Archean Chemical Industries Ltd

9th November, 2022

IPO NOTE

Recommendation	Subscribe
Price Band	Rs 386-407
Bidding Date	9th Nov – 11th Nov
Book Running Lead Manager	JM Financial, IIFL Securities, ICICI Securities
Registrar	Link Intime
Sector	Specialty Chemicals

Minimum Retail Application- Detail At Cut off Price	
Number of Shares	36
Minimum Application Money	Rs. 14,652
Discount to retail	0
Payment Mode	ASBA

Consolidated Financials (Rs Cr)	FY21	FY22
Total Income	741	1,130
EBITDA	262	467
Adj PAT	66	189

Valuations (FY22)	Lower Band	Upper Band
Market Cap (Rs Cr)	4,750	5,008
Adj EPS	15.33	15.33
PE	25	27
EV/ EBITDA	12	13
Enterprise Value (Rs Cr)	5,656	5,915

Post Issue Shareholding Pattern	
Promoters	53.4%
Institutions	21.9%
Bodies Corporates & Public	24.7%

Offer structure for different categories	
QIB (Including Mutual Fund)	75%
Non-Institutional	15%
Retail	10%
Post Issue Equity (Rs. in cr)	24.61
Issue Size (Rs in cr)	1,387-1,462
Face Value (Rs)	2

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BACKGROUND

Incorporated in 2003, Archean Specialty Chemicals Ltd (ACIL) is a leading specialty marine chemical manufacturer in India. It manufactures three major product categories such as bromine, industrial salts and sulphate of potash. As on Jun'22, it has served 18 global customers from 13 countries and 24 domestic customers. In FY21, it was one of the largest exporters of both bromine and industrial salts in India. It has the lowest cost of production globally.

Objects and Details of the Issue:

- Total issue of ~Rs. 1,462 Cr (at upper price band) consists of fresh issue worth Rs. 805 Cr and offer for sale worth Rs. 657 Cr
- To utilise an estimated amount of ₹ 644 Cr from the net proceeds towards redemption or earlier redemption of NCDs issued either in full or in part

Investment Rationale:

- Leading player in specialty marine chemical industry (mainly in bromine and industrial salt products)
- A business with high entry barriers limits the competition
- Focus on improving cost efficiencies
- Downstream expansion with bromine derivative performance products
- CAPEX investment in incremental capacities of bromine and industrial salt
- Aims to expand its global presence and enter new geographical markets

Valuation and Recommendation:-

A leading market position of Archean Chemical Industries Ltd has planned product innovation, and capex to expand existing as well as new manufacturing facilities ensures positive business growth. The company has delivered 36.3% / 77.7% growth in revenue and EBITDA between FY20-22, respectively. The company is expected to utilize its funds for the redemption of NCDs issued by company which will improve its debt to equity ratio up to ~1.0x from 2.6x as on Jun'22. Further, this will have a positive impact on the profitability given the significant reduction in the interest cost of NCDs (with yield to maturity at 17% p.a.). ACIL is valued at a discount based on its P/E of 26.6x, EV/EBITDA of 12.7x compared to its average valuation of peer companies. **We recommend 'SUBSCRIBE to the issue.**

Financials	FY20	FY21	FY22
Net Revenues	608	741	1,130
Growth (%)	*0.0%*	*21.8%*	*52.6%*
EBITDA	148	262	467
EBITDA Margin (%)	*24.3%*	*35.4%*	*41.3%*
PBT	(17)	90	251
Adjusted PAT	(36)	66	189
EPS	-2.94	5.40	15.33
ROCE	10.9%	20.5%	33.6%
EV/Sales			5.2
EV/EBITDA			12.7
P/E			26.6

Company Background

Incorporated in 2003, Archean Specialty Chemicals Ltd (ACIL) is a leading specialty marine chemical manufacturer in India. It manufactures three major product categories, such as bromine, industrial salts and sulphate of potash. As on Jun'22, it has served 18 global customers from 13 countries and 24 domestic customers. In FY21, it was one of the largest exporters of both bromine and industrial salts in India. It has the lowest cost of production globally.

