

RETAIL EQUITY RESEARCH

Chemcon Speciality Chemicals Limited.

Specialty chemicals

Sensex: 38,846

Nifty: 11,505

SUBSCRIBE

Price Range Rs. 338 - Rs. 340

A Niche player...at fair valuations

Chemcon speciality chemicals Ltd (CSCL), was incorporated on December 15, 1988 at Vadodara, Gujarat, India. CSCL is a leading manufacturer of specialised chemicals such as HMDS (Hexamethyldisilane) & CMIC (Chloromethyl isopropyl carbonate) which are predominantly used in pharmaceutical industry (pharmaceuticals chemicals) and inorganic bromides, predominantly used as completion fluids in the oilfields industry (Oilwell completion chemicals). CSCL's manufacturing facility is located at Manjusar, Vadodara, Gujarat.

- CSCL is the only manufacturer of HMDS in India and 3rd largest manufacturer of HMDS worldwide (as per Frost & Sullivan report) in terms of CY19 production with an opportunity to grow at CAGR of 15-20% over FY19-FY23.
- CSCL is the only manufacturer of zinc bromide and the largest manufacturer of calcium bromide in India in terms of production in CY19.
- Well positioned to substitute the imports from China and has an opportunity to grow total revenue at a CAGR of more than 25% between FY19-FY23.
- Strong customer base & long standing relationship with customers has supported in retaining CSCL's market share, increasing product base and reaching out to new customers.
- Revenue & PAT grew at a CAGR of 29% & 36% respectively over FY18-20.
- Has healthy balance sheet with stable cash flows, net debt is Rs.44cr with D/E ratio of 0.3 in FY20.
- At the upper price band of Rs340, CSCL is available at P/E of 25.5x on FY20, which is attractive when compared to peers. Considering healthy business performance, regular capacity expansions, strong customer base, expanding margin profile and improving outlook for the sector, we have a 'SUBSCRIBE' rating on this IPO.

Purpose of IPO

The proceeds from the offer for sale will go to the selling shareholders, while the amount received from the sale of fresh issue will be utilised to meet working capital requirement, capex towards expansion of manufacturing facility and general corporate purposes.

Key Risks

- ~30-35% of revenue comes from oil well chemicals, at a time when the oil sector is weak.
- Product portfolio is focused to Pharmaceutical and Oilwell completion chemicals, but we are very positive on pharma sector.
- ~59% of revenue from operations (FY20) is derived from top 5 customers.
- Procurement of raw materials from china. But the percentage of total expenditure is limited to ~20.5% in FY20.

Peer Valuation

Company	MCap (Rs cr)	Revenue (Rs cr)	EBITDA margin (%)	EPS	RoE (%)	P/E	EV/EBITDA
Chemcon Speciality	1,245	262	26.8	13	40	25.5	18.4
Aarti Industries	19,273	4,105	24.0	30	19	36.9	15.7
Vinati Organics	13,218	1,011	41.0	31	29	41.5	18.5
Atul Ltd	20,255	4,093	22.0	222	23	30.8	12.5
Paushak Ltd	1,344	138	31.0	105	17	41.5	10.9

Source: Geojit Research, Bloomberg; Valuations of Chemcon Speciality are based on upper end of the price band, Financials as per FY20

Issue Details			
Date of Opening	21 st September, 2020		
Date of Closing	23 rd September, 2020		
Total no. of Shares offered(cr)	0.94		
Post Issue No. of shares (cr)	3.7		
Price Band	Rs. 338- 340		
Face Value	Rs. 10		
Bid Lot	44 shares		
Minimum application for retail (upper price band for 1 lot)	Rs. 14,960		
Maximum application for retail (upper price band for 13 lot)	Rs. 1,94,480		
Listing	BSE & NSE		
Lead Manager	Ambit Capital Pvt. Ltd, Intensive Fiscal Services Pvt. Ltd.		
Registrars	Link Intime India Pvt Ltd		
Issue size (upper price)	Rs. Cr		
Fresh Issue	165		
OFS	153		
Total Issue	318		
Shareholding (%)	Pre Issue	Post Issue	
Promoters	100	74	
Others	0	26	
Total	100	100	
Issue structure	Allocation %	Size Rs.cr	
Retail	35	111.3	
Non -Institutional	15	47.7	
QIB	50	159	
Total	100	318	
Y.E March (Rs cr)	FY18	FY19	FY20
Sales	157	303	262
Growth (%)	-	93	-13.6
EBITDA	45	66	70
Margin%	28.7	21.8	26.8
PAT Adj	26	43	49
Growth (%)	-	63	13.5
EPS	7	12	13
P/E (x)	47.2	28.9	25.5
EV/EBITDA	27.9	19.3	18.3
RoE (%)	98.5	57.1	40.1

