



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 Jul 08, 2023

31.25

High Risk

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

Source: Morningstar

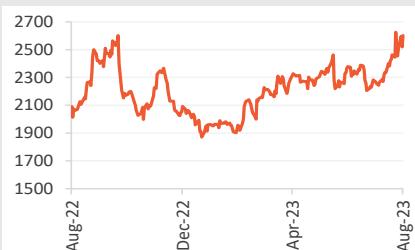
Company details

Market cap:	Rs. 31,003 cr
52-week high/low:	Rs. 2,727/1,830
NSE volume: (No of shares)	0.56 lakh
BSE code:	500411
NSE code:	THERMAX
Free float: (No of shares)	4.5 cr

Shareholding (%)

Promoters	62.0
FII	12.4
DII	15.5
Others	10.2

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	15.4	11.0	33.7	24.7
Relative to Sensex	14.9	4.5	24.0	11.5

Sharekhan Research, Bloomberg

Thermax Ltd

Multiple long-term growth levers in place

Capital Goods

Sharekhan code: THERMAX

Reco/View: Buy



Upgrade



Maintain



Downgrade

CMP: Rs. 2,602

Price Target: Rs. 2,950



Summary

- Consolidated Q1 numbers exceeded estimates led by strong sales and operating profits. Net profit came in flat as it was affected by a provision of "Rs. 51 crore w.r.t. a litigation.
- Company expects order intake to grow y-o-y in FY24, albeit, it will be largely driven by base orders of Rs. 500 crore or less.
- Thermax expects profitability to further improve as execution of high-margin orders, scaling up of chemicals business and benign commodity prices come into play.
- We maintain a Buy on Thermax with a revised PT of Rs. 2,950, as we expect the company's new focus areas would yield results in the long term despite near-term headwinds. We build in a ~16%/~33% revenue/PAT CAGR (FY23-FY25E). Further, a healthy balance sheet give us comfort.

Thermax reported a healthy set of operating numbers, which broadly matched our estimates. Net profit, however, was impacted by a one-time provision of Rs. 51 crore for a litigation. Consolidated sales grew by 16.8% y-o-y to Rs 1,933 crore led by strong opening order book in industrial products and industrial infrastructure divisions. Operating profit grew by 38% y-o-y to Rs 132 crore (versus our estimate of Rs. 128 crore). OPM came in at 6.8% (up 104 bps y-o-y) due to the impact of a decline in commodity prices in industrial products and chemical segments. Reported PAT was impacted by one-time provision of Rs. 51 crore related to a litigation and therefore came in flat at Rs. 59 crore. Adjusting for the exceptional loss, PAT rose ~86% y-o-y to Rs 110 crore (vs our estimate of Rs 88 crore) helped by strong operating performance and 2.6x increase in other income. Order book rose 10% y-o-y to Rs 10,505 crore, while order intake has also gone up by 11% y-o-y to Rs 2,567 crore led by healthy order bookings in industrial infra and green solutions segments.

Key positives

- Order book remained strong at Rs. 10,505 crore (up 10% y-o-y).
- Order inflow grew by 11% y-o-y to Rs. 2,567 crore.
- The company reported healthy revenue growth in industrial products, industrial infra and green solutions.
- Margins in industrial products and chemicals improved substantially on a y-o-y basis.

Key negatives

- Volume growth in the chemicals segment lagged expectations.
- EBIT margin of the industrial infra segment also declined by 290 bps y-o-y to 3.3% due to lower margins in projects under execution. A particular order incurred losses in Q1FY24.
- The enquiry pipeline for orders above Rs. 500 crore is muted and some of the orders may be delayed.

Management Commentary

- Thermax has a reasonably good pipeline of orders under Rs. 500 crore. The company has opportunities in refinery including a couple of international orders. However, some of the orders above Rs. 500 crore may get delayed.
- There are opportunities in water, desalination segments and orders in bio-CNG which are expected to contribute to the business in the long term.
- In the oil & gas space, the company is optimistic on order inflows from long-term perspective.
- The company recently executed its largest wind-solar hybrid captive power plant of 45 MW in Gujarat.
- The international order pipeline is the largest ever for the company.
- TOESL has more than Rs. 100 crore revenue run rate per quarter. Within couple of years, the company expects Rs. 800 crore of annual revenues for which the company would also be exploring international opportunities.
- Profitability in the industrial infra segment has been weak in Q1FY24. However, the management expects the profitability of industrial infra segment to improve for the full year.
- The company expects employee costs to go up in Q2FY24 as it has undertaken biggest compensation revision in the recent years in lower and medium ranks.

Revision in estimates: We have marginally tweaked our estimates to build in better revenue growth for FY25E.

Our Call

Valuation – Retain Buy with a revised PT of Rs. 2,950: 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, outlook for big-ticket orders from steel, oil and gas, refinery, and petrochemicals continues to be cautiously optimistic. 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. Further, its opex based model for wind and solar plants is gaining traction. International opportunities in biomass, waste heat recovery (WHR), and water desalination are increasing. Thermax focuses on launching innovative products in all its segments, which bodes well for long-term growth. Further, robust financials give us confidence. Hence, despite the run up, we reiterate our Buy rating on the stock with a revised price target (PT) of Rs. 2,950, valuing the stock on its FY25E EPS.

