



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

Updated Oct 08, 2022

31.25

High Risk

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

Source: Morningstar

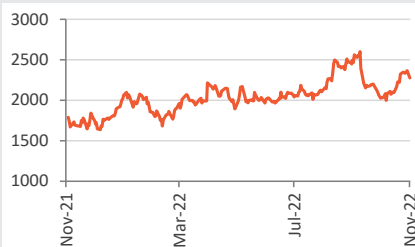
Company details

Market cap:	Rs. 27,119 cr
52-week high/low:	Rs. 2,679/1,420
NSE volume: (No of shares)	0.81 lakh
BSE code:	500411
NSE code:	THERMAX
Free float: (No of shares)	4.5 cr

Shareholding (%)

Promoters	62.0
FII	12.4
DII	20.8
Others	4.8

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	12.7	11.3	21.2	54.8
Relative to Sensex	4.6	7.1	6.9	51.6

Sharekhan Research, Bloomberg

Thermax Ltd

Order intake may moderate, optimistic on long-term growth

Capital Goods

Sharekhan code: THERMAX

Reco/View: Buy



Upgrade



Maintain



Downgrade

CMP: Rs. 2,276

Price Target: Rs. 2,790



Summary

- Thermax Limited's (Thermax) consolidated Q2 performance exceeded estimates, wherein energy, environment and chemicals posted strong revenue growth driven by healthy opening order book.
- Order inflow witnessed moderate growth of 9% y-o-y to Rs. 2,015 crore, while order book improved ~46% y-o-y to Rs. 9,485 crore. Order intake expectations particularly for big ticket orders are muted but overall demand scenario is promising.
- Margins are expected to improve in the coming quarters in energy and chemicals segment on account of price hikes in products/services business, easing supply chain constraints, and stability in commodity prices.
- We maintain a Buy on Thermax with a revised PT of Rs. 2,790, as we believe despite moderate order intake outlook, the long-term growth will be driven by increasing demand for green-energy solutions and improving margin trajectory.

Thermax reported a good set of numbers which exceeded our and street expectations on all fronts. The consolidated sales grew by 41% y-o-y to Rs 2,075 crore, led by strong opening order book. Operating profit increased by 27.8% y-o-y to Rs 141 crore (vs our estimate of Rs110 crore). OPM came in at 6.8% (declined 71 bps y-o-y) due to higher raw material cost but is above our expectations of 6.6%. Profit grew at a comparatively slower pace by 24% y-o-y to Rs 109 crore (vs our estimate of Rs 95 crore), helped by better-than-expected operating performance and lower tax rate. Segment wise – Energy revenue grew by 39% y-o-y, the environment grew by 44% y-o-y, and chemical segments grew by 48% y-o-y. The environment segment profitability has improved (EBIT at 6.4% vs 2%) due to higher revenue and better margins. The energy (EBIT at 5.5% vs 8% in Q2FY22) and chemical segment (EBIT at 13.4% vs 15.5% in Q2FY22) profitability has been impacted by higher input costs over the last year. The order book is up 46% y-o-y to Rs 9,485 crore, and order intake is up 9% y-o-y at Rs 2,015 crore.

Key positives

- Order book remained strong at Rs. 9,485 crore (up 46% y-o-y).
- The company reported healthy revenue growth across all the segments.
- Cash and cash equivalents and investments stood at Rs. 2,520 crore.
- Margin in the environment segment improved owing to operating leverage.

Key negatives

- Profitability of the chemicals and energy segment continued to be impacted due to higher input cost on y-o-y basis.
- The inquiry pipeline has moderated, particularly for large orders compared to last year.

Management Commentary

- Order pipeline is promising but has moderated from sectors like cement, steel, refinery and petrochemicals. The company does not expect to win any large order in the next 12 months from these industries.
- Energy segment margin has bottomed out and should improve from current levels due to lower commodity prices and higher-margin orders.
- The two FGD orders, which were low-margin orders, are 90% complete. The FGD residual order backlog margin is expected to improve by 100-200 bps.
- Water, solar and renewable sectors have a lot of potential and provide strong long-term opportunities. The company's subsidiaries are also expected to do well.

