



IPO Note- Clean Science and Technology Limited

05 July 2021

Clean Science & Technology Ltd. (CSTL) is a manufacturer of functionally critical specialty chemicals such as Performance chemicals, Pharma intermediates & FMCG chemicals. It is coming up with an IPO of Rs. 1,546cr which consists of only OFS. The key objective of the issue is to increase visibility through listing and generate liquidity for the promoter group.

Company Profile

CSTL manufactures specialty chemicals such as MEHQ, BHA, Guaicol, DCC, Anisole, 4-MAP & L-Acorbyl Palmitate (AP). It has 2 plants currently at Kurkumbh in Pune district of Maharashtra with 11 production lines & a cumulative capacity of 29,900 MTPA. It is the largest manufacturer globally of MEHQ, BHA, Anisole & 4-MAP in terms of manufacturing capacities with dedicated production lines for key products. CSTL is adding a 3rd unit at the same site that will further increase capacity of MEHQ & Anisole. It supplies primarily to clients in regulated markets. Some of its marquee clients are Bayer AG, SRF, Vinati Organics, Gennex Labs & Nutriad International. CSTL derives 68% of revenues from exports with the key export markets being China, USA, Europe, Japan, Korea & Taiwan. CSTL is led by an experienced promoter team of career technocrats who actively oversee the in-house development of catalytic processes that improve the efficiency of manufacturing processes. Most of the current processes are environment friendly.

Key Product Segments

Performance Chemicals (69% of Revenue):

It consists of the company's key products of MEHQ, BHA & AP. CSTL is the largest global manufacturer of MEHQ & BHA. MEHQ is used as a polymerization inhibitor in acrylic acids, acrylic esters & super absorbent polymers. MEHQ is a key intermediate for many agrochemicals. BHA is used as an anti-oxidant in the food & feed industry. AP finds application in infant food formulations, breakfast cereals and cosmetics.

Pharmaceutical Intermediates (16% of Revenue):

CSTL's two products of Guaicol & DCC are used in the pharma industry. Guaicol acts as a precursor to manufacture APIs for cough syrups & is a key raw material for the production of vanillin. DCC is used as a reagent in anti-retroviral drugs.

Rating	SUBSCRIBE
Issue Details	
Issue Opens	07-Jul-21
Issue Closes	09-Jul-21
Equity Offering (mn shares)	17.58
Face Value (Rs.)	1
Price Band (Rs.)	880-900
Bid Lot (# Shares)	16
Issue Size (Rs. bn)	15.46
Maximum Application for Retail Investor (Rs.)	1,87,200.0
Issue Type	100% Book Building
Listing	NSE/BSE
BRLMs	Axis Capital, JM Financial, Kotak Mahindra Capital
Registrar	Link Intime

Shareholding Pattern (%)

	Pre Issue
Promoter	94.65
Non Promoter	5.35

Issue Structure (In mn no. of shares)

Issue size	17.58
Fresh Issue	NIL
Break-up of net issue to public (%):	
QIB's portion	50.0
Non-institutional portion	15.0
Retail Portion	35.0

Source: ABML Research, RHP

Analyst Details

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FMCG Chemicals (12% of Revenue):

Anisole and 4-MAP find applications in various FMCG products. Anisole is a starting material for several perfumes, insect pheromones and pharmaceuticals. 4-MAP acts as a UV-blocker in sunscreens and other cosmetics. CSTL is the leading producer of both these chemicals. Majority of the Anisole produced is used for captive consumption.

Key Investment Rationale

1. Consistent track record of strategic R&D:

CSTL has successfully developed and commercialized several unique, eco-friendly & cost-effective manufacturing processes using catalysts that reduce the amount of effluents generated from the reactions as well as reduce the dependence on conventional raw materials. For instance, the company designed and developed a catalyst for manufacturing Anisole from phenol and methanol that eliminated the use of toxic conventional starting materials. The company's entire growth has been through the organic route with no acquisition of any asset or technology since inception. CSTL is looking to expand its product portfolio in the stabilizer and additives business.

2. Experienced management team:

CSTL is led by a highly experienced and qualified team of career technocrats who have wide experience across the various functions of R&D, procurement, manufacturing, sales and marketing. The senior management participates actively in the R&D and manufacturing functions of the company.

3. Leadership in products and strong entry barriers:

CSTL has historically entered into manufacturing of only those products that are produced only by limited players globally and enjoy strong structural demand. Further, the company continuously develops processes & catalysts that improve the overall efficiency of the facilities and create strong entry barriers. New entrants require significant capital investments, long gestation period and regulatory approvals to effectively compete against well-entrenched player like CSTL.

4. Diversified Client Mix across diverse geographies:

CSTL's specialty chemicals have a wide range of applications that cater to a diverse base of customers across countries and industries. It derived 68% of its revenues from exports with key market of China (33% of total revenues), Korea, Taiwan, USA and Europe. Its range of performance chemicals (70% of revenues) have a diverse end-use across several industries of paints, adhesives, agrochemicals and FMCG products.

5. Dedicated manufacturing facilities:

CSTL operates 2 manufacturing facilities with 11 production lines at Kurkumbh in Pune district of Maharashtra. It has multiple dedicated lines for several of its key products that reduce contagion risk. It operates 3 dedicated lines for catalysts that are used in its various manufacturing processes. These 3 lines identify, design, customize and re-generate the catalysts.

