

Fineotex Chemical Ltd

Bloomberg Code: FTXC IN

India Research - Stock Broking

BUY

Long Term Strategic Growth Drivers in Place...

Increased focus on specialty chemical to boost operating margin: Fineotex Chemical Limited (FCL) has posted consolidated revenue growth at CAGR of 8.0% over the period of FY12-16. EBITDA recorded significant growth at CAGR of 37.3% during same period whereas EBITDA margin has also grown by 819bps YoY to 24.7% in FY16 due to overall decline in raw material cost by 618 bps YoY. PAT Margin has grown by 301 bps YoY in FY16. We believe that the company will continue with growth momentum and it might record EBITDA and PAT growth of 24.6%-24.8% and 7.3%-9.5% respectively, during FY17E-18E on the back of robust demand by end user industries for higher yield specialty chemical production, onsite/offsite R&D facilities for product customization and niche clientele portfolio.

Capex to drive growth: FCL has planned for Rs. 80-100 mn capex for expanding manufacturing activities on recently acquired land in Nawada (Bihar), Khopoli (Maharashtra) and Ambarnath (Maharashtra) funded through 100% internal accruals. We believe that this capacity expansion will help to add topline growth by CAGR of 662 bps during FY16-18E.

Healthy Balance sheet with Zero debt: FCL is cash rich company with cash & equivalent of around Rs. 350-400 Mn (including investment in securities) & enjoying zero debt which will support to execute growth plans without affecting the financial performance of the company.

Valuation and Outlook

FCL majorly focuses on high margin specialty chemical business and capacity expansion plan with healthy financials coupled with zero debt and is currently trading at CMP of Rs.26.9, representing PE 15.1x FY18E EPS. We value the company at average P/E of 18.2x FY18E EPS. We initiate the coverage of the company with "BUY" recommendation on the stock with the target price of Rs. 33.0, representing an upside potential of 22.7%, for a time frame of 9-12 months.

Key Risks

- Intense competition.
- Foreign exchange risk.
- Switching sticky customers.

Exhibit 1: Valuation Summary

YE Mar (Rs. Mn)	FY14	FY15	FY16	FY17E	FY18E
Net Sales	867	1020	1087	1175	1236
EBITDA	92	165	265	289	307
EBITDA Margin (%)	10.7	16.2	24.4	24.6	24.8
Net Profit	65	129	170	187	200
EPS* (Rs.)	** 0.6	1.2	1.5	1.7	1.8
RoE (%)	10.6	18.3	20.3	18.9	17.5
PE (x) [#]	10.2	19.4	21.3	16.2	15.1

Source: Company, Karvy Research, *Adjusted for stock split of 1:5, **Adjusted bonus shares issued in proportion of 1:1 on face value of Rs. 10, # Represents multiples for FY14, FY15 & FY16 are based on historic market price

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Recommendation (Rs.)

CMP (as on Aug 29, 2016)	26.9
Target Price	33.0
Upside (%)	22.7

Stock Information

Mkt Cap (Rs.mn/US\$ mn)	3043 / 45
52-wk High/Low (Rs.)	38 / 18
3M Avg. daily volume (mn)	0.5
Beta (x)	1.2
Sensex/Nifty	27902 / 8607
O/S Shares(mn)	112.3
Face Value (Rs.)	2.0

Shareholding Pattern (%)

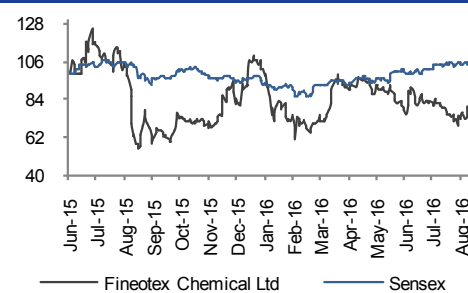
Promoters	71.72
FII	0.00
DII	0.03
Others	28.25

Stock Performance (%)

