



Chemcon Speciality Chemicals

- Caters to pharma and oilfield industries
- The company is among domestic and global leaders in certain speciality chemicals

IPO Advise: :Over Long Tong Investors Can Subscribe Minimum Qty

- **Risk Moderate**
- **Return: Expect 40 TO 50% Over Long Term Likely**

Incorporated on December 15, 1988, Chemcon Speciality Chemicals is a manufacturer of specialized chemicals, used in the pharmaceutical and Oilwell industries. It supplies its products to domestic customers and as well as customers outside India. It is the only manufacturer of HMDS (Hexamethyldisilazane/Hexamethyldisilane) in India and the third largest manufacturer of HMDS worldwide in terms of production in CY19. The company is the largest manufacturer of CMIC (Chloromethyl Isopropyl Carbonate) in India and the second largest manufacturer of CMIC worldwide, in terms of production and capacity in CY19. HMDS and CMIC are predominantly used in the pharmaceuticals industry. Further, it is the only manufacturer of Zinc Bromide and the largest manufacturer of Calcium Bromide in India, which are predominantly used as completion fluids in the oilfields industry (the "Oilwell Completion Chemicals") in terms of production in calendar year 2019.

In the Fiscal 2020, 2019 and 2018, its Pharmaceutical Chemicals collectively contributed 63.75%, 63.14% and 62.18% of its total revenue from operations, respectively. Within Pharmaceutical Chemicals, HMDS (including ancillary products) in Fiscals 2020, 2019 and 2018, contributed 50.08%, 43.00% and 41.37%, respectively of total revenue from operations, while CMIC contributed 12.92%, 15.67% and 20.74%, respectively, of total revenue from operations. Further, in Fiscal 2020, 2019 and 2018, its Oilwell Completion Chemicals collectively contributed 33.47%, 35.30% and 35.63%, respectively of total revenue from operations.

Kamalkumar Rajendra Aggarwal, Navdeep Naresh Goyal and Shubharangana Goyal are Promoters. The company was originally incorporated as Gujarat Quinone Private Limited ("Gujarat Quinone") at Vadodara, Gujarat on December 15, 1988. Chemcon Engineers Private Limited ("CEPL") was incorporated at Vadodara, Gujarat on April 30, 1996. CEPL, a company largely owned and promoted by the Promoters and Promoter Group of Gujarat Quinone, merged into Gujarat Quinone approving the Scheme of Amalgamation between CEPL and Gujarat Quinone. The name of the company was changed to "Chemcon Speciality Chemicals Private Limited" on July 27, 2004.

The company exports to countries including United States of America, Italy, South Korea, Germany, People's Republic of China, Japan, United Arab Emirates, Serbia, Russia, Spain, Thailand and Malaysia. In Fiscals 2020, 2019 and 2018, revenue from exports (including Deemed Exports) contributed 39.78%, 31.99% and 47.84%, respectively of revenue from operations. Revenues from exports (including Deemed Exports) have grown at a CAGR of 17.57% between Fiscals 2018 and 2020.

The key customers of Pharmaceutical Chemicals include Hetero Labs Limited, Laurus Labs Limited, Aurobindo Pharma Limited, Sanjay Chemicals (India) Private Limited, Lantech Pharmaceuticals Limited, Ind -Swift Laboratories Limited, Vivin Drugs & Pharmaceuticals Limited and Macleods Pharmaceuticals Limited and the key customers of Oilwell Completion Chemicals include Shree Radha Overseas, Water Systems Specialty Chemical DMCC and CC Gran Limited Liability Company.

Its manufacturing facility is located at Manjusar near Vadodara in Gujarat. The company has seven operational plants of which two plants are dedicated to the manufacturing of HMDS and ancillary products (including one plant dedicated to the manufacturing of hi-purity HMDS), one multipurpose plant, currently being used for manufacturing of HMDS and other pharmaceutical chemicals, two plants are dedicated to the manufacturing of CMIC and two plants dedicated to the manufacturing of Oilwell Completion Chemicals, along with three warehouses for the storage of products and raw materials. It also has an in-house laboratory at its manufacturing facility to test procured raw materials as well as products at the various stages of the manufacturing process. Further, it has five leased warehouses located outside manufacturing facility, in Manjusar, Vadodara.

The primary raw materials essential to the manufacturing of HMDS are TMCS (Trimethyl Chlorosilane), Ammonia and Hydrochloric Acid. It principally uses TMCS as the base chemical for manufacture of HMDS. However, it also manufacture a portion of its HMDS production using HMDO (Hexamethyldisiloxane) as an input raw material, by converting HMDO into TMCS and then using TMCS to manufacture HMDS. HMDO is a residual product which comes out during the process of utilization of HMDS by its customers. The company purchase the key raw materials required for manufacturing HMDS from suppliers in China and India.

