Stock Update

Result Update

Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

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 31.25

Updated Dec 08, 2022

High Risk

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

Source: Morningstar

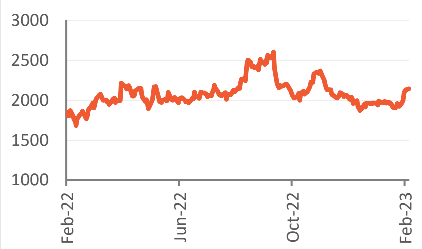
Company details

Market cap:	Rs. 25,534 cr
52-week high/low:	Rs. 2,679 / 1,651
NSE volume: (No of shares)	0.72 lakh
BSE code:	500411
NSE code:	THERMAX
Free float: (No of shares)	4.5 cr

Shareholding (%)

Promoters	62.0
FII	17.8
DII	15.3
Others	4.9

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	8.4	-9.4	0.8	10.6
Relative to Sensex	7.5	-9.6	-2.4	7.6

Sharekhan Research, Bloomberg

Thermax Ltd

Strong Q3, ample growth opportunities

Capital Goods	Sharekhan code: THERMAX
Reco/View: Buy ↔	CMP: Rs. 2,143 / Price Target: Rs. 2,790 ↔

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- Thermax Limited's (Thermax) consolidated Q3 performance exceeded estimates, led by strong sales and profitability in energy and environment segments on account of rise in execution given higher opening order book.
- Order inflow declined by 10% y-o-y to Rs. 2,204 crore, while order book was up ~33% y-o-y to Rs. 9,859 crore. The company does not expect big-ticket orders in the near to medium term; however, the company is bullish on small to mid-size orders.
- Margins are on an improving trajectory across all its segments, given stability in freight cost and commodity prices.
- We maintain Buy on Thermax with an unchanged PT of Rs. 2,790, as we expect the company would benefit from increasing demand for green energy solutions across sectors. Further, its healthy balance sheet, strong cash, and execution capabilities give us comfort on its long-term prospects.

Thermax reported a healthy set of numbers for Q3FY2023, beating our and street expectations particularly on the OPM and profitability front. Consolidated sales grew by 27% y-o-y to Rs. 2,049 crore, led by strong opening order book. Operating profit grew by 42.4% y-o-y to Rs. 161 crore (vs. our estimate of Rs. 154 crore). OPM came in at 7.9% (up 86 bps y-o-y) due to lower raw-material cost and a proportionate decline in employee cost. Profit jumped by 59% y-o-y to Rs. 126 crore (vs. our estimate of Rs. 116 crore), helped by strong operating performance and higher other income. Order book was up 33% y-o-y to Rs. 9,859 crore, while order intake declined 10% y-o-y to Rs. 2,204 crore, as last year the company had won a large order of ~Rs. 830 crore for FGD systems.

Key positives

- Order book remained strong at Rs. 9,859 crore (up 33% y-o-y).
- The company reported healthy revenue growth in the energy and environment segments.
- Margin in both environment and chemical segments improved on a y-o-y and q-o-q basis.

Key negatives

- Order intake was down 10% y-o-y due to the absence of any large order.
- The inquiry pipeline has moderated, particularly for large orders (in the refinery, petrochemicals, and steel sectors) compared with last year.

Management Commentary

- Order pipeline is robust in sugar, distilleries, pharmaceuticals, and food and beverage for small and medium ticket-size orders.
- Large refinery and petrochemicals orders are unlikely for a year as there has been no fresh announcements regarding capex in these sectors.
- The company is targeting 15% IRR for its solar and renewable energy business, which it is pursuing through its subsidiaries – First Energy Pvt. Ltd. and TOESL. The company would be putting total equity of Rs. 400 crore in both the subsidiaries.

Revision in estimates – We have maintained our estimates for FY2023-FY2025E.

Our Call

Valuation – Retain Buy with an unchanged 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, food and beverage, and sugar distilleries. However, it has provided a muted outlook for big-ticket orders from steel, 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 solar and renewable energy space. International opportunities in biomass, waste heat recovery (WHR), and water desalination also remain strong. However, sales growth may moderate in the near to medium term as order intake growth slows down. Nevertheless, in the long term, Thermax with its strong execution and technological capabilities in green energy and the wastewater industry should be able to deliver strong performance. Further, robust financials in terms of healthy cash balance and balance sheet give us confidence. Hence, we reiterate our Buy rating on the stock with an unchanged price target (PT) of Rs. 2,790, valuing the stock on its September 2024E EPS.

Key Risks

- Slowdown in private capex and absence of large orders may impact order bookings.
- Volatility in commodity prices and supply-side challenges may continue to impact sales in the near term.

