

## Meets expectations; Retain Accumulate

October 21, 2011

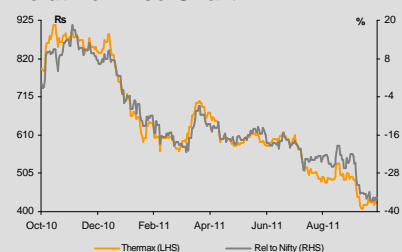
Reco	Previous Reco
Accumulate	Accumulate
CMP	Target Price
Rs 425	Rs 495
EPS change FY12E/13E (%)	NA
Target Price change (%)	NA
Nifty	5,050
Sensex	16,786

### Price Performance

(%)	1M	3M	6M	12M
Absolute	(16)	(28)	(37)	(46)
Rel. to Nifty	(14)	(21)	(26)	(34)

Source: Bloomberg

### Relative Price Chart



Source: Bloomberg

### Stock Details

Sector	Engineering & Capital Goods
Bloomberg	TMX@IN
Equity Capital (Rs mn)	238
Face Value(Rs)	2
No of shares o/s (mn)	119
52 Week H/L	927/407
Market Cap (Rs bn/USD mn)	51/1,019
Daily Avg Volume (No of sh)	171780
Daily Avg Turnover (US\$m)	1.7

### Shareholding Pattern (%)

	Jun-11	Mar-11	Dec-10
Promoters	62.0	62.0	62.0
FII/NRI	10.4	9.2	9.5
Institutions	13.0	14.5	14.9
Private Corp	1.9	1.8	1.4
Public	12.7	12.6	12.3

Source: Capitaline

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- **Meets expectations – (1) Revenue up 19% yoy to Rs13.0 bn (2) EBITDA% down 100 bps yoy to 10.8% - due to high RM prices (3) APAT up 19% yoy to Rs1.0 bn**
- **Order inflow momentum sustains – amongst few in ECG universe. Bags Rs12.8 bn orders (YTD 49% of FY12E target). Order book at Rs65.3 bn**
- **Shares not-encouraging outlook – (1) Pressure on EBITDA margins to continue (2) Subdued order inflows in near-term**
- **Already factored above concerns in our earnings estimates. Trading at attractive valuations of xxFY13E – but no near term re-rating catalysts. Have Accumulate rating. TP Rs495**

### Meets Expectations – Revenues up 19% yoy, Net profits up 14% yoy

Thermax Q2FY12 performance met expectations with net profit growth at 14% yoy (on a high base of Q2FY11). Revenue growth was healthy at 19% yoy to Rs13.0 bn – led by both segments Energy (up 16% yoy to Rs10.3 bn) and Environment (up 20% yoy to Rs3.0 bn). Operating margins continued to trend down – declining 100 bps yoy to 10.8% (below estimates). Decline in margins attributed to change in revenue mix and increase in raw material costs. However, high other income (up 56% yoy) offset decline in operating margins – hence net profit growth at 14% yoy to Rs1.0 bn met expectations.

### Energy revenues up 32% yoy, Environment up 19% yoy

Energy segment witnessed continued momentum on back of healthy order backlog. Revenues grew by at 16% yoy to Rs1.0 bn while EBIT margins improved by 40 bps yoy to 10.7% - in line with estimates. Environment segment posted strong revenue growth at 20% yoy to Rs3.0 bn – in line with estimates. However, EBIT margins fell sharply by 170 bps yoy to 10.8% (lowest in past 17 quarters) – owing to sharp rise in raw material (especially steel) prices.

### Order inflow momentum continues – Amongst the few in our universe

Thermax witnessed sustained momentum in order inflows – amongst the few in our ECG universe. It has maintained its quarterly run rate and secured orders worth Rs12.8 bn (down 12% yoy on high base) – YTD secured 49% of FY12E target order inflows. Order inflows dominated by oil & gas (30%) followed by Metals (12%), Cement (6%), Power (8%) and Textiles (7%). Order book declined marginally by 4% qoq to Rs65.3 bn.

### Key highlights shared during the concall on outlook... Not encouraging

- Thermax indicated no improvement in macro environment. While order enquiries remained strong, order finalizations continued to be delayed and deferred. Expects subdued order inflow growth in near term with wider revival in H2FY13E.
- No respite from competitive pricing pressure, especially in the case of large orders (+0.5 bn) – owing to depleting order backlogs amongst competition. Further, in the products segment, Thermax likely to see reduction in premium commanded.

