

# Megachem Limited

20 June 2022

## BUY (Maintained)

<b>BBG</b>	MGCM SP
<b>Market cap</b>	S\$62.7m
<b>Price (20 June 2022)</b>	S\$0.47
<b>52-week range</b>	S\$0.36 – S\$0.50
<b>Target Price</b>	S\$0.58
<b>Shares Outstanding</b>	133.3m
<b>Free Float</b>	15.1%
<b>Major Shareholders</b>	Chew Choon Tee (35.7%) Chori Co Ltd (30.0%) Tan Bock Chia (19.1%)

<b>P/BV (12/21)</b>	1.0x
<b>Net Debt to EBITDA (12/20)</b>	1.8x

Source: Company data, Bloomberg, SAC Capital

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## FY22 could be another record year

**FY22E is turning out to be another record year for Megachem**, after 51.4% gain in net profit in FY21. We are raising our FY22E net earnings estimates by 6.7%, to reflect higher ASP for specialty chemicals and improved margins. We expect FY22E net profit to grow by 2.6% yoy, or 11.7% if non-recurring government grants received in FY21 were excluded. The higher ASP for specialty chemicals is driven by higher upstream crude oil and petrochemical prices. From Jan-Apr 2022, price of crude had risen 58%, and petrochemical prices were up 14%, according to ICIS Petrochemical Index. Singapore's chemical export prices rose 6% in the first four months of 2022.

Major chemical distributors have reported strong 1Q22 improvement in revenue and operating income. Revenue of PT Lautan Luas, a commodity chemical distributor, surged +40.9% yoy and +10.2% qoq, with operating income +89.7% yoy and +2.7% qoq. Brenntag reported sales gain of +44.7% yoy and +12.1% qoq, with bigger gain in operating EBITDA by +54.2% yoy and +33.7% qoq.

**What has changed?** Supply chain disruption and demand uncertainty have caused Megachem's customers to rethink their strategy for raw material procurement. Instead of bulk purchases and hold stock, they are looking to suppliers with a diversified geographical network that can deliver goods on short notice and in smaller quantity. Megachem's global network of warehouses and logistic supply bases in 11 countries is a competitive edge.

EU nations have agreed on cuts in oil imports from Russia, which will reduce to 10-11% of its current level. The EU has also committed to reduce gas imports by two-thirds within a year. Ireland, Germany and Switzerland are amongst the top five chemical producing countries in the world. Disruption in oil and gas supply could negatively impact chemical exports out of EU, till the EU chemical producers find substitutes for the Russian imports. Customers could turn to specialty chemicals supply from Asia. About 55% of Megachem's sales are to the ASEAN markets, 13% to Europe, and 12% to North Asia.

**Maintain BUY at TP of S\$0.58.** Our revised FY22E and FY23E are premised on a 3% rise in chemical prices in FY22E and a 1% decline in FY23E, on weaker macro-economic environment in FY23. Gross margin in FY22E is expected to widen by 0.6% pt to 25.2%, aided by inventory stockpiled at end 2021. On the other hand, working capital needs have risen with higher input costs. Strong US\$ vs regional currencies pose some forex risks, as raw material procurement are in US\$, while sales to countries such as Indonesia, China and Vietnam are settled in the local currencies. Our DCF-derived TP is maintained at S\$0.58 (COE: 12%). BUY.

YE 31 Dec (S\$m)	FY19A	FY20A	FY21A	FY22E	FY23E
Revenue	113.8	105.2	138.9	145.9	148.8
EBIT	4.9	5.1	8.4	9.2	9.0
Net profit	3.8	5.1	7.8	8.0	7.8
EPS (S cents)	2.88	3.85	5.82	6.00	5.87
DPS (S cents)	1.50	1.50	2.00	2.00	2.00
Net cash / (debt)	(3.5)	(3.1)	(17.4)	(15.5)	(13.0)
<b>Valuation</b>					
EBIT margin (%)	4.3	4.8	6.0	6.3	6.0
ROIC (%)	7.8	7.5	12.0	12.1	11.3
EV/EBITDA (x)	10.8	10.4	8.4	7.4	7.3
P/E (x)	16.3	12.2	8.1	7.8	8.0
Dividend yield (%)	3.2	3.2	4.3	4.3	4.3

