Investment memo – Thejo **Date:14/10/2024**

Mcap (Rs bn)	27	Shares O/S (mn)	11
Promoter shareholding	54%	Price (Rs)	2,500
Pre-tax ROCE (exc. goodwill)	37%	Trailing P/E	51

Investment summary

Thejo is poised for strong growth (~15% CAGR in sales) in the coming years as:

1) Over the last 5-10 years, the company has made significant investments which are poised for bearing fruit –
    a. Breadth of product portfolio has been increased significantly led by investments into R&D and product development.
    b. Company has been able to tap marque global clients – Vale, BHP, Rio Tinto, for its products. The products have been tested and commercial supplies have started.
    c. There is significant scope to ramp up sales by deepening client relationships.
2) Thejo fits into our framework for investing into manufacturing sector in India –
    a. Manufacturing complexity is significant as there are multiple SKUs and products need to be customized as per local specs of the mine.
    b. Quality sensitivity of the client is high as a break down of these products could lead to stoppage of work leading to significant losses.
    c. There is significant component of servicing (maintenance and timely deliveries) on site.
    d. Clients typically don't change vendors for 5-10% lower price if execution (of incumbent) is good.
3) We expect Thejo to grow sales and earnings at 15% and 15-20% CAGR, respectively, led by –
    a. Market share gains from global players due to superior product positioning – same quality (proven) at 15-20% lower price with good service on site.
    b. As per our understanding, market share (products) is in low single digits, globally, and hence window for growth should be long (5 years atleast).
4) We have confidence on sound execution capability of the mgmt. in light of –
    a. Our channel checks (India only) suggest strong industry reputation.
    b. The company has established good quality credentials in some of high value added products like – adhesives and rubber consumables used in conveyer repair, filter press parts etc, which gives us confidence on the product development capability of the company.

In our view, stock should compound at >20% CAGR given potential for a bit of multiple re-rating given superior growth profile and good ROCE/FCF profile.

Company profile

- Thejo is a leading player (India only) in technical services (O&M mainly related to conveyer belts) in India, primarily for steel plants and iron ore mines. As per the mgmt., its market share in conveyer maintenance services in India is ~60-70%, in the organized sector. Ove the last 10 years, the company has pivoted its business model to focus on products as – a) entry barriers are higher, b) growth prospects are better.

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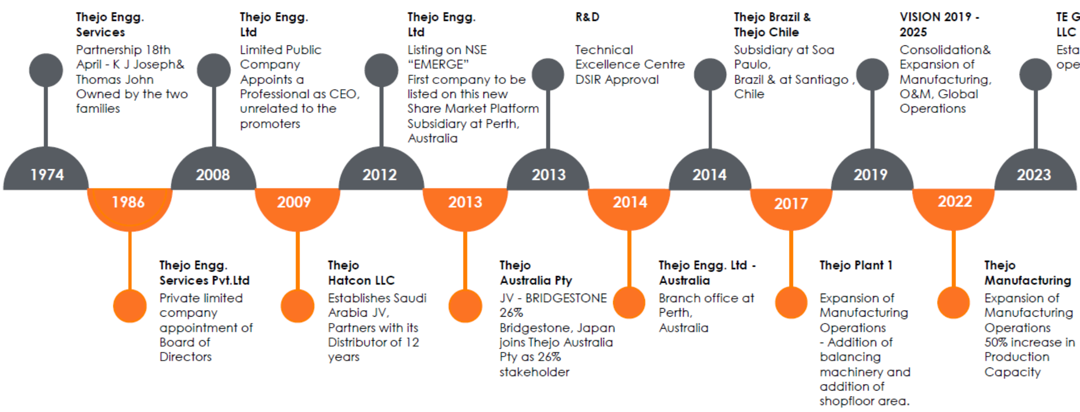
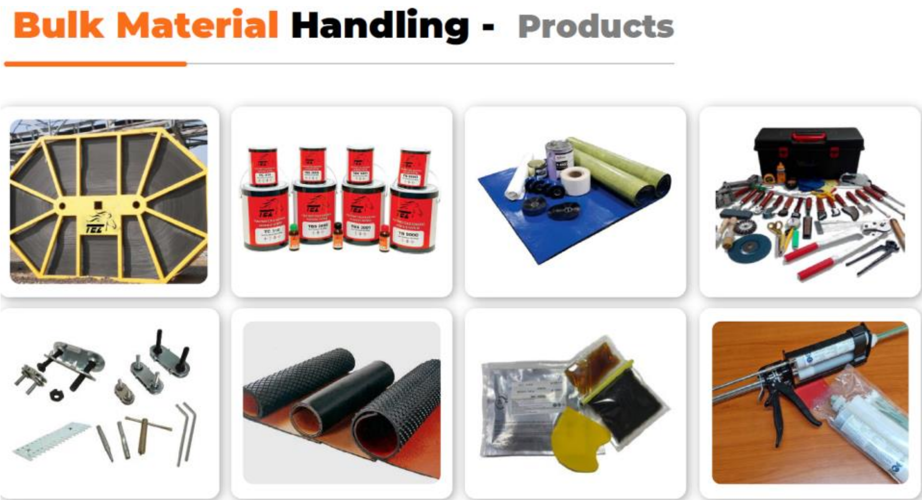
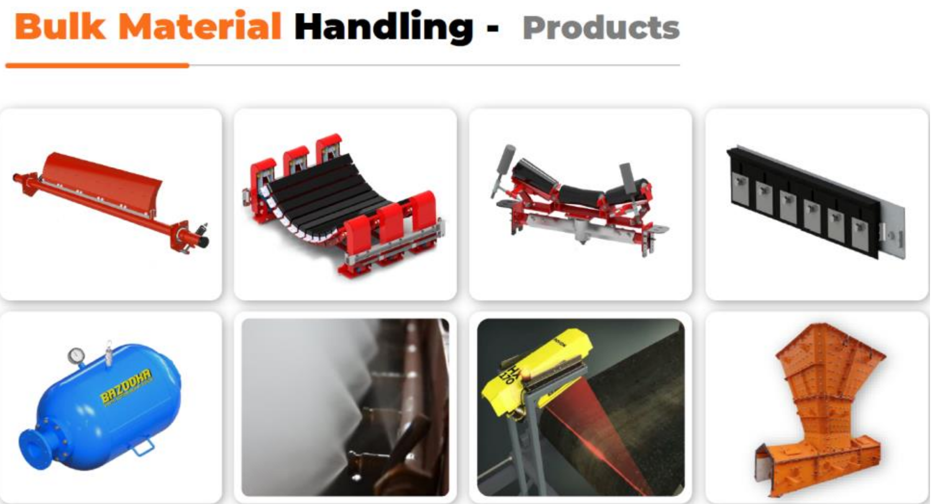
- Thejo was started as a service unit in 1974 by Mr. K J Joseph and Mr. Thomas John. It is now being run by the second generation – Mr. Manoj/Manesh Joseph and Mr. Rajesh John.
    - Mr. Manoj Joseph joined the company in 1991. He worked in various departments of the company before being elevated to the position of COO. He is now serving as MD (2021 onwards)of the company.
    - Mr Manesh Joseph has been working in Thejo for the last ~12 years. He was heading operations and maintenance (O&M) division of the company till Dec -23. He has been appointed as the CEO of Thejo Hatcon (subsidiary in Saudi Arabia).
    - Mr. Rajesh John joined Thejo in 2002. Before that, he worked for Tafe and GE Capital International Services. He has been designated as Deputy MD from 1st April 2024, onwards.
- Interestingly, the chairman (executive) of the board is Mr.V A George, who is not related to the promotor families at all. Mr. George was a banker earlier (he has worked at Syndicate Bank and Catholic Syrian Bank) who gave Thejo its first commercial loan. From that point onwards, the promoters started seeking his advice on strategic matters. Mr. George joined the Company in 2007 and served as its President & CEO till 2013 when he was appointed as the Managing Director. He served as President & CEO/Managing Director for about 13 years. He was then appointed as the chairman of the board from July 2021 and is currently the Executive Chairman. Typically, we have seen that promoters of smaller companies don't like to give control, so we find it quite admirable that Thejo has appointed a professional as chairman of the board and hence our confidence on corporate governance practices of the company is high.
    - Mr. George owns 1,30,000 shares of the company as per FY24 annual report.
- In its initial days Thejo was buying products (to be used in services) from 3rd parties. Bad experience in 3rd party products, led it to start manufacturing products in a limited manner (rubber sheeting to be used in conveyers and adhesives). Clients were happy to buy products from Thejo as its engineers were there on site 24X7 and hence had the confidence that any break down in products would be attended to quickly. Given good performance and value proposition of company's products, clients started giving it new products to develop.
- The company got serious about growing in the products business in early 2000s and started making investments in product development, 2005 onwards, by setting up a structured R&D department.
- Over the years, its products have got tested in some of the toughest/largest mines in the world and hence quality/performance/value proposition is proven as of now. The major product segments in terms of focus are (in descending order) – 1) Conveyer belt related products, 2) Filter press spares, 3) Mill liners (both rubber and composite).
- The company got listed on the NSE "EMERGE" platform in 2012 and on NSE in October 23.



