Sharekhan
by BNP PARIBAS

Thermax Limited

Quarter marred by the pandemic; Order intake a key monitorable

Sector: Capital Goods
Result Update

	Change
Reco: **Hold**	↔
CMP: **Rs. 751**	
Price Target: **Rs. 815**	↑

↑ Upgrade ↔ No change ↓ Downgrade

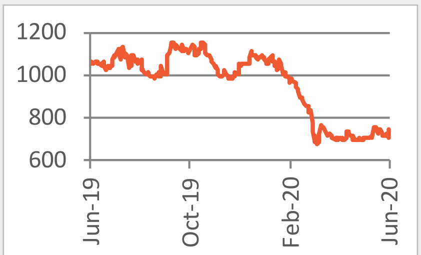
Company details

Market cap:	Rs. 8,950 cr
52-week high/low:	Rs. 1180/644
NSE volume: (No of shares)	1 lakh
BSE code:	500411
NSE code:	THERMAX
Sharekhan code:	THERMAX
Free float: (No of shares)	4.5 cr

Shareholding (%)

Promoters	62.0
FII	7.8
DII	17.6
Others	12.7

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	6	5	-29	-29
Relative to Sensex	-6	-12	-12	-16

Sharekhan Research, Bloomberg

Thermax's consolidated net revenue reported a sharp decline of 36.2% y-o-y in revenue for Q4FY2020 (lower than our estimates) at Rs. 1,323 crore due to impact of lockdown (loss of revenue of Rs. 400 crore-500 crore), wherein the decline in revenue was seen across segments. Operating profit margin (OPM) declined by 343 bps y-o-y, led by lower absorption of fixed costs on lower revenue. Hence, operating profit fell sharply by 63% y-o-y to Rs. 64 crore. Further, lower other income (-41% y-o-y to Rs. 30.7 crore) and higher depreciation (+25% y-o-y to Rs. 30.8 crore) impacted PBT (-70% y-o-y) and adjusted PAT declined by 70% y-o-y to Rs. 39 crore (sharply lower than our estimate). Order inflow declined by 17.7% y-o-y with FY2020 order intake at Rs. 5,498 crore (-2.4% y-o-y). Accordingly, order backlog dropped by 2.5% y-o-y to Rs. 5,238 crore (-4% q-o-q; 0.9x its FY2020 revenue). Weak international order inflows and limited visibility for big-ticket size domestic orders largely (in steel, cement, and fertilisers) led to management guiding for lower order inflows in FY2021 compared to FY2020, given the current uncertainties. However, management expects better ordering in its chemical business; and enquiries pipeline remains positive in food processing, FMCG, oil and gas refinery, and pharma in domestic markets. Management stated that all factories have started operating, which is currently at 40-45% utilisation levels and expect to return to normalcy by Q3FY2021. Further, 90-95% of the project sites are operating at 50-60% of labour, so execution will not be a challenge at present; and management expects more labour to come gradually as things improve. The fire at the adjoining facility of Dahej chemical factory affected its factory, which would lead to 30-40 days of production loss impacting the chemical division's revenue. We have tweaked our estimates for FY2021-FY2022, factoring lower order booking and challenges pertaining to the uncertainties related to execution and production. We retain our Hold rating with a revised price target (PT) of Rs. 815.

Key positives

- Strong improvement in operating cash flows during FY2020 as against FY2019.
- Better ordering expected in the chemical segment, while enquiries pipeline remains positive in food processing, FMCG, and pharma in domestic markets.

Key negatives

- Order booking declined by 17% y-o-y.
- Management has guided for lower order booking for FY2021 compared to FY2020.

Our Call

Valuation – Maintain Hold with a revised PT of Rs. 815: Lower carry-forward order book along with lower capacity utilisation in most core user industries is likely to impact order inflows for FY2021. Additionally, weak order intake outlook during FY2021 may lead to further depletion of order book by the end of FY2021. Hence, order inflow during the current fiscal year would be the key monitorable for the company. Further, H1FY2020 is expected to be remain weak owing to COVID-19 pandemic and damage caused at its Dahej facility. The company is expected to return to normalcy by Q3FY2021. On the positive note, the company has been able to improve its cash flow position during FY2020. We have tweaked our estimates for FY2021-FY2022, factoring lower order booking and challenges pertaining to uncertainties related to execution and production. We retain our Hold rating with a revised PT of Rs. 815.