The primary raw materials essential to the manufacturing of CMIC are MCF (Methyl Chloroformate), IPA and Chlorine. The company purchase such raw materials from suppliers in China and India.

The raw materials essential for the manufacturing of Calcium Bromide (solution and powder), Sodium Bromide (solution and powder) and Zinc Bromide (solution) are primarily HBR, Bromine and lime.

Impact of COVID-19

Since some of the chemicals manufactured by the company find application in the pharmaceuticals industry, its Pharmaceutical Chemicals were categorized as 'essential goods' and its Manufacturing Facility was only temporarily shut during the pandemic from March 24, 2020 till March 31, 2020.

The reduced demand for oil and gas in Fiscal 2021 has resulted in a reduced demand for Oilwell Completion Chemicals. Accordingly, the company is yet to resume manufacturing new batches of Oilwell Completion Chemicals since the country-wide lockdown was lifted.

The Offer and the Objects

The offer comprises of a fresh issue of 4852941 equity shares at upper price band of Rs 340 and 4881657 equity shares at lower price band of Rs 338 aggregating up to Rs 165 crore by the company and an offer for sale of up to 45,00,000 equity shares, aggregating to Rs 153 crore at upper price of Rs 340 and Rs 338 crore at the lower price band of Rs 338 by the selling shareholders. The company will not receive any proceeds from the offer for sale.

The net proceeds of the fresh Issue are proposed to be utilized in capital expenditure towards expansion of its manufacturing facility amounting Rs 41.033 crore, to meet working capital requirements of Rs 90 crore and balance in for general corporate purposes.

As of July 31, 2020, installed capacity for HMDS was 4,200 MT per annum and HMDS (hi-purity) was 600 MT per annum, for CMIC was 1,800 MT per annum and for Oilwell Completion Chemicals was 14,400 MT per annum, while our total volumetric reactor capacity was 374.85 KL.

The company is setting up two new plants and one laboratory, at its existing manufacturing facility at Manjusar, Vadodara. The company intends to build two additional plants with a total volumetric reactor capacity of 251.00 KL and one laboratory, out of the net proceeds of this Issue.

Strengths

India is currently a net importer of HMDS, with about 40% of India's domestic demand in CY19 being catered by imports majorly from China and Germany. India is expected to witness a demand growth for HMDS of 10.6% CAGR between CY19 and CY23. Chemcon Speciality Chemicals is the only manufacturer of HMDS in India.

Other countries of the world are dependent on China for their HMDS requirement. However, with changing environment regulations, the trade from the country is low, giving opportunity to Chemcon to target China's export customer base. Frost & Sullivan Report expects Chemcon to grow at a CAGR of 15-20% between CY19 and CY23.

Strengths

India and China are the only countries that produce CMIC. India's share in the global CMIC manufacturing capacity has increased from 7.07% in CY14 to 26.16% in CY19. India is a net importer of CMIC, with about 62% of India's domestic demand in CY19 being catered to by imports from China. As per Frost & Sullivan Report India, a major CMIC consumer market, is expected to witness a demand growth at a CAGR of 11.0% between 2019 and 2023. It further expects that the company is well positioned to substitute the imports from China and hence, has an opportunity to grow at a CAGR of more than 25% between 2019 and 2023

Chemcon Speciality Chemical is the only manufacture of Zinc Bromide and the largest manufacturer of Calcium Bromide in India. Further, since it commenced the sales of Oilwell Completion Chemicals in CY14, its share in the global production of the Oilwell Completion Chemicals has grown to 2.65% in CY19.

Around 68.61% of its total revenue from operations in FY20 was contributed by customers who have been consistently purchasing Chemcon products over the last five years. Its top seven customers for FY20 have been its customers for over four years.

The specialty chemicals industry in which it operates has high entry barriers due to the involvement of complex chemistry in the manufacture of its products, which is difficult to commercialize on a large scale and a long gestation period to be enlisted as a supplier with the customers, particularly in pharmaceutical industry.

With the completion of two additional plants, total volumetric reactor capacity at the manufacturing facility shall increase from volumetric reactor capacity of 374.85 KL to 625.85 KL and will enable it to significantly benefit from economies of scale

Weaknesses

The company has a limited product portfolio and its business may be adversely affected if any of its products do not continue to perform as expected or if competing products gain wider market acceptance. Further, if competitors are able to improve the efficiency of their manufacturing processes and thereby offer their products at lower prices, its revenues and profitability may decline

The company is dependent on a limited number of customers for a significant portion of its revenue. In the Fiscals 2020, 2019 and 2018 and 59.35%, 45.94% and 60.01%, respectively, of its revenue from operations were derived from its top five customers (in the respective periods).