- Company’s business can be split into product and services –
    - Products are mainly related to – a) conveyers – rubber sheets, adhesives, transfer chutes (and linings), conveyer parts, etc, b) filtration press spares, c) liners – mostly rubber and little bit composite.
    - Product sales (in FY24 as shown in the exhibit below) are almost equally split between India and outside India.
    - Broadly, product sales of Thejo Engineering India Ltd, which is responsible for most of the manufacturing are split (FY24) in the following manner – a) Material processing (includes liners) accounts for 45%, b) Bulk material handling accounts for 25%, c) Corrosion protection products account for 10% and d) service-related products like adhesives, rubber sheets account for 20% of sales.
    - In terms of exposure to various sectors, break up of product sales (FY24) is –
        - OEMs/Distributors/Service providers –~30%. Exact sectoral exposure data is not possible as Thejo does not have exact visibility on the end-use of its products.
        - Iron & Steel – ~30%
        - Mines – ~20-25%
        - Ports – ~5%
        - Cement – ~3%

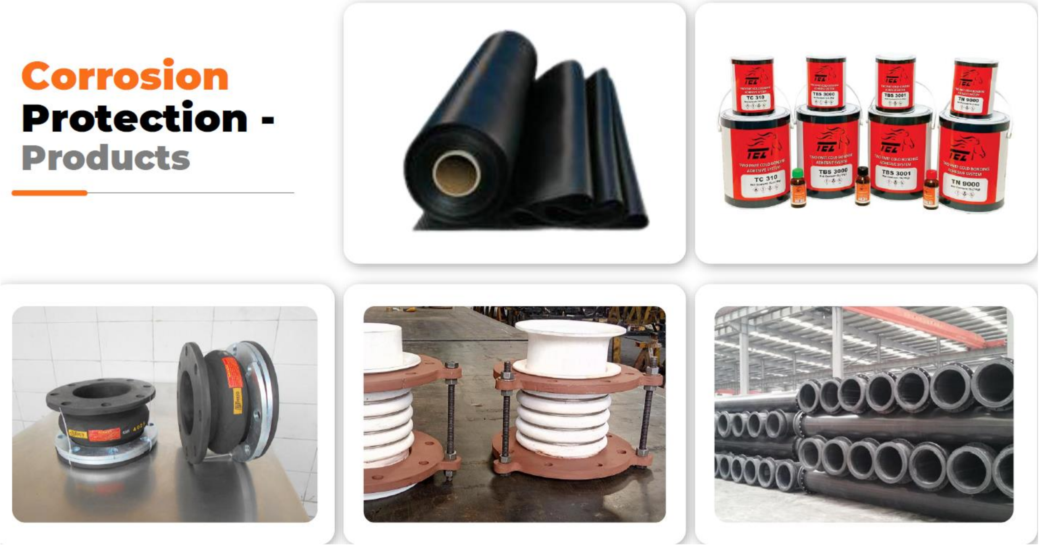




Bulk Material Handling		
Products	**Services**	**Equipment**
• **Conveyor Care** • Belting • Splicing/Repair Kits • Pulley Lagging • Tool Kits • **Transfer Points** • Transfer Chutes • Skirting • Belt Trackers • Impact Cradles • Dust Suppression • Flow Promoters • Wear Liners	• Belt Audits • Belt Scanning • Splicing & Pulley Lagging • Sustainable Synergetic Solutions • Project Commissioning • Operation & Maintenance	• Belt Monitoring • Belt Splicing Machines • Belt Winders & Stands • Belt Pullers

