February 3, 2012

Thermax Ltd (THERMA)

₹ 520

Rating matrix		
Rating	:	Sell
Target	:	₹ 401
Target Period	:	12 months
Potential Upside	:	26%

Key Financials

₹ Crore	FY10	FY11	FY12E	FY13E
Net Sales	3,185	4,893.9	5,284.7	4,915.9
EBITDA	384.1	566.1	553.3	554.7
Net Profit	141.4	381.8	391.5	367.7
EPS (₹)	11.9	32.0	32.9	30.9

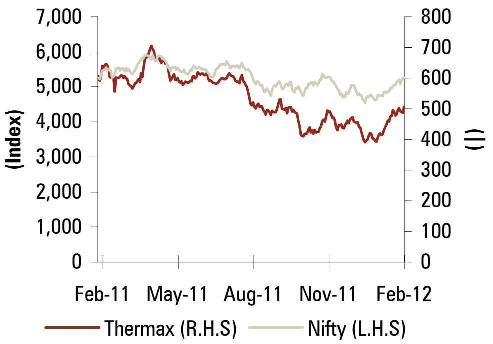
Valuation summary

	FY10	FY11	FY12E	FY13E
P/E	43.8	16.2	15.8	16.8
Target P/E	33.8	12.5	12.2	13.0
EV / EBITDA	14.5	9.9	10.1	9.9
P/BV	5.9	4.8	3.9	3.4
RoNW	13.5	29.6	24.9	20.4
RoCE	32.7	39.0	31.3	27.3

Stock data

Market Capitalization	₹ 6196.1 Crore
Total Debt (FY12E)	₹ 48 Crore
Cash and Investments (FY12E)	₹ 659.3 Crore
EV	₹ 5584.9 Crore
52 week H/L	705 / 391
Equity capital	₹ 23.8 Crore
Face value	₹ 2
DII Holding (%)	11.2
FII Holding (%)	11.1

Price movement



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WHAT'S CHANGED…

PRICE TARGET... Changed from ₹ 456 to ₹ 401
EPS (FY12E)...Unchanged
EPS (FY13E).. Changed from ₹ 38 to ₹ 30
RATING..Changed from Hold to Sell

Dismal order flows accentuate risk to growth…

Thermax delivered Q3FY12 results in line with our estimates. Reported revenues stood at ₹ 1269 crore vs. our expectation of ₹ 1303 crore. EBITDA margins at 10.7% were a tad above our estimate of 10.2%, even though execution of EPC projects was high during Q3FY12. Consequently, PAT declined 6% YoY to ₹ 96 crore. However, a dwindling standalone order book at ₹ 5104 crore (20% de-growth) crore poses a significant concern for FY13E revenue visibility, going forward. We expect revenue and PAT to decline by 7% and 6%, respectively, for FY13E on a YoY basis.

- **Dismal order backlog weakens revenue visibility…**

Significant headwinds in the power sector coupled with a challenging macro environment, led to a 40% YoY de-growth in order intake at ₹ 590 crore. The standalone order book at ₹ 5100 crore, registered a 20% YoY decline. A book to bill at 1.0x, coupled with client side delays in execution, poses significant challenges to revenue visibility for FY13E. Hence, we have revised down our revenue estimates for FY12 and FY13 by 2% and 12%, respectively.

- **…may lead to change in company's order bidding strategy**

Though the company maintained an EBITDA margin of 10.7% for the quarter, the sustenance of the same will come under attack if order inflows do not pick up as the company may bid for low margin orders. As such, we have factored the same in our estimates but perception risks will persist. We expect Thermax to report an EBITDA margin of 11.3% for FY13E.

Valuation

Valuations at 16.8x FY13E EPS are demanding given the challenging macro environment and dwindling revenue visibility. Hence, we have assigned a lower P/E multiple of 13x (from 14x earlier) to arrive at a fair value of ₹ 401 (₹ 456 earlier) and rate the stock as **SELL** from HOLD.