	1M	3M	6M	12M
Absolute	6	(10)	22	39
Relative to Sensex	7	(13)	1	32

Source: Bloomberg

Relative Performance*



Source: Bloomberg; *Index 100

Analyst Contact

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Company Financial Snapshot (Y/E Mar)
Profit & Loss (Rs. Mn)

	FY16	FY17E	FY18E
Net sales	1087	1175	1236
Optg. Exp (Adj for OI)	822	886	929
EBITDA	265	289	307
Depreciation	6	8	11
Interest	4	6	0
Other Income	33	36	38
PBT	289	311	333
Tax	91	98	106
Adj. PAT	170	187	200
Profit & Loss Ratios			
EBITDA margin (%)	24.4	24.6	24.8
Net margin (%)	15.7	15.9	16.2
P/E (x)	21.3	16.2	15.1
EV/EBITDA (x)	13.7	10.4	9.8
Dividend yield (%)	0.9	1.1	1.1

Source: Company, Karvy Research

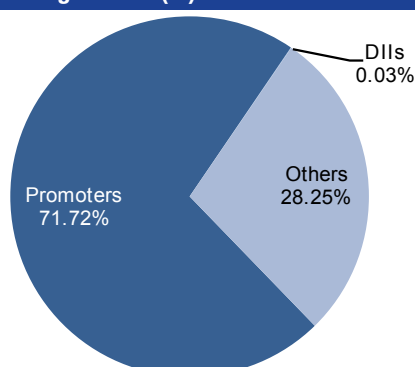
Balance sheet (Rs. Mn)

	FY16	FY17E	FY18E
Total Assets	1142	1302	1499
Net Fixed assets	131	203	271
Current assets	463	470	502
Other assets	548	628	725
Total Liabilities	1142	1302	1499
Networth	913	1062	1225
Debt	30	0	0
Current Liabilities	145	160	166
Other Liabilities	53	79	107

Balance Sheet Ratios

RoE (%)	20.3	18.9	17.5
RoCE (%)	22.0	20.3	18.5
Net Debt/Equity (x)	(0.1)	(0.1)	(0.1)
Equity/Total Assets (%)	0.8	0.8	0.8
P/BV (x)	4.0	2.8	2.5

Source: Company, Karvy Research

Exhibit 2: Shareholding Pattern (%)


Source: BSE, Karvy Research

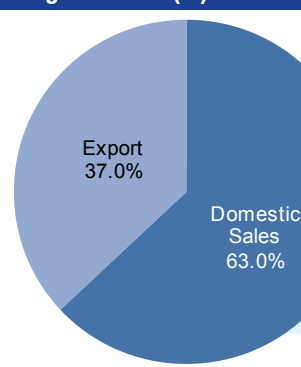
Company Background

Mumbai based Fineotex group was founded by Mr. Surendra Tibrewala in 1979. Later, in 2007, it was incorporated as Fineotex Chemical Ltd. Fineotex Chemical Ltd is an ISO 9001:2008, ISO 14001:2004, GOTS Version 4.0 & OHSAS 18001:2007 certified company and is one of the leading players in manufacturing & trading of Specialty Chemical segment across the globe and engaged in business more than 400 specialty chemicals and Enzymes, catering to various industries like Textile, Construction, Agrochemicals, Adhesives, etc. Over the years, the company has also successfully carved out a niche for itself and has strong global client portfolio along with global presence in almost 33 countries. The company has manufacturing facilities, located at Mahepe Navi Mumbai and Bangi, Malaysia with a combined production capacity of 22,000 MT/PA. FCL has 2 R&D laboratories in Mumbai, equipped with all modern age equipment. And, there is network of 68 to 70 distributors' pan-India and onsite R&D facility available across the region.