Products' end use applications:

Bromine

- Pharmaceuticals
- Agrochemicals
- Water treatment
- Flame retardant
- Additives
- Oil & gas
- Energy storage batteries

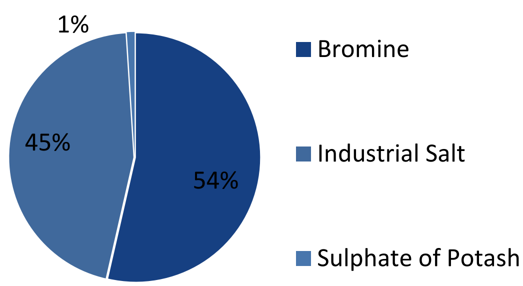
Industrial Salts

- Sodium carbonate (soda ash)
- Caustic soda
- Hydrochloric acid
- Chlorine
- Bleaching powders,
- Chlorates
- Sodium sulphate (salt cake)
- Sodium metal

Suplhate of Potash

- Used as a fertilizer and also has medical uses

Product Revenue Mix (FY22: Rs. 1,130Cr)



Indian Market Position and Volume Mix FY22

Product Mix	Market Position	FY22 Volume (MT)
Bromine	Largest export and leader in merchant sales	20,293
Industrial Salt	Largest exporter	35,86,269
Sulphate of Potash	Only producer in India	2,483

Source: RHP
Notes: Product Revenue Mix FY22: (1) Market share by volume for CY2021. (2) Merchant sales are traded bromine in the market rather than captive production.

Manufacturing Units and Installed Capacity

ACIL manufactures products from brine reserves in the Rann of Kutch (Gujarat) at their facility in Hajipur in Gujarat. It is an integrated production facility of its bromine, industrial salt and sulphate of potash operations. It has an installed capacity of 28,500 MTPA of bromine, 3,000,000 MTPA of industrial salts and 1,30,000 MTPA od sulphate of potash. The facility is located in close proximity to the captive Jakhau Jetty and Mundra Port where it transports its products to customers globally. The facility, salt fields and brine reservoirs span ~240 sq. km. It has one of the largest salt works at one single location in the world.

Company's industrial salt washing facility has three washeries, each having a capacity of 200 tons/hour. The facility is equipped with its own quality department, effluent treatment plant, sewage treatment plant and stockyard.

Product-wise Capacity Utilisation

Products	FY2022	As on Jun'22*
Bromine	71.20%	23.72%
Industrial Salt	119.54%	38.54%
Sulphate of potash	1.91%	0.0%

Source: RHP, Note: *not annualized

Focus on environment and safety

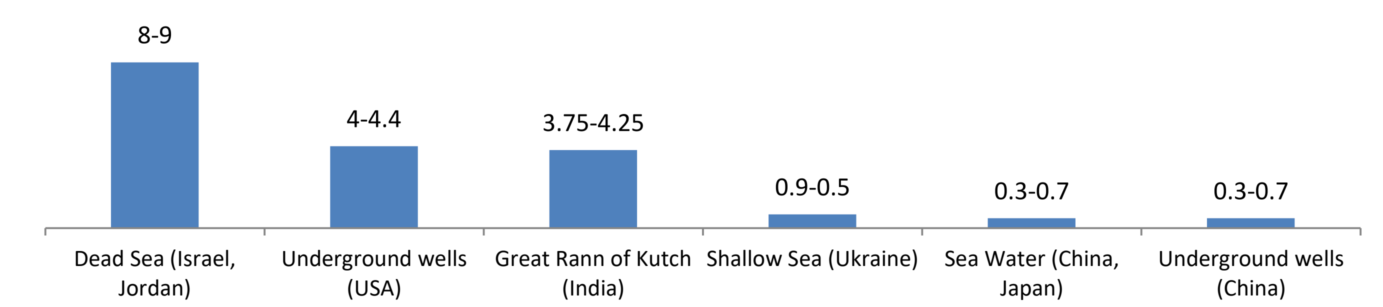
ACIL undertakes an annual environment and safety audit and strives to ensure that it does not discharge any harmful elements from its manufacturing operations. It has implemented environmental management plan as a part of its environmental and sustainability efforts. As of Jun'22, it had an environmental, health and safety team of 13 employees.