Mineral Processing - Products

Mineral Processing		
Products	**Services**	**Equipment**
• **Comminution** • Liners for Mills • Pulp Lifters • **Screening** • Screen Panels • Trommels • **Filtration** • Rubber Membranes • Filter Plates/Vats • Grids / Seals & Spares • Hoses / Pinch Sleeves • **Wear & Abrasion** • Liners • Wet Abrasion Sheeting	• Audits • Mill Wear Scanning • Liner Installation • Sustainable Synergetic • Solutions • Operation & Maintenance	• Re-engineering &Retrofitting • Design, Fabrication, Lining& installation



Corrosion Protection		
Products	**Services**	**Equipment**
• **Lining** • Pre-Cured Rubber • Un-Cured Rubber • Polyurethane Coating • Cold & Hot Adhesives • Repair Putties • Tool Kits • **Bellows & Expansion Joints** • **Hoses** • **Fabricated Rubber lined** • Pipes • Vessels	• Hot & Cold Lining • Project Commissioning • Rate Contracts	• Spark Testers • Rubber Removal Rigs

- Services business is comprised of 2 parts –
  - Technical services – Thejo is only responsible for repair and maintenance and is not managing day to day operations. This comprises of ~Rs2 bn out of a total Rs2.9 bn of service income (excluding products) in FY24. In most of the cases, where Thejo takes up repair and maintenance projects, it uses its own products.
  - ~Rs800 mn of service income in FY24 is related to O&M, where Thejo is responsible for day to day operations for a part (mostly conveyer) of the plant/mine, with specific SLAs (like maintaining minimum equipment availability and other related performance indicators like spillage, preventive maintenance, etc). In our view, this business is less value added in its current form and hence maybe not be scalable in the long term.
  - Almost 80% (FY24) of the service income is linked to transportation of materials (mainly conveyer belt).
  - Almost 20% of the reported service revenue is product sales as products used in services are billed as part of the service. We have presented break up of sales into products and service, after taking out product sales from reported service-segment revenues and including them as part of product sales.
  - Services sales are split 70:30 into India and outside India.

Break-up of sales after aggregating product revenues from reported sales under 'services'

(Rs mn)	2019	2020	2021	2022	2023	2024	CAGR (%)
Revenue	**2,295**	**3,039**	**3,271**	**4,245**	**4,745**	**5,594**	**19.5**
Products	1,120	1,440	1,293	1,842	2,068	2,726	19.5
Services	1,164	1,587	1,971	2,394	2,672	2,863	19.7

Segment numbers as reported by the company

Segment details	2019	2020	2021	2022	2023	2024
Net revenue (Rs mn)	**2,295**	**3,039**	**3,271**	**4,245**	**4,745**	**5,594**
Manufacturing Units	613	596	650	871	1,082	1,398
Service Units	1,465	2,192	2,394	3,017	3,323	3,865
Others	217	251	227	356	339	331
Segment results	**409**	**595**	**579**	**707**	**631**	**1,005**
Manufacturing Units	266	196	227	257	281	396
Service Units	164	383	331	391	309	498
Others	-21	16	21	59	40	111
Segment margins (%)						
Manufacturing Units	43	33	35	30	26	28
Service Units	11	17	14	13	9	13
Others	-10	6	9	17	12	34
Capital employed						
Manufacturing Units	482	517	434	579	912	1,086
Service Units	544	765	954	1,187	1,218	1,463
Others	19	41	64	101	103	227
ROCE (%)						
Manufacturing Units	55%	38%	52%	44%	31%	36%
Service Units	30%	50%	35%	33%	25%	34%
Others	-109%	40%	33%	59%	39%	49%

Entity level sales (Rs mn)	2019	2020	2021	2022	2023	2024
Thejo Engineering ltd. (Standalone)	1,465	2,192	2,394	3,017	3,323	3,865
Thejo Hatcon Industrial Services Company	145	158	163	230	214	234
Thejo Engineering Latino America SpA (Chile)	49	89	90	100	182	151
Thejo Brasil Comercio E Servicos Ltda	10	10	11	31	27	179
Thejo Australia Pty Ltd.	299	897	986	1,247	1,231	1,407
TE Global FZ-LLC (UAE)	-	-	-	-	-	-
Total	**1,968**	**3,347**	**3,643**	**4,625**	**4,977**	**5,836**
Entity level PAT (Rs mn)						
Thejo Engineering ltd. (Standalone)	136	137	215	292	276	381
Thejo Hatcon Industrial Services Company	26	48	32	77	49	59
Thejo Engineering Latino America SpA (Chile)	-8	5	0	7	33	19
Thejo Brasil Comercio E Servicos Ltda	-1	-2	-3	10	9	102
Thejo Australia Pty Ltd.	7	111	54	42	-2	40
TE Global FZ-LLC (UAE)	-	-	-	-	-	-6
Total	**160**	**298**	**298**	**429**	**366**	**594**

Nature of the industry

- Given lack of global peers with similar business and hence non-availability of data for the product segments of Thejo, we are unable to give precise numbers for the size of the global market and past growth trends in the market. Our hypothesis is that –
  - Thejo's market share is insignificant (low single digits at most) in most of the product segments, globally, and hence overall market size is not relevant to develop a

perspective on how scalable the product business can be in the long term. In our view, scalability of products business for Thejo, in the next 5-10 years, is more a function of its own on-the-ground execution and is not constrained by global market size.

