“Thermax Limited Q3FY17 Results Conference Call”

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MODERATOR:	**MR. ANKUR SHARMA – MOTILAL OSWAL SECURITIES**

Moderator: Ladies and Gentlemen, Good Day, and Welcome to the Thermax Limited Q3 FY17 Earning Conference Call hosted by Motilal Oswal Securities. As a reminder, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Ankur Sharma from Motilal Oswal Securities. Thank you and over to you, sir.

Ankur Sharma: Good Morning, Ladies and Gentlemen, and Welcome to the Q3'17 Post Results Earnings Call of Thermax Limited. With us today from the management team, we have Mr. M. S. Unnikrishnan – M.D. & CEO and Mr. Amitabha Mukhopadhyay -- Executive VP and CFO. We shall begin with the opening remarks from Mr. Unnikrishnan and then open the floor for the Q&A Session. Over to you, sir.

M.S. Unnikrishnan: Thanks a lot, Ankur, and a warm welcome to all my dear friends from the fraternity who have been consistently supporting us and have been with us all the while. One more quarter where a mixed bag of results, some good numbers, some not so good numbers.

Starting off with the "Order Intake", this time I will restrict my opening remarks only about the group level numbers; 19% improvement in the order intake; 1,190 crore Vs 1,000 crore last year. The domestic order booking remain muted and almost at the same level and there is hardly any improvement compared to the previous year. But major improvement in the international order intake, by 74%, at Rs.526 crores, has really helped us.

Now, coming to the "Order Balance"; it is 4% lower than last year same time though possibly better than the previous quarter : 4,653 crore for the entire group. Sales numbers have been a major disappointment for you as well as for us; it has come down by 20% at the group level, coming down to 967 crore from 1,203 crore. Domestic sales has taken the brunt where it has come down from 750 crore to 646 crore, dropping by 14%. I cannot blame demonetization only for it though part of the blame will go there. It has impacted us in three different ways – First of all as a B2B organization, there are no cash dealings in the company, which should have directly impacted us; however, a part of supply chain which remains in small and medium scale Industrial segment, they had difficulties of processing.

So some component input into our manufacturing process had an impact which would have reduced the output from one of our product-oriented factories. Equally, at the construction sites of our company, specifically in the month of November and a good part of December, though we were able to make our payments through contractors for labor, we saw departure of labourers from several sites on account of the lack of available currency, reducing the overall project movement in some of them. Though we participated with e-Wallet support for even workmen, opening bank accounts for the workmen of our contractors, not at every site we are able to manage it, despite Amitabha 's best efforts. I am sure there had been some amount of deceleration of activity at the sites.

In any case, executable revenue recognizable orders were not available sufficiently to have a growth for the last quarter. However, the various initiatives taken by us related to cost reduction and material, cost reduction also in manufacturing processes and the manpower rationalization which I mentioned in the last quarter have had a positive impact in the improvement of profitability. EBITDA has improved from 7.8% to 10%, at the PBT level. It has gone up from 7.1% to 8.9% for the group level. I am not specifically giving you numbers about the standalone, I am sure which in case if there anyone of you would like to know, Amitabha will certainly help you out.

Now, a couple of other indicators: You may want to know what has happened to our joint venture with the Babcock & Wilcox. We have not been able to register any orders in the current quarter, though there are two orders available to Babcock & Wilcox which they may want to certainly pass it on to our joint venture. They have not been able to get the sufficient funding support for the API project because of which there is a delay. So we will have to wait and watch as to how the global market start supporting coal fired power plants. So there is a challenge in that JV. Maybe one quarter we should be okay. Current order should go along up to possibly the end of June.

Going forward, there are not orders to be executed under the joint venture. Our small joint venture with SPX Corporation where we had invested 49-51 by us, where our investment is just about Rs.10 crores in equity. That particular portion which is known as Balcke-Durr, Germany is sold off by the parent SPX to a publicly listed private equity in Europe and Germany. That JV is not very consequential for the entire Thermax. It had turned almost profitable last year. We would expect it to continue to make marginal profit or loss in the current year. Certainly going forward, our relationship with the new PE owner versus how we are going to take at the JV is something which we will announce at the right time. Give us quarter to maybe 7-months' time. It is a good business; we have been able to establish air cool condenser business in India which possibly we should be able to manage on our own also.

Our enquiry inflow had been better both in the domestic and international markets in the last quarter, but finalizations in medium and large projects have not really happened. Very happy to inform you that in the first Bharat VI implementation project for refineries we won the first order and there are five more tenders in the anvil which will go into quotation level in Q4 and some of them may spill to Q1 and Q2. We are hopeful that we should be one of the major players to receive orders in that area. There are no movements in the cement sector, though there are a couple of orders to be concluded for waste heat recovery based power plants. We are expecting investments in sugar to improve in the coming year. Even in Q4 also, we do expect some orders there and in the distillery area too.

That is about overall situation. I would leave it to all of you to ask questions. Thanks a lot once again.

Moderator: Thank you. Ladies and gentlemen, we will now begin with the Question-and-Answer Session. The first question is from the line of Aditya Bhartia from Investec. Please go ahead.

Aditya Bhartia: Sir, my first question is on gross margin expansion wherein we have seen a significant improvement over the last few quarters. Just want to understand that the fact that Reliance order has got completed, contributing to this expansion and whether the current gross margins appear to be sustainable to us?