## Income Statement

FYE 31 Dec (S\$m)	FY19	FY20	FY21	FY22E	FY23E
<b>Revenue</b>	<b>113.8</b>	<b>105.2</b>	<b>138.9</b>	<b>145.9</b>	<b>148.8</b>
Cost of sales	(85.6)	(78.7)	(104.8)	(109.2)	(111.5)
<b>Gross profit</b>	<b>28.2</b>	<b>26.5</b>	<b>34.1</b>	<b>36.8</b>	<b>37.4</b>
Other income	0.6	1.9	1.1	0.6	0.4
Distribution cost	(15.5)	(14.9)	(17.6)	(18.7)	(19.4)
Administrative expenses	(5.5)	(5.7)	(6.3)	(6.5)	(6.5)
Other expenses	(2.9)	(2.8)	(3.0)	(3.0)	(3.0)
<b>Share of profit of joint venture</b>	<b>1.1</b>	<b>1.6</b>	<b>1.6</b>	<b>1.8</b>	<b>1.8</b>
Finance expenses	(1.0)	(0.7)	(0.8)	(1.1)	(1.1)
<b>Profit before tax</b>	<b>5.0</b>	<b>5.9</b>	<b>9.2</b>	<b>9.9</b>	<b>9.7</b>
Income tax expense	(1.0)	(0.7)	(1.2)	(1.7)	(1.6)
<b>Profit for the year</b>	<b>4.0</b>	<b>5.3</b>	<b>8.0</b>	<b>8.2</b>	<b>8.0</b>
<b>Profit/(loss) attributable to:</b>					
<b>Owners of the Company</b>	<b>3.8</b>	<b>5.1</b>	<b>7.8</b>	<b>8.0</b>	<b>7.8</b>
Non-controlling interests	0.1	0.1	0.2	0.2	0.2
<b>Basic and diluted earnings per share (S\$ cents)</b>	<b>2.88</b>	<b>3.85</b>	<b>5.82</b>	<b>6.00</b>	<b>5.87</b>

## Cash Flow

FYE 31 Dec (S\$m)	FY19	FY20	FY21	FY22E	FY23E
<b>Profit before tax</b>	<b>5.0</b>	<b>5.9</b>	<b>9.2</b>	<b>9.9</b>	<b>9.7</b>
Depreciation and amortisation	1.3	1.3	1.2	1.4	1.4
Associates & JV	(1.1)	(1.6)	(1.6)	(1.8)	(1.8)
Net finance expense	1.0	0.7	0.8	1.1	1.1
Non-fund items	0.1	(0.0)	(0.0)	-	-
Working capital changes	1.5	0.6	(16.5)	(1.8)	(1.1)
Interest paid	(0.9)	(0.6)	(0.6)	(1.1)	(1.1)
Dividend income	(0.0)	(0.0)	(0.0)	-	-
Tax paid	(1.1)	(0.8)	(0.9)	(1.7)	(1.6)
<b>Operating cash flow</b>	<b>5.7</b>	<b>5.5</b>	<b>(8.4)</b>	<b>5.9</b>	<b>6.6</b>
Capex	(0.5)	(2.8)	(3.5)	(1.3)	(1.3)
Net investments	0.7	0.4	0.6	-	-
Fixed assets disposal	0.0	0.0	0.0	-	-
Others	-	-	-	-	-
<b>Investing cash flow</b>	<b>0.3</b>	<b>(2.4)</b>	<b>(2.8)</b>	<b>(1.3)</b>	<b>(1.3)</b>
<b>Free cash flow</b>	<b>6.0</b>	<b>3.1</b>	<b>(11.2)</b>	<b>4.6</b>	<b>5.3</b>
Dividend paid	(1.8)	(2.1)	(2.4)	(2.8)	(2.8)
Borrowings	(1.4)	(0.1)	8.8	-	-
Equity	-	-	-	-	-
<b>Financing cash flow</b>	<b>(3.2)</b>	<b>(2.2)</b>	<b>6.4</b>	<b>(2.8)</b>	<b>(2.8)</b>
<b>Net change</b>	<b>2.7</b>	<b>1.0</b>	<b>(4.8)</b>	<b>1.9</b>	<b>2.5</b>