Revision in estimates – We have marginally revised our estimates downwards for FY2023-25E.

Our Call

Valuation – Retain Buy with a revised PT of Rs. 2,790: Thermax boasts of a healthy order book and has a promising enquiry pipeline for small ticket-size orders in cement, biomass, paper and pulp, and sugar distilleries. However, it has provided a muted outlook for big-ticket orders from steel, cement, oil and gas, refinery, and petrochemicals. We believe in the long run, Thermax is expected to benefit from India's transition to green energy as it has many offerings in the space. International opportunities in biomass, waste heat recovery (WHR) and water desalination also remain strong. However, profit growth may remain lower than sales growth in the near term and order intake growth may also moderate. In the long term, we believe margin improvement, export growth, and increasing contribution from products and services business would aid profitability. Given the robust financials and ample business opportunities, we reiterate our Buy rating on the stock with a revised PT of Rs. 2,790, valuing the stock on its September 2024E EPS.

Key Risks

- Slowdown in private capex would lead to muted order bookings
- Geopolitical tensions and supply-side challenges may continue to impact sales in the near term.

Valuation (Consolidated)

Particulars	FY22	FY23E	FY24E	FY25E
Net Sales	6,128	8,096	9,648	11,084
OPM (%)	6.9	7.1	7.5	8.1
Adj. Net Profit	312	422	537	681
% Growth y-o-y	20.5	35.0	27.5	26.8
Adj. EPS (Rs.)	26.2	35.4	45.1	57.2
PER	86.8	64.3	50.5	39.8
P/B	9.0	8.5	7.7	6.7
EV/EBIDTA	44.6	35.9	29.0	23.3
ROCE (%)	14.8	18.4	20.8	23.5
RONW (%)	10.7	13.6	16.0	18.1

Source: Company; Sharekhan estimates

Healthy revenue growth across all segments

Thermax reported a good set of numbers which exceeded our and street expectations on all fronts. The consolidated sales grew by 41% y-o-y to Rs 2,075 crore, led by strong opening order book. Operating profit grew by 27.8% y-o-y to Rs 141 crore (vs our estimate of Rs110 crore). OPM came in at 6.8% (declined 71 bps y-o-y) due to higher raw material cost but is above our expectations of 6.6%. Profit grew at a comparatively slower pace by 24% y-o-y to Rs 109 crore (vs our estimate of Rs 95crore) helped by better-than-expected operating performance and lower tax rate. Segment wise – Energy revenue grew by 39% y-o-y, environment grew by 44% y-o-y and chemical segments grew by 48% y-o-y. The environment segment profitability has improved (EBIT at 6.4% vs 2%) due to higher revenue and better margins The energy (EBIT at 5.5% vs 8% in Q2FY22) and chemical segment (EBIT at 13.4% vs 15.5% in Q2FY22) profitability has been impacted by higher input costs over the last year.

Robust order book, but enquiry pipeline seems to be moderating

Order book is up 46% y-o-y to Rs 9,485 crore, while order intake had a moderate growth of 9% y-o-y at Rs 2,015 crore. The order book has a healthy mix of orders from diverse industry sectors such as metals and steel (16%), refinery and petrochemical (11%), sugar/distillery (9%), power (9%), food and beverages (11%), chemical (12%), and cement (6%) among others. The company's enquiry pipeline from the steel, cement, chemical, and refinery sectors continues to be good due to increased capex plans in the private sector. However, the company stated that the pipeline seems to be moderating, particularly for large orders vs last year and therefore, Thermax may not win any large orders in the next 12 months. However, there is a lot of interest in biomass, water, solar and other renewable industries side and the company should be able to bag decent orders from these additional industries.