Industry Overview

Bromine

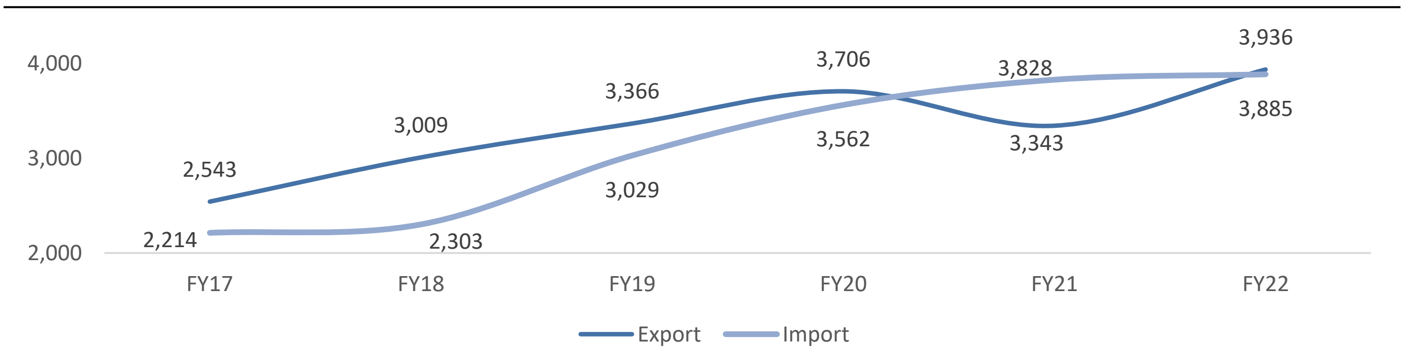
Bromine is a halogen chemical element. It is used as a reactant and catalyst for manufacturing a variety of products, such as agrochemicals, biocides, water disinfectants, pharmaceuticals intermediates, dyes, completion fluids, flame retardants, and photographic chemicals. It is a naturally occurring element and it is available in much higher concentrations are found in land seas and brine wells.

Global Natural resources by Bromine concentration (in ppm)



Source: RHP

Bromine Prices (USD/MT)



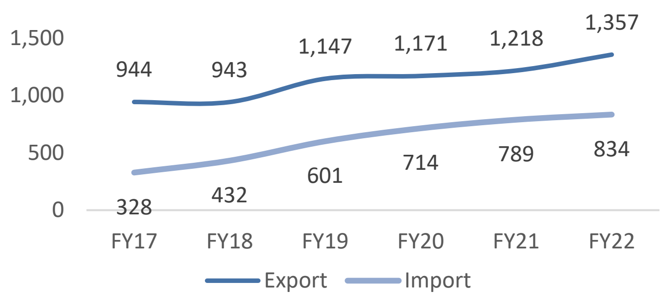
Source: RHP

Industrial Salts and Sulphate of Potash

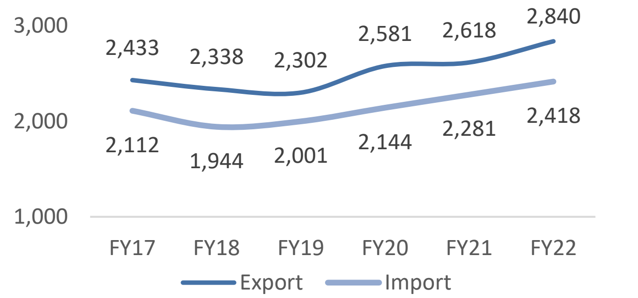
India is the third largest salt producing country in India (after US and China). Indian industrial salt production is expected to grow at 9.89% CAGR between FY21-FY25E. Indian industrial salt export is expected to grow at 14% CAGR between FY21-FY25E. China imports ~40% of its industrial salt requirement from India (5,056 KT industrial salt imported in FY21) which constituted 42% of India's industrial salt exports.

Sulphate of Potash (SOP), is also known as Potassium Sulphate, is a premium quality nutrient for the growth of high value crops. It can be used as a fertilizer, for medical uses or can be used in other industries, such as, glass, cosmetic, food and beverages, etc.

