

Megachem Limited

Date: 11 March 2022

BUY (Maintained)

BBG	MGCM SP	
Market Cap	S\$64.0 m	
Price (10 March 2022)	S\$0.48	
52-week range	S\$0.36 – S\$0.50	
Target Price	S\$0.58 (previously S\$0.55)	
Shares Outstanding	133.3 m	
Free Float	15.3%	
Major Shareholder	Chew Choon Tee	35.6%
	Chori Co Ltd	30.0%
	Tan Bock Chia	19.1%

P/BV (12/21)	1.1x
Net Debt to EBITDA (12/21)	1.8x

Source: Company data, Bloomberg, SAC Capital

Growth momentum to sustain, but at lower margins

Higher chemical prices and sales volumes driven by demand recovery and improving business environment propelled Megachem to a record year. For FY21, Megachem achieved a 32.0% topline growth to S\$140.3m and a 52.0% bottom line growth to S\$8.0m, beating our FY21E forecasts by 5.4% and 25.0% respectively. The sharp rise in net profit was due to better operating margin which improved from 4.8% to 6.0%. In addition, effective interest rate dropped to 13%, which is lower than our forecasted 20% (~S\$0.5m difference).

Continuous tailwinds. Growth momentum is expected to sustain into 2H22 driven by: 1) backlog as customers are restocking their inventories that were depleted during the pandemic; and 2) the surge in demand for chemicals as economic activities pick up across the world. The pandemic has resulted in a shift in business model as customers are opting for smaller and more frequent purchases from distributors. Megachem's established global logistic network has allowed them to fulfil this role. To the customers, Megachem is helping to hedge their inventory risks by ensuring the continuous provision and management of chemical supplies. While firmer oil and commodities prices are pushing up the prices of specialty chemicals, Megachem is able to mitigate some of the effect by passing on these costs to the customers.

Adaptable to changing demand. Megachem supplies a wide range of specialty chemicals used in many industries, and this insulates it from the vagaries of any single sector. In FY20, Megachem benefited from a surge in demand for specialty chemicals driven by cleaning and disinfection, technology and healthcare sectors and in last year, Megachem saw growth coming from the flavours, fragrance, construction and electronics sectors. Through its diversified sector and geographical coverage, Megachem has demonstrated that it is able to make quick adjustment to meet changing demand and supply to industries that are experiencing growth. The new Malaysia warehouse, which is near completion, will further expand Megachem's capability. We believe the new warehouse can ride on the semiconductor sector growth in Malaysia.

Maintain BUY at a higher target price of S\$0.58 (from S\$0.55). We raised our FY22E topline estimates by 4.4% as we expect sales to remain at the elevated level driven by demand. Global economic growth is estimated to be at ~4.4% and growth in emerging and developing Asia is at ~5.9% for 2022. However, we expect the exceptional operating margins to moderate to ~5.7% in FY22E and normalise further to ~5.1% in FY23E. Overall, our FY22E bottom line estimates still increased by 23.0%. Our DCF-derived (COE:9.3%) target price translates into FY22E P/E of 10.3x and P/B of 1.2x.

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Key Financials

Year ended Dec (S\$'Mil)	FY2019A	FY2020A	FY2021A	FY2022E	FY2023E
Revenue	113.8	105.2	138.9	140.3	143.1
EBIT	4.9	5.1	8.4	8.0	7.4
Net profit	3.8	5.1	7.8	7.5	7.1
EPS (S\$ cents)	2.88	3.85	5.82	5.65	5.32
DPS (S\$ cents)	1.50	1.50	2.00	2.00	2.00
Net Cash / (Debt)	(3.5)	(3.1)	(17.4)	(17.3)	(14.9)
Valuation					
EBIT Margin (%)	4.3%	4.8%	6.0%	5.7%	5.2%
ROIC (%)	7.6%	8.6%	10.2%	9.4%	8.7%
EV/EBITDA (x)	13.2	12.8	8.4	8.7	9.2
P/E (x)	16.6	12.5	8.2	8.5	9.0
Dividend Yield (%)	2.7	3.1	3.8	4.2	4.2

Income Statement (S\$'million)

FYE 31 Dec	FY19	FY20	FY21	FY22E	FY23E
Revenue	113.8	105.2	138.9	140.3	143.1
Cost of sales	(85.6)	(78.7)	(104.8)	(105.5)	(107.6)
Gross profit	28.2	26.5	34.1	34.8	35.5
Other income	0.6	1.9	1.1	1.1	1.1
Distribution cost	(15.5)	(14.9)	(17.6)	(18.2)	(19.0)
Administrative expenses	(5.5)	(5.7)	(6.3)	(6.7)	(7.2)
Other expenses	(2.9)	(2.8)	(3.0)	(2.9)	(3.0)
Share of profit of joint venture	1.1	1.6	1.6	1.7	1.7
Finance expenses	(1.0)	(0.7)	(0.8)	(0.8)	(0.8)
Profit before tax	5.0	5.9	9.2	8.9	8.4
Income tax expense	(1.0)	(0.7)	(1.2)	(1.2)	(1.1)
Profit for the year	4.0	5.3	8.0	7.7	7.3
Profit/(loss) attributable to:					
Owners of the Company	3.8	5.1	7.8	7.5	7.1
Non-controlling interests	0.1	0.1	0.2	0.2	0.2