Key Investor Update and Conference Call Highlights

Segment-wise order intake and backlog breakup: Out of total order inflows of Rs. 2,016 crore ore, energy orders increased by 4% y-o-y to Rs. 1,495 crores. Environment orders increased by 16% to Rs. 331 crore, while chemicals orders increased at a strong pace of 37% y-o-y to Rs 190crore. In the total order backlog of Rs. 9,485 crore, energy, environment, and chemicals' contribution stood at 70%, 29%, and ~1%, respectively.

Future business outlook: Inquiry pipeline is good, but it is moderating for sectors like cement, steel and pharmaceuticals as compared to last year when it was quite robust. In Q2FY2023, the company received major orders for waste heat recovery and bioenergy applications. There were not any large orders from refining and petrochemicals. The company also lost a couple of orders in refinery and petrochemical segment as it did not settle down for low margins. Also, in the next 12 months, the company does not expect any large FGD or refinery and petrochemicals orders. International order booking, however, has improved. Commodity prices are stabilising now and supply side challenges are moderating. Hence, the company feels that the execution cycle will be good. The company is also working towards more cost optimization by bringing changes in processes

Margin profile in all the segments would improve: Energy segment margin has hit the bottom and should improve from current levels as commodity prices are stabilising. However, in certain input products, the prices have moderated marginally, and the availability is also very low. Although overall prices have stabilized. Projects will have single digit margins as currently it has big portion of FGD. In services, however, double digit margin is achievable.

Huge opportunity in the water business: Water business has lot of potential and is a multi- decade bet as India has a lot of scope for waste water treatment and water based applications. The industry size is Rs 7,000-10000 crore on an annual basis and the company's market share is less than 10%. annually.

Update on Solar business: The company had planned to do 50 MW of orders in opex and similar on the capex side in its solar industry through its subsidiary, First Energy Private Limited. First Energy strives to set up open access based solar and solar hybrid farms, hybridising solar with storage and other solutions and delivering appropriate renewable power to customers. However, the company has not been able to achieve that, and therefore it incurred a loss in that unit. The company expects orders to flow from states like Tamil Nadu, Maharashtra and Gujarat. In the following year the unit should break even, and it expects good progress from FY2025 onwards. The company expects IRR of 16-19% in this business.

Update on two large FGD orders: The orders are in full execution mode and are 90% complete. The company expects that from past levels, the margin will start to increase in these projects on residual backlog and expects these projects to break even or deliver low single-digit margin following ease in commodity cost. Overall for FGD order backlog, the company expects the margin to be better by 100-200 bps higher than the 2-3% profitability envisaged earlier.

Update on international subsidiary: In Danstoker, there has been a strong enquiry flow for biomass-based boilers due to decoupling of Russia and rise in energy prices. The inquiry flow has been so strong that the company needs more capacity to take orders. The company is bullish on its prospects for next one year. PT Thermax International Indonesia is also witnessing better enquiry flow and win rate has also gone up. Hence, order backlog is also improving, and therefore the company expects strong performance in the next two-three quarters

Chemicals – In chemicals, 40% of business is resins, followed by oil-based chemicals, water treatment and construction. All the segments are doing well and currently the capacity utilisation is 50%. Given the demand scenario, the company may need a new plant soon and is planning additional capacity investment in the long term.