Industrial Salt Prices (INR/MT)

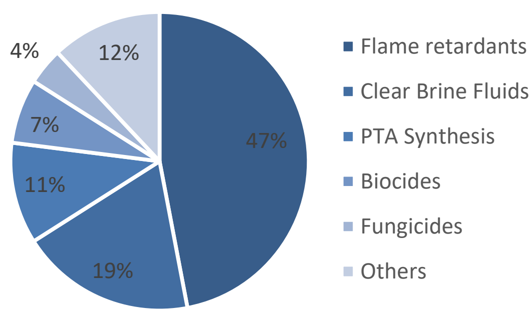


Suphate of potash price (USD/MT)

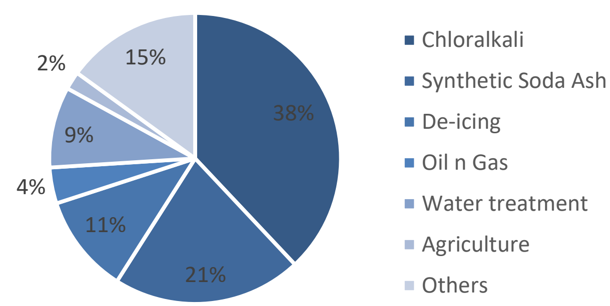


Source: RHP

Bromine application wise split FY21



Global Industrial Salt Usage FY21



Source: RHP

Key market details and expectations:

Particulars	2021	2025E	CAGR FY21-FY25	Particulars	2021	2025E	CAGR FY21-FY25
Global Bromine Market size (USD Bn)	3.13	3.92	5.80%	**India Industrial Salt Market (Mn MT)**			
Global Bromine market volumes (KT)	933	1056	3.10%	Production	24	35	9.89%
Indian Bromine Volumes (MT)				Domestic Demand	12	15	5.74%
Production	46,000	74,000	12.00%	**India Industrial Salt Export**	13	23	14.05%
Demand	39,520	50,168	6.00%	**Global Sulphate of Potash Market (Mn MT)**	7	9	6.26%
Indian Export - Import (MT)				**Indian Sulphate of potash market (MT)**	59,102	74,615	6.00%
Imports	9,972	11,172	3.00%	**Indian Sulphate of potash Export (MT)**	18,925	23,004	5.00%
Exports	9972	14,155	9.00%				

Source: RHP

Investment Rationale

Leading player in specialty marine chemical industry (mainly in bromine and industrial salt products)

A leader in specialty marine chemical manufacturer is a largest exporter of bromine and industrial salt by volume in FY21 with a lowest cost of production across the globe. The demand for bromine and bromine derivatives performance products is expected to grow on account of rise in demand for flame retardants, increase in consumption of oil well chemicals and use of hydrogen bromide in flow batteries. It exported 100% of its industrial salts production over the last 3 years. In FY21, it has exported 2.7 MT of industrial salt. The growth in food and beverage industry, chlor-alkali sector in the chemical industry, water treatment, agriculture and de-icing to drive the demand for industrial salts. Further, it is the sole producer of sulphate of potash from natural sea brine in India. Low Potassium levels have been linked to cancer and certain cardiovascular diseases, thus, sulphate of potash market is expected to grow with its use in fertilizers primarily for growing fruit and vegetables and medical uses.

The access to brine reserves at the Rann of Kutch, manufacturing facilities within close proximity to the captive Jakhau Jetty and Mundra Port, long standing relationship with global customers and its high-quality products are the key business drivers.

A business with high entry barriers limits the competition

The company operate within an industry which has high entry barriers. There is a limited availability of raw materials required for production, limited number of locations with a suitable climate and access to reserves, high cost and complexity of product development, investment in salt beds, lead time, R&D expenditure and strong customer relationships can be achieved through a long gestation period. Company's products are subject to high quality standards which goes through sensitive and rigorous product approval system. Further, its customers are also subject to stringent regulatory and industry standards, thus, any change in the vendor of the products may require significant time and expense for customers, that acts as an entry barrier in this industry. It limits the number of competitors involved in the manufacturing of its products.

Additionally, bromine and certain raw materials that are used in production are highly corrosive, hazardous and toxic chemicals. It requires a high degree of technical skill and specialized expertise to handle these chemicals. Company's existing brine fields were established over a period of three to four years before commercial cultivation was possible and, accordingly, the development time of brine reservoirs creates an entry barrier to potential domestic competitors. In addition, the Rann of Kutch brine fields are located in environmentally sensitive coastal areas which require a number of regulatory hurdles before production could be established.