M.S. Unnikrishnan: Aditya, the current gross margins have two factors there; one is related to the design improvement that you have done and cost reduction based on engineering innovation. That is 100% sustainable. A part of that maybe given up by us in the marketplace when competition becomes tougher. That is point #1. Second, there is the product mix change I mentioned earlier. When we have get a higher overhang of the large and mid-size projects, margins may suffer once in a while. So your conjecture is absolutely right, that currently there are no big projects under execution, though there are one or two of them in the current year -- RCF Thal project is under execution, there are a couple of captive power plants under execution where EPCs have a low margin. But our service income improvement and the product sales improvement have also certainly contributed to the margin improvement. To be precise, all the standard product businesses of the company have registered growth in the current quarter whereas the major drop had been in the project businesses. To give you an account of the main company standalone basis, in our larger Boiler business, our EPC business and their Pollution Control Project business, all the projects put together, there is a drop of approximately Rs.280 crore and the improvement in the businesses of the standard boilers, air pollution control, standard products, water treatment standard products and chemicals put together, would have contributed to a positive uptick of maybe Rs.70-80 crore. So that explains the net reduction of Rs.200 crore. So projects have come down, products have gone up which naturally will mean that products mix is in favor of better EBITDA.

Aditya Bhartia: Sir, even on the other expenses side, we have seen a sharp reduction on both standalone as well as consol entity. Is there any one-off or FOREX element that is involved here?

Amitabha Mukhopadhyay: No, I do not think anything has been contributed; this drop has not contributed by any one-time FOREX movement.

M.S. Unnikrishnan: I had been talking about the Water and Waste Solution business continuing to be in negative for almost three years. I need to say that after a gap of 14-quarters it turned profitable in the current quarter. Overall, we should be above breakeven in the current year also. That could be also be a swing contributor and going forward that is sustainable because after reshaping the business and moving out of the municipal corporation business altogether, both the industrial projects as well as the standard products turned positive in the current quarter. So that is also one of the contributors and that again is sustainable.

Aditya Bhartia: You mentioned that on Cement side, you are not seeing any major action. Is my understanding correct?

M.S. Unnikrishnan: There is one Greenfield project of Ultratech coming up for which there is no separate captive power as they already have surplus power available in that state. But there is a Waste Heat Recovery based power plant, small one, for which we already have received the order for the boiler. I think it would be registered in Q4, not in Q1 of next year. The second example of expansion is from Shree Cement in Karnataka which already is underway but there are no captive power orders there because they are going shift one of the existing captive power plants from the northern part of India. So these are the two. However, there are a few enquiries in the Waste Heat based power plants for cement industry. Enquiries are on, negotiations are on. Let me tell you it is a very tough competition because the maximum number of waste heat power plants in the world in cement industry is in China. So Chinese have also understood in India that there are possibilities, so they have started coming in and competing. But technically we are far better. Let us wait and watch. That is about the cement industry. Third, the cement industry has started at least collecting quotations for revised pollution control requirements. But all the orders are in small in size. One of the earliest cement plants which is going to get into de-NO_X has also come to us. Our portion is very small in that one. But there are 18 or 19 enquiries for de-NO_X systems. Some of them also for Flue Gas Desulphurization (FGD), already received by us. So that is another movement in the cement industry.

Aditya Bhartia: How big are these opportunity sir?

M.S. Unnikrishnan: Not big, de NO_x all of us expected that people may go for a conventional plan but honeycomb based complicated one. All of them are going for a technology known as SNCR, which would for a classical 1 mtpa cement plant… may go for Rs.2-3 crores, not the 20s and 30s that we expected it to be.

Moderator: Thank you. The next question is from the line of Sujit Jain from Yes Securities. Please go ahead.

Sujit Jain: Sir, just wanted to know the impact of the recent announcement of creating a mega oil company on the refinery expansion plans of oil companies or their Bharat VI upgrades, the opportunity that we had spoken about desulphurization orders of Rs.800 crores and refinery expansion to the tune of let us say Rs.700-800 crores per order?

M.S. Unnikrishnan: Bharat VI enquiries are already on and I think I mentioned that we received the first order also… we won the first tender in the last quarter and there are five more on the anvil at various stages of preparations, we are prequalified for all of them. Since we won the first, there is a price discovery in the market, I am sure, second onwards there will be undercutting. But going forward, all of them will get concluded in the next 12-15-months period and we are a strong contender for it and the size of the market which I mentioned to all of you in the last few quarters remain the same despite the price discovery. Next question was about the refinery expansion program itself. No enquiries released. Though we are aware of the fact that it is still resting with the ministry to go ahead with. There seems to be a pressure on the oil marketing companies, invest first in ethanol plant before they are getting into the refinery expansion which alone again can be fairly large in size. So that is what I understand. But I do not think we can continue to ignore expansion of refineries because post Cochin refinery expansion, nothing is done and if you look at the automobile company sales, whether it is passenger vehicles or whether it is maybe passenger cars put together, refining capacity is a major challenge. …and again only shares doing well in the market are two wheelers in the country. So put together, we need to have refined petroleum brought in a lot more. Cars too need a lot of plastics which will need petrochemicals, the downstream side. So I am very confident about the fact that oil & gas expansion is going to happen in the country. It is only a matter of time.

Sujit Jain: What is the size of this Bharat VI upgradation order that we won?

M.S. Unnikrishnan: It is between Rs.25-30 crore.

Sujit Jain: One last question about demonetization, it has impacted cement companies. You have spoken about the enquiries coming from them. In terms of timelines, is it going to affect the Waste Heat Recovery enquiries and eventually them coming up?

