“Thermax Limited Q3 FY2018 Results Conference Call”

February 07, 2018

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Moderator: Good morning ladies and gentlemen, welcome to the Thermax Q3 FY2018 Results 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 the operator by pressing "*" then "0" on your touchtone phone. 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: Thanks Lizaan. Good morning ladies and gentlemen and welcome to the Q3 2018 post results earnings call of Thermax Limited. With us today from the management, we have Mr. M.S. Unnikrishnan, Managing Director and CEO and Mr. Amitabha Mukhopadhyay, Executive VP and CFO. As always we shall being with the opening remarks from Mr. Unnikrishnan and then open the floor to Q&A. Over to you Sir!

M.S. Unnikrishnan: Thank you Ankur. A warm welcome and good morning to all my friends from the analyst community and our well-wishers for actively supporting us all the while and let me start on with Q3 performance.

The numbers from the last two quarters had been discussed only at the group level; details later. I am sure Mr. Amitabha Mukhopadhyay and his team will also help you out. Starting with order intake, it had been a good enough quarter. I would not say an excellent quarter, but good enough quarter where our group level order intake has improved by 20% from Rs. 1183 crore last year to Rs. 1413 crore and nine-month order intake is 46% above the last year's first nine months all the way up to Rs. 4782 crore, even exceeding the full year's order intake. This has helped us to increase our order carry forward at the end of third quarter by 27% to Rs. 5556 crore versus last year's Rs. 4375 crore – at least ensuring that we will have good year next year apart from the possibility of a better fourth quarter.

Revenues on expected lines from our side has improved by 14 percent at the group level moving from Rs. 998 crore to Rs. 1141 crore and at the nine month level, after three quarters, we are 1% lower at Rs. 3114 crore against Rs. 3155 crore. So this current quarter, after substantial number of quarters, we have been able to reverse a negative trend and declare a positive number. But certainly there are some concerns related to the margins and profitability. I am sure you would have already read the numbers. At the EBITDA level at the group we are at 103.9 versus last year's 97.9 a growth of 6%. At the PBT level it is 96 versus 91. At the net level we are 9.3% more than the previous year, going up from 54 to 59.

There are three specific factors, which I would like to bring to your attention for Q3 profitability coming down. Two of the subsidiaries of the company, the Danstoker Group and Thermax China have reported negative numbers. From these, Danstoker is a quarterly number, it will certainly be back to positive in the next quarter and the year-end too is going to be positive; however, Chinese subsidiary continues to be under pressure and we also had to make some provisions related to litigation in the local market. That is why the Chinese subsidiary has reported a larger loss and it has impacted profitability.

Second, even in the domestic business, some orders got executed in one or two of our divisions, which had very low margin. It was to ensure that the projects were completed on time instead of having again to renegotiate with customers – in some of the divisions the steel price increase over the last year where the projects got delayed in execution had an impact. We are still in discussion with the customers to ensure that, going forward, at least a part of that can be recovered.

Now, looking at the order carryforward at this juncture it is an indication that we should be able to improve the margins from the next quarter. Of course, there are so many ifs and buts when you run a project business, but our experience says that we should be able to improve it further next quarter. So, that is about the overall results, to give you an indication.

An update on Babcock & Wilcox joint venture of ours. No business was transected barring some very small supply issues continuing on the existing orders. Same with our joint venture with SPX Corporation also since SPX sold off their business for ACC and dry cooling to Paharpur. Our agreement will be expiring any moment and we will continue with the business of air cool condensers because we already absorbed the technology and started designing it and there is capability existing in the company. This is the update on both the JVs.

Update on Dahej factory: I am very happy to say that it has gone online and in the last quarter we have been able to commercially produce without any flaw good quality, world class resins from the plant. We have reached up to 400 meter cube per month and we expect, by June we should be able to reach the rated capacity for the plant for the first year – 1000-meter cube per month.

The Indonesian subsidiary manufacturing started. Orders have started coming in though I am not very happy about the order intake for the last quarter. But no order losses are reported, so we should be seeing a better order intake for Q4 and Q1 of the next year for the Indonesian subsidiary.

Now update on our Sri City manufacturing plant for absorption cooling. As promised, June quarter we should be able to start manufacturing from there and would stabilise thereafter in the second quarter and by H2 we should have regular production starting from the Sri City factory for absorption coolers.

That is all overall about the organization. With good quantum of order carry forward now the focus will also shift on to ensure that we are able to execute, to make use of the capability that we have built over the decades. So, that is by way of an overview from me. I will leave it to you to ask whatever queries and doubts you have and the explanations on the results. Thank you.

Moderator: Thank you. Ladies and gentlemen we will now begin with the question and answer session. We will take the first question from the line of Sujit Jain from HDFC Securities. Please go ahead.

Sujit Jain: Good morning gentlemen. The 18% rise in energy revenues in this quarter Y-o-Y versus nine-month fall of 2% in energy revenues. So this rise 18% came on what account and is this sustainable?

M.S. Unnikrishnan: Yes, it is sustainable. It is not in just one business of ours. It is embedded in heating, in cooling, boilers and heaters and the captive power businesses (that is the EPC one). All of them had a positive number. Carry forward orders except for the cooling business is also on a positive side. In the visible period, there is sustainability for this number. Percentage can vary here and there, but otherwise there is visibility.

Sujit Jain: You spoke about why the margins came lower this quarter, the EBITDA margins, but if I look at last quarter also the material cost were to the tune of 52%, 53% - as much as they are in the current quarter. So what kind of new normal margins one can eventually expect moving from the 18.5% that we have bagged during this quarter?

M.S. Unnikrishnan: Almost similar kind of situation prevailed last year when we spoke in the third quarter concall. Told you that we will try to improve and go closer to the double-digit. The current target is almost similar to that, but there are many things to be seen. As we are executing, one month is already over, and two very crucial months of February and March before us. Normally for us it is very important as to how you are able to ensure that we are executing the profitable orders on time. So that is where the numbers will go up. In any case, it will not worsen, do not worry; but it will only improve. It will improve.