Focus on improving cost efficiencies

Archean has an integrated production facility for its bromine, industrial salt and sulphate of potash operations located at Hajipur, Gujarat, which is located at Rann of Kutch brine fields. Its Jakhau Jetty is a fair-weather facility, operating for seven to eight months a year between the months of October/November through May. The Jakhau Jetty has a designed capacity of 5 million MT per annum and a capacity to load 28,000 MT. It is equipped with a twin conveyor system, diesel generator sets and is supported by a stockyard with storage capacity in excess of 350,000 MT to ensure continuous availability of products for customers.

It has invested CAPEX for improvement and maintenance of its facility, including investments in salt beds having three-to-four years gestation period and it has investments in ISO containers for the export of bromine. It has 228 owned and leased containers, as on Jun'22. These ISO containers provide an added advantage of scale at ports with safety and reliability in transport. These provide a cost advantage and greater flexibility for exporting its products. India's solar evaporation method of industrial salt production is more cost efficient than mining method. The company has increased the mechanization of production process which is expected to increase efficiencies and product consistency.

The cost of production for Industrial salt from sea water brine is about US$12 to 15 per MT, while ACIL costs are in the range of US$5.5-6 per MT. Further its quality of salt is on par with Grade 1 salt required by chlor-alkali producers. The best-in-class cost position along with the quality of its product has enabled it to be a competitive salt exporter to South East Asian markets and West Asia. In bromine production, India is among the top five cost competitive producers globally with China and Japan being more expensive and the United States (Arkansas), Israel and Jordan less expensive than India. Its cost competitiveness has helped ACIL to become the largest Indian exporter of bromine by volume and the leader in merchant sales (traded bromine in the market rather than captive production) in FY21. Its integrated manufacturing site with access to the Rann of Kutch reserves and a close connectivity to ports allows it to manage the production process efficiently and to deliver high quality and timely products to its customers.

Downstream expansion with bromine derivative performance products

ACIL has a plan to expand its product portfolio with an introduction of bromine derivative performance products over the next 2-3 years. These products are brominated flame retardants, clear brine fluids and bromine catalysts used for synthesis in PTA. It is setting up a new facility to manufacture bromine performance derivatives products through its subsidiary, Acume Chemicals Private Limited with an investment of ~Rs. 251.7Cr, which will be funded through internal accruals. The proposed facility will be constructed on 34,983 square meters parcel of land which has been allotted from the GIDC, Ankleshwar.
The facility is expected to commence commercial operations by Q2FY24 with an installed capacity of:

- High end Flame retardant - 10,000 TPA
- Clear Brine fluids – 13,000 TPA
- PTA – 5,000 TPA

Brominated flame retardants are used in the electronics industry, wire and cable compounds and in everyday commodities such as rubber, textiles, washing machine, computers, televisions and others. In respect of the production of flame retardant, it has entered into an agreement to design, engineer, construct, commission and operate the plant to produce with a Chinese technology provider. The technology tie up also includes buyback of minimum of 90% of the produced quantity by the Chinese technology provider at mutually agreed pricing terms.
Clear brine fluids are used to produce calcium bromide, which is used in oil drilling and organic synthesis, and sodium bromide, which is used in water treatment, and zinc bromide which is used in water treatment and flow batteries.
PTA is consumed in the development of polyester resins, such as polyester films, polyester fibre and yarn, and PET material bottles. PTA is also used as an intermediate in the manufacturing of liquid crystal polymers, plasticizers, polybutylene terephthalate, and others.

CAPEX investment in incremental capacities of bromine and industrial salt

It has added a feed enrichment section in FY21 at Hajipir site, Gujarat which will improve bromine recovery from sea bittern. This expansion added 18,000 metric tons per annum to its bromine capacity. In Bromine, it has installed capacity of 28500 MTPA and it is expected to add 12500 MTPA capacity by FY23 with an estimated investment of Rs. 17.884Cr, which will be funded through company's operating cash flow. In industrial salt, it has 3 washeries having a capacity of 200 tons/hour and by FY23, it expects to increase a washery with capacity of 250 tons/hour.