  - Most of the competition, comes from global companies, which are based out of developed markets. As per our understanding, Chinese companies are dominant in their home market and not so much outside China.
  - Mining consumables market (global) generally grows at 5-6% led by – a) underlying growth in consumption of 2-3% CAGR in metals as an aggregate, b) consistent decline in ore grades generally implies that growth in mining consumables would be 2-300 bps more than growth in consumption of metals (aggregate).

- Just to get a perspective on how large the market (products) could be in the focus segments of conveyer belt accessories and filtration plant spares, we have used the following data points
  - Conveyer belt related products - As per the mgmt., JSW's Ballari steel plant with a capacity of 12 mn tons with '00s of KM of conveyers running in the plant, consumes around Rs1 bn of conveyer related spares, per annum. Given that world ex-China produces about 0.8 bn tons of steel would imply that addressable market (global) for Thejo only in steel is about US$0.8bn. We would assume that the global market in this product would be growing at 4-5% CAGR in line with any other consumable being used in the mining and steel industry. Thejo is not present in all the markets and hence, might be able to tap only a fraction of the above opportunity.
    - JSW Ballari is not the best paymaster and in any case India is a hyper competitive market for all B to B products (non-patented) and hence in our view the market size we have arrived at using JSW Bellary as the benchmark understates the global market size in our view.
    - As per our channel checks, there are some companies in US, like Flexco and Martins, whose revenue from conveyer related parts (markets addressable by Thejo) is to the tune of Rs3.5-4 bn and Rs7 bn, respectively (they have other business segments as well). Both these companies market share is not dominant. Thejo sells (FY24) Rs700-800 mn worth of conveyer related parts; this implies that there is ample room for Thejo to drive growth in this product segment.
  - Filtration plant spares – Lot of mines where ore is transported in form of slurry for processing (for example iron ore mines) require filtration plants which de-water the slurry and return the cleaned water back into circulation. These plants use a lot of spares (rubber, polyurethane, high performance plastics and metal parts) which get worn off with use and need to be replaced. Options for a mine operator are:
    a) Buy the parts from OE (Metso is dominant) which supplied the filtration plant; OE's typically charge a premium for replacement parts.
    b) Buy the parts from dependable players like Thejo who can supply similar quality parts at a discount to the OE. Filter press parts are high value added (and critical as well) and hence the client needs to have 100% confidence on the quality systems of the vendor. In our view, Thejo has been able to establish itself in this market as it gained understanding of these parts as it was supplying (earlier not now) the same parts to Larrox/Metso which is the most dominant OE, globally in this product.

    As per our understanding, Thejo sells Rs550 mn (FY24) of filtration spares across 2-3 major clients, globally. Given the limited number of accounts/mines the company is servicing as of now we would presume that growth run way for the company is pretty long as of now.

  - Our confidence on Thejo's ability to scale this business comes from the fact that its products (filtration spares) have been tested by some of the largest names in mining, globally, at some of their largest mines in operation and are already being supplied on commercial basis. For example – Carajas mine (production capacity ~80 mn tons of iron ore per annum) of Vale (Brazil) is one of the clients in this business.
  - We would presume that this segment of products is also growing, globally, at 3-5% CAGR in line with any other mining consumable product.
- Thejo is also into rubber and composite mill liners though this segment is not a focus area in the next 1-2 years. As per reports on Tega Industries, total global mill liner market is ~US$2.2 bn (CY23), out of which ~US$ 380 mn is rubber and ~US$ 600 mn is composite liners, which are addressable markets for Thejo. Rubber mill liners are a relatively mature product hence growing at 2% CAGR. Composite mill liners are replacing steel liners in some of the applications and hence are growing faster (~7% CAGR).
  - As of now, liner revenues for Thejo are mainly from rubber liners. Company's rubber liners have been tested thoroughly and are in commercial use even in mines outside India.
  - Composite liners is a recent (last 2-3 years) addition to the portfolio. The company has been testing the product in India and has also deployed it commercially (in India mainly and recently in Australia and South America). As per the mgmt., product feedback is good and hence it is ready to start scaling this product outside India as well.
- Services business is India(~70% of total service sales) centric. The addressable market for Thejo in India is mainly services related to maintenance and repair of conveyer belts. Thejo prefers to take maintenance/repair service contracts mostly if it involves use of its own products; it comprises almost 70% of its service business. In its addressable markets, Thejo's market share in India is pretty high (60-70%) and hence scope for growth in India is not much; this business would grow in line (10-12% CAGR given underlying 7-8% CAGR growth in production of metals) with the overall industry volumes in India. Only way to drive growth is to try and expand the business outside India. However, for our investment case we have not built any significant growth acceleration in this business.
  - Rest 30% of the service business is pure O&M in which Thejo is responsible for day to day operations of a part (conveyer belt or any other part) of the plant, promising to maintain a certain minimum performance parameters. This does not involve sale of any of company's products. This part of the service business is commoditized and Thejo takes this kind of work only on insistence of the client. In its annual reports, the mgmt. always mentions that (O&M only) service business is non -differentiated and there is always pressure on margins, especially in India, where clients view it as a manpower outsourcing contract (cost plus). Hence, in its current form, it seems that growth prospects of O&M services business are limited in India.

Nature of the business

- In our view, product business of the company has high entry barriers –
  - Clients don't shift vendors for 5-10% lower price; price is not the starting criteria at all. Clients accept a new vendor very selectively only if – a) client is facing problems in existing vendors or is desperate in some other way, for example, plant need to restart

asap after a disruption, b) quality is proven (at a small commercial scale is also ok) and pricing is lower versus existing vendors. Reasons:

a) The products are essentially consumable spares which go into critical parts of the plant – conveyer belts and filtration plant for example,
b) Value of these spares is almost negligible (< 1%) compared to the turnover of the client. Clients are extremely sensitive to the quality of the product being supplied. Any problem in the product could lead to shutdown of the conveyer belt/filtration plant/mill, which could lead to shutdown of the entire plant implying huge losses for the client.