6. Strong Financial Track-Record:

CSTL has entirely grown organically through internal accruals with zero acquisition of assets or technology. There has been no equity dilution in the company over the past decade and is debt free. CSTL has a consistent track record of returning cash to shareholders through dividends and buyback. It consistently earns higher margins through cost optimizing in-house developed manufacturing processes, diversified raw material procurement, captive power generation, exports to regulated markets and leadership position in several of its key products.

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Industry Overview

The global specialty chemicals market is projected to grow at 5% CAGR to reach USD 1,089 bn by 2025. Some of the segments such as pharma APIs, agrochemicals, construction chemicals, home & personal care and additives are poised to grow at much higher rates than the overall industry. Rising awareness of ill-effects of certain toxic and polluting chemicals on the environment, climate and human health along with tightening environmental & regulatory norms have resulted in the world moving towards safe & sustainable chemistries that reduce emissions. Increasing changes in weather patterns have led to growing demand for high performance additives in construction chemicals, agrochemicals and food products. Global chemical majors have started diversifying their supply chains to reduce their dependence on China post the pandemic. India with its abundant technical expertise, cheap labour, dedicated manufacturing facilities and improved availability of raw materials is emerging as a credible alternative.

Risks and Concerns

Volatility in raw material prices: Phenols are an important raw material for CSTL contributing ~40% of the total raw material cost. Additionally several commodity chemicals like methanol, acetic anhydride, tertiary butyl alcohol and acetone are used in the manufacturing processes. Increased volatility in the prices of these along with absence of long term contracts with suppliers will affect the costs, profitability and subsequently competitiveness of the company.

Significant revenues from single product: CSTL derives ~ 48% of operating revenue from MEHQ which is primarily used as polymerization inhibitor in acrylic acids which in turn find applications in paints, adhesives and other polymers. Any negative impact on these end-user industries or development of an alternative to MEHQ would have a material impact on the company's revenues.

Outlook & Valuation

The specialty chemicals industry in India is on an upswing on the back of several favourable factors such as 'China + 1' sourcing strategies adopted by several MNCs, reduced production in China on the back of strict environment & pollution norms on the chemical industry, increasing manufacturing base of several end-user industries in India, favourable government policies such as the PLI scheme, dedicated chemical parks and protection through anti-dumping duties on imports especially from China. CSTL is the leading manufacturer in several of its products using internally developed processes and catalysts. It has joined the sustainable chemistry bandwagon by eliminating the wastes and discharges from its manufacturing facilities. It enjoys healthy return ratios and margins through creation of strong entry barriers. The IPO is valued at 48.2x FY21 EPS which we believe is reasonable when compared to the valuations of several of the specialty chemical companies in the listed universe. We assign **SUBSCRIBE** rating on the issue.

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Income Statement

<i>Rs. Cr</i>	31/03/2019	31/03/2020	31/03/2021
Net Sales	393.3	419.3	512.4
Other Income	11.3	10.9	25.6
Total Revenue	404.6	430.2	538.1
Expenses			
Cost of Materials Consumed	171.2	129.3	123.6
Employee Exp	24.9	31.0	43.6
Other Exp	60.9	73.8	86.3
Total OpEx	256.9	233.8	254.3
EBITDA	147.6	196.2	284.6
<i>Margin</i>	<i>38%</i>	<i>47%</i>	<i>56%</i>
D&A	11.0	13.7	17.2
EBIT	136.6	182.5	267.4
Finance Cost	--	--	--
Excep Items	--	--	--
PBT	136.5	182.3	267.3
Tax	38.9	42.7	68.9
PAT	97.7	139.6	198.4
Basic EPS (Rs.)	9.19	13.15	18.68
Diluted EPS (Rs.)	9.19	13.15	18.68

Key Ratios

	31/03/2019	31/03/2020	31/03/2021
RoE (%)	35.9	40.8	36.8
RoCE (%)	50.8	58.5	73.9
Net Fixed Asset Turnover (x)	3.1	2.5	2.8
Blended Capacity Utilization (%)	67.9	63.0	71.9
Net Working Capital Days	69	60	47
Inventory Days	34	30	38
Receivables Days	55	61	53
Payables Days	21	31	43

Source: ABML Research, RHP

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Balance Sheet

Rs. Cr	31/03/2019	31/03/2020	31/03/2021
Assets			
Non-Current			
PPE	124.9	162.6	182.6
CWIP	3.9	3.4	55.0
ROU Assets	1.9	2.7	3.0
Other Non-Current	4.2	4.1	24.2
Total Non-Current	134.9	172.9	264.8
Current			
Inventories	37.0	34.6	52.9
Receivables	59.8	69.8	74.2
Investments	75.2	133.0	232.1
Cash & Cash Equivalents	9.4	9.2	15.6
Other Current	11.1	10.3	20.2
Total Current	192.6	257.0	395.1
Total Assets	327.5	429.9	659.9
Equity			
Share Capital	1.4	1.3	10.6
Other Equity	270.6	340.8	529.0
Total Equity	272.0	342.1	539.7
Liabilities			
Non-Current	14.3	10.8	18.3
Current			
Payables	22.3	35.7	61.0
Total Current	41.1	77.0	102.0
Total Liabilities	55.4	87.8	120.3
Total Equity & Liabilities	327.5	429.9	659.9

Source: ABML Research, RHP

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ABML research is also accessible in Bloomberg at ABMR

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