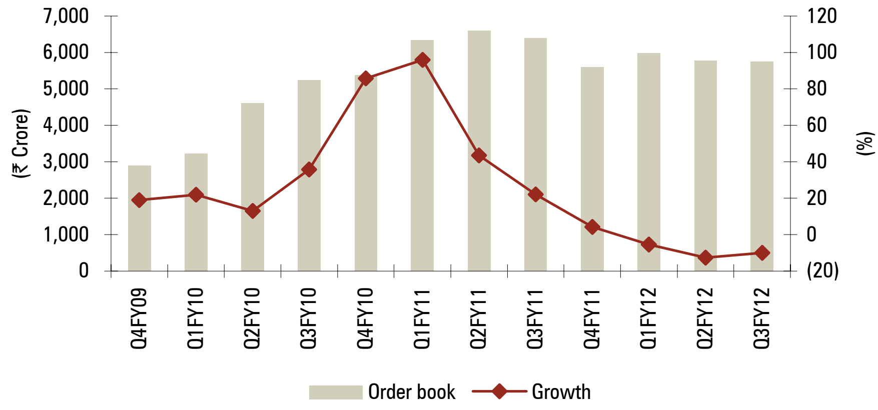
Exhibit 1: Financial Performance

(₹ Crore)	Q3FY12	Q3FY12E	Q3FY11	Q2FY12	QoQ (Chg %)	YoY (Chg %)
Total Operating Income	1269.3	1303.6	1241.2	1303.5	-2.6	2.3
EBITDA	135.4	136.6	146.4	140.5	-3.6	-7.5
EBITDA Margin (%)	10.7	10.2	11.8	10.8	-11 bps	-113 bps
Depreciation	12.0	9.9	10.6	11.7	2.3	13.5
Interest	0.7	0.8	0.0	1.1	-37.3	NA
Other Income	15.7	13.4	11.7	20.8	-24.7	34.0
Reported PAT	95.5	94.7	99.3	101.7	-6.1	-3.8
EPS (₹)	8.0	7.9	8.3	8.5	-6.1	-3.8

Source: Company, ICICIdirect.com Research

The backlog has declined by 20% YoY as order inflows for Q3FY12 declined by 40% YoY. Thermax order backlog and inflows for Q3FY12 stood at ₹ 5104 crore and ₹590 crore, respectively

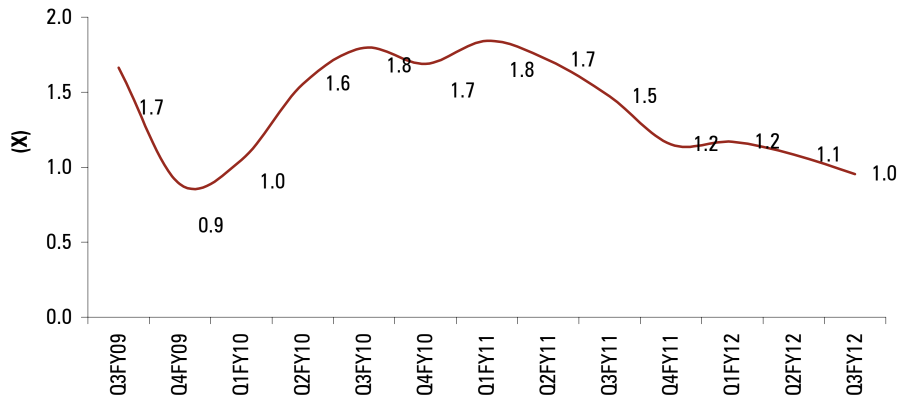
Exhibit 2: Trend of order backlog for consolidated business



Source: Company, ICICIdirect.com Research

The book to bill ratio has continuously deteriorated and currently stands at 1x TTM revenues