Key Risks

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

Valuation (Consolidated)

Particulars	FY22	FY23	FY24E	FY25E
Net Sales	6,128	8,090	9,546	10,855
OPM (%)	6.9	7.4	8.7	9.3
Adj. Net Profit	312	451	651	801
% Growth y-o-y	20.5	44.3	44.5	23.1
Adj. EPS (Rs.)	26.2	37.8	54.7	67.3
PER (x)	99.3	68.8	47.6	38.7
P/B (x)	8.9	8.0	7.2	6.3
EV/EBIDTA (x)	52.8	38.4	27.7	22.2
ROCE (%)	11.7	15.0	18.2	20.2
RONW (%)	9.3	12.2	15.9	17.4

Source: Company; Sharekhan estimates

Strong quarter

Thermax reported a healthy set of operating numbers, which broadly matched our estimates. Net profit, however, was impacted by a one-time provision of Rs. 51 crore for a litigation. Consolidated sales grew by 16.8% y-o-y to Rs 1,933 crore led by strong opening order book in industrial products and industrial infrastructure divisions. Operating profit grew by 38% y-o-y to Rs 132 crore (versus our estimate of Rs. 128 crore). OPM came in at 6.8% (up 104 bps y-o-y) due to the impact of a decline in commodity prices in industrial products and chemical segments. Reported PAT was impacted by one-time provision of Rs. 51 crore related to a litigation and therefore came in flat at Rs. 59 crore. Adjusting for the exceptional loss, PAT rose ~86% y-o-y to Rs 110 crore (vs our estimate of Rs 88 crore) helped by strong operating performance and 2.6x increase in other income. Order book rose 10% y-o-y to Rs 10,505 crore, while order intake has also gone up by 11% y-o-y to Rs 2,567 crore led by healthy order bookings in industrial infra and green solutions segments.

Healthy order book would drive growth

The order book rose 10% y-o-y to Rs. 10,505 crore, while order intake grew by 11% y-o-y to Rs. 2,567 crore. The order book had a healthy mix of diverse industry sectors such as refinery and petrochemical (20%), chemicals (109%), transportation (9%), food and beverages (11%), metals and steel (18%), sugar/distillery (11%) 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 updates and conference call highlights

- ♦ **Optimistic order inflow outlook:** The company has reasonably good pipeline of orders under Rs. 500 crore. The company has opportunities in refinery including a couple of international orders. However, some of the orders above Rs. 500 crore may get spilled over to the next year.
- ♦ **Horizon is expanding for long-term opportunities:** There are opportunities in water, desalination and bio-CNG orders, which are expected to contribute to the business in the long term.
- ♦ **Hydrogen opportunity would scale up in 3-5 years:** Hydrogen is a 3-5 year play and it will scale up with the support of the state and central governments as it requires substantial funding. 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.
- ♦ **OMCs' capex cycle would take time to turn up again:** In oil & gas, refining capex goes in cycle and most of the OMCs have finished their capex in the recent past. However, from long-term perspective, the company is optimistic on orders coming from this segment.
- ♦ **Update on First Energy Private Limited (FEPL):** The company recently executed its largest wind-solar hybrid captive power plant in Gujarat of 45MW. A 20 MW project in Tamil Nadu is in advanced stage of execution.
- ♦ **Thermax Onsite Energy Solutions Limited (TOESL):** TOESL has more than Rs. 100 crore revenue run rate per quarter. Within couple of years, the company expects Rs. 800 crore of annual revenues for which it would also be exploring international opportunities as well.
- ♦ **Capital allocation for FEPL and TOESL:** The borrowings stand at Rs. 500 crore for both FEPL and TOESL, while equity invested is Rs. 250 crore in FEPL. In TOESL, the company would be putting in Rs. 65 crore of equity.
- ♦ **Strong pipeline of international orders:** The pipeline in the international orders is quite promising. Currently international business contributes 20% to the orders and 25% to the total consolidated revenue.

- ♦ **Chemicals biz performance to improve going forward:** The volume growth has not been satisfactory in the chemicals business. The Dahej plant is stable now and Thermax would continue to invest in chemicals to cover more applications to make the segment bigger and more profitable.
- ♦ **Profitability in industrial infrastructure segment to improve:** The profitability in the industrial infra segment has been challenging. This quarter, one of the projects under execution reported losses which impacted the segment margin. However, the management expects profitability of industrial infra segment to improve for the full year.
- ♦ **Employee costs to rise in Q2FY24:** The company expects employee expenses to go up in Q2FY24 as it has undertaken substantial compensation revision in lower and medium ranks.
- ♦ **Segment-wise order intake and order backlog break up:** Out of total order inflows of Rs. 2,567 crore, industrial product orders increased by 5% y-o-y to Rs. 1,198 crore. Industrial infra orders increased by 14% y-o-y. Green Solutions were up by 152% y-o-y, while chemical orders were up by 7% y-o-y. The enquiry pipeline from metal, sugar/distillery, food & beverages, waste to energy sectors continues to be strong. In Q1FY24, the company bagged multiple boiler orders from steel and distillery segments. In the total order backlog of Rs. 10,505 crore, industrial products/industrial infra/green solutions/chemicals contributed 32%/61%/6%/1%, respectively.