Results (Consolidated)

					Rs cr
Particulars	Q2FY23	Q2FY22	YoY %	Q1FY23	QoQ %
Revenue	2,075	1,469	41.2	1,654	25.4
Operating Profit	141	110	27.8	96	46.4
PBT	143	114	24.8	81	75.1
Adjusted PAT	109	88	24.1	59	84.9
Reported PAT	109	88	24.1	59	84.9
EPS (Rs.)	9.7	7.8	24.1	5.2	84.9
Margin (%)			BPS		BPS
OPM	6.8	7.5	(71)	5.8	97
NPM	5.3	6.0	(72)	3.6	169
Tax Rate	23.3	23.1	24	27.5	(423)

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Ample growth opportunities

Industries such as steel, and cement are undergoing capacity expansion which bodes well for Thermax. Further, the Indian Government's Union Budget announcement for infrastructure & development and PLI package will support the demand in the coming quarters. The government's National Infrastructure Plan (NIP), where total capital expenditure is projected at ~Rs. 111 lakh crore during FY2020-2025 also augurs well for growth of capital goods players. During the same period, sectors such as energy (24%), roads (18%), urban (17%), and railways (12%) would amount to ~71% of projected infrastructure investments in India. The huge outlay towards infrastructure is expected to provide healthy growth opportunities for companies in the space.

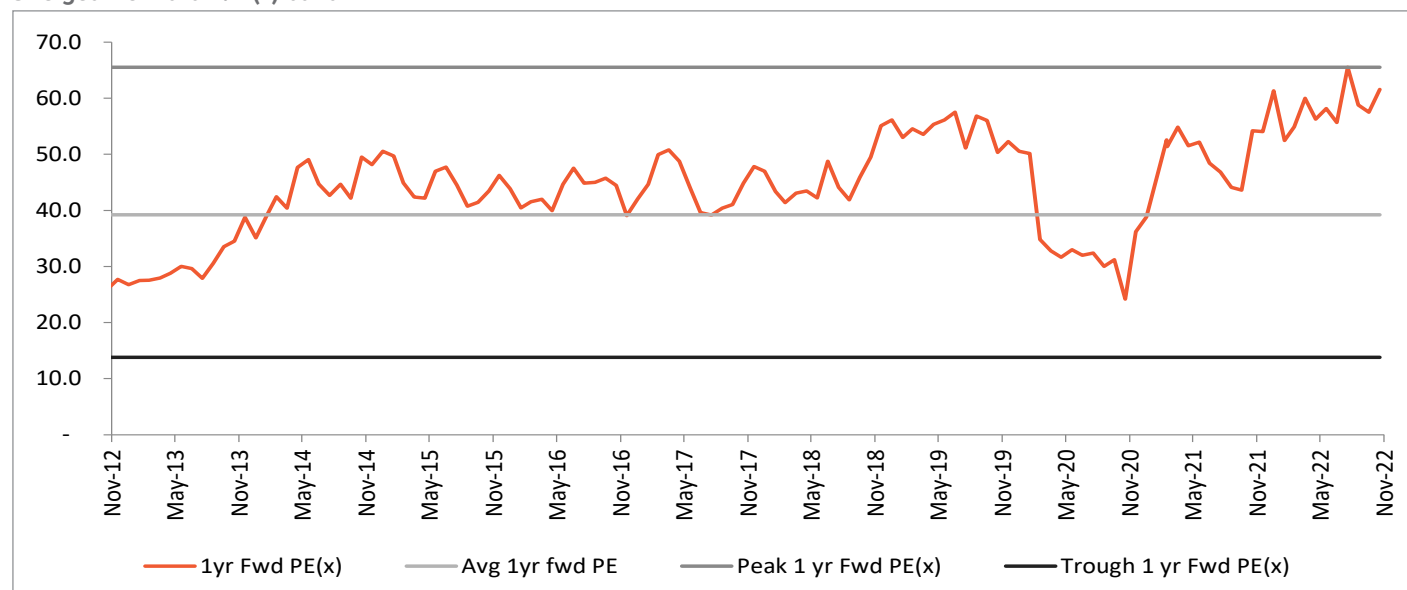
■ Company outlook - Capitalising on opportunities

Management commentary on the enquiries pipeline remains positive for small ticket-size orders across food processing, chemicals and pharmaceuticals in domestic markets, including large charges from oil and gas, FGD, and chemical. Management highlighted big-order opportunities in waste heat recovery in cement and steel sectors, both in domestic and export markets. On the commodity front, management highlighted that there are challenges due to commodity headwinds. However, the company can hedge the price for more minor contracts as it buys the material in around 30 days before signing the agreement. Thermax is also contemplating opportunities across newer and green technologies, which will provide the next leg of growth.