Sujit Jain: So just to add to this question is the Dangote order in Q1 the $43 million captive cement power plant order in UAE and the domestic chemical plant order – are these fixed price contracts?

M.S. Unnikrishnan: Yes all of them are fixed price contracts. See unless you take a Steel Authority of India order, maybe some oil companies, there is no price variation today in this market and it had been the same; however, whenever a major increase in any raw material price happens we always have a dialogue with the customer. But PSUs are incapable of helping us whereas a private customer sometimes agree for some amount of sharing in the increase in the cost. You should recognize the fact that steel prices have gone up almost by a 38% to 40% in the last one-year and the ability of a company to pass on the cost increase to the clients in a biased market is not so good. The same thing would happen in a seller's market when all of us are plum with orders and our order book is full then we can always say sorry we cannot take it. So that is the current situation. It has not improved. Thermax has improved the order intake but I may not be able to say the same thing about my smaller competitors who are still struggling in the market. So it will take a little longer time and a better turnaround of the market.

Sujit Jain: One last question is on nine-month order inflow standalone. What is the breakup between energy and environment?

M.S. Unnikrishnan: Amitabha would you want to help him out?

A. Mukhopadhyay: The order booking on Energy is Rs.965 Crores, Enviro Rs.252 Crores, and Chemical Rs.80 Crores total Rs.1297 Crores. These are the standalone order intake. At the consolidated level, Rs.1080 Crores Energy, Rs.252 Crores Enviro, Rs.81 Crores Chemical and total Rs.1413 Crores, so these are the quarterly order intake.

Sujit Jain: For the nine months?

A. Mukhopadhyay: For nine months on a standalone basis Energy Rs.3418 Crores, Enviro Rs.568 Crores, Chemicals Rs.238 Crores and total Rs.4224 Crores. At a consolidated level

Energy Rs.3959 Crores, Enviro Rs.568 Crores, and chemicals Rs.255 Crores and total Rs.4782 Crores.

Sujit Jain: Thanks. I will come back in the queue.

Moderator: Thank you. The next question is from the line of Harish Biyani from SBI Mutual Fund. Please go ahead.

Harish Biyani: Good morning. Sir again on the margins, rupee has appreciated in the past couple of months in fact a year or so now and if you look at the commodity price they have been inching up and all the contracts that you have been getting over the past couple of years those are all competitively fought with much correction, so despite that whatever performance has come in the energy segment is commendable clearly, but incrementally despite all these pressures we still kind of believe that margins are inching upwards to double-digits in the next couple of years. Is that a fair understanding?

M.S. Unnikrishnan: There are two or three assumptions that we have in our mind. Number one and foremost is our ability to continue to operate with the cost tightness – which we have been able to manage. Any laxity in that certainly will be pointing towards reduction in margins, which we will not allow, point number one. Second, we are not expecting the rupee to strengthen any further. It is a debatable issue I am sure.

Even today the forwards are available at 66, which means the global markets are indicating that with the American economy going to strengthen and Indian economy not going to strengthen as much, and with inflation not in the twos and threes and fours, you may not find any further strengthening, so going forward our anticipation is that that rupee will loosen a little more. Now will it be 65 or 66 or 68 is anybody's guess, but in my opinion, it cannot be coming down to the version some of you do talk about coming down to 60, so that is an assumption, which I have in my mind. Beyond that I am not expecting commodity prices to strengthen. The minimum import price was something advocated by all of us to make sure that the steel industry in India survives and flourishes, but not enter the level of profiteering. So, certainly they have almost come to a level where I can today import at whatever is their MIP. We will have to relook at 'make everything in India' or do I buy certain things prefabricated from other countries where the steel prices may not be as bad as India? If my levelised pricing were to happen then we would have been able to pass it down and the next assumption is that I am seeing some green shoots in the infra area barring power. If selectively they were to start moving upwards not on Indian cue…the American economy is stabilizing and moving upwards, global economy itself is talking about at least 20 basis point improvements in the global GDP; barring the German political uncertainty Europe currently is not talking anything negative, and Japan after a decade is talking about growth and again no more negatives from China. The global economy is now looking up and the lack of investment of almost a decade. India survives because of their impetus sensibly given by the then government, UPA government 2008, but despite all of the stimulus the investment cycle really caught on in the developed world, which I think is also going to the gap of eight to 10 years. Some amount of pickup is going to happen in the larger economies of the world. So these are all again conjectures and inferences from various data points. If there is a recovery going to happen, I am not trying to say that 2003 to 2010 is going repeat in India, but selectively and going towards investment cycle then the prices should improve in the market also. Even if the prices do not improve our ability to pass on the cost increase at least for pass through level should happen. We do not want to do profiteering. So when I compare that with those good days when we made maybe up to maybe profits in teen numbers Thermax is 13% also, so the ability of the organization remains. My suggestion or a talk related to, we would want to aim for double-digit is a realistic assumption, but it is not one item, multiple items can derail us. All of them can also support us. That is real.

Harish Biyani: Fair Sir. My second question is if we compare the previous upcycle versus say hypothetically in the next couple of years we have an upcycle or a start of an upcycle do you see any industries, which were there in the previous upcycle, which may not participate in this particular upcycle because one issue is the availability of coal or certain industries may not want to put in more capex. They would want to go a little asset light, so what are you looking at in the coming upcycle whenever it is?