Cash Flow (Rs. Mn)

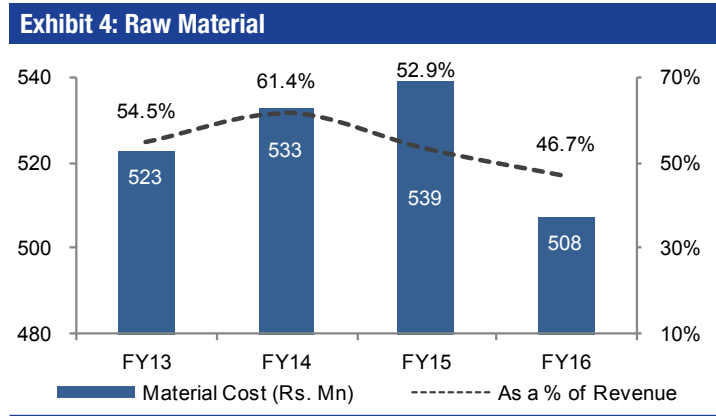
	FY16	FY17E	FY18E
PBT	289	311	333
Depreciation	6	8	11
Tax	(91)	(98)	(106)
Changes in WC	(58)	6	(15)
Others	(56)	(30)	(38)
CF from Operations	89	197	186
Capex	(20)	(80)	(80)
Others	(64)	(42)	(56)
CF from Investing	(84)	(122)	(136)
Change in Debt	20	(30)	0
Interest Paid	(4)	(6)	0
Dividends & Others	(12)	(37)	(37)
CF from Financing	4	(73)	(37)
Change in Cash	9	1	13

Source: Company, Karvy Research

Exhibit 3: Revenue Segmentation (%)


Source: Company, Karvy Research

Increasing footsteps in high margin special chemical manufacturing business:



Source: Company, Karvy Research

FCL posted consolidated revenue stream growth CAGR of 8.0% from FY12 to FY16 and EBITDA recorded significant growth at CAGR of 37.3% during same period whereas EBITDA margin has also grown by 819bps YoY to 24.4% in FY16 due to overall decline in raw material cost to the tune of 618 bps YoY. PAT Margin has grown by 301 bps YoY in FY16 due to management eye on high margin specialty chemical business. We expect that the company is likely to record EBITDA and PAT to grow at 24.9% and 9.5% YoY, respectively in FY17E. on the back of robust demand by end user industries for higher yield specialty chemical production based on increase quality expectation and fashionable textile products, available assistant for onsite/offsite R&D facilities for product customization and niche clientele portfolio.

Capex to drive growth; Funding through internal accruals:

FCL has planned for Rs. 80-100 Mn capex (funded 100% from internal accruals) for expansion manufacturing activities on recently acquired land in Ambernath (Maharashtra), Newada (Bihar) and Khopoli (Maharashtra). FCL is expected to generate Free Cash Flow (FCF) in the range of Rs. 106-117 Mn during FY17E-FY18E. This will bring much needed synergy to specialty chemical business and bring in optimization in use of various utilities and manpower which is currently available with the company. Currently, the company operates at 53%-55% capacity utilization from overall production capacity i.e., 22000MT/PA which is normal in this industry under same capacity. FCL has therefore set the target of its capacity utilization at 60% in next couple of years by way of adding machine and equipments on existing and new facilities. Such strategy could ramp up to meet additional orders in the course of business that requires higher production time. We believe that this capacity expansion will help to add topline growth by ~8.0% in FY17E.

Innovation will add value to the product and improve margin:

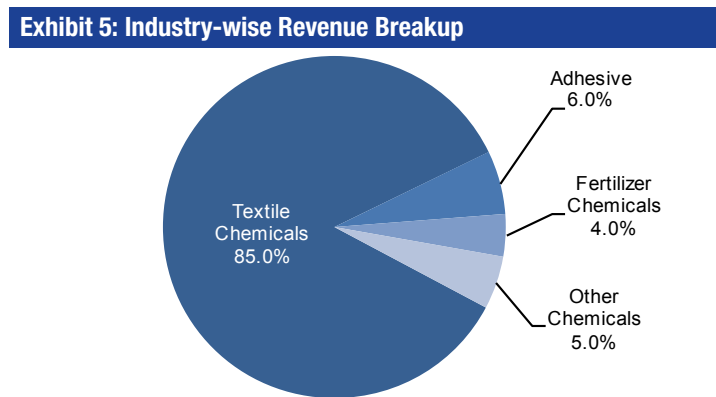
FCL has well established R&D based in Navi Mumbai with customization capabilities which suit to all types of substrates, processes and machines, which not only improve properties of the final product with higher efficiency but also help meet client demand of onsite/offsite product customization services. Continuing focus on new product will scale up organic growth of the company. The growing share of value-added products will make it possible for the company to enhance margin of the business.

