Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Thermax Ltd

A good quarter, Innovative products to pave growth path

Capital Goods	Sharekhan code: THERMAX		
Reco/View: Buy ↔	CMP: Rs. 2,243	Price Target: Rs. 2,600 ↓	

↑ Upgrade ↔ Maintain ↓ Downgrade

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 May 08, 2023

High Risk

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

Source: Morningstar

Company details

Market cap:	Rs. 26,725 cr
52-week high/low:	Rs. 2,679/1,831
NSE volume: (No of shares)	0.49 lakh
BSE code:	500411
NSE code:	THERMAX
Free float: (No of shares)	4.5 cr

Shareholding (%)

Promoters	62.0
FII	17.5
DII	15.6
Others	4.9

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	10.6	8.3	4.2	3.8
Relative to Sensex	-3.6	7.1	4.1	-13.1

Sharekhan Research, Bloomberg

Summary

- Thermax Limited's (Thermax) consolidated Q4 performance was broadly in-line with estimates, led by strong sales and profitability. However, order intake declined 34% y-o-y due to absence of large orders.
- The company is realigning its strategies to focus on innovative products in the field of green energy which would drive the growth going forward. Further, it wants to scale up the chemicals business and aims to expand capacity.
- We believe increasing contribution of high margin subcomponents and innovative products coupled with stability in commodity prices, would lead to substantial margin expansion going forward.
- We maintain a Buy on Thermax with a revised PT of Rs. 2,600, as we expect the company's new focus areas would yield results in the long-term despite near-term headwinds. Further, strong cash & investments of Rs. 2,741 crore and execution capabilities give us comfort.

Thermax reported a healthy set of numbers, broadly in line with our estimates barring a marginal miss on OPM and net profit. The consolidated sales grew by 16% y-o-y to Rs 2,311cr, led by strong opening order book. Operating profit grew by 48% y-o-y to Rs 200 cr (vs our estimate of Rs205 cr). OPM came in at 8.7% (up 186 bps y-o-y) due to a decline in raw material cost. Profit jumped by 53% y-o-y to Rs 156 cr (vs our estimate of Rs 172cr) helped by strong operating performance and higher other income. The order book is up 11% y-o-y to Rs 9,752 crore, order intake, however, went down by 34% y-o-y at Rs 2,254 cr as last year there were two large orders of ~Rs 1,700 crore. Thermax has reclassified its business segments into four categories: Industrial Products, Industrial Infra, Green Solutions and Chemicals. This gives a better perspective of the order backlog, margins and profitability of its projects and products business.

Key positives

- Order book remained strong at Rs. 9,752 crores (up 11% y-o-y).
- The company reported healthy revenue growth in Industrial Products, Industrial Infra and Chemicals.
- Margins in Industrial Products, Industrial Infra and Chemicals improved substantially on a y-o-y basis.

Key negatives

- Order intake was down 34% y-o-y due to the absence of large orders as compared to Q4FY22.
- The company may struggle to continue the pace of order inflow growth in FY24.

Management Commentary

- The company finds it challenging to grow its order inflow on the base of FY23, as the order booking is tapering off due to the absence of large orders. However, the company is bullish on base orders and product-related orders, which would drive the order intake, and any large order win can add to the growth.
- In large orders, the company is seeing strength in the steel industry and some new energy projects are lined up.
- The company plans to enter into electrolysers from manufacturing capability perspective. The company believes substantial progress can be made on this front in a year or so. The company wants to build its own, and operate hydrogen projects for industrial customers
- Thermax sees many growth opportunities in the chemicals business and expects growth of 15-20% y-o-y. Thermax also plans to expand capacities in the segment.
- In the green solutions business, Thermax would be deploying further equity in the next 12-24 months of around Rs. 500-600 crore. The company would also raise debt of Rs.1,500-2,000 crore at the project level. It is looking for external partners for equity infusion if and when a higher level of equity is required at the project level.

Revision in estimates – We have tweaked our estimates for FY2024-FY2025E.