M.S. Unnikrishnan: It will shift by quarter-to-quarter. If you really look at the capacity utilizations certainly dipped in this industry. But in our own dialogue with the CEOs of the cement companies, they are not unduly bothered about that. In any case ,these are intended for depreciation benefit n the balance sheet, which in any case all of them are profitable…and they aren't getting into negatives barring one or two cement companies. I think they should go ahead with that. What is the reason for it? There is a renewable purchase obligation which is getting implemented for the major carbon dioxide emitters of the country. Other than power, steel and cement are identified by the government and Central Pollution Board as major CO_2 emitters and they have got RPO – renewable purchase obligation . So to offset the RPO obligation, they have the option of converting waste heat to energy, meaning reduction in carbon footprint. These kinds of projects normally would take maybe 24-months for it to be fully operational, though 18-20 months is the project time. Going forward, that's the driver . Currently, all the cement, steel industry are so cautious about signing a cheque for any investment, in fact, even if there is a repair of a plant needed, they would rather prefer to do a patching up rather than putting up that money. So let us be very cautious about it. They are waiting for the construction industry to pick up. I hope you have read the budget , there is a commitment of 133 Kms per day of total roads, so far we were hearing only about the NHAI program from the ministry. 133 Kms per day when you compare with 78 Kms per day, village roads, state highways and interstate highways put together…your cement consumption is going to be literally pushing up because what was used for village roads in the earlier past when the central funding was not available was asphalt and maybe tar. So when that also gets converted into cementation and concrete road, you will have a real uptick in cement consumption. I am quite hopeful that next year by the time the dissemination of the money happens, Rs.64,000 crores are also allocated we should see some of the money flowing into cement companies balance sheet. It is a matter of couple of quarters.

Moderator: Thank you. The next question is from the line of Ravi Swaminathan from Spark Capital. Please go ahead.

Ravi Swaminathan: Just wanted to know regarding exports from which geographies we are seeing kind of traction and if you can give us split between the order intake between exports and domestic it would be really helpful?

M.S. Unnikrishnan: Numbers Amitabha will give to you, but let me tell you the geographical split; it has been from virtually every part; however, we had project orders coming from Middle East in the oil sector and Southeast Asia for sugar as well as for food, food processing sector and rice milling which I list in the food sector. There are no major orders which have come from African continent in the quarter under consideration. Going forward also, I think there are possibilities of expansion programs happening in the Middle East markets.

Amitabha Mukhopadhyay: Consolidated orders intake for this quarter, exports Rs.526 crore, and domestic Rs.664 crore; corresponding quarter last year was Rs.303 crore and Rs.697 crore respectively.

Ravi Swaminathan: So we have seen a significant jump in terms of exports and can this trajectory continue, in the sense, are we looking at new markets, I believe we are setting up a facility in Indonesia, can it drive growth further, how are you looking at this?

Amitabha Mukhopadhyay: I will just give you the YTD number which may help you before Unni gives the answer; YTD exports is Rs.1527 crore consolidated compared to Rs.1102 crore same period last year, so it has gone up from Rs.1102 crore to Rs.1527 crore.

M.S. Unnikrishnan: Ravi, there are two components to the international numbers that you are talking about; one is locally procured for local supply and the second, procured for export out of India. Both will have different connotations. You asked a specific question related to Indonesia. The factory should be up and going by April-May, the factory construction is almost completed, machineries barring one or two critical machines should be there by end of February. So installation to be completed by end of March, early April, we should be up and going in the market as a local manufacturer, also, looking at the entire ASEAN countries to be fed by this facility, starting with the heating business of the company. Now, we have got almost 60 people on ground in the entire ASEAN market for marketing and servicing which 24 months back would have been 10-11 people. So we have also got local capabilities built in for proposal making for the Heating business and we have seen orders already coming into the balance sheet. Now, how the market is going behave? Currently, Indonesia was in a little depressed condition for maybe almost two or three quarters. We are seeing a lot more of positives prevailing in the market right now. So my expectation is FY'18 we should have a better traction in order intake and should help us. Our target is that Southeast Asian market all put together should contribute to $100 million in order intake for the company in FY'18. If the enquiries on hands were to be converted into order registration, whether to be made in Indonesia or made in India and send from here for projects, products and services put together, we should be able to hit that number, and that will be the first market wherein we will hit that triple digit number. So that is why the investment has happened. We hear only about the factory but without marketing, servicing, proposal making, project management, local supply chain, capacity building – areas where we have already invested. In fact, the balance sheet that you see currently is after investing all of that. That is going to help us. Second is in terms of medium size projects which we get from the entire Asian market, Middle East and Africa and once in a while in South America. I thought it is an improvement in the order enquiry platform right now. Captive power plants based on gas sector enquiries are better than the previous year and we are a major contender in that area along with the global biggies from America, Japan and maybe Europe but we have been able to compete against them and take some orders. All this will depend upon how the competition behaves in the international market. As an Indian company we have a brand deficiency but our experience and representation which are across the globe today is also giving us an equal footing and we are able to financially or maybe commercially compete against them. So that should help us. However, when we fight in the marketplace, sometimes we will have to really see because one thing about Thermax is we do not compromise margins beyond a level just to get an order. There had been occasions where we were almost very well placed in some order in the Southeast Asian market but all of a sudden somebody came and the prices came to such a level, we were given a counter offer by the customer : "Take at this price, I am getting it at this price from some other country." If it is not profitable, we will not take those orders. Domestic orders are breakeven, we will take because we know how to make a profit on to those orders. International orders we cannot do any refinement in engineering and reduction in anything by which you can convert a loss into a profit while executing. That is the answer, Ravi.

Ravi Swaminathan: In terms of domestic market, any movements in steel and aluminum sector that you are seeing?

M.S. Unnikrishnan: Aluminum sector prices firmed up, steel sector prices firmed up, so negative balance sheets of most of the Indian steel companies are now coming closer to breakeven and some of them have moved into profits. But the overhanging leverage of balance sheets are going to be the problem for at least a year to two years. The global uncertainty which is going to prevail in the market for at least one calendar year as to the change of American government…its implications are something that is going to restrain the investment in very large sectors like steel, power, aluminum. But for aluminum across the globe there is an improvement, let me say that. But the current capacities which are already there in the country which were put up by two major groups in the country, both Hindalco and Aditya Birla Group have not reached up to 100% capacity utilization…Thermax was involved in their projects and we commissioned air pollution control equipments, our treatment plants. So any aluminum investment in the country at least in my opinion are 24-months away. First, ferrous metallurgy has got to increase the capacity, then it happens for non-ferrous metallurgy. That is a normal practice in the world.