Valuation (Consolidated) Rs cr

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	81.8	60.6	47.5	37.5
P/B	8.5	8.0	7.2	6.4
EV/EBIDTA	41.7	33.7	27.2	21.8
ROCE (%)	14.8	18.4	20.8	23.5
RONW (%)	10.7	13.6	16.0	18.1

Source: Company; Sharekhan estimates

Strong quarter on all fronts

Thermax reported a healthy set of numbers, beating our and street expectations particularly on the OPM and profitability front. Consolidated sales grew by 27% y-o-y to Rs. 2,049 crore, led by strong opening order book. Operating profit grew by 42.4% y-o-y to Rs. 161 crore (vs. our estimate of Rs. 154 crore). OPM came in at 7.9% (up 86 bps y-o-y) due to lower raw-material cost and a proportionate decline in employee cost. Profit jumped by 59% y-o-y to Rs. 126 crore (vs. our estimate of Rs. 116 cr), helped by strong operating performance and higher other income.

Order intake remains healthy despite the absence of large projects

Order book was up 33% y-o-y to Rs. 9,859 crore, while order intake declined 10% y-o-y to Rs. 2,204 crore as last year there was a large order of ~Rs. 830 crore for FGD systems. Order inflow had a healthy mix of orders from diverse industry sectors such as metals and steel (10%), refinery and petrochemical (10%), sugar/distillery (12%), fertilizer (15%), food and beverages (7%), refinery and petrochemicals (10%), and transportation (8%) among others. The company's enquiry pipeline from the steel, cement, and chemical 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 in refinery, petrochemical as well as steel sectors. However, there is lot of action taking place in biomass, sugar, distilleries, water, solar, and other renewable industries side, which should help the company achieve a reasonable order inflow run rate in the near to medium term.

Key Investor Update and Conference Call Highlights

- **Segment-wise order intake and backlog breakup:** Out of total order inflows of Rs. 2,204 crore, energy orders increased by 34% y-o-y to Rs. 1,558 crore. Environment orders decreased by 56% y-o-y to Rs. 501 crore, while chemicals orders witnessed a decline of 11% y-o-y to Rs. 145 crore. In the total order backlog of Rs. 9,859 crore, energy, environment, and chemicals' contribution stood at 70%, 29%, and ~1%, respectively. Energy and environment order book is up by 40% and 22% respectively, while the chemical segment declined by 8% y-o-y.
- **Order intake from various industries in Q3FY2023:** During Q3FY2023, the company received orders for waste heat recovery boilers from a leading cement manufacturer in India. The company also received multiple orders to set up Bio CNG plants and one order from agro-chemical company for setting-up the power plant on EPC basis. Steady flow of inquiries was seen from key sectors such as cement, steel, and chemical.
- **Order inflow pipeline is strong in small to medium orders:** The company expects topline growth to be lower than the current rate going forward due to a decline in the number of large orders (over Rs. 800 crore). The company is witnessing strong inflows for Rs. 10-50 crore orders and has a strong order pipeline in that range. The company is seeing reasonably good order momentum associated with energy transition related to biomass orders. Further, momentum from industries such as sugar, ethanol, and distillery would continue to be strong for another year or so. In cement as well, new capacities are being added, which would lead to waste heat recovery orders being awarded in the medium to long term. Also, the inquiry pipeline from industries such as pharmaceuticals, food, and beverage has been good. The company said that if small orders keep coming in huge numbers, it may be able to hold the current order inflow run rate. There has not been a big petrochemical project announcement even in the Middle East region. Therefore, the company is not very optimistic about any large refinery or petrochemical orders in the near to medium term.
- **Update on the solar and renewable energy business:** The company has a subsidiary named, First Energy Pvt. Ltd., which provides access-based solar and solar hybrid farms, hybridising solar with storage and other solutions, and delivering appropriate renewable power to customers. The company's another subsidiary, TOESL would support domestic and multinational customers on their decarbonisation journeys in a variety of industries including pharmaceuticals, chemicals, food, and metals. The company has 90% market share in offerings, which it provides through its subsidiary TOESL. In the competitive landscape, there is not much competition for liquid to biomass plants. The company would be putting total equity of Rs. 400 crore in both the subsidiaries. The company is aiming for a 15% IRR in this segment.

Results (Consolidated) Rs cr

Particulars	Q3FY23	Q3FY22	Y-o-Y %	Q2FY23	Q-o-Q %
Revenue	**2,049**	**1,615**	**26.9**	**2,075**	**(1.3)**
Operating Profit	161	113	42.4	141	14.6
PBT	165	108	52.9	143	15.9
Adjusted PAT	**126**	**79**	**59.1**	**109**	**15.8**
Reported PAT	126	79	59.1	109	15.8
EPS (Rs.)	**11.2**	**7.1**	**59.1**	**9.7**	**15.8**
Margin (%)			**BPS**		**BPS**
OPM	7.9	7.0	86	6.8	109
NPM	6.2	4.9	125	5.3	91
Tax Rate	23.3	26.5	(313)	23.3	2

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 and development and PLI package will support 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.