Company Description

Chemcon speciality chemicals Ltd(CSCL), was incorporated on December 15, 1988 at Vadodara, Gujarat, India. CSCL is a leading manufacturer of specialised chemicals such as HMDS (Hexamethyldisilane) and CMIC (Chloromethyl isopropyl carbonate) which are predominantly used in pharmaceuticals industry (pharmaceuticals chemicals) and inorganic bromides, predominantly used as completion fluids in the oilfields industry (Oilwell completion chemicals). As per *Frost & Sullivan report 2019*, CSCL is the only manufacturer of HMDS in India and third largest manufacturer of HMDS worldwide in terms of production. Further, CSCL is the largest manufacturer of CMIC in India and the second largest manufacturer of CMIC worldwide in terms of production according to *Frost & Sullivan report 2019*. CSCL manufacturing facility is located at Manjusar, Vadodara, Gujarat.

Revenue generation

CSCL earns revenue primarily from following categories.



Source: RHP, Geojit Research

Sale of Products: Revenue generated from the sale of products (~93% of revenue from operations in FY20) which includes sale of Pharmaceutical Chemicals and Oilwell Completion Chemicals, domestically and through exports (including deemed exports).

Job work services: Revenue derived from sale of services (~6% of revenue from operations in FY20) in the form of job work services to customers in India for the pharmaceutical sector.

Other Operating revenues: Other operating revenues includes export incentives, lifting charges, sales commission and miscellaneous income received by the company.

Revenue segmentation as follows:

Particulars	Revenue from sale of products			Revenue from sale of Services		
	% of revenue from operations			% of revenue from operations		
	FY18	FY19	FY20	FY18	FY19	FY20
Pharmaceutical chemicals	59.2	60.2	57.4	2.98	2.9	6.3
HMDS(including ancillary Products)	38.5	40.4	43.8	2.9	2.6	6.3
CMIC	20.7	15.7	12.9	0.0	0.0	0.0
Other pharma chemicals	0.0	4.2	0.7	0.1	0.3	0.0
Oil well completion chemicals	35.6	35.3	33.5	0.0	0.0	0.0
Total(excluding others)	96.6	96.8	93.2	3.0	2.9	6.4

Source: RHP, Geojit Research

Strong customer base coupled with long standing relationships...

CSCL top five customers and top ten customers contributed ~59% and ~72% respectively to revenue from operations in FY20. The key customers of Pharmaceutical Chemicals include Hetero Labs Limited, Laurus Labs Limited, Aurobindo Pharma Limited etc and the key customers of Oilwell Completion Chemicals include Shree Radha Overseas, Water Systems Specialty Chemical DMCC and CC Gran Limited Liability Company. 68.6% of total revenue from operations in FY20 was contributed by customers who have been consistently purchasing products over the last five years. Top seven customers for FY20 have been customers of CSCL for over four years. Chemcon supplies its products to domestic customers and also exports to countries including USA, Italy, South Korea, Germany, China, Japan, UAE, Serbia, Russia, Spain, Thailand and Malaysia.

Particulars	Pharmaceutical chemicals			Oilwell completion chemicals		
	% of total revenue from operations			% of total revenue from operations		
	FY18	FY19	FY20	FY18	FY19	FY20
Domestic sales	43.6	47.4	53.5	6.7	19.1	3.9
Export sales*	18.6	15.7	10.2	29.0	16.2	29.6
Total	62.2	63.1	63.8	33.5	35.3	35.6

* Includes deemed exports

Source: RHP, Geojit Research

CSCL has derived ~40% of revenue from operations from exports (including deemed exports) in FY20 and has grown at a CAGR of 17.6% over FY18-FY20. Hence, the strong customer base and long standing relationship with customers has supported in retaining CSCL's market share, increasing product base and reaching out to new customers.