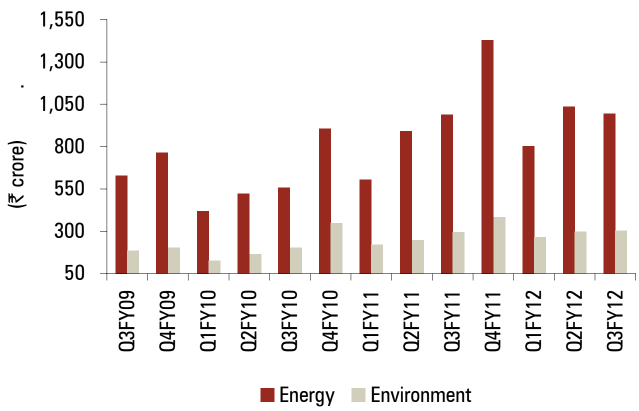
Exhibit 3: Book to bill ratio trend



Source: Company, ICICIdirect.com Research

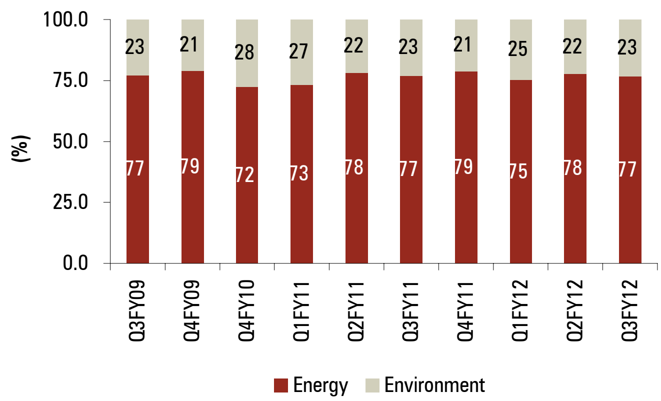
Revenue growth of 2% YoY was a tad below our expectations. Out of the total revenues, 78% came from the energy segment while 22% of the revenues came from the environment segment. Export revenues came in at ₹ 469 crore, up 18% YoY Going ahead, we expect a bleak backlog to lead to 7% revenue decline in FY13E

Exhibit 4: Trend in segmental revenues



Source: Company, ICICIdirect.com Research

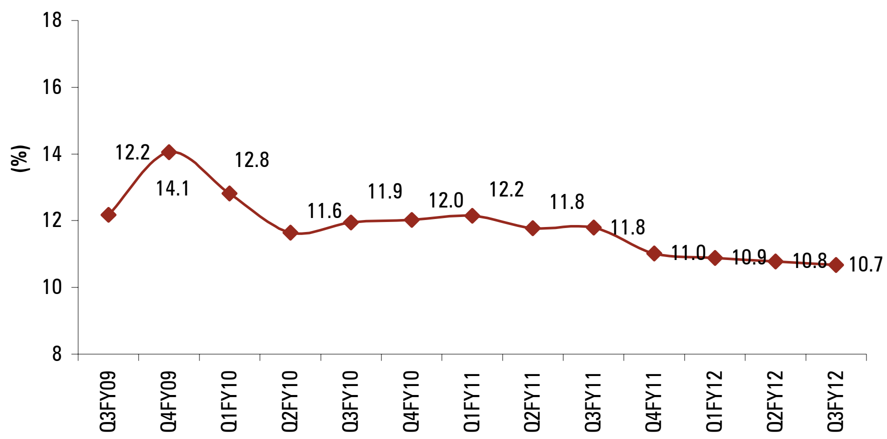
Exhibit 5: Energy segment dominates revenue mix



Source: Company, ICICIdirect.com Research

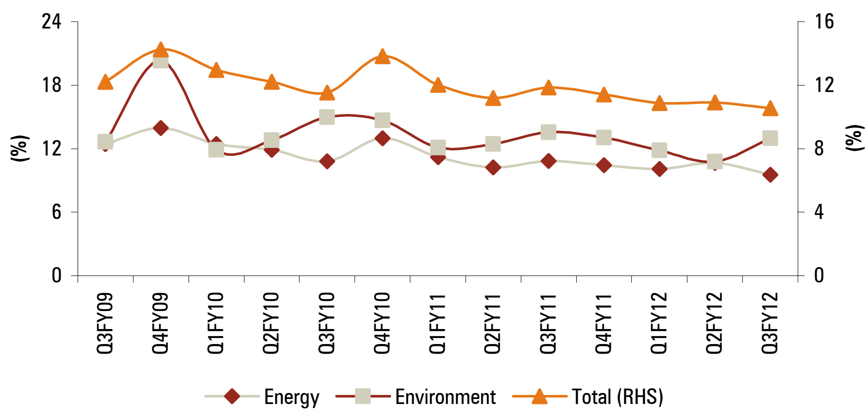
EBITDA margins at 10.7% were above our estimates as energy revenues were flattish but the environment segment reported a modest 2% YoY jump. On a YoY basis, margins contracted by 110 bps

