended the investment rating and price target for this stock, either because there is not a sufficient fundamental basis for determining, or there are legal, regulatory or policy constraints around publishing, an investment rating or target. The previous investment rating and price target, if any, are no longer in effect for this stock and should not be relied upon.
NA	–	**Not Available or Not Applicable.** The information is not available for display or is not applicable
NM	–	**Not Meaningful.** The information is not meaningful and is therefore excluded.
NOTE	–	Our target prices are with a 9-month perspective. Returns stated in the rating scale are our internal benchmark.

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