Focus on expanding into new markets...

CSCL aims to capitalise on the potential growth of the HMDS and CMIC market in India by expanding manufacturing and sales of HMDS and CMIC. India is a net importer of CMIC and HMDS (as per Frost & Sullivan Report) and the company aims to expand manufacturing and sales operations of CMIC and HMDS to substitute such imports. The trade dispute between the USA and China, may impact China's HMDS exports to the US. The company has already started supply of HMDS to US customers, utilising the opportunity created due to the trade dispute. CSCL aims to expand the sales of the Oilwell Completion Chemicals in existing and new geographies including Nigeria, Malaysia, China and Ghana.

Manufacturing facility with dedicated plants & focus on capacity expansion...

The company currently has seven operational plants of which 2 plants are dedicated to manufacturing of HMDS & ancillary products (including one plant dedicated for hi-purity HMDS), 2 plants dedicated to the manufacturing of CMIC and 2 plants dedicated to the manufacturing of oilwell completion chemicals alongwith 3 warehouses for the storage of products and raw materials. The company has 5 leased warehouses located outside Manjusar facility. As of July 31, 2020, the installed capacity for: (a) HMDS was 4,200 MT per annum and HMDS (hi-purity) was 600 MT per annum; (b) CMIC was 1,800 MT per annum and; (c) Oilwell Completion Chemicals was 14,400 MT per annum, while total volumetric reactor capacity was 374.85 KL. CSCL is setting up two new plants with a total volumetric reactor capacity of 251.00 KL within the manufacturing facility. With the completion of such expansion, the total volumetric reactor capacity at the manufacturing facility shall increase from current volumetric reactor capacity of 374.85 KL to 625.85 KL.

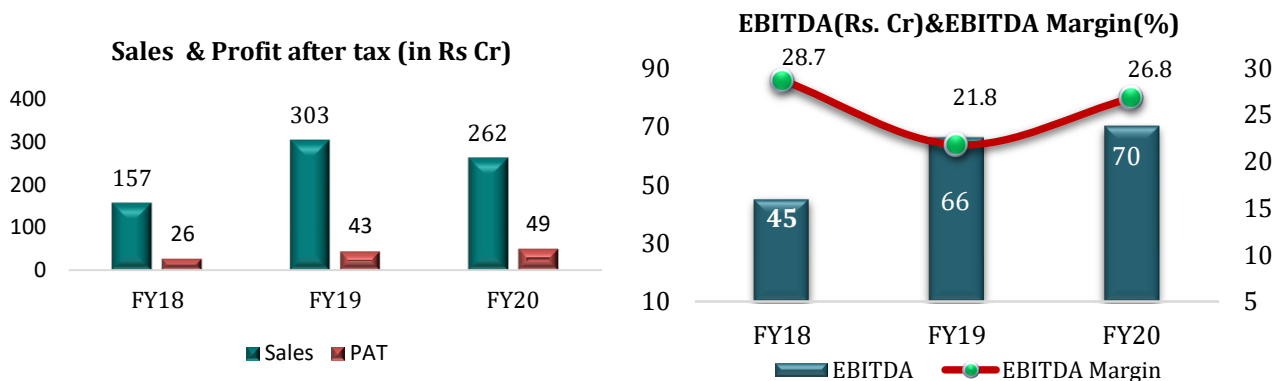
Product	Product Category	Plant	As on July 31, 2020	
			Installed Capacity (in MT per annum)	Volumetric Reactor Capacity (in KL)
HMDS and ancillary products	Pharmaceutical Chemicals	P-3	2,400	52.60
		P-7 ⁽¹⁾	1,800	125.20
		Total (P-3 + P-7)	4,200	177.80
HMDS (hi-purity)		P-2 ⁽²⁾	600	13
CMIC		P 4 & P 6	1,800	121.75
Calcium Bromide (Solution), Sodium Bromide (Solution) and Zinc Bromide (Solution)	Oilwell Completion Chemicals	P-5 ⁽³⁾	14,400	57.30
Calcium Bromide (Powder)		P-1 ⁽³⁾	600	5
Total Volumetric Reactor Capacity				374.85

Source: RHP, Geojit Research

The company intends to continue to be cost efficient in the production of its products. This efficiency is achieved through strategies like having a large single location manufacturing facility, dedicated plants for each product, process reengineering for efficient raw material consumption and being a sizeable player in the industry in each of the products. Economies of scale will also enable the company to continuously improve its operational efficiencies.