### Consolidated Financial Snapshot

Rs Mn

YE-	Net	EBITDA		EPS	EPS	ROE		EV/	
Mar	Sales	(Core)	(%)	(Rs)	%Chg	(%)	P/E	EBITDA	P/BV
FY10	33,678	4,154	12.3	2,593	21.8	(8.4)	19.5	9.7	4.7
FY11	53,350	5,855	11.0	3,820	32.1	47.3	28.8	7.2	3.8
FY12E	58,692	6,604	11.3	4,331	36.3	13.4	26.6	11.7	3.1
FY13E	62,563	6,515	10.4	4,298	36.1	(0.8)	23.0	11.8	2.6

## Standalone Quarterly Results

Rs mn	Q2FY11	Q3FY11	Q4FY11	Q1FY12	Q2FY12	YoY (%)	QoQ (%)	YTD'12	YTD'11	Gr (%)
<b>Revenue</b>	<b>10,916</b>	<b>12,412</b>	<b>17,713</b>	<b>10,444</b>	<b>13,035</b>	<b>19.4</b>	<b>24.8</b>	<b>23,479</b>	<b>18,814</b>	24.8
<b>Expenditure</b>	<b>9,630</b>	<b>10,948</b>	<b>15,762</b>	<b>9,307</b>	<b>11,630</b>	<b>20.8</b>	<b>25.0</b>	<b>20,937</b>	<b>16,569</b>	<b>26.4</b>
Consumption of RM	7,432	8,646	12,831	7,282	9,131	22.9	25.4	16,412	12,682	29.4
as % of sales	68.1	69.7	72.4	69.7	70.0			69.9	67.4	
Employee Cost	990	975	969	905	985	-0.4	8.9	1,890	1,742	8.5
as % of sales	9.1	7.9	5.5	8.7	7.6			8.1	9.3	
Other expenditure	1,208	1,327	1,962	1,121	1,514	25.3	35.0	2,635	2,144	22.9
as % of sales	11.1	10.7	11.1	10.7	11.6			11.2	11.4	
<b>EBITDA</b>	<b>1,286</b>	<b>1,464</b>	<b>1,951</b>	<b>1,137</b>	<b>1,405</b>	<b>9.3</b>	<b>23.6</b>	<b>2,542</b>	<b>2,245</b>	<b>13.2</b>
Depreciation	105	106	116	111	117	11.6	5.7	228	211	8.2
<b>EBIT</b>	<b>1,181</b>	<b>1,359</b>	<b>1,836</b>	<b>1,026</b>	<b>1,288</b>	<b>9.1</b>	<b>25.5</b>	<b>2,314</b>	<b>2,035</b>	<b>13.7</b>
Other Income	133	117	133	147	208	56.0	41.1	355	273	30.1
Interest	5	2	10	4	11	142.8	192.7	15	10	46.1
<b>PBT</b>	<b>1,309</b>	<b>1,473</b>	<b>1,959</b>	<b>1,170</b>	<b>1,485</b>	<b>13.4</b>	<b>26.9</b>	<b>2,654</b>	<b>2,298</b>	<b>15.5</b>
Total Tax	414	471	694	371	468	12.9	26.1	839	741	13.2
<b>Adjusted PAT</b>	<b>895</b>	<b>1,002</b>	<b>1,265</b>	<b>799</b>	<b>1,017</b>	<b>13.6</b>	<b>27.3</b>	<b>1,816</b>	<b>1,557</b>	<b>16.6</b>
Extra ordinary items	0	0	0	0	0	NA	NA	0	0	NA
<b>Reported PAT</b>	<b>895</b>	<b>1,002</b>	<b>1,265</b>	<b>799</b>	<b>1,017</b>	<b>13.6</b>	<b>27.3</b>	<b>1,816</b>	<b>1,557</b>	<b>16.6</b>
<b>Adjusted EPS (Rs)</b>	<b>7.5</b>	<b>8.4</b>	<b>10.6</b>	<b>6.7</b>	<b>8.5</b>	<b>13.6</b>	<b>27.3</b>	<b>15.2</b>	<b>13.1</b>	<b>16.6</b>

Margins (%)						(bps)	(bps)			(bps)
EBIDTA	11.8	11.8	11.0	10.9	10.8	-100	-10	10.8	11.9	-110
EBIT	10.8	10.9	10.4	9.8	9.9	-90	10	9.9	10.8	-100
EBT	12.0	11.9	11.1	11.2	11.4	-60	20	11.3	12.2	-90
PAT	8.2	8.1	7.1	7.6	7.8	-40	20	7.7	8.3	-50
Effective Tax rate	31.6	32.0	35.4	31.7	31.5	-10	-20	31.6	32.2	-60

- Thermax expects working capital situation to deteriorate with continued delays in realization of receivables due.
- In view of above, the company expects operating margins to remain stressed. Thermax guided for operating margins of 10-11% for FY12E
- Sectoral outlook for order inflows (1) Power – Rise in merchant power rates and pro-policy / reforms announcements imperative for resumption of orders (2) Power BTG – Expects high competitive intensity in the near to medium term, given new planned capacity additions expected over the next 1-2 years. (3) Cement – Expects resumption of order inflows after 3-4 quarters, with new capacities commissioned and prices stabilized (4) Thermax shared positive outlook for food processing, refining & petroleum and basic chemicals.