- The products are difficult to develop considering –
  - Products need to be customized (some changes in the formulation of materials involved) as per operating conditions on client site.
  - Product chemistry (rubber formulations etc) or specs are difficult to get 100% right for somebody new, as there is not much scope for trial and error given limited opportunity for on-ground trials on client sites. Also sustained investments in product development and R&D are required to be able to tweak products as per changing client requirements or operating conditions on the ground.
  - Number of SKUs is high and one needs a basket of products to sell to a client. It is difficult for a client to engage with a new vendor just for a limited set of products.
- Being able to manufacture good products is not the only criteria driving success in this business. The business is a combination of precision manufacturing and a strong sales and service organization, both of which need to perform in tandem to be able to get business from a client.
  - Products are of non-bulk nature. They need to be customized as per mine or plant specs. Technical service/sales teams on the ground need to be competent to understand local conditions and define product specs accordingly.
  - Product development and R&D teams should be able to tweak products as per requirements on the ground.
  - There needs to be solid service support on the ground close to the site of client operations so that any maintenance requirement can be serviced quickly. For the client it is extremely important that servicing is quick as each hour of plant/mine shutdown implies huge losses. Hence, a well-trained technical service team which can reach client site within defined timelines, is a must.
  - Sales reps require technical know-how to be able to position the product in the right manner; pricing as a variable of discussion comes only after the technical sales process is over.

Given customization involved in manufacturing and element of service attached with the product, this business has requirement for better quality of labor/employees and hence the business is inherently difficult to build. Requirement of quality manpower is amply visible in the employee cost to sales ratio for Tega (Thejo's product business is similar) which has ranged around 10% (standalone) of sales in the last few years. This is versus 5-7% for some of the bulk manufacturing businesses like Apollo Tyres, CEAT, Amara Raja Batteries etc.

Cost structure of Tega, consolidated, March fiscal year-ends (%)						
Margins						
Gross profit	3,764	4,110	4,817	5,491	6,864	8,472
Gross margin (%)	**59%**	**60%**	**60%**	**58%**	**57%**	**57%**
EBITDA margin (%)	**15%**	**16%**	**23%**	**19%**	**22%**	**21%**
Expenses as % of sales						
Raw Material Consumed	41%	40%	40%	42%	43%	43%
Power & Fuel Cost	3%	3%	3%	3%	3%	3%
Employee Cost	18%	17%	15%	15%	13%	15%
Other Manufacturing Expenses	6%	6%	5%	5%	5%	5%
General and Administration Expen	11%	11%	9%	11%	9%	8%
Selling and Distribution Expenses	1%	1%	1%	1%	1%	1%
Miscellaneous Expenses	5%	7%	4%	4%	3%	4%

    - In our view, entry barriers mentioned above would have worked against Thejo as well, hence it might seem very surprising that a small company has been able to position its products against global companies and win business. This might also lead someone to believe that entry barriers are not as significant as pointed out above. In our view, Thejo has been able to establish itself in the product business despite all odds on account of its close touch with its clients through its services business. Thejo's employees are there in client's plant 24X7 running critical facilities and hence the client has confidence that if anything goes wrong with the product, he has somebody from Thejo to catch, who will address the problem quickly. Thejo has used this close client connect to push its clients to try its products commercially and hence was able to prove quality credentials which has led to scaling up of its products vertical.

- We haven't done much work on pure services part of the business as we view the business as not so critical to our long-term investment case on the business. We are primarily banking on the product business to drive growth in the long term. However, here are our thoughts on the business.
    - Technical services (mainly repair and maintenance) involving some element of product sales is a good business as it helps to push high margin products. We expect this business to grow at 10-12% CAGR (in line with growth in production volume growth of 5-7% CAGR, mainly in iron and steel, in India). We are assuming higher growth versus underlying growth in volumes on account of inflation in HR cost which is significant part of cost structure of this business.
    - As explained above O&M service is perceived as low value-added offering by clients and hence, we don't expect Thejo to scale this business in any significant manner, in its current form. The company is trying to re-position this business in a manner which has the potential to boost growth and margins. It is trying to include supply of spares and equipment, manufactured by Thejo, as part of the contract. Since this is a new sales approach, it could take time to gain acceptance from clients (if at all) and hence we are not assuming any positive impact of the same and in our view, this business should grow at mid/high single digit in the long term.
    - Given that services business does not require any capital deployment except working capital, we would presume that the service business is not dilutive to the overall ROCE of the company.
- In our view, margins should be stable and in the long term, overall business should be able to generate a good ROCE (pre-tax of ~25% and above even when business scales up). Tega Industries, which is a similar business as Thejo but more scaled one (it has a decent market

share globally in rubber and composite liners), has delivered average pre-tax ROCE (ex-goodwill) of ~23% in the last few years. Thejo's pre-tax ROCE has averaged much higher around ~34% in the last 5 years. In our view, that could be on account of –

- It has services business as well, which does not need any capital investments apart from working capital, which might be increasing the overall ROCE.
- Thejo has been built as a scrappy organization. It is easier to achieve this this at a lower scale.
- Scale of the business is small and hence it is possible to choose business with higher margins in mind.

In our view, as Thejo scales up, some of the above advantages it enjoys might not remain and hence, there is a decent probability that ROCE should start trending towards its more mature peer (Tega), in the very long term (10 years); however, in our investment horizon of 3-5 years, pre-tax ROCE should remain ~25% atleast, in our view. We will not be worried (in case ROCE starts trending down) as long as pre-tax ROCE remains around ~25% and the company is able to drive growth (sales) at ~15% CAGR in the next 3-5 years.