The commercial success of its pharmaceutical chemicals business depends on the demand for the products for which such chemicals are utilized. Any downturn in the demand of such products, including due to the development of alternative products without its pharmaceutical chemicals as ingredients, may conversely result in a reduction in the demand for the pharmaceuticals chemicals

Certain key raw materials have witnessed volatility in their prices. For instance, the global price of TMCS, a key raw material in the manufacturing of HMDS, fell from \$3.6 per kg to \$1.1 per kg between first quarter of calendar year 2013 and fourth quarter of calendar year 2014, rose to \$10.3 per kg by the third quarter of calendar year 2018 and subsequently fell to approximately \$2.4 per kg in the fourth quarter of calendar year 2019

Further, it purchases certain of key raw materials from suppliers based in China. Its ability to purchase such raw materials from its suppliers in China, may be hampered due to inter alia supply chain issues, change in government policies (including anti-dumping measures) and international geo-political situations or any other circumstances which are beyond its reasonable control

The company is dependent on the global prices for its products. There has been volatility in the global prices of certain of its products. For instance, the global price of HMDS have increased from \$3.5 per kg in the first quarter of calendar year 2017 to \$18.5 per kg in the third quarter of calendar year 2018 and subsequently fell to approximately \$8.2 per kg in the fourth quarter of calendar year 2019

Some of the raw materials that it uses as well as its finished products are corrosive and flammable and require expert handling and storage. While it takes adequate care and follow all relevant safety measures, there is a risk of fire and other accidents, at its manufacturing facility and warehouses.

Oilwell Completion Chemicals collectively contributed 33.47%, 35.30% and 35.63%, respectively of total revenue from operations in Fiscal 2020, 2019 and 2018. Oil exploration industry is currently under severe stress.

Some of the promoters/ promoter group are facing/have faced regulatory actions, family disputes and criminal proceedings.

Valuation

Consolidated revenues fell 14% to Rs 262.05 crore in FY 2020. However, operating margins rose 500 bps to 26.8% resulting into 6% increase in operating profits to Rs 70.26 crore. Net profit was up 14% to Rs 48.85 crore.

At the higher price band of Rs 340, the offer is made at around 25.5 times its FY 2020 EPS of Rs 13.3 on a post-issue equity share capital of Rs 36.63 crore of face value of Rs 10 each. Listed industry peers of the company are Aarti Industries, Vinati Organics, Fine Organics Industries and Neogen Chemicals.

Aarti Industries trades at 36.9 times its FY 2020 EPS of 30 at the current market price of Rs 1107. Vinati Organics trades at 41.3 times its FY 2020 EPS of 32.5 at the current market price of Rs 1341. Fine Organics Industries trades at 54.7 times its FY 2020 EPS of 54.3 at the current market price of Rs 2969. Neogen Chemicals trades at 57.3 times its FY 2020 EPS of 12.3 at the current market price of Rs 707.

Currently most of the chemical companies are trading at high P/Es, mainly due to the fancy for the China replacement story in the chemicals sector. Only time will tell whether they will perform so well in future to justify these valuations.

Chemcon Speciality Chemicals: Issue Highlights	
Fresh issue (in Rs crore)	165
Offer for sale (in Rs Crore)	
- in Upper price band	153
- in Lower price band	152.1
Price Band (Rs)	338-340
For Fresh Issue Offer size (in no of shares)	
- in Upper price band	4852941
- in Lower price band	4881657
Pre issue capital (Rs crore)	31.78
Post issue capital (Rs crore)	
- in Upper price band	36.631
- in Lower price band	36.659
Pre issue promoter shareholding (%)	100.00
Post issue Promoter shareholding	
-On lower price band (%)	74.47
-On higher price band (%)	74.41
Bid Size (in No. of shares)	44
Issue open date	21-09-2020
Issue closed date	23-09-2020
Listing	BSE, NSE
Rating	45/100

Chemcon Speciality Chemicals: Financials				
Particulars	1703 (12)	1803 (12)	1903 (12)	2003 (12)
Total Income	87.69	157.16	303.34	262.05
OPM	9.9	28.7	21.8	26.8
Operating Profits	8.66	45.10	66.08	70.26
Other Income	0.10	0.75	1.99	3.97
PBIDT	8.76	45.85	68.07	74.23
Interest	2.00	3.04	4.00	4.68
PBDT	6.77	42.81	64.07	69.54
Depreciation	2.34	2.26	2.86	4.62
PBT Before EO	4.43	40.55	61.20	64.92
EO	0.00	0.00	0.00	0.00
PBT after EO	4.43	40.55	61.20	64.92
Provision for Tax	1.61	14.08	18.09	16.04
Profit after Tax	2.83	26.47	43.11	48.88
PPA	0.00	0.09	0.07	0.03
Net profit after PPA	2.83	26.38	43.04	48.85
EPS (Rs)*	0.8	7.2	11.8	13.3
*EPS is on post issue equity capital of Rs 36.63 crore of face value of Rs 10 each				
# EPS not annualized due to seasonality of business				
Figures in Rs crore				
Source: Capitaline Corporate Database				

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Date source: NSE India/Steelcitynettrade.com/CAPITAL Market