Basic and diluted earnings per share (S\$ cents)	2.88	3.85	5.82	5.65	5.32
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Balance Sheet (S\$'million)

FYE 31 Dec	FY19	FY20	FY21	FY22E	FY23E
Cash and bank balances	14.9	16.2	11.5	11.6	14.1
Financial Assets	0.2	0.4	0.6	0.6	0.6
Trade and Other Receivable	22.9	24.2	31.1	28.0	28.5
Inventories	25.4	24.4	36.5	40.8	41.6
Others	2.4	2.5	4.5	4.5	4.5
Total current assets	65.9	67.7	84.2	85.4	89.3
PPE	10.3	12.7	15.2	15.3	14.9
ROU assets	2.8	2.7	2.8	2.6	2.4
Investment in associate	6.6	7.6	8.0	9.7	11.4
Others	0.5	0.7	0.7	0.7	0.7
Total non-current assets	20.2	23.6	26.7	28.3	29.4
Total assets	86.2	91.3	110.9	113.7	118.7
Bank Borrowings	17.6	16.8	27.5	27.5	27.5
Trade and Other Payables	12.1	13.5	18.0	15.9	16.2
Finance leases	0.3	0.2	0.4	0.4	0.4
Others	0.3	0.4	0.6	0.6	0.6
Total current liabilities	30.3	30.9	46.5	44.4	44.7
Bank Borrowings	0.9	2.6	1.4	1.4	1.4
Others	2.6	2.6	2.6	2.6	2.6
Total non-current liabilities	3.4	5.1	4.0	4.0	4.0
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	50.9	55.4
Equity attributable to owners of the Company	49.6	52.4	57.3	62.1	66.6
Non-controlling interests	2.8	2.9	3.1	3.2	3.3
Total equity	52.4	55.3	60.4	65.3	69.9
Total equity and liabilities	86.2	91.3	110.9	113.7	118.7

Cash Flow Statement (S\$'million)

FYE 31 Dec	FY19	FY20	FY21	FY22E	FY23E
Profit before tax	4.0	5.3	8.0	7.7	7.3
Depreciation charges	1.3	1.3	1.2	1.3	1.3
Share of profit of joint ventures	(1.1)	(1.6)	(1.6)	(1.7)	(1.7)
Others	1.0	0.7	1.1	0.8	0.8
Changes in working capital	1.5	0.7	(16.5)	(3.3)	(1.1)
Net Cash (used in)/ from operations	7.5	6.8	(7.8)	4.9	6.7
Purchase of PPE	(0.5)	(0.4)	(3.5)	(1.2)	(0.8)
Others	0.7	0.4	0.6	0.0	0.0
Net Cash (used in)/ from investing	0.3	(2.4)	(2.8)	(1.2)	(0.8)
Net Increase in Debt	0.2	(1.6)	2.1	(0.8)	(0.8)
Dividends paid	(1.7)	(2.1)	(2.4)	(2.8)	(2.7)
Others	(2.5)	0.9	6.1	0.0	0.0
Net Cash (used in)/ from financing	(4.1)	(2.8)	5.8	(3.6)	(3.4)

Ratios

FYE 31 Dec	FY19	FY20	FY21	FY22E	FY23E
Profitability (%)					
Gross profit/(loss) margin	24.8	25.2	24.6	24.8	24.8
Profit/(loss) before tax margin	4.4	5.6	6.6	6.3	5.8
Net margin	3.5	5.0	5.8	5.5	5.1
Liquidity (x)					
Current ratio	2.2	2.2	1.8	1.9	2.0
Quick ratio	1.3	1.4	1.0	1.0	1.1
Interest coverage ratio	5.9	9.2	12.4	12.1	11.4
Net Debt to Equity (%)	6.8	5.7	28.8	26.5	21.3
Valuation (x)					
P/E	16.6	12.5	8.2	8.5	9.0
P/B	1.2	1.2	1.1	1.0	0.9
Returns (%)					
Return on equity	7.9	10.0	14.2	12.6	11.0
Return on asset	4.6	5.8	7.7	6.7	6.1
Return on invested capital	7.6	8.6	10.2	9.4	8.7
Dividend payout ratio	52.0	39.0	34.4	35.4	37.6

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