■ Valuation - Retain Buy with a revised PT of Rs. 2,790

Thermax boasts of a healthy order book and has a promising enquiry pipeline for small ticket-size orders in cement, biomass, paper and pulp, and sugar distilleries. However, it has provided a muted outlook for big-ticket orders from steel, cement, oil and gas, refinery, and petrochemicals. We believe in the long run, Thermax is expected to benefit from India's transition to green energy as it has many offerings in the space. International opportunities in biomass, waste heat recovery (WHR) and water desalination also remain strong. However, profit growth may remain lower than sales growth in the near term and order intake growth may also moderate. In the long term, we believe margin improvement, export growth, and increasing contribution from products and services business would aid profitability. Given the robust financials and ample business opportunities, we reiterate our Buy rating on the stock with a revised PT of Rs. 2,790, valuing the stock on its September 2024E EPS.

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 73% to the revenue, whereas the environment business contributes 21% and the chemical business contributes 9%. 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 the Asia Pacific, Africa, the Middle East, CIS countries, Europe, the US, and South America

Investment theme

Green shoots of 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. 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

- ♦ Slowdown in private capex would lead to muted order booking.
- ♦ Geopolitical tensions and supply-side challenges may impact the exports business in the near term.

Additional Data

Key management personnel

Mrs. Meher Pudumjee	Chairman
Mr. Pheroze Pudumjee	Non-Independent Director
Mr. Ashish Bhandari	Executive Director-CEO-MD
Mr. Rajendran Arunachalam	Group Chief Financial Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Kotak Mahindra Trustee Co Ltd	7.03
2	Nalanda India Equity Fund Limited	6.86
3	SBI Magnum Midcap Fund	2.43
4	Tata Aia Life Insurance Company Ltd	1.63
5	Kotak Mahindra Trustee Co Ltd	7.03
6	Nalanda India Equity Fund Limited	6.86
7	L&T Mutual Fund Trustee Limited	0.90
8	Aditya Birla Sun Life AMC	0.85
9	Vanguard Group Inc.	0.74
10	Pheroze N. Pudumjee	0.01

Source: Bloomberg (Old Data)

Sharekhan Limited, its analyst or dependant(s) of the analyst might be holding or having a position in the companies mentioned in the article.

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 deteriorating 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

Know more about our products and services

For Private Circulation only

Disclaimer: This document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This Document is subject to changes without prior notice. This document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved) and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other reports that are inconsistent with and reach different conclusions from the information presented in this report.

This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst has not dealt or traded directly or indirectly in securities of the company and that all of the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst and SHAREKHAN further certifies that neither he or his relatives or Sharekhan associates has any direct or indirect financial interest nor have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report nor have any material conflict of interest nor has served as officer, director or employee or engaged in market making activity of the company. Further, the analyst has also not been a part of the team which has managed or co-managed the public offerings of the company and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Limited or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either, SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

Compliance Officer: Ms. Binkle Oza; Tel: 022-61150000; email id: compliance@sharekhan.com;

For any queries or grievances kindly email igc@sharekhan.com or contact: myaccount@sharekhan.com.

Registered Office: Sharekhan Limited, The Ruby, 18th Floor, 29 Senapati Bapat Marg, Dadar (West), Mumbai – 400 028, Maharashtra, INDIA, Tel: 022 - 67502000/ Fax: 022 - 24327343. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O/ CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183.

Disclaimer: Client should read the Risk Disclosure Document issued by SEBI & relevant exchanges and the T&C on www.sharekhan.com; Investment in securities market are subject to market risks, read all the related documents carefully before investing.