Robust Balance sheet with Zero debt:

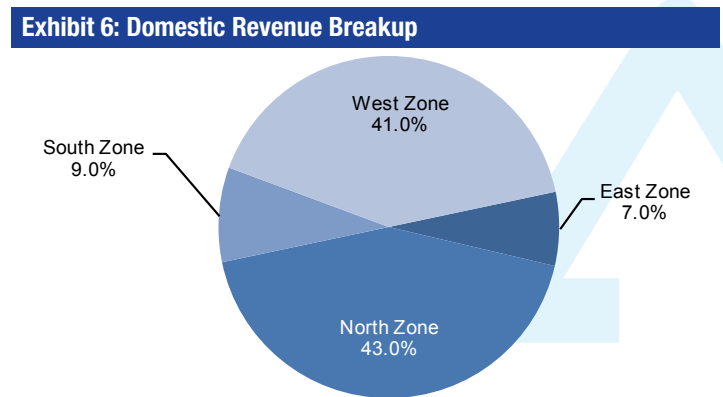
FCL is cash rich company with cash & equivalent of around Rs. 350 - 400 Mn (including investment in securities) in FY16 having zero debt to support organic and inorganic growth of the company. Further, the company has recorded healthy operating cash flow which helps to grow its operations. We believe that cash rich position helps the company to execute growth plans without adversely affecting the financial performance of the company.

Major Revenue Player - Textile Segment:

FCL manufactures the entire value chain for the textile industry including pre-treatment, dyeing, printing and finishing process. Textile contributes to 85.0% of total revenue stream and rest from other industries. The company is one of the strongest players in finishing textile chemicals segment in India, with a higher focus on all type of textile applications like cotton, polyester, polyester Lycra, polyester wool etc which have higher applicability in textiles products and are more profitable. It consumes more than 300 raw materials like DCDA, DMA, 2 Ethyl Hexanol, Maleic Anhydrite, Acrylamide, Organic Surfactants, Butyl & Styrene Acrylate, Deta, Para formaldehyde etc.