## Attractive valuations; Retain 'BUY' rating

Post our revision in earnings (carried out in our report "Delusional optimism to reality" dated 19 Oct'11), the implied earnings growth for H2FY12E stands at a comfortable 4% yoy. We have already factored slowdown in order inflows & order execution and pressure on operating margins – the 2 principle concerns and risk to earnings. At Rs36.1 per share, we are lower by 8% to consensus FY13E estimates.

At CMP, stock is trading at attractive valuations of xx FY13E earnings of Rs36.1 per share, considering healthy return ratios (+25% ROE - second best only to BHEL), healthy cash flow generation, debt-free balance sheet and low risk to earnings. However, there are no re-rating catalysts in the near-medium term. We have an Accumulate rating with a target price to Rs495 (@ 13.7X FY13E earnings).

**Segmental Performance**

Rs mn	Q2FY11	Q3FY11	Q4FY11	Q1FY12	Q2FY12	YoY (%)	QoQ (%)	YTD'12	YTD'11	Gr (%)
<b>Segment Revenues</b>										
Energy	8,910	9,904	14,299	8,024	10,348	16.1	29.0	18,372	14,975	22.7
Environment	2,482	2,943	3,826	2,647	2,968	19.6	12.1	5,616	4,703	19.4
Less: Intersegment	475	436	412	227	282	-	-	509	864	-
<b>Total</b>	<b>10,916</b>	<b>12,412</b>	<b>17,713</b>	<b>10,444</b>	<b>13,035</b>	<b>19.4</b>	<b>24.8</b>	<b>23,479</b>	<b>18,814</b>	<b>24.8</b>
<b>Segment Results</b>										
Energy	913	1,073	1,494	810	1,102	20.8	36.2	1,912	1,593	20.0
Environment	308	399	499	313	320	3.7	2.2	633	577	9.6
<b>Total</b>	<b>1,221</b>	<b>1,472</b>	<b>1,993</b>	<b>1,123</b>	<b>1,422</b>	<b>16.4</b>	<b>26.7</b>	<b>2,545</b>	<b>2,170</b>	<b>17.2</b>
Add- Unall Income / (Exp)	93	3	-25	51	73	-	-	124	137	-
Less- Interest Exp	5	2	10	4	11	142.8	192.7	15	10	46.1
<b>PBT</b>	<b>1,309</b>	<b>1,473</b>	<b>1,959</b>	<b>1,170</b>	<b>1,485</b>	<b>13.4</b>	<b>26.9</b>	<b>2,654</b>	<b>2,298</b>	<b>15.5</b>
<b>Segment Cap. Employed</b>										
Energy	1,143	1,396	1,705	2,598	3,516	207.5	35.3	3,516	1,143	207.5
Environment	1,395	1,152	1,404	1,671	1,826	30.9	9.3	1,826	1,395	30.9
Unallocated	9,397	10,412	9,814	9,462	9,289	-1.1	-1.8	9,289	9,397	-1.1
<b>Total</b>	<b>11,935</b>	<b>12,959</b>	<b>12,923</b>	<b>13,731</b>	<b>14,630</b>	<b>22.6</b>	<b>6.6</b>	<b>14,630</b>	<b>11,935</b>	<b>22.6</b>
<b>Segment Margins (%)</b>										
						<b>(bps)</b>	<b>(bps)</b>			<b>(bps)</b>
Energy	10.2	10.8	10.4	10.1	10.7	40	60	10.4	10.6	-20
Environment	12.4	13.6	13.0	11.8	10.8	-170	-110	11.3	12.3	-100
<b>Average</b>	<b>10.7</b>	<b>11.5</b>	<b>11.0</b>	<b>10.5</b>	<b>10.7</b>	<b>0</b>	<b>20</b>	<b>10.6</b>	<b>11.0</b>	<b>-40</b>