Ravi Swaminathan: In terms of the rising input cost, will it have any near-term impact in terms of margin especially for the short cycle orders that we have secured over the past two-three quarters?

M.S. Unnikrishnan: In my dip stick calculation, almost the carry forward orders of 85% for specialized steel, all that is covered. Hereon, 15% of my carry forward orders on the conventional steel, especially where we do only spot purchase for fabrication by us or by our suppliers is exposed to the commodity price increase. That may have 10 basis points on my EBITDA, may be that is already factored in by us. However, going forward, we already revised our prices. But I agree with you all what we could have received, which Amitabha would have been wanting to hold on to his balance sheet all that hard work he and his team has put into save cost, will have to compromise that in the market in the next year is the one which is going to be deciding, can we improve or retain the margin. I would presume that there is a market stability visible in the capital goods industry currently which is not the case may be a one year back or prior to that. There was such an uncertainty that maybe closure of medium scale companies are going to happen. All of them are sustaining. I have not come across any company closing down. Their profit expectations have come down because of which ferocity of competition though may remain, will not increase any further. So margin maintenance could be a possibility. Unless otherwise we have got bulky, chunky orders happening, then people will kill each other, for medium size orders, they would not kill each other, they will possibly try to take daggers on, but the orders can happen and we do get a premium in the market.

Ravi Swaminathan: My last question is on TBWE JV. What has been the execution that we have done in the first nine months and what has been the profitability of our share, the order book balance that is there and in terms of future visibility?

Amitabha Mukhopadhyay: As on date, the order backlog whichever there is Rs.242 crores, total revenue is Rs.216 crores and the net margin from this joint venture, our share is negative less than Rs.2 crores.

Ravi Swaminathan: Apart from that Babcock & Wilcox orders which could be potentially there, any domestic order that we are eyeing sir?

M.S. Unnikrishnan: Currently, there are no tenders in the offing in the country. I have to be honest, open with you, the government themselves have declared that the need for new thermal power plant based on call in the country up to 2022, is not very positive from the government itself. Now, each one of us can have our own opinion, conjecture about that, but that is open statement made by the government itself. So it may not happen that barring isolated projects, NTPC in any case is not coming with any more tenders for some time, they have to be executing many of them which are under different levels of execution, state governments a couple of them may happen. We have enquiries from international markets supporting B&W but there again there is a lull in execution of coal-based power plants across the globe, the banking system post COP 21 Paris has taken not official stand but silent stand that let us wait and watch to fund coal fired power plant. That is why I mentioned earlier that our joint venture partners have two orders on hand, one from African continent and other from maybe I think Latin America. Both of them have not started executing because the financial closures are still lingering. Unless otherwise those kinds of clarities happen, there are challenges that we are foreseeing in the future for the joint venture also.

Moderator: Thank you. The next question is from the line of Bhavin Vithlani from Axis Capital. Please go ahead.

Bhavin Vithlani: Unni, I have three questions; one is we have seen a tough last five or six years. If you could highlight the efforts or the building blocks that you have done over the last few years, that could take the company higher in terms of profitability irrespective of capital goods cycle turning up because no one knows whether cycle goes up? Two is if you could give some clarity on the Dangote order because that has also been lingering since long, so any update on that would be very useful? Third is if you could also talk about the chemicals and the chiller update, when do we see the facility and the kind of revenue forecast like you give for the Indonesian company?

M.S. Unnikrishnan: Starting on with the work done by us in the past few years related to how will they support the company to retain margins, and maybe sustain the company. I am very happy to say that why we are able to declare results like it is only on account of the products that we have come out in the last few years. The heating standard products business of the company has already introduced four different varieties in the last three years and some of them have now reached almost 30% market share, otherwise we would have slipped down in there. The newer designs of sleeker better performing but consuming less material which means costs are lower. We were not for example if one were to look at solid fuel fired boilers, whether it is biomass or coal, we started at maybe 2 tons and above and totally did not look at half a ton capacity boiler, 1 ton capacity, 1.5-tons and with the advent of industrialization catching on in the country, these were sold in thousands in the country by local manufacturers. But our cost was the constraint for us to enter this market. So we created a very sleek and good product and today we have already sold after introduction of this in just one year in triple digit numbers we already reached and we recognize even this market is willing to pay a little more provided we can give a classical Thermax automated boiler. The newer version of automated boiler is in such small range are going to be introduced by the company in the next year, by which I will take a substantial market share in that area. Now, this may be insignificant for Rs.5,000 crores Thermax balance sheet when you talk about Rs.50 or 60 or 70 or 100 crores kind of market to be pictured. But in that if I am able to make Rs.10 crores out of that, so that such is the kind, like similarly say in we were the people who introduced Thermax Fluid Heating into the country 43-44-years back. 44-years we continued with the particular type of a design in different variants. We have introduced for the first time altogether different conceptual design into the product, it is in the market right now. So that is an area where our market share was going down in the smaller area because we could compete with the smaller people. So that we are picking on. I gave example of this earlier. Water Treatment which Amitabha is personally looking into, the standard products of the company today are world-class. So we started exporting it out of India. We started getting orders from Middle East, Southeast Asia which was purely domestic. We saw the development which were done should help us to strengthen our position in the products businesses because these projects may not happen. So we are going to be focusing on that. This we were earlier selling in India. We have expanded into the rest of the markets. I mentioned to you in some of the concalls earlier that entire size of Southeast Asian markets were standard products of the company, all the countries put together is as big as India. So what we created in India is the first 50-years as a standard product business which will be in excess of maybe Rs.1,000 plus crores what is waiting for us, where we currently have maybe 4% or 5% market share. So I have opportunity to take it to double digit percentage. So that is one part. Even in the project side of the business, we created gasifiers because COP21 Clean Energy, all this put together is going to be putting a lot of pressure on the larger manufacturers of India from using coal as is where is condition. Now, clean coal technology gasification. Now gasification existed in India in a smaller way but a major company getting into gasifications are max. Now, my product is already in the market. I should be able to conclude the first contract in the current year and I am looking forward to that helping me in the next few years to be opening up a new market. Then in the EPC business of the company, we were focusing purely on power and captive power. Now, we have started solar hybridization. We were lucky to get the first order competing against many country people and NTPC and all the existing power plants have planned for hybridized solar thermal, all of them. Why hybrid will work? That is the point which I am going to mention to you. Current government and the future governments going to happen in India will have to take care of the renewable purchase obligation as a signatory for the COP 21 Paris agreement. Irrespective of what the American President may say, this is something which has to be done by India. That is going to be making hybridization to solar, an easy route for existing power plant for the obligation to be met. So I would imagine a good market opening is going to happen and I am the first to pick the order in the country, first mover advantage. Now that we are currently working on indigenizing many of the things which are going to be important for the first order which should bring the cost down and improve the feasibility for it. That is another thing which we are starting in the EPC business. Next item in the EPC area is we were possibly wedded to only power. My competency for us in EPC is engineering, procurement and construction and the sector which are investing in the country currently are food and food processing. I do not have technology to make a food processing equipment, but I can have technology purchase done or alliances with people. So capacity utilization of engineering in this area where investment is going to happen is the next area that we are gearing up for. I may have some other news to tell you maybe in the next few quarters about major entry that we are going to make into a non-power area in the EPC also, which should help us. Every business of ours is currently entering into areas that we have not done earlier or newer solutions which should sustain irrespective of I do not want to also continue telling, no cement investment, no steel investment, we also want to grow which I should see happening from next year second half onwards in terms of order intake in newer areas.

