

Pak Elektron (PAEL)

Reiterate Buy

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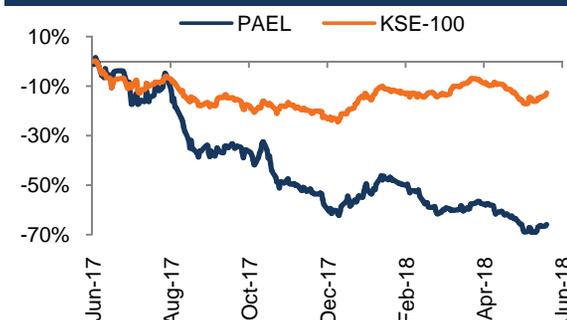
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Earnings Revised - 'Buy' Maintained

- We reiterate our 'Buy' stance on Pak Elektron (PAEL), Pakistan's one of the biggest home appliance and power equipment manufacturers, despite its weak performance in 1Q2018 (owing to strategic reasons to some extent while increasing competition also affected sales).
- After incorporating 1Q result, we tweak our assumptions for PAEL and tone down its EPS estimates by 15/22/32% to Rs5.3/6.0/6.3 in FY18E/FY19F/FY20F.
- However, since the stock has come down 18/65% in 2018/FY18YTD and has underperformed the market by 26/57%, this provides an attractive entry point in our view.
- We ignore the recent market noise/rumors of any disruption in PAEL's distribution network as our dealer and channel checks indicate encouraging sales so far.
- Moreover, contrary to market perception, the company's power division seems to be progressing fine despite World Bank's debarment of PAEL and its affiliates back in Feb-Mar 2018.

KATS Code	PAEL
Bloomberg Code	PAEL PA
Reuters Code	PKEL.KA
Market Price	Rs38.52
Market Cap	Rs19.2bn/US\$165.8mn
Free float Market Cap	Rs9.6bn/US\$82.9mn
1-Yr Avg. Daily Vol. (mn)	5.4
1-Yr Avg. Daily Val. (mn)	Rs333.6/US\$3.1
1-Yr High/ Low	Rs117.8/34.3
Estimated free float	50%
Share outstanding (mn)	497.68
Index weight	0.44%

PAEL vs KSE-100 Index



Source: PSX, Topline Research

Earnings Revised - 'Buy' Maintained

- We performed a survey in Karachi's key markets while also spoke to over a dozen dealers in Punjab region to gauge PAEL's overall positioning.
- As per our findings, Chinese brand Haier is taking the lead in refrigerators (which accounts for more than 60% of PAEL's appliances sales) in some regions, owing to its affordability (10-15% cheaper than PAEL).
- Similar observation was seen in Air Conditioners (AC) as well, the second biggest sales contributor to PAEL's appliances segment. Here, another Chinese appliance manufacturer Gree is the preferred choice despite the fact that it was 5-8% expensive than PAEL.
- However, in other regions, PAEL was competing neck to neck with Chinese entrants and Dawlance (a local home appliance player which was acquired by the Turkish firm, Arcelik in 2016) in both refrigerators and ACs.
- In our Karachi survey, we observed that the imported Turkish model of Dawlance refrigerator has recently paved its way to the market. Though it is catering to higher end consumers, competing with imported brands like Samsung and is 2-3x expensive than local brands.
- Our overall impression is that, while competition has certainly risen in home appliances segment, owing to Chinese entrants, PAEL still stands favorably well, especially in refrigerators.

Earnings Revised - 'Buy' Maintained

- Moreover, appliances industry is showing double digit growth where refrigerator, AC, and Deep Freezer segments are growing by 8-10%, 10-15%, 8-10% while Microwave and Water Dispensers markets are growing by 20% each, annually, where PAEL's share has also increased, as per channel checks.
- We believe that the peak appliance season and anticipation of a convincing sales in 2Q2018 should lend credence to the company's performance going forward.
- We flag, 1) increase in raw material costs and the company's inability to pass it on, 2) greater than expected PKR devaluation against US\$, 3) higher financial charges to fund working capital and 4) greater competition due to new entrants key risks for PAEL.

PAEL: Key Numbers

	2016A	2017A	2018E	2019F	2020F
EPS	7.4	6.6	5.3	6.0	6.3
Earnings Growth	27%	-10%	-21%	14%	5%
PE at Rs39	5.3	5.9	7.4	6.5	6.2
Dividend Yield	8%	7%	5%	6%	7%
ROE	22%	12%	9%	10%	10%
PBV	1.2	0.7	0.7	0.6	0.6

Source: Company Accounts, Topline Research

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Neutral	Stock will perform in line with the average total return of stocks in universe
Sell	Stock will underperform the average total return of stocks in universe

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Rating	Sector’s Proposed Weight in Portfolio
Over Weight	> Weight in KSE-100 Index
Market Weight	= Weight in KSE-100 Index
Under Weight	< Weight in KSE-100 Index

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