Exhibit 6: EBITDA margin trend



Source: Company, ICICIdirect.com Research

Exhibit 7: Segmental EBIT margins



Source: Company, ICICIdirect.com Research

Due to weak order flows and a dismal outlook in terms of order flows mainly from the power sector, we have revised our revenue estimates by 2% and 12% for FY12 and FY13, respectively. Similarly, PAT estimates have been pruned down by 6% and 19% for FY12 and FY13, respectively

Exhibit 8: Revised earning estimates

Particulars	FY12E			FY13E		
	Old	New	% Change	Old	New	% Change
Revenue	5,376.0	5284.7	(1.7)	5,587.0	4915.9	(12.0)
EBITDA	596.0	553.3	(7.2)	632.0	554.7	(12.2)
EBITDA Margir	11.1	10.5	-62 bps	11.3	11.3	-3 bps
PAT	418.0	391.5	(6.3)	453.0	367.7	(18.8)
EPS	35.1	32.9	(6.4)	38.0	30.9	(18.8)

Source: Company, ICICIdirect.com Research

Other highlights for Q3FY12:

- The company is on track with respect to the capacity expansion JV with B&W, which is likely to commence operations from September 2012
- The net working capital is still positive for the company. The amount of cash has declined by ₹ 100 crore to ₹ 590 crore as of Q3FY12
- In terms of order inflows, the company has received a ₹ 70 crore order from the metal sector. The company is also witnessing good traction from sectors such as food processing and chemicals

Financial summary

Profit and loss statement

(₹ Crore)

(Year-end March)	FY10	FY11	FY12E	FY13E
Total operating Income	3,185.5	4,893.9	5,284.7	4,915.9
Growth (%)	-2.4	53.6	8.0	-7.0
Raw Material Expenses	2,058.5	3,415.9	3,706.6	3,452.5
Employee Expenses	256.7	290.7	368.6	426.1
Other Operating Expenses	495.6	452.2	543.3	598.7
Administrative Expenses	0.0	0.0	0.0	0.0
Other expenses	0.0	0.0	0.0	0.0
Total Operating Expenditure	2,808.4	4,212.4	4,626.5	4,470.4
EBITDA	384.1	566.1	553.3	554.7
Growth (%)	-7.3	47.4	-2.3	0.3
Depreciation	40.4	43.2	46.0	49.8
Interest	1.5	0.0	3.0	4.8
Other Income	49.8	52.3	67.8	48.8
PBT	277.1	575.1	572.1	548.9
Others	0.0	0.0	0.0	0.0
Total Tax	135.6	190.6	180.6	181.1
PAT	141.4	381.8	391.5	367.7
Growth (%)	-50.8	170.0	2.5	-6.1
EPS (₹)	11.9	32.0	32.9	30.9

Source: Company, ICICIdirect.com Research

Cash flow statement

(₹ Crore)

(Year-end March)	FY10	FY11	FY12E	FY13E
Profit after Tax	141.4	381.8	391.5	367.7
Add: Depreciation	40.4	43.2	46.0	49.8
(Inc)/dec in Current Assets	-348.6	-392.0	-437.5	193.7
Inc/(dec) in CL and Provisions	774.5	188.0	155.8	-341.3
Others	3.3	3.0	5.0	5.0
CF from operating activities	607.7	221.0	155.7	270.0
(Inc)/dec in Investments	-201.7	-26.2	0.0	0.0
(Inc)/dec in Fixed Assets	-87.9	-54.7	-42.8	-42.9
Others	0.0	0.0	0.0	0.0
CF from investing activities	-290.4	-77.9	-42.8	-42.9
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	0.0	48.0	0.0	0.0
Dividend paid & dividend tax	-69.5	-124.5	-111.5	-139.4
Inc/(dec) in Sec. premium	0.0	0.0	0.0	0.0
Others	0.0	7.6	0.0	0.0
CF from financing activities	-52.5	-92.7	-111.5	-139.4
Net Cash flow	264.8	50.4	1.3	87.7
Opening Cash	342.7	607.5	658.0	659.3
Closing Cash	607.5	658.0	659.3	747.0