Aims to expand its global presence and enter new geographical markets

In FY22, ACIL exported products to 18 global customers across 13 countries. It has long standing relationship of 5-7 years with its top ten customers. It aims at increasing its business share with existing customers. ACIL has a focus to expand its reach globally through existing as well as new direct end use customers in new markets by having dedicated sales and marketing teams whose primary focus will be on business development in global markets and mainly in Asia and Europe.

High Risks and concerns

- **Reliance on major customers:** ACIL's Top 10 / Top 20 customers contributed 61.99% / 80.94% of overall revenue in FY 22, respectively. Business loss from any one of these customers may have a material adverse impact on company's financials. Some of its major customers include Sojitz Corporation (20.56% of FY22 revenue), which is a technology partner and stakeholder in the Company, Shandong Tianyi Chemical Corporation, Unibrom Corporation, Wanhau Chemicals and Qatar Vinyl Company Limited.

- **Reliance on relatively few products:** ACIL mainly relies on three products for its business on a fixed sales contract basis with agreed pricing and volumes for domestic and non-domestic bromine customers and industrial salt customers. However, in the event non-renewal of such contracts or not extending new fixed sales contracts or any failure to retain customers or decrease in orders from a major customer for specific products could be materially and adversely affect the financial performance.

- **Price volatility in key raw materials and end products** may have a material impact on company's profitability.

Valuation and Recommendation

A leading market position of Archean Chemical Industries Ltd in the marine specialty chemical industry with the expected plans of product innovation, and capex to expand existing as well as new manufacturing facilities ensures positive business growth.

The company has delivered 36.3% / 77.7% growth in revenue and EBITDA between FY20-22, respectively. In FY22, ROE and ROCE reported at 72.2% and 33.6%, respectively. The company is expected to utilize its funds for the redemption of NCDs issued by company which will improve its debt to equity ratio up to ~1.0x from 2.6x as on Jun'22. Further, this will have a positive impact on the profitability given the significant reduction in the interest cost of NCDs (with yield to maturity at 17% p.a.). ACIL is valued at a discount based on its P/E of 26.6x, EV/EBITDA of 12.7x compared to its average valuation of peer companies.

We recommend 'SUBSCRIBE' to the issue.

Industry Peers

FY22 Figures (Rs. in Cr)	Tata Chemicals	Deepak Nitrite	Aarti Industries	Neogen Chemicals	Average	Archean Chemicals Industries
Revenue	12,622	6,802	7,000	488	6,728	1,130
CAGR (FY20-22)	10%	27%	29%	26%	23%	36%
EBITDA Margin	18.3%	24.2%	27.6%	18.0%	22.0%	41.3%
Asset Turns (x)	0.7	2.6	0.7	0.6	1.2	0.7
Working Cap Days	50	58	47	206	90	49
Pretax CFO/EBITDA	34.0%	23.3%	33.8%	15.5%	27%	21%
ROCE	7.0%	31.3%	22.1%	14.3%	19%	34%
ROE	5.5%	23.7%	28.0%	14.4%	18%	72%
Debt/Equity	0.2	0.1	0.2	0.3	0.2	3.2
EV/EBITDA	13.1	18.5	15.1	42.9	22.4	12.7
P/E	22.8	29.8	20.4	80.4	38.3	26.6

Source: RHP, Company data, NBRR

Financials

P&L (Rs. Cr)	FY20	FY21	FY22	Q1FY22	Q1FY23
	Consol	Stand	Consol	Stand	Consol
Net Revenue	**608**	**741**	**1,130**	**201**	**400**
% Growth		*22%*	*53%*		
Raw Materials	0	9	39	0	5
% of Revenues	*0.1%*	*1.2%*	*3.5%*	*0.0%*	*1.2%*
Employee Cost	34	35	38	9	10
% of Revenues	*5.7%*	*4.8%*	*3.3%*	*4.2%*	*2.4%*
Other expenses	425	434	586	112	225
% of Revenues	*69.9%*	*58.6%*	*51.8%*	*55.9%*	*56.1%*
EBITDA	**148**	**262**	**467**	**80**	**161**
EBITDA Margin	***24.3%***	***35.4%***	***41.3%***	***39.9%***	***40.2%***
Depreciation	52	55	67	16	18
Other Income	9	14	12	1	9
Interest	122	130	162	40	39
Exceptional item	0	0	0	0	0
PBT	**(17)**	**90**	**251**	**25**	**113**
Tax	20	24	62	6	28
Tax rate	*-117%*	*26%*	*25%*	*25%*	*25%*
Minority Interest	0	0	0	0	0
Adj. PAT (norm. Tax)	**(36)**	**66**	**189**	**19**	**84**
% Growth		***-284%***	***184%***		***352%***
EPS (Post Issue)	**(2.94)**	**5.40**	**15.33**	**1.52**	**6.86**