Our Call

Valuation – Retain Buy with a revised PT of Rs. 2,600: Thermax boasts 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 remain strong. Thermax focuses on launching innovative products, which bodes well for long-term growth. Further, robust financials give us confidence. Hence, we reiterate our Buy rating on the stock with a revised price target (PT) of Rs. 2,600, valuing the stock on its FY2025E 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	FY23	FY24E	FY25E
Net Sales	6,128	8,090	9,546	10,809
OPM (%)	6.9	7.4	8.7	9.3
Adj. Net Profit	312	451	623	765
% Growth y-o-y	20.5	44.3	38.1	22.9
Adj. EPS (Rs.)	26.2	37.8	52.3	64.2
PER (x)	85.5	59.2	42.9	34.9
P/B (x)	7.6	6.9	6.2	5.5
EV/EBIDTA (x)	44.9	32.7	24.4	19.5
ROCE (%)	11.7	15.0	17.5	19.5
RONW (%)	9.3	12.2	15.2	16.8

Source: Company; Sharekhan estimates

Healthy performance on operational front

Thermax reported a healthy set of numbers, broadly in line with our estimates, barring a marginal miss on OPM and net profit. The consolidated sales grew by 16% y-o-y to Rs 2,311 crore led by strong opening order book. Operating profit grew by 48% y-o-y to Rs 200 crore (vs our estimate of Rs205 crore). OPM came in at 8.7% (up 186 bps y-o-y) due to a decline in raw material cost. Profit jumped by 53% y-o-y to Rs 156 crore (vs our estimate of Rs 172 crore) helped by strong operating performance and higher other income. Order book is up 11% y-o-y to Rs 9,752 crore, order intake, however, went down by 34% y-o-y at Rs 2,254 crore as last year there were two large orders of ~Rs 1,700 crore. Thermax has reclassified its business segments into four categories: Industrial Products, Industrial Infra, Green Solutions and Chemicals. This gives a better perspective of the order backlog, margins and profitability on its projects and products business.

Order intake to moderate in the absence of large projects

The order book was up 11% y-o-y to Rs. 9,752 crore, while order intake declined 34% y-o-y to Rs. 2,254 crores as last year there were two significant orders from the Industrial Infra segment. The order book had a healthy mix of demands from diverse industry sectors such as refinery and petrochemical (16%), power (11%), transportation (9%), food and beverages (13%), metals and steel (9%), sugar/distillery (9%) 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, and steel sectors. However, there is a 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

The segment-wise order intake and order backlog break up: Out of total order inflows of Rs. 2,254 crore, industrial products orders increased by 27% y-o-y to Rs. 1,190 crores. Industrial infra orders decreased by 63% y-o-y. Green solutions were up by 28% y-o-y, while chemical orders were up by 27% y-o-y. The enquiry pipeline from metal, sugar/distillery, food & beverages sectors continues to be strong. At the same time, the company bagged EPC orders from a petrochemical major and received an order from a public sector company to renovate and modernise ESP. In the total order backlog of Rs. 9,752 crore, industrial products/industrial infra/green solutions/chemicals contributed 29%/65%/5%/1% respectively.

Order inflow guidance: The company finds it challenging to grow its order inflow on the base of FY23 as the order booking is tapering off due to the absence of large orders. However, the company is bullish on base orders and product-related orders which would drive the order intake, and any large order win can add to the growth. In large orders, the company is seeing strength in the steel industry, and there are some new energy projects.

Chemicals segment to grow at a healthy pace: The company sees many growth opportunities in the chemicals business and expects growth of 15-20% y-o-y. Thermax also plans to expand capacities in the segment.

Update on hydrogen business: The company plans to enter into electrolysers from manufacturing capability perspective. The company believes substantial progress can be on this front in a year or so. The company wants to build and operate hydrogen projects for industrial customers.

Update on green solutions/ solar and renewable energy business: The company is keen on deploying further equity in the next 12-24 months of around Rs. 500-600 crore. The company would also raise debt of Rs.1,500-2,000 crore at the project level. The company is looking to onboard external partners for equity infusion if and when a higher level of equity is required at the project level. The company is also taking up a few innovative products in biomass energy.

Results (Consolidated) — Rs cr

Particulars	Q4FY23	Q4FY22	YoY %	Q3FY23	QoQ %
Revenue	**2,311**	**1,992**	**16.0**	**2,049**	**12.8**
Operating Profit	**200**	**135**	**47.8**	**161**	**24.1**
PBT	214	131	62.9	165	29.6
Profit After Tax	**156**	**102**	**52.7**	**126**	**23.8**
EPS (Rs.)	**13.9**	**9.1**	**52.7**	**11.2**	**23.8**
Margin (%)			**BPS**		**BPS**
OPM	8.7	6.8	186	7.9	79
NPM	6.7	5.1	160	6.2	58
Tax Rate	27.2	22.1	511	23.3	383

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 the 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 the 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.