Key Risks

Slower-than-expected revival in private capex resulting in muted order picking.

Valuation (Consolidated) Rs cr

Particulars	FY19	FY20	FY21E	FY22E
Revenue	5,973	5,731	5,168	5,856
OPM (%)	7.7	7.1	7.0	8.5
Adjusted PAT	325	212	250	353
% YoY growth	40.8	(34.7)	17.8	41.2
Adjusted EPS (Rs.)	28.9	18.9	22.2	31.4
P/E (x)	26.0	39.8	33.8	24.0
P/B (x)	2.8	2.8	3.2	2.8
EV/EBITDA (x)	12.3	14.5	15.8	11.1
RoNW (%)	14.6	7.1	8.9	12.9
RoCE (%)	18.7	13.2	11.6	16.6

Source: Company; Sharekhan estimates

Weak performance for the quarter: Thermax's consolidated net revenue reported a sharp decline of 36.2% y-o-y during Q4FY2020 (lower than estimates) at Rs. 1,323 crore due to impact of lockdown (Rs. 400 crore-500 crore impact), wherein the revenue decline was seen across segments. Operating profit margin (OPM) declined by 343 bps y-o-y due to higher other expenses (one-time warranty provisioning, bad debts written down, higher freight and site expenses) and lower revenue. Hence, operating profit fell sharply by 63% y-o-y to Rs. 64 crore. Further, lower other income (-41% y-o-y to Rs. 30.7 crore) and higher depreciation (+25% y-o-y to Rs. 30.8 crore) impacted PBT growth (-70% y-o-y) and adjusted PAT declined by 70% y-o-y to Rs. 39 crore (sharply lower than our estimates) due to lower revenue and margins.

Declining order book remains a concern: Order inflow declined by 17.7% y-o-y, with FY2020 order intake at Rs. 5,498 crore (-2.4% y-o-y). Accordingly, order backlog dropped by 2.5% y-o-y to Rs. 5,238 crore (-2.5% y-o-y and -4% q-o-q; 0.9x FY2020 revenue). Weak international order inflows and limited visibility for big-ticket size domestic orders largely (in steel, cement and fertilisers) led to management guiding for lower order inflows in FY2021 compared to FY2020, given the current uncertainties. Management expects better ordering in its chemical business; and enquiries pipeline remains there in food processing, FMCG, oil and gas refinery, and pharma in domestic markets. The company expects better exports from the chemical division due to opportunities arising from pharma API factories (for boilers, water treatment etc.) and orders from international markets (North America).

Key conference call highlights

- **Order inflow guidance:** Weak international order inflows and limited visibility for big-ticket size domestic orders largely (in steel, cement and fertilisers) led to management guiding for lower order inflows in FY2021 compared to FY2020, given the current uncertainties.
- **Procurement from China:** Management highlighted that procurement from China compared to overall procurement from other countries remains miniscule (currently at Rs. 154 crore).
- **Domestic market order intake scenario:** In the domestic market, the company expects better ordering in its chemical business; and enquiries pipeline remains positive in food processing, FMCG, and pharma in domestic markets.
- **FGD Orders:** The company has bid for some flue-gas desulfurization (FGD) orders in Lot-5 and would be bidding for more orders in LOT-6 of FGD bidding. Thermax seems less interested for bidding for State Electricity Boards (SEB) FGD orders due to cash crunch in most SEBs.
- **Current factory status after lockdown:** Management stated that all factories have started operating, which is currently at 40-45% utilisation levels, and expects to return to normalcy by Q3FY2021. Further, project sites are operating at 90-95% levels and have retained 50-60% of labour so execution will not be a challenge at present and management expects more labour to come gradually as things improve.
- **International business update:** The company's factories in Denmark, Germany, Poland, and Indonesia were operational. Further, Danstoker continues to be loss making and is expected to be closer to breakeven by FY2021 end. Further, Indonesia plant is loss making at present but losses are coming down.
- **Impact from Coronavirus outbreak:** Due to COVID-19 led lockdown, the company was unable to dispatch products and raw materials, which led to lower revenue recognition (impact of Rs. 400 crore-500 crore) during Q4FY2020.
- **Fire at Dahej factory some time back:** Management highlighted that there was fire in its Dahej chemical factory sometime back (earlier reported) and it lost 30-40 days of production, which impacted revenue. However, the company expects better exports from the chemical division due to opportunities arising from pharma API factories (for boilers, water treatment etc.) and orders from international markets (North America).