Bhavin Vithlani: Just a follow up on this; because I recollect the meeting you and the top management in 2014 where you talked about hybrid boiler and the constraint at that point of time was high price of solar panel. I believe that constraint is no longer there with the price of solar panel. So is that business picking up, what is the status on this?

M.S. Unnikrishnan: Those were not the PV panel, those are parabolic truss which had to be hybridized. That business I cannot say picking up, it is already doing quite okay. I today have at least maybe 25 installations running in the country. There are at least equal number of enquiries on the anvil. A couple of industries are already caught on to that. Dairy as an industry is almost standardizing on solar as hybrid along with that. There are textiles industry currently doing it. Hotels having roof, some of them are moving into that. So that is picking up. What happened is PV was so overwhelming. The way the prices crash in PV which is $4 million MW which prevailed in 2007-08 or'09 has today come down to maybe 600,000-700,000 for the panel I am talking about. Because of which thermal took a beating. All the white now poor chap has started reversing, in fact, India is yet to be catching up. I am told there are four power plants on solar thermal coming up in the Middle East and it is catching on including solar cooling also. India may take some time to accept it but it is going to happen in India also.

Bhavin Vithlani: So the baby boilers that you are looking to hybridize is something which is growing now?

M.S. Unnikrishnan: Yes, it is already moving in the market. Regarding Dangote, it is not an order with me. So whatever I say is speculative, let us say that, Thermax is we are working an order becomes an order only when I have the advance available, it is not an order. So I want to clarify. It is something which there is an opportunity, let me say. There the financial closure is not completed; however, there are many contractors or suppliers who have already signed the contract and collected advances for this particular project and land reclamation is completed and in the public domain itself it is available that project is going to be on take-off stage in the coming year. Then you asked me about the chemical and chiller factory. Chemical factory is on the verge of machinery installation. Construction almost completed. I would presume that we postpone the commissioning on the plant by one quarter. There were some reasons for it because we wanted to automate one part of the end portion of the packaging area. So that has taken maybe three to four months time from us. That is okay for us. So the plant should be commissioned in my understanding by June-July of the coming year. I will personally be visiting there this weekend to see I will reconfirm that it is going to happen, it should happen by that time. So commercial production from that unit will start in FY'18.

Bhavin Vithlani: What is the peak revenue that you are looking at like you said $100 million in Indonesia in FY'18, how do we see in chemical?

M.S. Unnikrishnan: Indonesia, the factory was not going to be giving $100 million. Southeast Asia is going to give to Thermax $100 million. No doubt should be there. There will be some projects also, all put together. Now this factory the first level machinery which is getting installed over there is going to be 12,000 meters cube capacity per annum and 8,000 will be created with the very minimal line balancing and some shifting is going to happen from existing factory in Maharashtra, taking it to 20,000. The master plan for the factory is to double into 40,000 as we are able to selling more. Now, the current year I would be doing with an existing capacity of 10,000 meters cube, Rs.165 crores of business in the resin manufacturing. When it becomes 4x, it naturally will become Rs.650 crores or Rs.700 crores but our design capacity is Rs.850 crores because prices also do go up as and when we reach there. So the challenge for the company have to be shifting it is our ability to be selling in the international markets. So we had already started a lot more of activity related to that. Because we are not selling commodity resins, we are going to be manufacturing predominantly Specialty Resin from this factory and that is where the margins are better. We do have competition from DuPont, we have competition from Lanxess and Mitsubishi Chemicals are the other main competitors, Plethora Chinese come in with their in the commodity range. So here what one needs is we will have to be entering into the process of accustom, for example, say, MGC glycol process we have created new products which is not in existence MGC and it started selling in Saudi Arabia to the refinery. Now we are approaching every refinery which is doing an MGC manufacturing which will reduce their costs. So these are the kind of newer application which we need to create. So we have got a team of people working. We started selling in Europe. Just an entry within maybe year and a half we started, currently our sales have already caught on to maybe $4-5 million in the coming year. America is already selling $12 million, Japan is selling. So it is possible for us to write some once we have the capacity. Our constraint was we did not have the capacity earlier. So that is a ultimate size that I am talking about. You can ask me a question when do you reach if not 800 at least 750 the name plate capacity. I would presume for us to be reaching there 5-6-year period minimum and it depends a lot on our ability to be taking away the orders from some of the big names which I mentioned about. Coming now to chiller factory, it has taken a longer period of time to be getting permission to start the construction. Unfortunately, though we only have a paint booth for painting the chiller, some rule which is enacted by the UPA-2 government made anybody having a paint booth treated as a chemical factory which needed government permission from Delhi. I am very honest to know that. You know what Thermax governance practices around this. So I am very happy to inform you that we got all the permissions from the central and state government, construction contract is on the verge of being awarded. Initially, we were planning 18-month period for construction but I am not giving that time period for our people. We should be completing a plant maximum within 15-months period from the time when we will do the foundation stone, which should happen by April in the current year. So that is about the chiller factory.