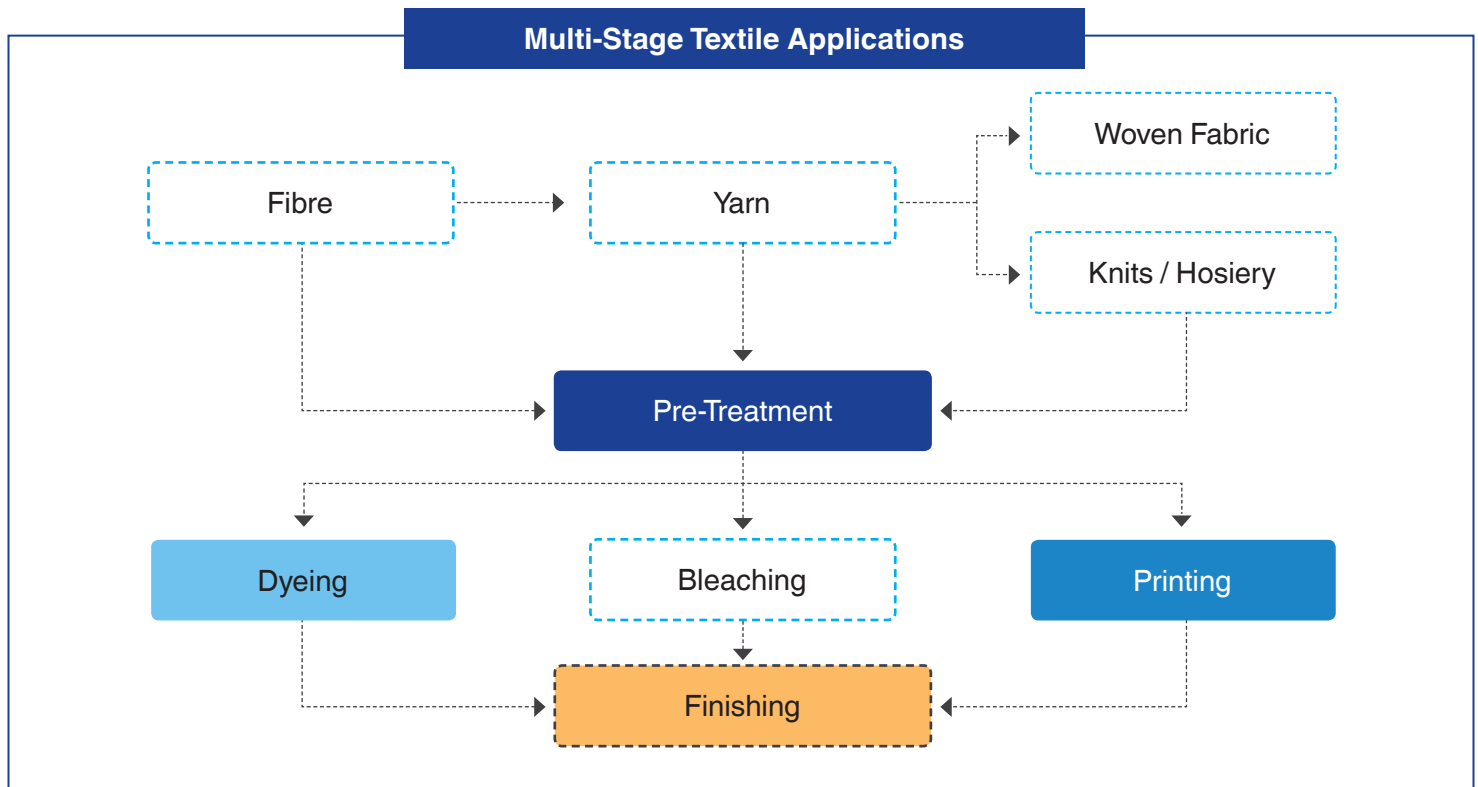


Source: Company, Karvy Research



Source: Company, Karvy Research

Overseas sales grew by 8.8% YoY to Rs. 435 Mn in FY16, recorded at the exchange rate prevailing on the date of the transaction across 33 countries including Argentina, Bangladesh, Indonesia, UAE, Thailand, Pakistan, Colombia, Vietnam, Singapore, Sri Lanka, Iran and Tanzania etc.



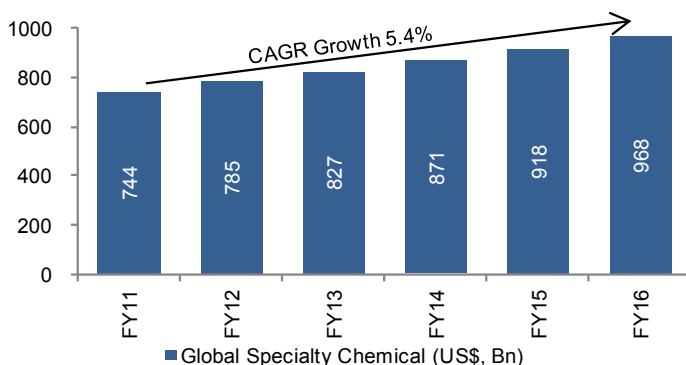
Industry Outlook:

Indian Specialty chemical sector to grow on the back of GDP Expansion, increase demand by end user industries:

The Indian Specialty Chemical sector has huge potential for growth and it is highly fragmented and rooted in science, provide valuable services and used as inputs into large number & different type of industries. Specialty Chemical businesses are low volume and high profitable business which is derived from basic chemicals and sold on the basis of their functionality, demanded by various industries needs like textile, dye and pigment, paint, adhesives, electronic chemicals, water management chemicals, oilfield chemicals, flavors and fragrances, rubber processing additives, paper additives, industrial cleaners and fine chemical. Sealants, coatings, catalysts also come under this category.