M.S. Unnikrishnan: There are two distinct differences. Number one: during the last upcycle Thermax was a domestically oriented company with very little export orientation. If the current upcycle is going to be global, we will be present as much in India as in the international market, so there should be an upside on the internationalization initiative of the company., Number two is negative – I am very clear about the fact that the conventional coal fired or fossil oriented power will not come back to normalcy even if the upcycle were to peak. I may take an exception for captive power to a certain extent because of lack of investments over the past four to five years and India had been adding only frugal levels of capacity in thermal oriented power plants where coal is still available in the country. So, imagine if a two and a half trillion economy were to grow at maybe an 8% or 9% for a period of four to five years the energy intensity of Indian economy is 1:1. There is no way we will be able to bridge the power gap unless people go for captive capacity – that is an assumption. Now that is something we will have to live with, that is my assumption. Steel is another item where I would have expected things not to grow, but I am privy to the fact that the government itself has constituted a very senior committee comprising three to four secretaries and some industry experts to plan for a capacity upgradation from 130 to 300 million tonnes per annum. It is a humongous task and we have an ambitious plan. But if it were to happen, a predominant part of the steel industry in India is private in nature and there are global players who can come because not all balance sheets are stressed in the world. So, will the government give protection? If the current budget is an indicator, then the Government of India overnight can decide about barriers being created. We were bringing down our customs duty regime to a single-digit and today there are items, which are at 20% duty also. The mobile phone that you buy will have components coming at 15% and some of them will get into the 15% to 20% duty regime, so it is an indication that the government can protect industry and WTO is not such a tool anymore the way it prevailed in the last cycle. So, with a weakened WTO, I presume that India will invest, and that even steel is also a possibility. Cement in any case is a local industry. Nobody is going to bring in cement from some country. It is impractical to get in cement from outside India. So, if a cycle were to pick up the answer I want to give is -barring main thermal power every infra oriented larger investment will go up. Now one item I missed out is fertilizer. Well, the government policy currently is not to favor urea beyond a level. We believe that we are going to discourage its use and possibly move to NPK (Nitrogen-Phosperous-Potassium). The moment we are going to move to NPK, the investment cycles will come down. So our opportunity in a classical fertilizer plant should have a couple of hundred Crores worth captive power plant – sometimes as high as Rs.300 to Rs.400 Crores in the combined cycle kind of energy plants. It may come down substantially, so even if fertilizer were to turnaround I do not think every company is going to benefit substantially from it. So that is the overall take, Harish, from the turnaround possibility. These are all conjectures and inferences that I am putting out.

Harish Biyani: Yes Sir agree. Thanks so much Sir. This is very helpful. Thanks so much. All the very best.

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

Renu Baid: Good morning Sir. Sir a couple of questions. First we did speak about the overall cycle panning across and the orders that we have seen, but if you can help us understand that this kind of growth and orders that you have seen across segmental sectors how do they stack up, sector wise, the broad mix with respect to YTD inflows or order backlog, the top five industries and how do they compare with the 2008-2010 days, and how different was that mix? Are we seeing a mix now improving, a move towards cyclical sectors compared to consumption driven sectors?

M.S. Unnikrishnan: I can only talk about the orders we received and this cannot be reflective of India because in the first nine months, 49% of the orders that we have received, 49.3% to precise, came from overseas markets. It is almost 50:50 domestic versus international, so any inference on Thermax's improved order booking due to Indian economy turning around will be a wrong assumption. But if we look at international plus domestic where we had been successful, oil and refinery petrochemicals as a single segment makes up almost 30% of the order intake in the current year, which I have never seen earlier, barring one quarter when we had the Reliance order when a big Rs. 1700 crore came in. The first nine months of the current year, it was the refinery petrochemicals segment leading. This is a surprise – with the oil prices having come down how can it happen. Well people are still believing that electric vehicles is a distant dream. It is a political dream not an economic dream. It will happen, but it is going to take time.

Second is the cement industry. It's more domestic, maybe except for one order from UAE's Sharjah Cement. Indian cement industry had been keeping all the money on their balance sheet without understanding what to do with the money as the capacity utilization was not picking up. So, with government pressure, all of them have invested… also for waste heat recovery based power plants. So, we participated there and benefited from it. Additionally, the Pollution Control Act, had multiple items related to the particulate emission, SOx emission, NOx emission, etc. They have pushed the cement industry on SOx and particulate emissions, saying 'You guys are sitting on a pile of money, at least do this much. .' and that has initiated an ordering for augmentation of the existing pollution control equipment. So the cement industry, including international and domestic, has contributed to 17% of the company's order intake. Now there have been some sporadic investment in chemical industry, bulk chemicals larger ones not the distributed chemicals. Thermax has been lucky to get some orders in that industry and one large order certainly would have contributed to 16%. But the real winner is the consumption sector, which I continue talking about. Orderings from food processing, alcohol, beverages, textiles all of them have been continuing. Everybody has been investing, so 17% of my orders have come from that sector. I do not have too much of that sectoral order booking in the international market at this point in time, but we are trying with Indonesia. So that is the next one. We also see isolated investment in other non-ferrous metal happening in various areas. So these are the main sectors to talk about in the first nine months. Going forward which are other sectors? Fertiliser, I mentioned there will be bulk ordering going to happen for may be couple of quarters for two or three plants. Similarly oil, if I give you a number, in Q3 alone we have won orders for 135 Crores from Bharat-VI. So, the ordering is almost over for the Bharat-VI stage 1. Stage 2 ordering can be another 400 Crores to 500 Crores, so refinery will continue to be ordering Bharat-VI and two specific refineries, AL is ready with the request for quotations are going to be out in the market. That is about it.

Renu Baid: This is pretty helpful Sir. And second question if you can help us understand though you did mention Danstoker was a bit weak this quarter, but if we see this revenues also have declined and losses obviously have mounted, if you can help us a little more in granularity what was the kind of provisions done in China and do we expect the revenue execution run rate in the international or the subs for us to pick up again now and then how is the overall outlook at the Danstoker level?

M.S. Unnikrishnan: We have got three operating companies. Number one is Danstoker in Denmark, Boiler Works in Denmark and the new edifice we started in Poland. Now Danstoker per se had to book all expenses towards acquisition of the company in Poland. That Polish deficit is booked in the current quarter. Apart from that the two orders that they have executed had challenges, very specifically in the margins, so we are negative in the current quarter. Boiler Works is positive. Poland has just started. The outlook for it is that we are seeing the European economy is on a positive momentum, Poland has just started moving in that direction. After observing all that, current year Danstoker group is going to be a positive and profitable company. There is no doubt about that, but profitability in the current year will be lower. We will be able to see an improvement in performance of the Danstoker group, next year.