Robust financial performance...

CSCL has a track record of operations of over two decades and has a strong balance sheet with stable cash flows. The company has showcased sustained growth in various financial indicators including revenue and PAT, as well as a consistent improvement in the balance sheet position in the last three Financial years. Further, the company has been able to maintain low debt position on the back of healthy business performance. The total outstanding borrowings is Rs44.5cr while debt/equity ratio is 0.31 in FY20. The healthy business performance was on the back of regular capacity augmentation, diversification of customer base and optimizing costs of sourcing raw materials and other fixed costs.



Source: RHP, Geojit Research

Industrial Chemicals Market Overview

Global Market Overview

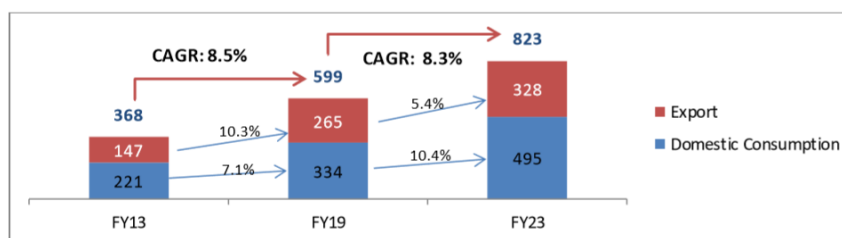
Pharmaceutical intermediates are the chemical compounds that form the building blocks used in production of active pharmaceutical ingredient (API). The global market of chemicals used as pharma intermediates was valued at about USD 27 bn in 2019 and is expected to grow at a CAGR of 4% between 2020 and 2023. North America is the biggest and most attractive market and benefits from the presence of major pharmaceutical companies and better infrastructure. It is anticipated to dominate the global market of chemicals used as pharma intermediates over the forecast period. Asia Pacific is anticipated to be the fastest growing market of chemicals used as pharma intermediates due to presence of large number of contract manufacturing organizations in the region.

India Market Overview

Domestic consumption for chemicals used as pharma intermediates is dependent upon bulk drugs manufacturing (domestic consumption as well as captive consumption by integrated players). Majority of large bulk drug players are forward integrated through presence in formulations as well. However, backward integration for large players through intermediates manufacturing is limited. The players in chemicals used as pharma intermediates domain mostly have footprints in specialty chemicals, which are supplied to pharmaceutical sector in addition to other sectors. CRISIL research estimates that domestic consumption of chemicals used as pharma intermediates remained at Rs~322 Bn (~USD 4.9 Bn) in FY19, growing at ~7% CAGR since FY13. During the same period, bulk drugs production (including exports) also grew at ~7% CAGR.

Outlook for Chemicals used as pharma intermediates

The overall market of chemicals used as pharma intermediates is anticipated to grow at 7-9% CAGR over the 5 year forecast period. Market for Chemicals used as pharma intermediates includes domestic consumption and exports. Exports (in Value) grew at ~10.1% CAGR between fiscals 2013 and 2019.



Source: CRISIL Research, Frost & Sullivan Analysis

Source: RHP, Geojit Research

Opportunities for growth of domestic manufacturers are: Government initiatives such as bulk drugs parks focussing on streamlining the pharmaceutical industry, Programs such as Jan Aushadhi Scheme: Private players can participate in such schemes through competitive tenders and use their operational GMP compliant sites to supply medicines, Shut down of Chinese chemical plants due to environmental concerns.

Oil Well Completion Chemicals Markets Overview

The oil and gas industry is experiencing its third price collapse in a decade. This time it is a combination of supply shock with an unprecedented demand drop. Globally there is a wide scale destruction of demand associated with COVID-19. In April 2020, for the first time in history, oil recorded negative prices. US oil benchmark West Texas Intermediate (WTI) recorded prices of negative ~USD 38. On the other side Brent Crude remains more stable and reached a multiyear low of USD 18 in the month of April. EIA expects monthly Brent spot prices will average USD 43 per barrel during the second half of 2020 and rise to an average of USD 50 per barrel in 2021.