According to FICCI Specialty Chemical report and 12th Five year plan document, the Global Specialty Chemical industry growth is pegged at 22% to 23% which comes around \$740 Bn market size on the back of higher demand from various end user industries. In terms of CAGR, the industry is expected to grow at 5.4% annually to reach at ~ \$970 Bn market size by 2016 due to incremental demand by interlinked industries across the globe, especially Asian and emerging markets.

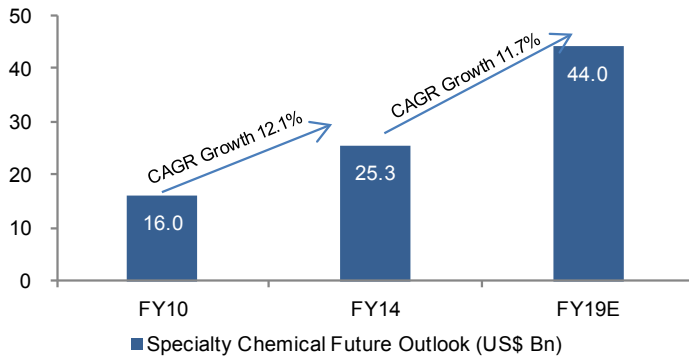
Exhibit 7: Global market size of specialty chemicals



Source: FICCI Specialty Chemical report and 12th Five year plan document, Karvy Research

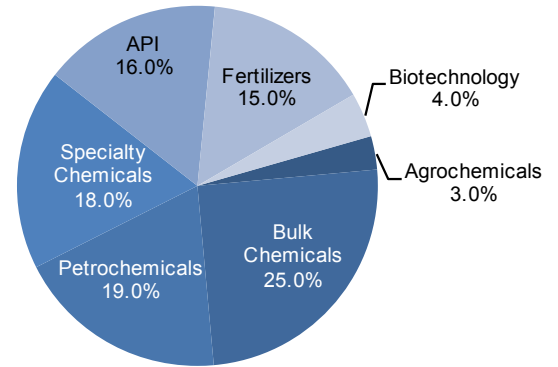
Furthermore, the Indian Chemical Industry is playing a critical role in nation building and enhancing the quality of life. It accounts for around \$17.7 bn (excluding agro chemicals, dyes & pigments) market size which is estimated to grow at CAGR of 17%, driven by end user industries growth, increased consumption level by end user industries, growing export market and Government of India's permission for 100% FDI in chemical industry. The growth potential consumption of specialty chemicals is strong and is expected to reach approximately \$44 bn by FY19E.

Exhibit 8: Indian Specialty Chemical Future Outlook (US\$ Bn)



Source: FICCI report, 2015, Karvy Research

Exhibit 9: Market Share of Indian Chemical Industry



Source: FICCI report, 2015, Karvy Research

Robust Client Network:

FCL has strong global footprint with presence across 33 countries majorly in Europe and Asian regions. FCL enjoys longstanding relationships with marquee clients in domestic markets also. Presently, FCL is a key supplier for around 65 corporate customers for textile industry and non-textile players like Sutlej, Himatsingka, Chenab, Birla, Grasim, Reliance, GHCL, Arvind, Jayasree, Bhaskar, Raymonds, Denim, Windsor, Pidilite, Clariant, etc.

TEXTILE INDUSTRY CLIENTS



OTHER INDUSTRY CLIENTS



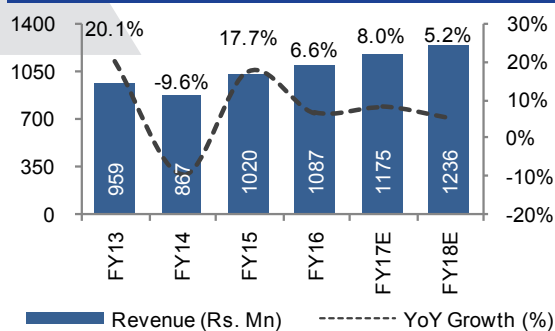
Future Business Outlook:

FCL has made gradual capital allocation to increase capacities as needed and runs its facilities at optimum utilization before planning any new capex. Presently, the company is taking priority to enhance its capacity in textile chemical segment with more product range i.e., more than 400 specialty chemicals and its novel applications and also looking to penetrate specialty chemical for non-textile segment by tapping broad clientele base.