China is a challenge and well, I mentioned about some provisions to be also we had to make on some legal cases. We see a tendency over there. If India is having some difficulty and Indian companies face difficulties for some of the country-to-county issues, this is something, which we need to wait and watch. So I won't push for sales in China for some time unless we are clear about the local stand of Indian companies over there. We already have business coming from the rest of the world part of which is already fulfilled from the Chinese side. So we will certainly relook, currently we are only waiting and watching. We were expecting it to turn EBITDA positive even the current year, but I do not have to insist on that and then later have some difficulty. It is not a major issue. Thankfully it is a small business not something large in nature. So among the positives to talk about – the Indonesian factory started manufacturing boilers. They have made the first despatch from there and enquiries have started increasing since we are a local company right now, but of course it is going to take time, but next year there will be a little reportable turnover, some number to come from there. Thereafter it should stabilise over there. We started with the heating business, and we will also be moving on to air pollution control, which also started booking orders from Southeast Asia using the local capability. Water business also will move in with standard plants.

Renu Baid: Sure. Thank you so much Sir and I will back in the queue for more questions.

Moderator: Thank you. The next question is from the line of Nitin Arora from Axis Mutual Fund. Please go ahead.

Nitin Arora: Good afternoon. Sir, just one question related to emission pricing norms, which already you have been guiding us throughout many quarters. I just want to know specifically for one bid, which are placed by NTPC in Telangana, just wanted your sense on the pricing from there and where we stood when we were bidding for it in terms of pricing that is all from my side?

M.S. Unnikrishnan: The first ever bid for a similar plant was for Hardwar Ganj, 60 megawatt. We were the L1 and others were distant L2. So, the current Telangana opening is at par with our L1 price of Hardwar Ganj. We have included our designs and localized many other assets, so our competing capability in the market will be positive. Now, somebody can commit a suicide and again bring the price down the way it happened for supercritical boilers. We will not be in the group of people who commit suicide, we will be alive. So depending upon how it is going to turn out, we will participate in the next tenders. There are multiple tenders already put in by the company. Now, the winning party of Telangana if it is not a big player in this area, I do not know whether they understand what air pollution controllers are, because that is not a business that they pursue...whereas we have been in the business from 1970 before the Indian Pollution Control Act was drafted. So we have a reputation to live by and it is not the only market that we will be working on. So we will play the game as it comes, so currently I would not be able to commit if we are going to be the winners.

Nitin Arora: Fair point Sir. Thank you very much.

Moderator: Thank you. We will move on to the next question that is from the line of Ravi Swaminathan from Spark Capital. Please go ahead.

Ravi Swaminathan: Sir, I have a couple of questions. Sir, one is this Tata Steel's expansion of Kalinganagar stage 2, do we see an opportunity from that? Secondly there have been some of these large steels companies acquiring distressed capital power plants. Tata Steel also had mentioned about one. What would you think about, is it a risk of them not going for CPPs especially the larger ones like Tata Steel or Jindal?

M.S. Unnikrishnan: Ravi, anybody going for a blast furnace route for manufacturing of steel – it's the only way currently available in the world for an integrated steel plant…though some technologies have been tried out. They do not have a choice, but to go for a captive power plant. It is not just that they are going to burn fuel in the blast furnace. You got hot gases coming out that needs to be quenched before you send it out into the atmosphere; this gives us an opportunity to convert into steam and generate power. In this area, other than the largest public sector company of India, we are the only ones who supply the similar kind of capacity. Kalinganagar plant was done by us. Tata Steel was done by us and earlier plants of JSW were done by us. If Kalinganagar were to go forward for the next expansion, which I presume is already approved by the Tata Steel Board, it is routed through Tata power because the captive power plants of all the Tata Group is consolidated under Tata Power balance sheet. So if one set is awarded to Tata Power, I am sure we will be a strong contender.

Secondly, post NCLT clarity coming on the distressed assets. All the larger players barring Tata Steel I suppose, are looking forward to also the sale of those assets. If anyone wants to takeover their assets then they will not go for an immediate expansion, they will have an overstressed balance sheet. I think the other party will go ahead with that. So I am expecting this to be commercially in the markets for placing the order in Q2 to Q3 of next year, so we will be a strong contender for that. If they were to go for an EPC I will be very happy. If they again go for the boiler certainly we will be the strongest contender

Ravi Swaminathan: Got it Sir and in terms of waste heat recovery for cement is it an ongoing process that you see looking actually cement or other players are also going for it or is it like it is a business as usual and there would not be that great attraction? What is you feeling on that and how is the competition from Chinese players on this?

M.S. Unnikrishnan: First and foremost, cement industry, steel industry and building material industry – that is ceramic tile manufactures – are identified by the Government of India as guzzlers of energy and a directive has already gone to them for reducing their energy intensity or else have every possible waste converted into usable energy. So cement companies are now willfully into the process and it also makes commercial sense at this point of time. See all the solar prices of Rs. 2.5 to Rs. 2.2 unnecessarily clouds our minds. In reality the purchase price of electricity by any of these bulk buyers not having a captive power plant will go all way to Rs.6. So it makes sense for them to recover whatever is being wasted by them. So waste heat recovery based power plant for the sector has been going on. Earlier we had to do a pioneering effort for almost a decade to sell the first plant and then second and third happened with longer gaps. Today, there are multiple enquiries, but there are only 24 locations in the country where one could go for waste heat recovery based power plants and I do not know how many of them have ordered. I have not taken stock of it. My team is fully aware of that. Many orders got placed in the last year and current year up to this point of time. In my understanding there are some of them left, which will get over by end of the next year. But as standard practice the new Greenfield capacity that are getting created will have inbuilt captive power plant based on waste heat recovery.

There are cement plant makers also who can possibly come up with a waste heat recovery solution including an association or consortium arrangement with Chinese partners. But we are an active player because many in India burned their hands buying from China though one Chinese company has also localized part of it. But there are some technical capabilities needed to execute an order in the cement plant without harming their operation, and those are the kind of capabilities, which our company has created in project management and construction which stand us in good stead.