Capital efficiency parameters for Tega

Working capital (Rs mn)	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**
Inventories	1,211	1,326	1,586	2,521	2,896	3,701
Sundry debtors	2,103	1,852	2,209	2,765	4,031	4,473
Other current assets	216	232	191	221	120	180
Short term loans and advances	270	246	195	320	492	436
Trade payables	807	653	987	967	1,119	1,834
Other current liabilities	874	825	982	1,207	1,390	2,418
Working capital (no. of days)	**122**	**116**	**100**	**140**	**151**	**111**
Inventories	70	71	72	97	87	91
Sundry debtors	121	99	100	106	121	109
Other current assets	12	12	9	8	4	4
Short term loans and advances	16	13	9	12	15	11
Trade payables	46	35	45	37	34	45
Other current liabilities	50	44	44	46	42	59
Cash flow parameters						
Operating cash flow (ex. Interest)	461	1090	1565	30	1620	2217
Capex	-262	-278	-486	-410	-922	-554
FCF	**200**	**812**	**1079**	**-380**	**698**	**1663**
Asset turns (x)	**1.66**	**1.75**	**1.73**	**1.92**	**1.13**	**1.27**
ROE (%)	8%	14%	22%	16%	18%	16%
ROCE (%)	12%	14%	27%	20%	21%	23%
ROCE (%) (ex. goodwill)	13%	15%	30%	22%	22%	24%

Capital efficiency parameters for Thejo	2019	2020	2021	2022	2023	2024
Working Capital (in Rs mn)	**610**	**836**	**721**	**1,017**	**967**	**1,323**
Inventories	362	339	382	522	590	625
Sundry debtors	639	1,012	927	1,066	1,080	1,356
Other current assets (inc. short term loans)	124	137	197	183	269	308
Trade payables	252	277	399	346	474	407
Other current liabilities	264	375	387	409	498	559
Working Capital (No. of days)	**97**	**100**	**80**	**87**	**74**	**86**
Inventories	58	41	43	45	45	41
Sundry debtors	102	122	103	92	83	88
Other current assets (inc. short term loans)	20	16	22	16	21	20
Trade payables	40	33	45	30	36	27
Current liabilities	42	45	43	35	38	37
Operating Parameters						
Asset turns (x)	**1.4**	**1.7**	**2.3**	**2.2**	**1.4**	**1.7**
Gross block	**814**	**846**	**554**	**856**	**1,436**	**1,593**

Note: For calculating asset turns, we have considered only product sales.

Investment rationale

- We see strong growth (atleast 15% CAGR) in the product business which would drive strong growth in earnings.
  - Over the last 5-10 years, Thejo has made significant investments in developing products and has been able to sell some of the high value added products (filtration plant spares, diaphragms etc) to some of the largest miners in the world.
  - Some of the large miners to whom Thejo is supplying its products are – Vale, Econdida (world's largest copper mine operated by BHP), Rio Tinto.
    - Thejo sells filtration press parts (set of 20-24 parts) to Escondida. It got the first contract in 2017. This became a good reference point when Thejo pitched for business from other clients. Thejo could establish its quality credentials in this account as it used to supply the same parts to Larrox (OE for filtration solutions; acquired by Metso) which was an OE supplier to this mine.
    - Vale wanted to restart its filtration plant at one of its largest iron ore mines. This is after Vale had suffered a major accident (2019) in one of its mines in Brazil. OE supplier Larrox (Metso) was the only option at that point for Vale. Thejo bid for this order and given- a) its good reference from Escondida, b) comparable product quality to Larrox and c) good pricing, it got the order. Vale has also been giving orders for some of the other high value-added products (diaphrams) to Thejo.

- In our view, given that credentials of Thejo, have been established with some of the biggest miners in the world since the last couple of years, it has the possibility of opening up big opportunities by way of –
    - Cross- selling other products to existing clients. Products Thejo has sold to some of its large clients (mentioned above) are high value added products (within its product basket) and hence we would assume that quality/service credentials are already established. Given that these accounts are some of the largest in the world in the addressable segments, in our view, there is significant scope to increase revenues from these accounts.
        - There is significant scope to increase market share in these accounts in the products being supplied currently as Thejo is supplying materials to only few of the mines of these companies. Given established quality/service credentials and value proposition (good price as well), Thejo should be able to increase market share in existing product segments as well.
    - Given that Thejo products have been commercially tested at some of the biggest mines of global mining giants, it should open doors for the company at other mining companies as well.
- Our confidence on Thejo's credentials (product quality/service) in the product segment comes from –
    - Marquee names in the mining industry are giving recurring orders in preference to some of the big global brands in mining consumables.
    - Products are being used in some of the largest mines in the world.
    - Our channel checks (limited) at some of the large steel companies in India indicate very positive feedback on product (related to conveyer belts) quality.
        - One of the large private sector steel companies in India mandates the use of Thejo's conveyer belt spares and adhesives to any company doing O&M for the conveyer belt.
        - Thejo has got 50-60% market share in adhesives (used to repair conveyer belts) in India. The other dominant player is Rema Tip Top which is a German company. Adhesive (to be used on conveyer) is a high technology product in our view. Hence, even though the product is small (~Rs400 mn sales in FY24), the fact that Thejo has been able to develop and commercialize it organically, says a lot about the quality of internal R&D and product development capabilities.
    - Thejo has gained significant knowledge about its products as it has been supplying these to some of the largest global players in mining equipment and spares like Metso (not sure if Metso is still a client).
    - As per the mgmt., Thejo has developed all the products grounds-up and hence its product development team is quickly able to pin-point source of problem (in case of any issue on the ground) and quickly rectify it.
- There is a large growth opportunity in the rubber and composite liners market. As mentioned above, global market in rubber and composite mill liners is US$380 and US$600 mn (CY23), respectively. Thejo's market share as of now is negligible and hence there exists a significant opportunity to drive growth for the company in the long term. As of now, liners is not a focus area for the company, however, in the long term the company would start getting aggressive in this segment as – a) it is a large volume market globally, b) it helps in building quality credentials in other products as well.
    - Company's product in rubber liners is established as it has been tested commercially in and outside India.