Results (Consolidated) Rs cr

Particulars	Q4FY20	Q4FY19	YoY %	Q3FY20	QoQ %
Net sales	**1,323.0**	**2,074**	**-36.2%**	**1,410**	**-6%**
Net raw material	673	1,255	-46.4%	785	-14%
Employee Expenses	197	205	-3.8%	200	-1%
Other Expenses	389	443	-12.1%	312	25%
Operating profit	**63.6**	**171**	**-62.8%**	**113**	**-44%**
Other Income	31	52	-40.9%	26	19%
Interest	4.9	3.5	39.6%	1.9	154%
Depreciation	31	25	24.8%	32	-3%
PBT	59	195	-69.9%	105	-44%
Tax	20	65	-70.0%	20	-4%
Adj. PAT	**39.0**	**128.9**	**-69.7%**	**85**	**-54%**
Rep. PAT	**39**	**127**	**-69.2%**	**85**	**-54%**
EPS (Rs.)	3.5	11.3	-69.2%	7.5	-54%
Margin			**bps**		**bps**
OPM	4.8%	8.2%	(343)	8.0%	(322)
PATM	3.0%	6.2%	(327)	6.0%	(308)
Tax rate	33.4%	33.6%		19.4%	

Source: Company, Sharekhan Research

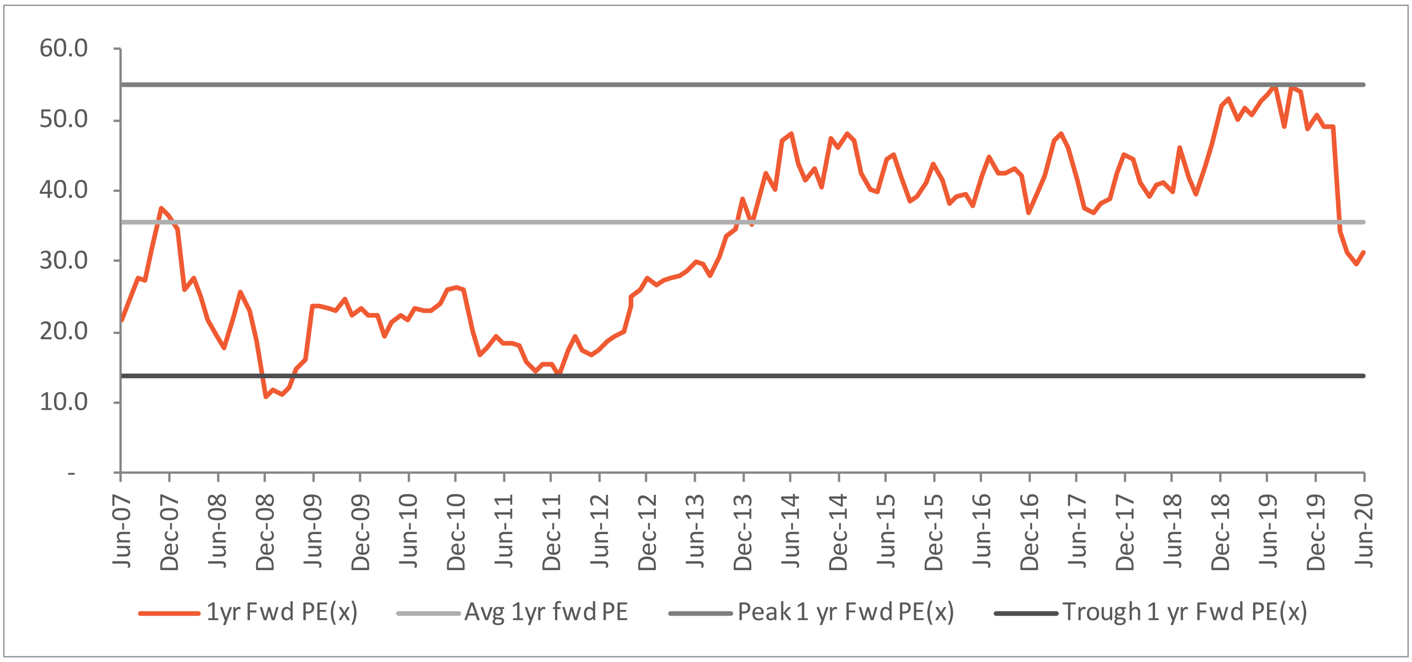
Outlook

Cautious on near-term recovery in order tendering: Management sounded cautious on a short-term recovery in order tendering. Weak international order inflows and limited visibility for big ticket-size domestic led to management guiding for lower order inflows in FY2021 compared to FY2020. Management also expects more FGD orders for tendering in domestic markets and would be bidding accordingly. Management expects better ordering in its chemical business. Further enquiries pipeline remains positive in food processing, FMCG, oil and gas refinery, and pharma in domestic markets. The company expects better exports from the chemical division due to opportunities arising from pharma API factories (for boilers, water treatment etc.) and orders from international markets (North America).

Valuation

Maintain Hold with a revised PT of Rs. 815: Lower carry-forward order book along with lower capacity utilisation in most core user industries is likely to impact order inflows for FY2021. Additionally, weak order intake outlook during FY2021 may lead to further depletion of order book by the end of FY2021. Hence, order inflows during the current fiscal year would be the key monitorable for the company. Further, H1FY2020 is expected to remain weak owing to COVID-19 pandemic and damage caused at its Dahej facility. The company is expected to return to normalcy by Q3FY2021. On the positive note, the company has been able to improve its cash flow position during FY2020. We have tweaked our estimates for FY2021-FY2022, factoring lower order booking and challenges pertaining to uncertainties related to execution and production. We retain our Hold rating with a revised PT of Rs. 815.