Ravi Swaminathan: Got it Sir. Thanks.

Moderator: Thank you. We will take the next question from the line of Venkatesh Balasubramaniam from Citi Research. Please go ahead.

Moderator: Sir, the lines of the current participant had dropped off the queue, we will move on to the next question that is from the line of Bhavin Vithlani from Axis Capital. Please go ahead.

Bhavin Vithlani: Sir, I have two questions on you. One is if you can help us with the size of our short cycle of these business, which is the BB boilers, the chillers and the base business of air pollution and the water treatment and how has that been growing in and what can we see the growth in this business as opposed the Indonesian facility and the Sri City facility. That's question one. And the second part of question is again coming back to margins wherein if you can delve a bit, how would be we protecting ourselves given the volatility in the input prices and are we seeing competition also easing out on the pricing given that domestic has not revived as yet?

M.S. Unnikrishnan: Still it depends on how we see the growth potential for the heating and cooling business, going forward, from the two facilities, one of which has already gone live and the second will go online in June. We have made these facilities for two reasons. First, we wanted to have an alternative to Pune. So that is one strategic decision related to heating and cooling. Second is to cater to the global market for cooling from closer to the port, and a much bigger modern facility for heating of course in Indonesia. So what we had in the mind, apart from the alternate facility portion, is catering to an annual growth ranging between 6% in a bad year to 12% in a good one. So let me average it to an 8% to 8.5% growth expectation from the businesses going forward.

Bhavin Vithlani: And how large would if these two businesses the heating business and the cooling business full year annual size?

M.S. Unnikrishnan: Heating globally including the Indonesia and Danstoker. We are heading close to a four digit number in the current year. I should cross that in the next year in any case. In cooling, including the orders picked up by our European and American enterprise, and supported by India and China we are a little above Rs.300 crore plus, which is a niche market. There has been a contraction in one part of that market, related to the heat pump, but the remaining cooling business is growing at a rate of may be 3% to 5% at this point of time.

Moderator: Thank you. The next question is from the line of Venkatesh Balasubramaniam from Citi Research. Please go ahead.

Venkatesh B: Sir, actually I got disconnected when the line got cut. The first question was the fact that you won a lot of orders in the first three quarters and we have not seen this kind of order inflows for a very long time, now despite that we have not had great margins in this quarter, which has declined and I believe last year you ended at around 9.7% and you did mention earlier that you expect that you will get closer to the double-digit mark, but given the market environment and given your carry forward, your order backlog is it possible to expand margins by 100 to 150 basis points or even 200 basis points over the next couple of years given that with the carry forward out of backlog you should be able to do 20% kind of topline growth, so is there an element of operating leverage that can play out or is it like given that these orders have been won competitively they are fixed price contracts in a rising commodity price environment even getting to 10% would be an achievement and expecting like 11% to 12% margin is not reasonable?

M.S. Unnikrishnan: Yes your questions are very, very valid. Based on past experience, there are certain assumptions that we make to improve the margin. The input price cannot be negotiated beyond a level. It is a global phenomenon and for steel it is a local phenomenan with the protection provided by the government that we will have to live with. Yes, there is a challenge specifically for a commodity known as tubes. There are only limited guys who can supply. Public sector units, traditional manufacturers of tubes have capacity constraints. So we will have to resort to buying it from outside. Thank God, a good part of the order intake is international in nature, which allows me to be import duty-free or claim the reversal later. So, there are some advantages for the international orders from that front, whereas challenges are on the domestic front. Other than the government tenders where we are going to be L1, orders are finalized on the negotiation table and 60% to 65% of Thermax orders come from repeat customers. So there is an established brand and an experience of the customer, hence there will be a transparent discussion. I would presume that we could go above the current level in the current year with one quarter left, to what extent can I come closer to 10% is a question. But going forward we can, because whenever there is a challenge we always come with the solution, which is more technical in nature. We have introduced new products, and have been able to manage cost reduction. There are products that we have been able to get a cost reduction in almost double digits, which should translate into maybe a 3% to 4% in the selling price, but I cannot get that from the market, so I can at least come down and pick orders with decent margin. There is one factor, which can help but I should not say this to an Indian audience – let the

Rupee go back to 68 and I will certainly come back and guarantee that we will be making double digit profit. I am sure the government will not like it. Crude oil price has gone up, but the indications are that Rupee would not strengthen any further may be you guys can advise me on that account... It is a tougher play to go ahead with, but you also asked will I have margins tweaking on an account of the size going up. To a certain extent it is alright, but for the larger projects, you budget and cost for each of the project. If it is an automobile industry where you get standard products, it could have been better. One unknown thing to all of you is that we have a service arm embedded in our businesses, which do not shrink the margin and the growth from that can compensate for margin pressures in other areas. Today if I look at my service business alone, we will be touching 14% of the total topline in our organization, That is not the normal margins of single digit, but better and in double digit.

Venkatesh B: Sir, the second question is slightly more strategic. Sorry if this question seems a little harsh, as we are coming to a close on FY2018 and as we look at numbers it looks like most probably you are going to end up with something like 290 Crores kind of profits and as I look back in time 2008 also we ended with 290 Crores, so basically in 10 years you basically not grown the profits and we have taken lots of initiatives in the interim period. We have expanded in China, we have expanded in Europe, you have looked at opportunities in biomass, you have looked at opportunities in supercritical boilers, we have talked about Namami Ganga as an opportunity, you have talked about the pollution opportunity, but that does not seem to be translating into numbers and we have had time and time again we have expanded in, you know taken a new initiative, gone to a new country, put up manufacturing facilities or made an acquisition and then we have written it off. Now as we see that you are moving into, you have put up this facility in Indonesian now one thing, which we wonder is whenever we see an opportunity there is an opportunity, but are we to some extent underestimating our competition from behaving irrationally. Now we are in an environment globally where there are not enough capital goods orders and everybody is behaving irrationally because everybody is trying to fill up facilities. Is it better to anchor down and possibly instead of expanding capacity possibly payout higher dividends and is that some strategy, which you have thought about or what exactly do the promoters communicate to you from time-to-time in terms of what exactly are we trying to achieve? Are we trying to become bigger in size? Are we trying to generate more cash flow? What is the key success factor on which you are judged and you are asked to operate on? Sorry if it seems like a very harsh question.