Moderator: Thank you. The next question is from the line of Abhishek Puri from Deutsche Bank. Please go ahead.

Abhishek Puri: Firstly, just on the outlook for the next year, you have received good number of orders in the last two quarters, there is more than a double-digit growth and we are looking at new factories to start up; however, on the TBW side, you said that the orders will finish by June. So can we expect a strong double digit growth coming back from next year and what is the order cycle that we have received for the orders, I am assuming these are short cycle orders?

M.S. Unnikrishnan: From the orders that I am carrying forward, maybe 10% of that will spill over to the year after that and the pace of execution of some projects may not be as fast that we expect but it will be better than the current year. We have been predicting earlier double digit but there is an uncertainty in the global market, in the domestic market as you see the order booking that we have had improvement is from the international market. There is an uncertainty prevailing in the last maybe a month-month and a half. So order finalization delays do happen. That is only doubt. Otherwise it will be a better year next year. I would rather wait for the Q4 to be over before I am commenting on how the next year is going to be panning out because what will make a difference for Thermax in terms of balance sheet improvement on top line is the project orders, it is not the product orders. As I told you in the opening statement itself, projects came down by 280 in a one quarter, products could lift only 80 bags. So that is where the offsetting. If I get offsetting project orders which we had luckily in the last quarter, current quarter I am expecting one or two to be getting finalized. Those are solid numbers which will lift me up in a double digit as we expect. To be precise, if I were to get say maybe two or three EPC orders in triple digit size and maybe between Rs.50-100 crores size for the larger heaters of boilers, then I would have straightaway told you, yes, I am guaranteeing you 10% growth. I do not have as many though enquiries are there. So let the order finalization or at least conclusion happen, then I would be very confident in committing that to you.

Abhishek Puri: Secondly, more on the longer-term structure, you have been able to offset the operating leverage impact by increasing your gross margins from almost 35% to 55% in this quarter though I understand we should not look at it on quarterly basis but there has been structural shift which has happened. Is it only because of the base orders or the core products and products are running 50% gross margin for you or it is that the services income is such big proportion of your overall income and if you can quantify that?

M.S. Unnikrishnan: Services income has increased and its contribution to the price also increased. So that has got a major support for the company, for example, my income from outside the country for pure services would hit almost $10 million next year which is operation and maintenance business which we started off in India and now moved outside. Now, we are an insignificant player in the international market for operation and maintenance and pure services. As we become a significant player, then there will be competition and having strategy to defeat them. So how do I overcome the barrier? Today, barrier is me. Tomorrow my barrier is going to be my competition. So if I am able to retain my margins and then take orders as per my growth plan, then certainly it is absolutely sustainable. You will grow, you will retain profits also. But sometimes it can happen that I pick some big chunky order just because I did not want to lose that order which may give me very single digit margin in the lower range like EPC, you may find one or two quarters but it never coming down. But on principle, let me tell you, the way we are moving is we are going to have a significant boost given to product side of a business and service side of a business. So that should continuously help us to be retaining the kind of margins that we are used to and we want to be retaining. Another thing is earlier we were retaining manpower also in anticipation of orders. I did mention last quarter that though it is not for us to take at some unhappy decisions related to manpower optimization. So we will be very careful going forward. Why did we retain manpower for maybe four or five years? The reason is that none of us expected India to come down to low investment for the larger projects. All of us thought that there will be a cycle maybe a gap of one or two years, but it is almost five years since major steel plants were announced in the country…major I am talking about after Kalinganagar of Tera Steel, which was announced in 2009, they awarded the orders maybe 2011-12, there was not a single steel plant which has happened in the country of that particular sort. That is not the way the country of this sort should be implementing projects. There is not a single new aluminum expansion. Copper, no expansion happening. Now, please remember cyclical investment pattern which is followed by the global commodity industries were gotten to India, you continue to be investing irrespective of the cycle. That is the way the principles are for that one. But if India has not invested at all for this, we are going to suffer, commodity prices have started strengthening if you look at last one year, there is not a single metal commodity where the prices have gone up by 25-30%, some of them have gone all the way to 80-85%. So, if somebody would invest is going to be minting money I am assuming. So those are the kind of vagaries which I am unable to answer right now. If that will catch up, then we go back to the kind of growth pattern that you see not only Thermax, many companies like Thermax in the last maybe one decade. That is it.

Abhishek Puri: You are saying that for big revenue jump, you need big size EPC and projects business to start kicking in. Having said that, if you get those projects, the gross margin there would definitely be lower, right?