One-year forward P/E (x) band



Source: Sharekhan Research

About company

Thermax provides solutions in the energy and environment space. The energy business contributes 75-78% to revenue, whereas the environment business contributes 15-16% and chemical business contributes 7-8%. The company operates globally through 33 international offices and 13 manufacturing facilities, seven of which are in India and six are overseas. Thermax is present in 86 countries across Asia Pacific, Africa, Middle East, CIS countries, Europe, US, and South America.

Investment theme

Green shoots of a revival in private capex are visible in a few segments (metals and cement), with most other companies resorting to brownfield expansions. However, a broad-based recovery is key for Thermax. While historically, Thermax's growth has been led by the domestic market, incremental growth from international markets exposes Thermax to the risk of rising commodity prices, given fixed-price contracts.

Key Risks

- Slower-than-expected revival in private capex resulting in muted order picking
- Slowdown in tendering activities, and slower pick-up in its subsidiary companies.

Additional Data

Key management personnel

Meher Pudumjee	Chairman
Nawshir Mirza	Additional Independent Director
M S Unnikrishnan	Managing Director
Pheroz Pudumjee	Non Executive Promoter
Anu Aga	Non Executive Promoter

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	RDA Holdings Pvt Ltd	53.99
2	ARA TRUSTEESHIP COMPANY PVT LTD	7.99
3	SBI Funds Management Pvt Ltd	3.36
4	PineBridge Investments LP	3.17
5	Kotak Mahindra Asset Management Co	2.27
6	Goldman Sachs Group Inc/The	1.64
7	Franklin Resources Inc	1.63
8	L&T Mutual Fund Tustee Ltd/India	1.53
9	Life Insurance Corp of India	1.48
10	Reliance Capital Trustee Co Ltd	1.22

Source: Bloomberg

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