Venkatesh B: I love questions like this because is also gives insights to sharpen our way of thinking. See, organizations, which are declining on topline and on profitability, ultimately there is only death for them. So I am sure as an investor or somebody who advises investors, you are don't want a healthy organization to die. So, you may plan for any number of things, but the market does not support you. Our largest miscalculation or maybe the environmental factor, which had been negative was TBWES. Well we have passed through that. There is nothing to worry about that because we make money, we lose money, but in business you have ability to standby and continue to believe that you can still make money. I am not naming, but there are companies in this country who have gone down under including the largest capital goods company of the country who reported in excess of 1000 Crores of loss in a particular year. I hope you are aware of that for the aggressive decision they made.There is another capital goods company which possibly may reach NCLT. Even listed companies in material handling who got a market cap going all the way to half a billion dollars have gone down under. But you still have Thermax sustaining and talking that it will grow. This is the capability that we have. Our best time was Rs. 6000 Crores and we were a billion dollar company and then came down to Rs. 4300 crore. In the subsequent year we were still very close for double digit profit. Do you believe that? We have done it in a market where hardly anything was in existence. You got to try in every avenue possible and we do not expect to win in everything. Well, for that you got to be God, we are not. So we are clear about the fact that we are into energy and environment and we will look at every possibility. We do not guarantee that everything is going to be a success, but looking at our average success rate, we are possibly better off than many others in the field. Our China investment is in trouble today on account of the stand-off between the two countries. So these things are unpredictable when you make a business plan, no matter who makes it. In a business you rate an organisation by its agility and ability to withstand environmental pressures, which we have seen in the most difficult times and have been able to re-spond. Thank God we did not get into negative and red. We are positive and possibly what you guys value is based on what you perceive is our strength. So we will continue to win. Let me guarantee to you that we will continue to buy companies, set up capabilities and facilities outside, if I did not go to a Asean market where in my opinion the standard production is going to be exceeding India's demands in the next five to six years' time, if I don't aim to be a player over there somebody else would have come there. Today I am there so my competition will think multiple times before they set up a facility, and the first mover advantage which I will get. If Indonesia were to follow the model of the second largest economy of the world in terms of certain policies, well I may not be able to sustain over there also, but that may not be the case. Now the next level for me is wanting to participate in the developed world. We have shied away from buying companies in European continent after a misadventure in the 1990s which many of you are not aware of - ME Engineering. We bought Danstoker knowing fully well Omnical there was a negative company, but a classical Indian company thought we can turn it around and try it out, we turned out a German this is not an easy task. Eventually we closed it, but today it is a profitable business. I mean how many European capital goods companies are making money. Thermax and Danstoker will report profits even today in the current year and we are looking at other acquisitions. It is also possible to increase service business on the equipment business also. The service around the customer is something, which can improve your margin, life cycle management, which we have not been able to start it in the European enterprise. I would not be telling that we are not going to shy away even from the North American market of manufacture is going to come back over there, so we will do that because heating, cooling and captive generation of energy in different forms will have to remain in the business. And if manufacturing is going to die in the world, well there is no opportunity for me. I presume that maybe, I am sorry for giving you a long lecture, but to tell you precisely of 7.5 billion human being available approximately an 18% to 20% of them are well provided, another may be a 25% to 30% are getting provided, half of them do not even have the basic requirements. I very strongly believe as somebody in the industry that investments are going to happen in creating capacity in the underdeveloped and developing world and we are targeting and we will continue to do that.

Venkatesh B: Sir, thank you for the very detailed answer and I hope your next three years are very, very different from the last three years and all the very best. Thank you.

Moderator: Thank you. The next question is from the line of Kirthi Jain from Sundaram Mutual Fund. Please go ahead.

Kirthi Jain: Congratulations first of all for good state of performance in the quarter. First question is with regard to chemical business we are seeing some drop in the profitability Sir any of reasons or is it normal profitability, what is the thing?

M.S. Unnikrishnan: It is the PBT number you are seeing. Last quarter we have commissioned the Dahej with an investment of Rs.145 to Rs. 150 Crores. So the depreciation would have been already there, we normally declare PBT numbers. So if I were to add the depreciation back it has not deteriorated to that extent though they could have been in the early quarters if there is chunky, which could have something better otherwise nothing to worry on that account. Why should I not tell you about that styrene prices have gone up in the world when crude petroleum has moved up to 65 and I am very minor buyer so I cannot do a bulk buying or a super tanker. So, there will be input price pressure to a certain extent, but it is not going to be impacting beyond a level, because not only the resin we are also into the construction chemicals and performance chemicals. There margin maintenance is a possibility. We will not compromise on that. Quarter-over-quarter once in a while you may find this kind of a thing and going forward also for the yearly result of the next few years the depreciation is going be there and just to clarify to you I have already cleared the phase 2 expansion program for Dahej plant and we will be commissioning that by possibly March of FY2019, so depreciation can increase further. There is reason for it some other time I will let you know about it.

M.S. Unnikrishnan: Yes certainly yes. Let me clarify to you. Our entire intention of Dahej plant is to ensure that one day it becomes our resin plant for the future. The phase 1 of this plant is 12000-meter cube capacity whereas in the current year my demand is almost closer to 17000 up to end of March. Next year the demand is going to be 18500 to maybe even 20000 if I am able to pick some bulk orders. So that is why phase 2 is there. Since you asked the question I have to clarify to you. We will not run both the plants together. So, at a very quick succession I want to reach it up to 22000 metre cube so that I will take care of the capacity requirement up to FY2020. Then, phase 3 also will happen over there to raise it to 40000 metre cube. That is the ultimate master plan for that factory which will go up only as and when the market improves. We had been selling this predominately in America and many other countries. Our next target market is the Europe. In America we are selling approximately 14 to 15 million dollar worth of resins. We want the same thing replicated in Europe. We have already started the marketing initiatives for it. So the growth in the business to reach 40000 will predominately come from Europe and the rest of the world. So currently I need to run both plants. Mind you, the manufacturing plant in Dahej is a fully automated and computerized facility and we need to be very clear that we create the production algorithms. It does take time to scale up production and till such time we commission the second phase which is going to be possibly March 2019, I will have to run the earlier plant, the Maharashtra one.