**Order Backlog Details - Consolidated**

Rs mn	Q2FY11	Q3FY11	Q4FY11	Q1FY12	Q2FY12	YoY (%)	QoQ (%)	YTD'12	YTD'11	Gr (%)
Order Inflows	14,578	12,496	12,563	16,880	12,840	-11.9	-23.9	29,720	35,157	-15.5
Order Backlog	72,760	71,540	64,460	68,040	65,310	-10.2	-4.0	65,310	72,760	-10.2

## Key Consolidated Financials

## Income Statement

Y/E, Mar (Rs. mn)	FY10	FY11	FY12E	FY13E
<b>Net Sales</b>	<b>33,678</b>	<b>53,350</b>	<b>58,692</b>	<b>62,563</b>
Growth (%)	-2.5	58.4	10.0	6.6
<b>Expenditure</b>	<b>29,524</b>	<b>47,495</b>	<b>52,088</b>	<b>56,048</b>
Materials Consumed	20,452	36,474	39,540	42,648
Employee Cost	3,300	4,597	5,175	5,516
Manufacturing Exp	2,883	2,918	3,211	3,422
Other Exp	2,891	3,505	4,163	4,461
<b>EBITDA</b>	<b>4,154</b>	<b>5,855</b>	<b>6,604</b>	<b>6,515</b>
Growth (%)	-2.0	4.1	1.3	-0.1
<b>EBITDA margin (%)</b>	<b>12.3</b>	<b>11.0</b>	<b>11.3</b>	<b>10.4</b>
Depreciation	442	541	584	610
<b>EBIT</b>	<b>3,712</b>	<b>5,314</b>	<b>6,019</b>	<b>5,905</b>
<b>EBIT margin (%)</b>	<b>11.0</b>	<b>10.0</b>	<b>10.3</b>	<b>9.4</b>
Other Income	314	467	539	582
Interest expenses	20	41	41	21
<b>PBT</b>	<b>4,005</b>	<b>5,740</b>	<b>6,517</b>	<b>6,467</b>
Tax	1,416	1,967	2,233	2,216
Effective tax rate (%)	35.4	34.3	34.3	34.3
<b>Adjusted PAT</b>	<b>2,589</b>	<b>3,773</b>	<b>4,284</b>	<b>4,251</b>
Growth (%)	-8.5	45.7	13.5	-0.8
<b>Net Margin (%)</b>	<b>7.7</b>	<b>7.2</b>	<b>7.4</b>	<b>6.9</b>
(Profit)/loss from JVs/Ass/MI	-4	-47	-47	-47
<b>Adj. PAT After JVs/Ass/MI</b>	<b>2,593</b>	<b>3,820</b>	<b>4,331</b>	<b>4,298</b>
E/O items	-1,150	-4	0	0
<b>Reported PAT</b>	<b>1,443</b>	<b>3,817</b>	<b>4,331</b>	<b>4,298</b>
Growth (%)	-50.0	164.4	13.5	-0.8

## Cash Flow

Y/E, Mar (Rs. mn)	FY10	FY11	FY12E	FY13E
<b>PBT</b>	<b>4,004</b>	<b>5,737</b>	<b>6,564</b>	<b>6,514</b>
Depreciation	442	516	584	610
Interest Provided	20	41	41	21
Other Non-Cash items	133	-1,149	0	0
Chg in working cap	3,709	-910	450	146
Tax paid	-1,439	-1,911	-2,233	-2,216
<b>Operating Cashflow</b>	<b>6,869</b>	<b>2,324</b>	<b>5,407</b>	<b>5,074</b>
Capital expenditure	-840	-1,507	-500	-500
<b>Free Cash Flow</b>	<b>6,030</b>	<b>818</b>	<b>4,907</b>	<b>4,574</b>
Other income	0	0	0	0
Investments	-2,263	-544	0	0
<b>Investing Cashflow</b>	<b>-2,263</b>	<b>-544</b>	<b>0</b>	<b>0</b>
Equity Capital Raised	0	0	0	0
Loans Taken / (Repaid)	39	1,166	-1,400	0
Interest Paid	-20	-41	-41	-21
Dividend paid (incl tax)	-697	-695	-1,238	-1,207
Income from investments	-82	-84	0	0
Others	0	173.5	0	0
<b>Financing Cashflow</b>	<b>-760</b>	<b>520</b>	<b>-2,679</b>	<b>-1,227</b>
<b>Net change in cash</b>	<b>3,006</b>	<b>794</b>	<b>2,228</b>	<b>3,347</b>
Opening cash position	3,696	6,702	7,496	9,724
<b>Closing cash position</b>	<b>6,702</b>	<b>7,496</b>	<b>9,724</b>	<b>13,071</b>