The global clear brine fluids market can be segmented on the basis of products into potassium chloride, calcium chloride, sodium chloride, potassium bromide, sodium bromide, calcium bromide and others. Oil & gas sector is expected to be the most dominating end-user of the global clear brine fluids market and is expected to keep this trend over the estimated period. North America accounts for ~65% of the total clear brine fluids market and is expected to witness a significant growth in the forecast period. The government is increasing its energy security which will enhance the business growth for the market of the region.

The Asia Pacific accounts for ~15% of total clear brine fluids market and is likely to witness robust growth for clear brine fluids due to the presence of a number of shale reservoirs in the region. Also, the occurrence of various drilling activities in countries like India and China are boosting the growth of the clear brine fluids market.

The Middle East & Africa is a major region for the oil & gas industry. The region has large oil & gas reserves in regions like Libya, Syria, Egypt and others. The large presence of oil & gas reserves has augmented the growth of the market in the region. Latin America is expected to witness a moderate growth over the years to come owing to the emerging markets especially in countries such as Brazil, Argentina etc. in the region. Some of the major players operating in the global clear brine fluids market are Israel Chemicals Ltd., Albemarle Corporation, Chemtura Corporation (acquired by LANXESS), TETRA etc.

With crude oil prices at their lowest levels in nearly two decades, oil companies are safeguarding themselves by resorting to production cuts. Companies in US, Colombia, etc. have cut production and reduce exploration as crude prices stay at lower levels and production costs remain high. Many companies have also reduced their operations and cut-down on explorations. Many oil exploration companies have demobilised their technical staff and shut down operations due to the spread of Covid-19. Several new projects have been stalled across the globe to curtail spreading of pandemic. This has resulted in lower oil exploration and thereby impacting demand for Oil Well Completion Chemicals. The exploration activities are expected to bounce back in a phased manner beginning second half 2020 resulting in a better market outlook for oil well completion chemicals manufacturers.

Promoter and promoter group

Mr. KamalKumar Rajendra Aggarwal, Mr. Navdeep Naresh Goyal and Ms. Shubharangana Goyal are the Promoters of the Company. CSCL has ten Directors on Board, of whom five are Independent Directors. Of such Independent Directors, one Director is a woman Director.

Brief Biographies of Directors

- **Kamalkumar Rajendra Aggarwal** is the Chairman and Managing Director of the company. In the past, he was associated with CEPL in the capacity of director. He has more than 23 years of experience in the specialised chemicals industry. He has been on Board since January 19, 2004.
- **Navdeep Naresh Goyal** is the Deputy Managing Director of the company. He is currently associated with SILPL in the capacity of director (operations). He has more than 10 years of experience in operations. He has been on Board since April 1, 2015.
- **Rajesh Chimanlal Gandhi** is a Whole-time Director and the Chief Financial Officer of the company. In the past, he was associated with CEPL in the capacity of Accounts & Finance Manager. He has more than 20 years of experience in finance & accounts and related operations. He has been on Board since May 1, 2012.
- **Himanshu Purohit** is a Whole-time Director of the company. In the past, he has been associated with CEPL in the capacity of production manager. He has more than 20 years of experience in production related operations. He has been on Board since May 1, 2012.
- **Rajveer Aggarwal** is a Whole-time Director of the company. He is currently associated with Medicap Healthcare Limited in the capacity of director (operations). He has more than five years of experience in operations. He has been on Board since October 1, 2017.
- **Lalit Chaudhary** is an Independent Director of the company. He has been associated with Chaudhary Crains Private Limited as a director since 1993. He has more than 20 years of experience as an entrepreneur. He has been on Board since April 29, 2019.
- **Bharat Shah** is an Independent Director of the Company. In the past, he has been associated with Bank of Baroda in various roles. He has more than 37 years of experience in the financial services sector. He has been on Board since April 29, 2019.
- **Neelu Shah** is an Independent Director of the company. She has been engaged by “Dageena-the Jewellery Shoppe” since the year 2014, as a sales manager. She has 5 years of experience in sales. She has been on Board since April 29, 2019.