Results (Consolidated)

					Rs cr
Particulars	Q1FY24	Q1FY23	YoY %	Q4FY23	QoQ %
Revenue	1,933	1,654	16.8	2,311	(16.4)
Operating Profit	132	96	37.7	200	(33.9)
PBT	142	81	74.9	214	(33.4)
Adjusted PAT	110	59	85.5	156	(29.8)
Reported PAT	59	59	(0.2)	156	(62.4)
Reported EPS (Rs.)	5.2	5.2	(0.2)	13.9	(62.4)
Margin (%)			BPS		BPS
OPM	6.8	5.8	104	8.7	(181)
NPM	5.7	3.6	210	6.7	(108)
Tax Rate	22.1	24.0	(188)	27.2	(504)

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 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.

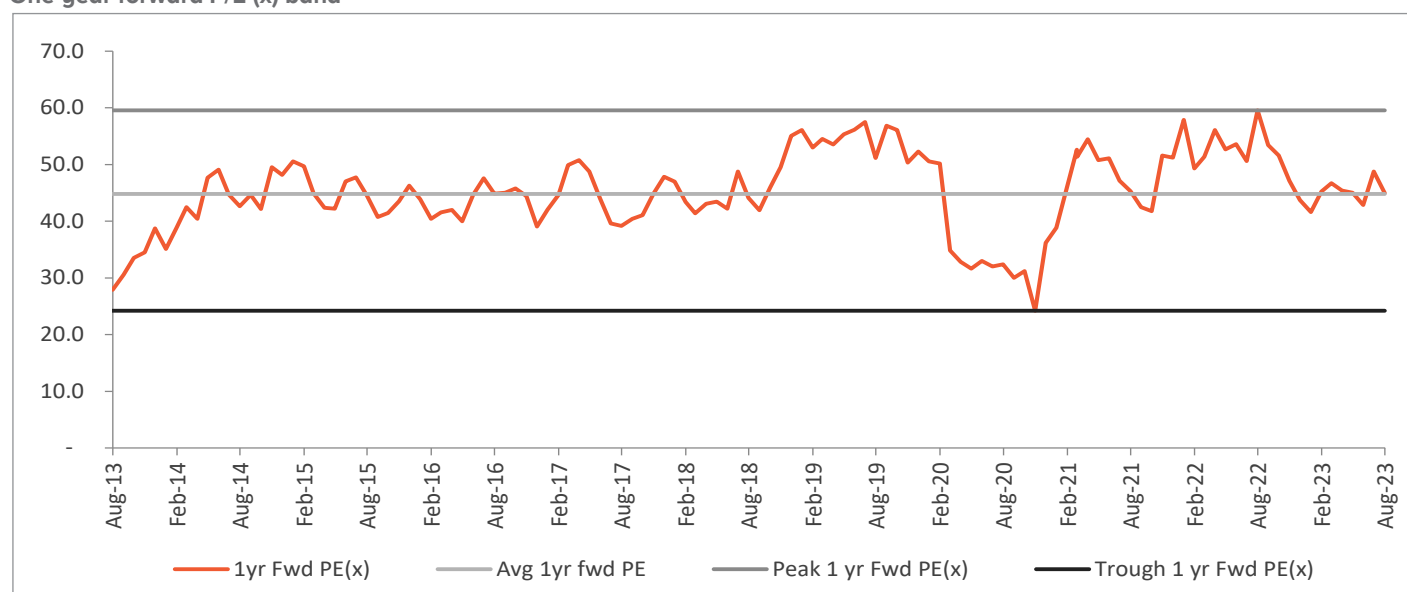
■ Company outlook - Capitalising on opportunities

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. 2,950

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, outlook for big-ticket orders from steel, oil and gas, refinery, and petrochemicals continues to be cautiously optimistic. 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. Further, its opex based model for wind and solar plants is gaining traction. International opportunities in biomass, waste heat recovery (WHR), and water desalination are increasing. Thermax focuses on launching innovative products in all its segments, which bodes well for long-term growth. Further, robust financials give us confidence. Hence, despite the run up, we reiterate our Buy rating on the stock with a revised price target (PT) of Rs. 2,950, valuing the stock on its FY25E 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. 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	RDA Holdings Private	53.99
2	Kotak Mahindra Asset Management	6.98
3	Kotak Infrastructure	6.94
4	Nalanda India Equity Fund	6.86
5	SBI Funds Management	2.78
6	Tata AIA Life Insurance	1.32
7	FundRock Management	1.15
8	Vanguard Group Incorporation	1.03
9	Mirae Asset Global Investments	0.84
10	Tata Asset Management	0.83

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 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

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