Kirthi Jain: So what kind of growth?

Moderator: Sorry to interrupt Mr. Jain. Sir, we would request that you return to the question queue?

Kirthi Jain: Thank you.

Moderator: Thank you. The next question is from the line of Kapil Joshi from Stewart and Mackertich. Please go ahead.

Kapil Joshi: Good afternoon Sir. Just wanted to know the future of the chemical like this quarter we have not seen much growth in chemical segment like only 6% growth YOY and QOQ just wanted to know what kind of growth we can see in next two to four years?

M.S. Unnikrishanan: We were restrained by the capacity for the resin business. There is no capacity constraint for the rest of them. My expectation of chemical business growth for the next if you take a five-year block should go at the rate of 15%. This is what I am expecting.

Kapil Joshi: Average?

M.S. Unnikrishanan: Yes, average is 15%

Kapil Joshi: Thank you.

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

Bhavin Vithlani: Thank you for the opportunity again. Just a recap of the questions on the margin; so we saw for environment business also volatility in the margins can you help us what is the steady state margins in the environment and how do we see the growth in environment now picking up. You spoke about some opportunity in cement sector for air pollution?

M.S. Unnikrishanan: Bhavin, environment will not be able to match up with the profitability level of energy because predominant part of environment business is air pollution control and water and wastewater treatment. In the water treatment it is possible get better margins, but wastewater treatment and air pollution control are seen by the industry as a burden on them rather than as a social obligation, so margins normally come under pressure. To improve margins one may have to make compromises on the offering which you know Thermax will never do it that way. So we get the premium in markets as a company that delivers what we really commit. As the size of orders go up, smaller competitors cannot come into the fray, so only when there is an even level play available we will be able to see betterment of margins. Secondly, as I mentioned predominately we are an Indian operator for both these businesses. We are branching out outside India, and the Southeastern initiative through the Indonesian plant was only for boiler in the beginning. One would like to localize this offering of water and wastewater which we are able to make double digit profit most of the time in India.

We also started making forays into the Middle East. I am very happy to inform you that we have got an order from the Municipal Corporation of Kuwait for a water treatment plant. We have inquiries in those markets which do give you a better recovery also, but even then I cannot foresee… maybe there could be a quarter or maybe some time when we get a chunky good price order we may have an improvement in margin. But, otherwise we always trail behind the energy for profitability.

Bhavin Vithlani: Thank you so much. That answers my question.

M.S. Unnikrishanan: Thank you Bhavin.

Moderator: We will take the next question from the line of Sanit Visaria from CRISIL. Please go ahead.

Abhishek Puri: Good afternoon sir. This is Abhishek Puri from Deutsche Bank. Sir, congratulations for getting back to the double-digit growth that you have been waiting for some time and it is good to see that your capital is also strong in the emerging business and the margins are growing. Just quickly I think some balance questions you know should we assume the environmental business margin should be between 2% and 3% where we are reporting right now. Last year we had about 8% or 9% margin in the last three quarters of the year. I do not know why your EBITDA margins were lower?

M.S. Unnikrishanan: Environment can report 8% to 9%. I don't want to bet right now, certainly not 2% to 3%. Even the water business which was negative has now turned positive and we are trying to improve the profitability in that area. There were very few ordering in the air pollution control business and it's the only division which got impacted by the steel price increase. You may not recall right now, but may be seven or eight years back in concalls, I used to talk about that, the only business of Thermax where steel price increase can impact very quickly is air pollution control on account of the fact that in boiler or cooling business there are specialised things that we buy. We even got rate contracts for project within seven days of receipt of the order and advance from the customer. We would have placed our orders for the specialised team, whereas for air pollution control we used very ordinary steel, very normal structural, ducting and plain steel which nobody in the country will be willing to sign a rate contract with us. It is normally ordered out only at the time when you are executing the order and once the customers give 10% advance, it is very difficult to move on the price curve. If the price variation is up to Rs.1 to Rs.2 per kg, its Rs.1000 to Rs.2000 per tonne it is manageable, that kind of contingencies are available in the business. But when it has gone up all the way from Rs.28 in the beginning of the year to Rs.40, that is really killing and short cycle orders we will always be able to execute quickly but the medium cycle where we may not have delayed the project but the customer himself is delaying the project where he will shell out this extra price and on principle Thermax is a company which will never walk away from an order from a customer. That is why we have repeat orders coming from the customers because they know even when I am supplying it I am making losses, he will say okay next time, I will help you out. So to retain relationships organisations like Thermax become a little emotional than being contractual when we are executing it. So that has played into the current year's balance sheet. Last year it was not there. So currently steel price has stabilized at 40+ and I do not expect the price to go beyond, at least conventional steel will go within the range of Rs.1 to Rs.2 maybe Rs.3, which is absorbable by the company or transferable to the customer. Is that okay Abhishek?

Abhishek Puri: Fair enough Sir. Second question is on the order break up that you gave into five segments, cement, bulk chemicals and consumption could you give us a sense that this order book growth of 20% that we are seeing for the last three quarters is likely to continue, is there a pipeline that probably you can share with us, you know that gave this confidence that 20% growth can continue in quarter to come?

M.S. Unnikrishanan: It is a very tough question to answer. When I look at the enquiry on hand for finalization, I think, one more quarter can pass through. Beyond that prediction is very difficult.

Abhishek Puri: Thank you so much, and all the very best.