Ratios & Others	FY20	FY21	FY22	Q1FY22	Q1FY23
Debt / Equity	160.1	13.9	3.7	11.3	2.6
EBITDA Margin (%)	24.3%	35.4%	41.3%	39.9%	40.2%
PAT Margin (%)	-6.0%	9.0%	16.7%	9.3%	21.1%
ROE (%)	-605.1%	91.8%	72.2%	82.7%	97.8%
ROCE (%)	10.9%	20.5%	33.6%	23.4%	49.3%

Turnover Ratios	FY20	FY21	FY22	Q1FY22	Q1FY23
Debtors Days	27	34	49	41	25
Inventory Days	59	55	39	55	31
Creditor Days	100	55	36	229	90
Asset Turnover (x)	0.4	0.5	0.7	0.6	1.0

Valuation Ratios	FY20	FY21	FY22
Price/Earnings (x)			26.6
EV/EBITDA (x)			12.7
EV/Sales (x)			5.2
Price/BV (x)			19.2

Balance Sheet (Rs. Cr	FY20	FY21	FY22	Q1FY22	Q1FY23
	Consol	Stand	Consol	Stand	Consol
Share Capital	19	19	19	19	19
Other Equity	(13)	53	242	71	326
Networth	**6**	**72**	**261**	**90**	**345**
Total Loans	**958**	**1,007**	**965**	**1,019**	**888**
Other non-curr liab.	211	171	128	155	127
Trade payable	167	112	112	126	98
Other Current Liab	86	71	63	68	148
Total Equity & Liab.	**1,429**	**1,432**	**1,530**	**1,459**	**1,606**
Fixed Assets & CWIP	1,040	1,026	1,063	1,021	1,072
Right-of-use-asset &	36	33	39	32	50
Deferred Tax Assets	77	53	0	47	0
Inventories	99	111	121	122	137
Other non Curr. asse	14	19	29	25	12
Cash	24	32	12	3	32
Bank	0	0	46	31	72
Debtors	44	68	153	92	113
Other Current assets	94	90	66	86	118
Total Assets	**1,429**	**1,432**	**1,530**	**1,459**	**1,606**

Cash Flow (Rs. Cr)	FY20	FY21	FY22	Q1FY22	Q1FY23
Profit Before Tax	(17)	90	251	25	113
Provisions & Others	184	197	228	66	68
Op. profit before WC	**167**	**287**	**479**	**91**	**181**
Change in WC	(20)	(168)	(165)	(53)	(5)
Less: Tax	0	0	0	0	(5)
CF from operations	**148**	**119**	**315**	**38**	**171**
Int & Div Received	1	1	1	0	1
Purch from sale of m	(46)	7	31	3	(55)
Investment in/matur	0	(0)	(46)	(31)	(26)
Payment for PPE	(152)	(11)	(97)	(9)	(25)
CF from Investing	**(197)**	**(2)**	**(110)**	**(37)**	**(104)**
Proceeds from borro	118	10	2	9	0
Repayment from bro	(1)	(9)	(16)	(10)	67
Change in wc borrow	0	0	0	0	0
Repayments toward	(8)	(11)	(12)	(3)	(4)
interest paid	(83)	(100)	(198)	(25)	(111)
CF from Financing	**26**	**(110)**	**(224)**	**(29)**	**(47)**
Net Change in cash	**(23)**	**6**	**(19)**	**(28)**	**20**
Cash & Bank at begir	47	24	32	32	12
Cash & Bank at end	24	32	12	3	32

Source: Company data, NBRR

Disclosure:

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