Consolidated Financials

Profit & Loss Account

Y.E March (Rscr)	FY18	FY19	FY20
Sales	157	303	262
% change	-	93	-13.6
EBITDA	45	66	70
% change	-	46.5	6.3
Depreciation	2	2.9	4.6
EBIT	43	63	66
Interest	3	4	5
Other Income	1	2	4
Exceptional Items	0	0	0
PBT	41	61	65
% change	-	51	6.1
Tax	14	18	16.1
Tax Rate (%)	34.9	29.7	24.8
Reported PAT	26	43	49
Adj	-	-	-
Adj PAT	26	43	49
% change	-	63.0	13.5
No. of shares (cr)	3.66	3.66	3.66
Adj EPS (Rs)	7	12	13

Cash Flow

Y.E March (Rscr)	FY18	FY19	FY20
PBT	41	61.2	64.9
Non-cash adj.	5.2	6.8	9
Changes in W.C	(31.5)	(56.9)	(63.0)
C.F.O	14.2	11.0	10.5
Capital exp.	(8)	(14.3)	(17)
Change in inv.	(0)	(10.3)	(2)
Sale of investment	0	0.8	1.0
Other invest.CF	0	0	1.0
C.F - investing	(8)	(24)	(16.6)
Issue of equity	0	0	0
Issue/repay debt	(3)	16.2	11
Dividends paid	0	0	0
Other finance.CF	(2)	(3.8)	(5)
C.F - Financing	(6)	12.4	6.5
Chg. in cash	0.6	(0.3)	0.4
Closing cash	0.9	0.6	1.0

Balance Sheet

Y.E March (Rscr)	FY18	FY19	FY20
Cash	1.5	12.0	14.0
Accounts Receivable	30.0	64.1	88.9
Inventories	21.0	46.0	48.1
Other Cur. Assets	12.0	8.0	20.0
Investments	2.0	2.0	1.9
Net Fixed Assets	29.6	39.5	47.4
CWIP	0.0	0.7	3.7
Intangible Assets	0.0	0.0	1.4
Other Assets	2.0	1.2	0.2
Total Assets	97	173	225.8
Current Liabilities	21.0	41.0	33.0
Provisions	5.0	1.0	1.0
Debt Funds	16.0	32.0	43.0
Minority Interests	0.0	0.0	0.0
Def. Tax	2.0	2.0	2.0
Equity Capital	8.0	32.0	32.0
Reserves & Surplus	46.0	65.0	115.0
Shareholder's Fund	54.0	97.0	146.0
Total Liabilities	97	173	225.8
BVPS (Rs)	15.0	27.0	85.0

Ratios

Y.E March	FY18	FY19	FY20
Profitab. & Return			
EBITDA margin (%)	28.7	21.8	26.8
EBIT margin (%)	27.3	20.8	25.0
Net profit mgn.(%)	16.8	14.2	18.6
ROE (%)	98.5	57.1	40.1
ROCE (%)	80.5	45.7	32.6
W.C & Liquidity			
Receivables (days)	69	56	107
Inventory (days)	99	66	115
Payables (days)	40	28	38
Current ratio (x)	2.5	3.2	5.1
Quick ratio (x)	1.5	1.9	3.1
Turnover & Lev.			
Net asset T.O (x)	5.3	8.8	6.0
Total asset T.O (x)	1.6	2.2	1.3
Int. covge. ratio (x)	14.1	15.8	14.0
Adj. debt/equity (x)	0.3	0.3	0.3
Valuation ratios			
EV/Sales (x)	8.0	4.2	4.9
EV/EBITDA (x)	28	19.3	18.4
P/E (x)	47.2	28.9	25.5
P/BV (x)	23.2	12.8	4.0

General Disclosures and Disclaimers

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We, Sheen. G and Rajeev T author(s) of this Report, hereby certify that all the views expressed in this research report reflect my personal views about any or all of the subject issuer or securities. This report has been prepared by the Research Team of Geojit Financial Services Limited, hereinafter referred to as Geojit.

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Geojit confirms that:

- (i) It/its associates have no financial interest or any other material conflict in relation to the subject company (ies) covered herein.
- (ii) It/its associates have no actual beneficial ownership greater than 1% in relation to the subject company (ies) covered herein.

Further, the Analyst confirms that:

(i) he, his associates and his relatives have no financial interest in the subject company (ies) covered herein, and they have no other material conflict in the subject company.

(ii) he, his associates and his relatives have no actual/beneficial ownership greater than 1% in the subject company covered

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