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

Karan Rathod: Hello. This is Karan Rathod from ICICI Securities. Just two quick questions. Firstly, could you help with some guidance for FY2018 considering that we have marginally grown for nine months. So what could be possibility of new growth for the full year?

M.S. Unnikrishanan: Well, that question I am unable to answer even to the board of my company. One month has already passed, you read about E way bill is going to kill us. Thank God the system crashed and we escaped the run. So the next run has started in all our factories to ensure that keep producing to ensure that there is a growth in the current year, but it cannot be major growth. Though orders may be on hand larger ones have come in the recent past, so revenue recognizing them beyond a level is impractical and we would not push for growth, but there will be growth. Guidance is something, which on principle we do not give on account of the fact that we do not want to fail or do something wrong by giving a commitment. We should be growing in the correct year.

Karan Rathod: Okay sir. So just as an assumption could you assume that it could be in the low single digit?

M.S. Unnikrishanan: Well you guys are known for arithmetic far superior than mine. You will have all the numbers in front of you, you have the answers also to be arrived at. So it will certainly be in single digit that is for sure. See, one wants better growth. We will grow in the current year that much I can guarantee.

Karan Rathod: Thank you for taking my questions. Thank you.

Moderator: Thank you. We will take the next question is from the line of Sujit Jain from HDFC Securities. Please go ahead.

Sujit Jain: Sir just to understand for FY2017 or for 9 months, in the energy revenue if you could break up that revenue for FY2018 9 months so us to understand where we have headed to break up that revenue between captive, heating, cooling and EPC?

M.S. Unnikrishanan: That level of granularity we do not normally give. Amitabha can you give you energy environment he has already given.

Sujit Jain: We do not want exact numbers but just to have some sense.

M.S. Unnikrishanan: Even I myself has not gone through the numbers in front of me. The way we started reporting is the way we reviewing. The numbers are available. Approximate cooling is the smallest one. What is the total of the energy itself for the revenue?

A Mukhopadhyay Energy revenue for the 9 months is 2384 Crores in the nine months revenue at a consolidated level.

M.S. Unnikrishanan: So year-end I tell you cooling will be just about 300 odd number at the year end, balance will be between heating and ….part of that gets reported into the EPC of business. So it is absorbed by them. And the boilers are supplied both by the B&H (the large boiler business group) as well as the smaller standard boiler business. Because these days people go for cogeneration power plants where the boiler is made by the standard heating division itself, not by the B&H division. There was a time when only B&H was linked only with the EPC business. See it is not a boiler alone, that's where the difficulty happens, each division what they are giving when you do a project it is a component which is supplied, like in the heating smaller products, full product is made in the factory and dispatched. So we do not track it that way though the SBUs numbers will be available but how much of that is embedded as a captive consumption by the power business, EPC business, we learn to offset it.

Sujit Jain: Just a follow-up on this question: is that eventually if the captive power business and heating business were to shift to solar power then what is the answer from Thermax to that kind of disruption?

M.S. Unnikrishnan: Of the total energy business, cooling is going to be independent, so is heating. If at all people were to go for solar, we also have a solution for solar hybridisation for heating. As I mentioned about in the current year, entire global heating business would be touching closer to 1000, in that cogeneration portion could be a 20% let us say globally. But that may not get impacted. Current year we will be doing almost may be a Rs. 750 plus crores in the EPC business for captive power overall in that some of them are cogen oriented. The pure captive, like may be coal fired boiler generating power all put together could be in the region of around 500 to 600 crores let us say. On a total number of 3000 in the full year. So how much will that be, around 20% will be impacted, let us say. The captive power will have a 20% impact on the energy basis,

Sujit Jain: So you are saying within the EPC business roughly 500 will be coming from pure captive and about 250 could be waste heat recovery?

M.S. Unnikrishnan: Correct and we are also now into solar, current year it should be touching 60 to 70 Crores PV rooftop and order booking is improving. We are not really pushing it beyond a level because that will show with number, bottom will be very small which will not keep you happy.

Sujit Jain: Correct but microgrid kind of opportunity for industrial what is our footprint there?

M.S. Unnikrishnan: With the solar?

Sujit Jain: Solar.

M.S. Unnikrishnan: Opportunities are there, see like there you are going to invest money and become an owner and develop. It is not an area that you would want to leave because the business is going to face shakeout in the near future and China will control the global market and if they decide to sweat the market tomorrow, many people who want to invest may find it difficult. We will grow in the solar rooftop business, we also bid but we have got a cut off point beyond which we will not come down. There are lots of fund taken by the people while bidding in anticipation of reduction in price of the solar panels, they do take orders and many of them have been successful ensuring that prices came down. They were lucky enough, but that is not the way we would do business. So, we are also continuing with the solar option – solar thermal and solar PV, but in a very small way.

Sujit Jain: Thanks all the best to you.

M.S. Unnikrishnan: Thank you.

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

Renu Baid: Thanks Sir for the long call and that is the last question. This is for Amitabha Sir, if you can share the order backlog breakup between energy, environment for the group and for the standalone. That's it Sir?

A Mukhopadhyay: Order backlog, I will give you the consolidated breakup 4812 energy, 713 environment and 31 chemical, total 5556 is the total value.

Renu Baid: For standalone?

A Mukhopadhyay: Energy 4404, environment 713, and chemical 27, total 5144.

Renu Baid: Thank you so much Sir. All the best. That is it from my side.

M.S. Unnikrishnan: Thank you Renu.

Moderator: Thank you. Ladies and gentlemen that was the last question, I now hand the conference over to the management for their closing comments.

M.S. Unnikrishnan: Thanks a lot once again to each one of you for being with us and being supportive and asking very, very incisive questions. But I really appreciate questions like the way Venkatesh asked, because these are kind of things which will make us also think, many a times we believe we are doing the right thing. When you ask questions of that sort, it will also set us to think and many a times come with different answers. So again thanking you and be with us. Let us work and report back to you, three months down the line. Thank you.

Moderator: Thank you. Ladies and gentlemen that concludes today's conference. Thank you for joining us. You may now disconnect your lines. Thank you.