Source: Company, ICICIdirect.com Research

Balance sheet

(₹ Crore)

(Year-end March)	FY10	FY11	FY12E	FY13E
Liabilities				
Equity Capital	23.8	23.8	23.8	23.8
Reserve and Surplus	1,026.9	1,268.1	1,548.0	1,776.3
Total Shareholders funds	1,050.8	1,291.9	1,571.8	1,800.2
Total Debt	0.0	48.0	48.0	48.0
Deferred Tax Liability	17.2	20.1	20.1	20.1
Minority Interest / Others	0.0	0.0	0.0	0.0
Total Liabilities	1,068.0	1,360.1	1,640.0	1,868.3
Assets				
Gross Block	649.7	678.9	715.2	751.6
Less: Acc Depreciation	177.1	208.9	247.0	287.7
Net Block	472.6	470.0	468.2	463.9
Capital WIP	11.2	29.7	29.7	29.7
Total Fixed Assets	483.7	499.7	497.9	493.6
Investments	378.2	404.4	404.4	404.4
Inventory	246.4	282.3	292.4	242.0
Debtors	747.1	1,001.3	1,293.1	1,202.5
Loans and Advances	301.4	309.4	424.8	453.0
Other Current Assets	328.7	422.5	442.8	361.9
Cash	607.5	658.0	659.3	747.0
Total Current Assets	2,231.0	2,673.5	3,112.3	3,006.4
Creditors	729.9	801.6	862.1	801.6
Provisions	97.5	162.1	172.4	160.3
Total Current Liabilities	2,044.2	2,232.3	2,388.0	2,046.8
Net Current Assets	186.8	441.2	724.3	959.6
Others Assets	0.0	0.0	0.0	0.0
Application of Funds	1,068.0	1,360.1	1,640.0	1,868.4

Source: Company, ICICIdirect.com Research

Key ratios

(Year-end March)	FY10	FY11	FY12E	FY13E
Per share data (₹)				
EPS	11.9	32.0	32.9	30.9
Cash EPS	15.3	35.7	36.7	35.0
BV	88.2	108.4	131.9	151.1
DPS	5.0	9.0	8.0	10.0
Cash Per Share	51.0	55.2	55.3	62.7
Operating Ratios (%)				
EBITDA Margin	12.1	11.6	10.5	11.3
PBT / Total Operating income	8.7	11.9	10.9	11.3
PAT Margin	4.4	7.8	7.4	7.5
Inventory days	29.4	19.9	20.0	20.0
Debtor days	85.6	75.5	90.0	90.0
Creditor days	83.6	60.4	60.0	60.0
Return Ratios (%)				
RoE	13.5	29.6	24.9	20.4
RoCE	32.7	39.0	31.3	27.3
RoIC	38.1	49.8	35.4	30.2
Valuation Ratios (x)				
P/E	43.8	16.2	15.8	16.8
EV / EBITDA	14.5	9.9	10.1	9.9
EV / Net Sales	1.8	1.2	1.1	1.1
Market Cap / Sales	1.9	1.3	1.2	1.3
Price to Book Value	5.9	4.8	3.9	3.4
Solvency Ratios				
Debt/EBITDA	0.0	0.1	0.1	0.1
Debt / Equity	0.0	0.0	0.0	0.0
Current Ratio	1.1	1.2	1.3	1.5
Quick Ratio	0.8	0.9	1.0	1.1

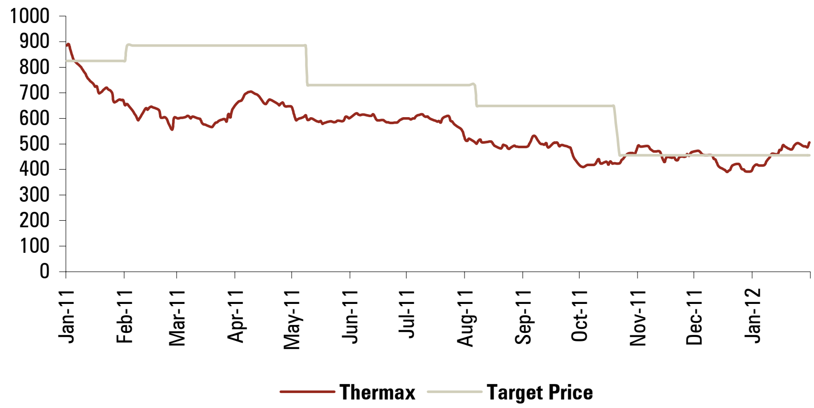
Source: Company, ICICIdirect.com Research