## Balance Sheet

FYE 31 Dec (S\$m)	FY19	FY20	FY21	FY22E	FY23E
Cash and bank balances	14.9	16.2	11.5	13.4	15.9
Financial Assets	0.2	0.4	0.6	0.6	0.6
Trade and Other Receivable	22.9	24.2	31.1	32.0	32.6
Inventories	25.4	24.4	36.5	35.9	36.7
Others	2.4	2.5	4.5	4.5	4.5
<b>Total current assets</b>	<b>65.9</b>	<b>67.7</b>	<b>84.2</b>	<b>86.4</b>	<b>90.3</b>
PPE	10.3	12.7	15.2	15.3	15.3
ROU assets	2.8	2.7	2.8	2.7	2.5
Investment in associate	6.6	7.6	8.0	9.7	11.5
Others	0.5	0.7	0.7	0.7	0.7
<b>Total non-current assets</b>	<b>20.2</b>	<b>23.6</b>	<b>26.7</b>	<b>28.4</b>	<b>30.1</b>
<b>Total assets</b>	<b>86.2</b>	<b>91.3</b>	<b>110.9</b>	<b>114.8</b>	<b>120.4</b>
Bank Borrowings	17.6	16.8	27.5	27.5	27.5
Trade and Other Payables	12.1	13.5	18.0	16.4	16.8
Finance leases	0.3	0.2	0.4	0.4	0.4
Others	0.3	0.4	0.6	0.6	0.6
<b>Total current liabilities</b>	<b>30.3</b>	<b>30.9</b>	<b>46.5</b>	<b>45.0</b>	<b>45.3</b>
Bank Borrowings	0.9	2.6	1.4	1.4	1.4
Others	2.6	2.6	2.6	2.6	2.6
<b>Total non-current liabilities</b>	<b>3.4</b>	<b>5.1</b>	<b>4.0</b>	<b>4.0</b>	<b>4.0</b>
Share capital	15.9	15.9	15.9	15.9	15.9
Reserves	(3.9)	(4.2)	(4.7)	(4.7)	(4.7)
Retained earnings	37.6	40.7	46.1	51.4	56.6
<b>Equity attributable to owners of the Company</b>	<b>49.6</b>	<b>52.4</b>	<b>57.3</b>	<b>62.6</b>	<b>67.8</b>
Non-controlling interests	2.8	2.9	3.1	3.2	3.3
<b>Total equity</b>	<b>52.4</b>	<b>55.3</b>	<b>60.4</b>	<b>65.8</b>	<b>71.1</b>
<b>Total equity and liabilities</b>	<b>86.2</b>	<b>91.3</b>	<b>110.9</b>	<b>114.8</b>	<b>120.4</b>

## Ratios

FYE 31 Dec	FY19	FY20	FY21	FY22E	FY23E
<b>Profitability (%)</b>					
Gross margin	24.8	25.2	24.6	25.2	25.1
EBIT margin	4.3	4.8	6.0	6.3	6.0
<b>Liquidity (x)</b>					
Current ratio	2.0	1.9	1.7	1.8	1.8
Net Debt/EBITDA	0.6	0.5	1.8	1.5	1.3
Interest coverage ratio	6.0	8.7	11.9	9.8	9.7
Net Debt to Equity (%)	6.8	5.7	28.8	23.6	18.3
<b>Valuation (x)</b>					
P/E	16.3	12.2	8.1	7.8	8.0
P/B	1.2	1.1	1.0	1.0	0.9
EV/EBITDA	10.8	10.4	8.4	7.4	7.3
<b>Cash Conversion Cycle</b>					
Trade receivable days	110	115	106	120	120
Inventory days	75	82	73	80	80
Trade payable days	52	60	55	55	55

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