## Balance Sheet

Y/E, Mar (Rs. mn)	FY10	FY11	FY12E	FY13E
Equity share capital	238	238	238	238
Reserves & surplus	10,544	12,911	16,004	19,095
<b>Net worth</b>	<b>10,782</b>	<b>13,149</b>	<b>16,243</b>	<b>19,334</b>
<b>Minority Interest</b>	<b>94</b>	<b>520</b>	<b>520</b>	<b>520</b>
Secured Loans	80	1,476	76	76
Unsecured Loans	0	4	4	4
<b>Loan Funds</b>	<b>80</b>	<b>1,479</b>	<b>79</b>	<b>79</b>
Net deferred tax liability	144	298	298	298
<b>Total Liabilities</b>	<b>11,099</b>	<b>15,447</b>	<b>17,140</b>	<b>20,231</b>
Gross Block	7,418	10,677	11,531	12,031
Less: Depreciation	2,048	2,824	3,408	4,017
<b>Net block</b>	<b>5,369</b>	<b>7,853</b>	<b>8,124</b>	<b>8,014</b>
Capital work in progress	115	354	0	0
<b>Investment</b>	<b>3,703</b>	<b>2,415</b>	<b>2,415</b>	<b>2,415</b>
<b>Current Assets</b>	<b>23,477</b>	<b>28,650</b>	<b>32,797</b>	<b>37,618</b>
Inventories	4,916	6,155	6,114	6,517
Sundry debtors	7,984	10,672	12,478	13,301
Cash & bank balance	6,702	7,496	9,724	13,071
Loans & advances	3,282	3,596	3,750	3,998
Other current assets	594	731	731	731
<b>Current lia &amp; Prov</b>	<b>21,566</b>	<b>23,826</b>	<b>26,196</b>	<b>27,816</b>
Current liabilities	20,581	22,193	24,563	26,182
Provisions	985	1,633	1,633	1,633
<b>Net current assets</b>	<b>1,912</b>	<b>4,824</b>	<b>6,602</b>	<b>9,802</b>
Misc. exp	0	0	0	0
<b>Total Assets</b>	<b>11,099</b>	<b>15,447</b>	<b>17,140</b>	<b>20,231</b>

## Key Ratios

Y/E, Mar	FY10	FY11	FY12E	FY13E
<b>Profitability (%)</b>				
EBITDA Margin	12.3	11.0	11.3	10.4
Net Margin	7.7	7.2	7.4	6.9
ROCE	38.0	43.6	40.3	34.7
ROE	24.4	28.8	26.6	23.0
RoIC	137.8	184.5	118.2	121.2
<b>Per Share Data (Rs)</b>				
EPS	21.8	32.1	36.3	36.1
CEPS	25.5	36.6	41.3	41.2
BVPS	90.5	110.4	136.3	162.3
DPS	6.0	9.0	10.4	10.1
<b>Valuations (x)</b>				
PER	19.5	13.3	11.7	11.8
P/CEPS	16.7	11.6	10.3	10.3
P/BV	4.7	3.8	3.1	2.6
EV / Sales	1.2	0.8	0.7	0.6
EV / EBITDA	9.7	7.2	5.8	5.4
Dividend Yield (%)	1.4	2.1	2.4	2.4
<b>Gearing Ratio (x)</b>				
Net Debt/ Equity	-1.0	-0.6	-0.7	-0.8
Net Debt/EBITDA	-2.5	-1.4	-1.8	-2.4
Working Cap Cycle (days)	29.8	23.0	35.5	47.9

**Recommendation History: Thermax – TMX IN**

Date	Reports	Reco	CMP	Target
19/10/2011	<a href="#">Engineering and Capital Goods Sector Update</a>			
25/07/2011	<a href="#">Thermax Q1FY12 Result Update</a>	Buy	610	735
04/05/2011	<a href="#">Thermax Q4FY11 Result Update</a>	Buy	613	735
28/01/2011	<a href="#">Thermax Q3FY11 Result Update</a>	Buy	664	943

**Recent Research Reports**

Date	Reports	Reco	CMP	Target
16/08/2011	<a href="#">McNally Bharat Q1FY12 Result Update</a>	Buy	135	201
16/08/2011	<a href="#">Punj Lloyd Q1FY12 Result Update</a>	Hold	56	76
08/08/2011	<a href="#">Larsen and Toubro Q1FY12 Result Update</a>	Buy	1,630	1,936
05/08/2011	<a href="#">Cummins India Q1FY12 Result Update</a>	Buy	614	687

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