ICICIdirect.com Research coverage universe (Capital Goods)

Thermax					NP (₹ Cr)	EPS (₹)	PE (x)	P/BV (x)	RoCE (%)	RoE(%)
Idirect Code	THERMA	CMP	519	FY11	382	32.0	15.8	4.7	39.0	29.6
		Target	401	FY12E	418	32.9	15.4	3.8	31.3	24.9
Mcap (₹ Cr)	6176	Upside (%)	-22.7	FY13E	453	30.9	16.4	3.3	27.3	20.4
BGR Energy										
Idirect Code	BGRENE	CMP	241	FY11	314	43.6	5.5	1.7	24.7	36.2
		Target	296	FY12E	327	37.9	6.4	1.3	16.4	23.7
Mcap (₹ Cr)	1735	Upside (%)	22.8	FY13E	340	37.1	6.5	1.1	13.7	19.5
Hindustan Dorr										
Idirect Code	HINDOR	CMP	35	FY11	54	7.5	4.7	0.9	22.1	20.8
		Target	53	FY12E	21	2.9	11.9	0.8	11.1	6.7
Mcap (₹ Cr)	252	Upside (%)	51.4	FY13E	39	5.3	6.6	0.7	14.3	11.5
Sterlite Technologies										
Idirect Code	STEOPT	CMP	39	FY11	135	3.6	10.7	1.4	12.4	13.1
		Target	31	FY12E	47	1.2	32.8	1.4	6.8	4.4
Mcap (₹ Cr)	1385	Upside (%)	-20.5	FY13E	127	3.2	12.1	1.3	11.7	10.9
KEC International										
Idirect Code	KECIN	CMP	59	FY11	205	8.0	6.9	1.5	17.8	21.7
		Target	68	FY12E	179	7.9	7.5	1.3	16.1	18.3
Mcap (₹ Cr)	1487	Upside (%)	15.3	FY13E	218	8.5	6.9	1.1	18.0	16.9
Jyoti Structures										
Idirect Code	JYOSTR	CMP	48	FY11	110	12.7	3.8	0.7	23.4	17.4
		Target	60	FY12E	88	10.7	4.5	0.6	19.1	13.2
Mcap (₹ Cr)	384	Upside (%)	25.0	FY13E	99	12.0	4.0	0.5	19.4	13.1

Source: Company, ICICIdirect.com Research

Exhibit 9: Recommendation History



Source: Bloomberg, ICICIdirect.com Research

Exhibit 10: Recent Releases

Date	Event	CMP	Target Price	Rating
22-Jul-10	Q1FY11 Result Update	809	825	ADD
8-Oct-10	Q2FY11 Preview	804	825	ADD
28-Oct-10	Q2FY11 Result Update	855	884	ADD
10-Jan-11	Q3FY11 Preview	805	884	ADD
31-Jan-11	Q3FY11 Result Update	669	730	BUY
8-Apr-11	Q4FY11 Preview	696	730	BUY
5-May-11	Q4FY11 Result Update	600	648	HOLD
6-Jun-11	Q1FY12 Preview	619	648	HOLD
25-Jul-11	Q1FY12 Result Update	609	648	HOLD
5-Oct-11	Q2FY12 Preview	408	648	BUY
24-Oct-11	Q2FY12 Result Update	425	456	HOLD
6-Jan-12	Q3FY12 Preview	419	456	HOLD

Source: Company, ICICIdirect.com Research

RATING RATIONALE

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Strong Buy: >15%/20% for large caps / midcaps, respectively, with high conviction;
Buy: > 10%/ 15% for large caps / midcaps, respectively;
Hold: Up to +/-10%;
Sell: -10% or more;

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