M.S. Unnikrishnan: Then you will have to think about an ROC consent, not ROA consent. When you are working on manufacturing orientation, you go for something different because in any case I am going to put one more factory even imagine that if I take Rs.100 crores order at 6% margin versus what I am able to give 10% EBITDA today. I am going to put one more factory to it. So on the existing assets, I have a higher productivity. So currently, it is a season of ensuring that your asset productivity is not your intention, your return on sales is more important. We are as a company never looked at top line growth as absolute must. The way many of you look at balance sheet is not the way some of us do look at. For us today if asset is prevailing can I utilize without having any major thing done to my factory? My manpower is idling. In any case it is the fixed expense for me. Variable expense if I add on only for that, if I am able to get 6% on the same assets without Amitabha keeping the money with him rather than putting on a mission, if I am able to get a little more of money why would not I do that? Of course, there are challenges related to the risk in project. That is where. The risk profile is what looks at it. In terms of technological risk, commercial risk and payment risk, I would not do Rs. 100 crores job and maybe Rs.25 crores out of that is retained with the customer, then all my calculation making Rs.6 crores profit of that, I will become (-19). So we look at plus Rs.6 crores if it is confirmed we get in, then I would not bother for the profitability at all. That time I may compromise my gross margin on the company level but I would not compromise on a product profitability level. That is the way we are going to look at it. You go back to the time when I made Rs.6000 crores turnover and Rs.600 crores profit. It is on equity base as far as investment is con. On Rs.23.5 crores equity base, if I am able to give Rs.600 crores profit, currently in the year if I am giving you the X crores of rupees. If I give Re.1 more than that, it is beneficial for the investors. If I were to borrow money from the bank to do that, then you should catch me by my neck, and say, what are you doing equivalent. I am assuming. That is the way.

Abhishek Puri: The other expenses of about Rs.1400-1450 crores, is there any variable component in that?

M.S. Unnikrishnan: Amitabha tells me that there is nothing which is of any substantial denting nature in the current quarter and on the YTD level also.

Moderator: Thank you. The next question is from the line of Renu Baid from IIFL. Please go ahead.

Renu Baid: Sir, just wanted to first understand on a factor that we have seen some impact on sales coming in this quarter on account of demon. Do you think things are broadly stabilized and 4Q should now be back to normal and probably we should look at similar kind of probably much better improvement in execution now or you perceive any incremental headwinds on the way?

M.S. Unnikrishnan: Demonetization related sentiments are turning around, not turned around totally. My expectation is impact of that will be reduced in Q4 and it will be tapered down to almost a nil level by end of June. But there is one more caveat to this; of the Rs.15-odd crores currency withdrawn from the market, they remonetized up to maybe Rs.11 plus crores by this time, they are stuck at Rs.7.5 crores for reasons known to them very clearly. So it is going to be less lubricated economy going to be prevailing, so people getting used to that. That is the only issue which I may think about. One more point which nobody discuss or maybe I also forgot to inform all of you is that 1st of July we are going to have GST kicking in and I have never come across any society or a country sovereign when they introduced GST as a concept, inflation has not happened. So there will be inflationary pressures unless my economics is wrong. Second is you will also have challenges to overall sectors whenever they do it. The longest it has taken to stabilize the GST maybe in the olden days could be maybe 4-5-yaers. In the latest that one hears about the modern societies are equivalent of maybe a couple of quarters minimum. So how India is going to be behaving? It is a prediction that all of us will have to wait and watch. So that will have an impact next year. So we are prepared for it. I am sure Amitabha has spent a lot of money for GST implementation.

Renu Baid: That is for the GST but rather would be more of a quarter-to-quarter impact for the entire financial year probably first half is impacted, second half will surely catch up if we do not see any structural headwinds there, right?

M.S. Unnikrishnan: Demonetization related structural headwinds, I am not anticipating to get Thermax in anyway other than Q4 in a minor way. Next year I am not even factoring that in my budget. GST, I have not factored in anything but how will India manage it is what I am considering. It is like getting readjusted to a totally different mechanism which is not perfect or so. The way all of you put together financial community perceived it to be happening is not there was the government is doing it. Because of which randomness is a necessity. So that is the only thing which all of us is going to be factoring in. But these are patterns we are used to all. All of us are used to so much of difficulties in running business. One more difficult added. We will have to manage it.

Renu Baid: Will it be possible to marginally quantify the hit on account of demonetization in the last quarter the sales slippages which have happened on EPC side or project side?

M.S. Unnikrishnan: All put together, 5-7% is what I put across because some of my people also will take average under that for manufacturing, they will also come and tell me, I did not get the component and they will say it is because of demon. That is why it was a range of 5-7% could have been the possibility.

Renu Baid: Amitabha, if you could help us with the order inflow and order book breakup for group and standalone split between energy and environment?

Amitabha Mukhopadhyay: Standalone order inflow for energy is Rs.812 crores, Environment is Rs.201 crores, total Rs.1013 crores for the quarter. Group Energy Rs.979 crores, Enviro Rs.211 crores, total Rs.1190 crores. Order balance for Energy Rs.3392 crores, Enviro Rs.583 crores, total Rs.3975 crores standalone. Coming to Group, Rs.4053 crores for Energy, Rs.600 crores for Enviro and total Rs.4653 crores.

Moderator: Thank you. The next question is from the line of Charandeep Singh from B&K Securities. Please go ahead.

Charandeep Singh: Sir, we have been preparing ourselves in this challenging times by taking lot of initiatives forward. Do we see these initiatives fructifying in a big way from FY'19 onwards and then sustaining a good amount of growth momentum for our company for maybe a couple of years. Which of these initiatives do you think can become really large enough to be meaningful for the growth?