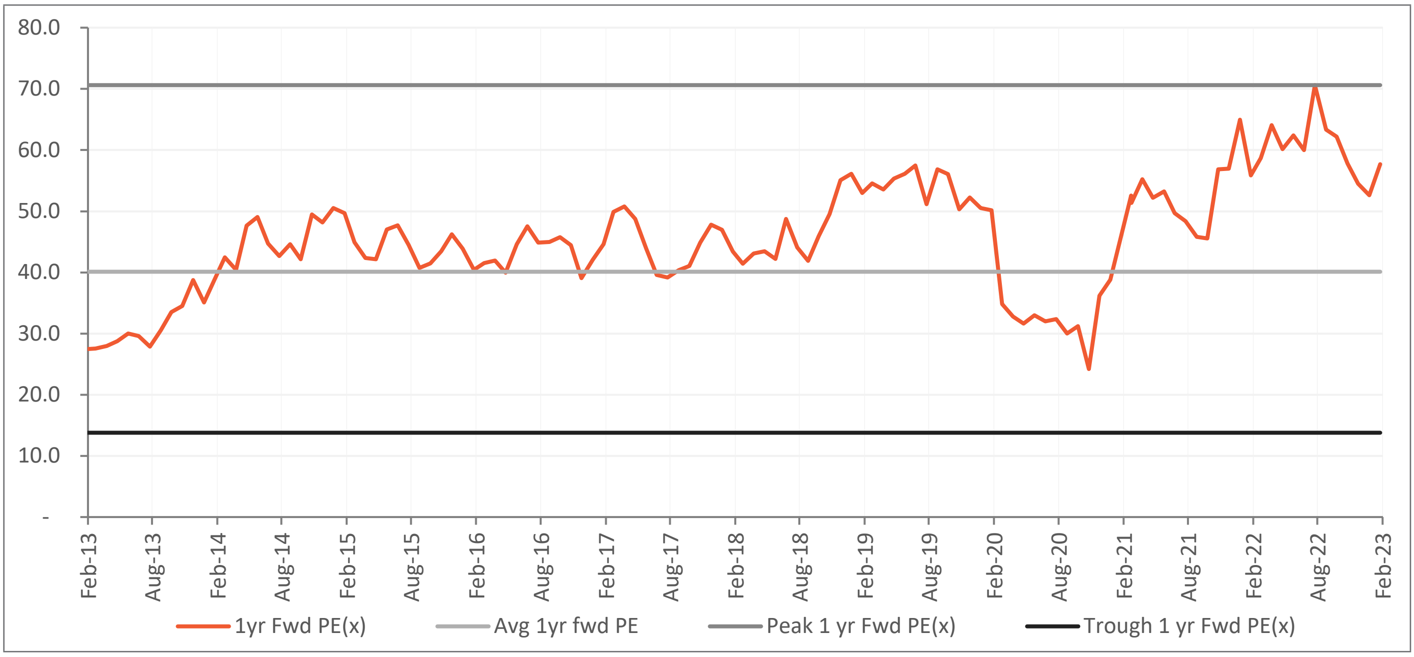
■ Company Outlook – Capitalising on opportunities

Management commentary on the inquiries 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 an unchanged 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, food and beverage, and sugar distilleries. However, it has provided a muted outlook for big-ticket orders from steel, 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 solar and renewable energy space. International opportunities in biomass, waste heat recovery (WHR), and water desalination also remain strong. However, sales growth may moderate in the near to medium term as order intake growth slows down. Nevertheless, in the long term, Thermax with its strong execution and technological capabilities in green energy and the wastewater industry should be able to deliver strong performance. Further, robust financials in terms of healthy cash balance and balance sheet give us confidence. Hence, we reiterate our Buy rating on the stock with an unchanged price target (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 Asia Pacific, Africa, the Middle East, CIS countries, Europe, the U.S., 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. Pheroz Pudumjee	Non-Independent Director
Mr. Ashish Bhandari	Executive Director-CEO-MD
Mr. Rajendran Arunachalam	Group Chief Financial Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	RDA Holdings Pvt. Ltd.	53.99
2	Kotak Mahindra Asset Management Co. Ltd.	6.97
3	Nalanda India Equity Fund Ltd.	6.86
4	SBI Funds Management Ltd.	2.48
5	Vanguard Group Inc.	1.20
6	FundRock Management Co. SA	1.14
7	Tata AIA Life Insurance Co. Ltd.	1.08
8	Mirae Asset Global Investments Co. Ltd.	0.83
9	Tata Asset Management Pvt. Ltd.	0.71
10	L&T Mutual Fund Trustee Ltd.	0.65

Source: 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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