- The company has been working on composite liners (steel + rubber) since the last 3-5 years. It has tested the product commercially in India and is now confident of launching the same in international markets. The company has taken a different view towards development in this product –
  - The leaders (Tega and Metso) buy Hardox steel from Austria and bind it with internally developed rubber to create a composite offering.
  - Tega has developed its own proprietary steel castings to be used in composite liners and hence if the product is commercially successful it have more value add (contribution margin) in the product versus the leading companies.
- The company has been tying-up with dominant equipment (mills) suppliers, to supply rubber/composite liners for their equipment.

Slides from the company presentation elaborating on growth strategies

Opportunities for Growth – Key Drivers

Product Category	Product Type	Current Situation	Opportunity	Market
Mineral Processing	Mill Liners – Rubber	Focus of sale limited to India, with few international clients and focus on export markets	Extend presence and sales to international markets	Untapped markets of South America, Australia, Africa, North America
	Mill Liners - Composite	Established increased inhouse production capacities, and supply arrangements with foundries/alloy metal plate manufacturers for special compositions of casting for higher life expectancy	Large SAG Mills which are the primary users brought into scope of sales.	South America, Australia, Africa, North America
	Wet Abrasion Resistant Sheeting	Market leadership is held by Weir and many companies today offer substitute sheeting. We need to compete on price to secure larger share of the market.	Sufficient product capacity available inhouse.	Global
	Cyclones & Replacement Spares	Technical competence and capability for manufacturing cyclone spares available but not focused on this business.	Supply partnership with established Cyclone manufacturers, ensuring higher capacity utilization of production capacities.	Australia, South America, Africa & India

Opportunities for Growth – Key Drivers

Product Category	Product Type	Current Situation	Opportunity	Market
Mineral Processing	Filter Press Rubber Spares	Large range of Rubber Membranes, seals and other spares established in the market.	Developing latest models of Rubber membranes for established leaders in the filter presses	Global
	Filter Press non-rubber spares	Initial supply of non-rubber spares developed and trailed have been very successful.	Expanding the range of products to cover engineering plastic's and steel component spares widens the scope of business in press filter	Global
	Screens and Screen Spares	Spread of clients for the product across the market is thin. Limited long-term supply contracts. Price sensitivity is high. MOU with Screen design expert for manufacture of Screening machines is underway.	Consumable requiring periodic replacement. To pursue supply contracts for longer term. Focus on Dewatering screen panels.	Australia, South America, North America and Africa
	Pinch Valve Sleeves	Possess the technical expertise and manufacturing capabilities required for the design and production of pinch valve sleeves. Currently has supply contracts with few global leading valve manufacturers.	Explore expansion of product range and further supply partnership with established manufacturers.	Global

Opportunities for Growth – Key Drivers

Product Category	Product Type	Current Situation	Opportunity	Market
Bulk Material Handling	Cold Vulcanising Adhesive	Focus of sale has been limited to India and very few global markets. We have already ramped up production by 80% in the	Quality of our product being comparable with the best, we intend to extend sales to more markets through distributors	North & South America, Australia, Middle East, and Africa
	Lagging Sheeting	Offers the complete range of Rubber lagging sheets primarily in India. Have also established Ceramic lagging and polyurethane solutions.	There is huge demand in the global market. Capability of supplying cold adhesives makes opportunity better.	Global
	Vulcanizing Machines	Offers both hydraulic and pressure bag type vulcanizing presses. Being an end user of these presses, it has helped in better design and continuous improvement of the presses.	Matching leading suppliers in quality and technology at competitive prices, gives good scope of business.	Australia, Africa, Middle East, America
	Belt Handling Equipment	Offers customized products for clients in India, Australia and Middle East.	Quality product offered by us at competitive prices should give us enhanced sales opportunities.	Global

Opportunities for Growth – Key Drivers

Product Category	Product Type	Current Situation	Opportunity	Market
Bulk Material Handling	Conveyor Belt Accessories	Offers complete range of IP protected products in belt cleaning, belt tracking, belt impact cushioning, and blet spillage control.	Quality of products being comparable with the best in the world, we intend to extend sales to more markets through a wide distributor network.	Global
	Air Blasters for Flow promotion	Late entrant into the industry. Possess an IP product that has registered superior performance against competition. Primarily focused on replacement market and not Projects.	With the IP product and domestic production of superior technology product, we enjoy a price advantage over global competitors. To focus on the potential project orders, for cement industry.	Global
	Intelligent Belt Monitoring Systems	Combined offering of products from inhouse with that of our partners ROXON-Finland and RMS-South Africa is an innovative approach in India.	Competition is limited in the specific areas that are currently being addressed by THEJO under IBM.	India, Middle East, Australia, Africa

Opportunities for Growth – Emerging Markets

Africa

- **Copper:**
  - Zambia and the Democratic Republic of Congo (DRC) are significant players in copper mining. The DRC alone produced 1.6 million metric tons of copper in 2022.
- **Cobalt:**
  - The DRC is also the largest producer of cobalt, accounting for over 70% of global production.
- **Gold:**
  - Ghana and South Africa are major gold producers, with Ghana producing 130 metric tons in 2022.

Latin America

- **Lithium:**
  - Chile and Argentina are key players in lithium production. Chile produced 18,000 metric tons of lithium in 2022, making it one of the largest producers globally.
- **Copper:**
  - Chile is the world's largest copper producer, with an output of 5.7 million metric tons in 2022.
- **Gold:**
  - Peru and Mexico are significant gold producers, with Peru producing 128 metric tons in 2022.

Asia-Pacific

- **Nickel:**
  - Indonesia has emerged as a leading producer of nickel, with production increasing from 34% to 52% of the global share between 2020 and 2023.
- **Iron Ore:**
  - Australia is a major player in iron ore production, with an output of 880 million metric tons in 2022.
- **Rare Earth Elements (REEs):**
  - China dominates the production of REEs, accounting for over 60% of global production.

North America

- **Lithium:**
  - The United States is ramping up its lithium production, with significant investments in new mining projects.
- **Copper:**
  - The U.S. produced 1.2 million metric tons of copper in 2022, with significant reserves available for future exploitation.
- **Gold:**
  - The U.S. is also a major gold producer, with an output of 200 metric tons in 2022.