M.S. Unnikrishnan: Significant to the company would be the internationalization that we are doing. It should because if you look at it, at the turn of the century, we were maybe just about early teens in terms of our international business. We have taken it to 20% by 2010 and now we are talking about maybe 30% plus percentage, so the next stop for us is 40%. So that is the activities related to both. Earlier, we were doing products alone but the projects also we started. So that should help us. So if you really ask me the most important lever going to help us, stabilize and continue to grow is internationalization. In that we have not used the inorganic beyond a level. With the balance street strength available of the organization, we can do better. So we are a little more conservative than a conventional company because of which I would say that lever will also be utilized in the internationalization more than what we have done in the last decade. That is the point #1. Second area is technology being used for reducing the cost and giving better products. What I did not mention about is that we are working lot on the IoT orientation for our products. Our chillers have now become smart chillers. Their remote performance is monitored. There are 70 of them across the globe which monitoring is done from India and that is adding on to surreal business. Now 200 more of them are in the anvil. For all chillers that Thermax is going to be selling from FY'18 are going to be smart chillers. On the boiler side, we have already started creating the artificial intelligence and big data analysis oriented algorithms for it. So boilers are going to be smart. So these are the kind of things that technology orientation where what is the value at that I am going to give in a stream generation. So that should help us. I have only given one or two but it is going to be across the company, modernizing and possibly making as good as an American or an European manufacturer, the way we are taking it up. That is the second lever that should be helping us. Third one in my understanding is that peripheral area that we are going to move into which are not purely the boiler business, the heater business or chiller business, beyond that, for example, in chilling we were earlier doing only absorption chillers. We started making dry coolers. Technology oriented new products entry is not like a consumer product. It does take time for you to be creating a brand and experience for the customers. You need a reference creation to be done for each sector. So today it has already reached a double digit crores of rupees business and you heard about when I spoke about SPX we will already have air cool condensers available. So cooling per se will move away or move far ahead of absorption cooling which is traditional business for the company since 1989 till maybe two years back. So that should be having a major impact coming in, so peripheral. Chemicals business for the company was restricted to only resin. I do not talk about that we are already into construction chemicals business which will be clocking maybe Rs.15 crores turnover in the current year, it will turn profitably a year after that. We are not making any splash about it. Certainly, we have just got land in Perundurai in Tamil Nadu for a blending unit, Jaipur in Rajasthan for a blending unit, third, I am intending to be getting to Odisha for the eastern part. I am expecting that should become a triple size of a business at least in the next five years period of time. So stabilizing such business would take an investment in time and also market penetration. So these are the peripherals which were not there available to Thermax when we were entering into. So these are the three pillars in my opinion that will make the new Thermax where I can talk about we have become maybe five-digit crores business also, not too far away, our target is that we should be able to reach that by at least maybe 2020.

Charandeep Singh: Ultimately, our dependence on coal-based business is going to go down significantly and air pollution control is also a very big opportunity which we are seeing with more and more raw material conscious is happening. So what is the view on that side and is there a scalability which can happen in that area?

M.S. Unnikrishnan: Water scalability will be limited for Thermax having withdrawn from the government business because with the new legislation which is passed in the parliament, nationalizing on the water resources, water business is going to be strangle hold of state government and central government, both normal water and also you are talking about waste water of the kind. So we will restrain from being there. So we are already chopping one part of the major markets availability. However, industrialization as it picks up we will have the benefit. But the standard products which is getting into consumer and other segment, will help us certainly to grow the water business. More importantly, we are a technology player even in water. Our withdrawal from municipal business has helped us to be further creating better technologies which we are working currently on. Some of which are getting treasured, for example, a sequential batch reacted in which was not there for the company earlier, so we created, we have already done two projects and dairy oriented zero liquid discharge something which we already started, gas generation from the affluent, all that. Those new areas of entry once is stabilized in India, we are now moving out of India. Again, Southeast Asian market is another where we are focusing and concentrating on with industrialization happening substantially over there, we have got references available. So water has got an opportunity but limited in the industrial and standard products. Then air pollution control, once power does not grow in thermal area, you will have a restriction again, whereas the cement, steel, which again are not going to grow beyond a level in India, there is an opportunity. My understanding is that we need to be moving out even for air pollution control outside India. We started that movement in the last one year. Of the orders that we registered in air pollution control in the last quarter we have got at least in 20% of that coming from Southeast Asia, Thailand has given me maybe multiple number of orders, we are currently negotiating orders in Indonesia. So it is possible for us to do air pollution business outside India which we did not do earlier. So these two offer opportunity, limited in India, unlimited outside India, let me say that.

Charandeep Singh: In terms of the number of employees which we have, how do we see with all these new initiatives and new capacity being set up, what is our outlook for that?

M.S. Unnikrishnan: Redeployment is the first one and some amount of manpower addition is needed which will be of specialized nature. Whatever we are moving into our peripherals are competitive, that is the way we do. It is possible for an engineer who worked in for example say an EPC or power to do an EPC for tomorrow ethanol or maybe say food processing plants, it is possible for us to do. But you may need an expertise purchase. That we will do certainly.

Moderator: Thank you. That was the last question. I now hand the floor over to the management for their closing comments.

M.S. Unnikrishnan: Thanks a lot for being with us in tough times and more importantly whenever I dialogue with you, I told you I clarify my thinking and I am able to articulate it because you ask me the right questions and you are asking in a very tough time also the questions which are related to the future rather than getting into what happened in a quarter. That is the kind of support I am looking forward to. We have to certainly grow which is very clear in our minds that capital goods industry may undergo difficulty for some more time and that is no excuse for us to be not growing so. We are working towards that and let us continue, be in this association to support each other. Thanks a lot once again.

Moderator: Thank you. Ladies and gentlemen, on behalf of Motilal Oswal Securities, that concludes this conference. Thank you for joining. You may now disconnect your lines.