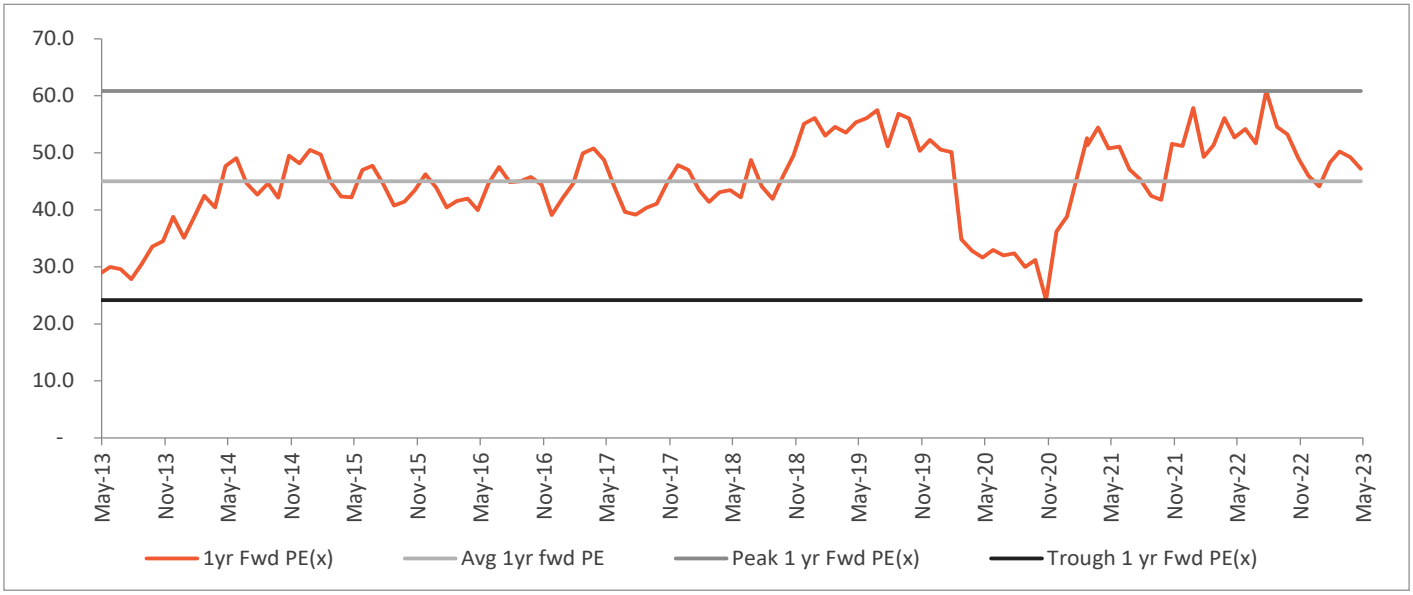
■ Company outlook - Capitalising on opportunities

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 domestic and export markets. On the commodity front, management highlighted challenges due to commodity headwinds. However, the company can hedge the price for more minor contracts as it buys the material 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. 2,600

Thermax boasts 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 remain strong. Thermax focuses on launching innovative products, which bodes well for long-term growth. Further, robust financials give us confidence. Hence, we reiterate our Buy rating on the stock with a revised price target (PT) of Rs. 2,600, valuing the stock on its FY2025E 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, 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 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 the muted order booking.
- Geopolitical tensions and supply-side challenges may impact the export 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

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Kotak Mahindra Asset Management Company	6.98
2	Kotak Infrastructure Fund	6.94
3	Nalanda India Equity Fund	6.86
4	SBI Funds Management	2.78
5	Tata AIA Life Insurance Company	1.30
6	Vanguard Group Incorporation	1.20
7	FundRock Management Company SA	1.14
8	Mirae Asset Global Investments Company	0.87
9	Tata Asset Management	0.80
10	DSP Investment Managers	0.70

Source: Bloomberg

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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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