Europe

- **Lithium:**
  - Portugal is emerging as a significant player in lithium production, with increasing investments in mining projects.
- **Nickel:**
  - Finland and Russia are notable producers of nickel, contributing to the region's growing importance in the global market.

- Earnings growth should be higher than growth in sales driven by operating leverage.
    - Over the last 5 years, Thejo has made significant investments into building an organization in places like Brazil, Australia, Saudi Arabia etc; however, business from these new geographies is still in the process of reaching an adequate scale. Hence, there is operating leverage inherent in the business which would be realised with product sales growing at ~15% CAGR or more. Hence, we expect earnings growth to be a bit higher than growth in sales.
    - Another way to create a perspective on operating leverage is that outside India business of the company is sparse –
        - There are limited clients in each geography.
        - Existing clients are buying limited products from Thejo, both in terms of value and SKUs, versus their overall procurement of those products.

      Hence, as the company adds more clients in the same geography and existing clients scale up, the costs which are being incurred in sales and marketing and servicing won't increase as much and hence creating a trend of improving margins with rising product sales.

- Thejo is a quality manufacturing business which ticks all the boxes in our framework of investing into manufacturing in India.
    - Nature of manufacturing is not bulk. The company manufactures lot of SKUs which are customized as per clients' requirements.
    - Entry barriers are high as explained above.
    - As explained above, this business has requirement of better quality labor/employees and hence difficult to build.
    - ROCE and FCF characteristics are good; growth can be comfortably funded by internal accruals. Given that we don't have enough information to segment the balance sheet of Thejo into products and services, we demonstrate our point through financials of Tega. Tega's pre-tax ROCE (ex – goodwill) has ranged upwards of 20% in the last few years and cash flow from operations has been more than enough to fund the required capex to sustain growth at ~15% CAGR.

<u>Perspective on valuation and potential returns</u>

The stock is quoting at ~51X trailing EPS (FY24) and hence looks a bit expensive. However, our analysis suggests, that the company could be on cusp of a long-term growth cycle; we expect sales and PAT growth of 15% and 15-20% CAGR, respectively in the next 3-5 years. Hence, given – a) expectation of good earnings growth, b) good business characteristics in terms pre-tax ROCE (average ROCE of >30% last 5Y) and FCF, c) good promotors, and d) scope for consistent growth even beyond our investment horizon of 3-5 years, we are comfortable with the current valuation. In our view, the stock would compound in line with earnings growth.

<u>Risks</u>

- Metal prices have been correcting across the board and steel and iron ore markets seem to be particularly impacted on account of lack of demand in China. Given Thejo is a very small player in the global markets it might be difficult to gain market share when the overall macro environment in the underlying market is weak. Hence, our growth story could fall apart in the short to medium term till the time underlying market remains weak. One could argue both ways on the growth angle –

  - Thejo could still grow at the projected rate despite the market as its market share is insignificant and hence market reverberations might not impact it at all.
  - On the other hand, weak macro environment could lead clients to stall projects or reduce production. Also, global competitors might become more active in defending their market share by lowering prices.

  We have no view on which way things will swing in case of Thejo, nevertheless, we view slowing macro as a risk.
- In our view, Thejo is in the initial stages of product acceptance outside India. Though the company has been supplying products on commercial basis since the last few years, there exists a risk that a problem with product performance could set its growth journey back a few years.
- Thejo is a very small player in the global market. Size of its P&L is pretty small. Hence, it could be constrained in its ability to deploy expensive human resource (sales, service etc) to grow its business outside India. It could happen that the company might need to take a call on either – a) growing the business (outside India) by making investments which could constraint its margins or b) protecting its margins in the short/medium term and compromise on growth. Hence, probability exists that the company might disappoint on margins and hence growth in earnings could be lower than our estimates. From our perspective, we would prefer if the company prioritizes growth over margins and hence from the perspective of our investment case, we would benchmark the company's performance on growth in sales in the product business and would ignore any disappointments on margins in short/medium term.
- As per our understanding, Thejo's service organization outside India, particularly in LATAM is not well developed as scale of the business is not as much to afford a service organization which is at par with its global competition. In the long term, the company would need to invest significantly to build its service organization outside India in order to achieve the growth rates which we are projecting, otherwise growth rate itself won't materialize. In some cases, such investments might need to be done in anticipation of the business which might or might not come. From our point of view, we hope that the company is able to make these investments, otherwise our growth projections in all probability won't materialize.

Financial summary, consolidated, (Rs mn)

P&L, March fiscal year-ends (Rs mn)	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**
Sales	2,295	3,039	3,271	4,245	4,745	5,594
EBITDA	315	488	498	685	592	1,003
EBITDA (%)	**14%**	**16%**	**15%**	**16%**	**12%**	**18%**
Other income	11	6	31	15	34	32
Depreciation	65	63	88	105	122	204
EBIT	250	424	411	580	470	798
PBT	216	384	405	563	458	766
PAT	148	304	294	425	348	594
PAT (after minority interest)	134	251	265	376	324	556
EPS	39	73	75	35	30	52
Balance sheet						
Equity	837	1,130	1,440	1,857	2,195	2,726
Debt	310	357	99	166	159	142
Current liabilities	516	652	786	755	972	966
Other non-curent liabilities	-0	-1	70	232	298	276
Total sources of funds	**1,663**	**2,138**	**2,395**	**3,009**	**3,624**	**4,109**
Fixed assets	336	318	460	662	1,119	1,084
Current assets	1,276	1,770	1,880	2,275	2,459	2,971
Cash	151	282	374	504	520	682
Other non - current assets	50	51	55	72	45	55
Total uses of funds	**1,663**	**2,138**	**2,395**	**3,009**	**3,624**	**4,109**
Cash flow statement						
Cash from operations	154	148	486	242	540	454
Capex	-68	-49	-131	-147	-494	-225
FCF	86	100	355	95	46	229
Return ratios (%)						
ROE	16%	22%	18%	20%	15%	20%
ROCE (pre-tax)	25%	35%	35%	38%	26%	37%

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