Exhibit 10: Business Assumptions

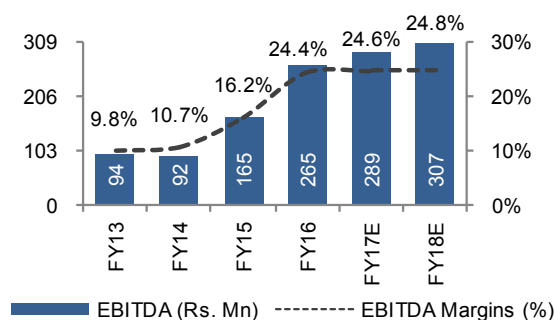
Y/E Mar (Rs. Mn)	FY15	FY16	FY17E	FY18E	Comments
Revenue	1020	1087	1175	1236	We expect the revenue to grow at CAGR 6.6% during the FY16-18E on the back of capex expansion, increased domestic demand and value addition of existing products.
Revenue Growth (%)	17.7	6.6	8.0	5.2	
EBITDA	165	265	289	307	
EBITDA Margins (%)	16.2	24.4	24.6	24.8	We expect that EBITDA margin would vary in the range of ~24%-25% during FY17E-18E due to strategic change & focus on higher margin specialty chemicals.
PAT (normalized)	129	170	187	200	Margin expansion led to robust PAT.
Fully Diluted EPS (Rs.)	1.2	1.5	1.7	1.8	Adjusted sub-division of one equity share having face value of Rs. 10/- into five equity shares of face value Rs. 2/- during FY13-16.
Fully Diluted EPS Growth (%)	98.7	32.2	9.3	7.3	
Capex (ex. Acquisition) - cash capex	52	20	80	80	Planned capex in the range of Rs. 80 Mn for next two years, could accelerate business growth.
Net CFO	120	89	197	186	Moderate top line growth and improved margin could drive cash flow from operation.
Net Debt	(82)	(120)	(90)	(64)	Debt free status puts the company in an advantageous position in terms of expanding business, thereby, increasing its existing market share.
Free Cash Flow	68	68	117	106	For any further expansion, we expect that internal accruals may be used during the next couple of financial years.

Source: Company, Karvy Research

Revenue to grow at CAGR of 6.6% during FY16-FY18E
Exhibit 11:


Source: Company, Karvy Research

FCL has experienced growth of revenue at a CAGR of 8.0% during FY12-16. Growth momentum continued further, expected to grow at CAGR of 6.6% during FY16-18E on the back of capex expansion, increased domestic demand, increasing valued share of existing clients & tapping newer clientele base.

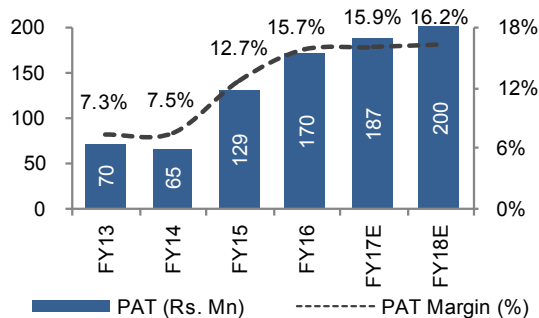
EBITDA to increase at a CAGR of 7.6% during FY16-FY18E
Exhibit 12:


Source: Company, Karvy Research

FCL has posted double digit EBITDA margin of 24.4% during FY16 due to focus on higher yield products led to low raw material cost. We expect that EBITDA margin to be better in the event of higher capacity utilization of its existing plants and majorly focus on value added product sales going forward, could accelerate margin growth in the range of 24.6-24.8% during FY16-FY18E.

PAT to increase at a CAGR of 8.4% during FY16-18E

Exhibit 13:

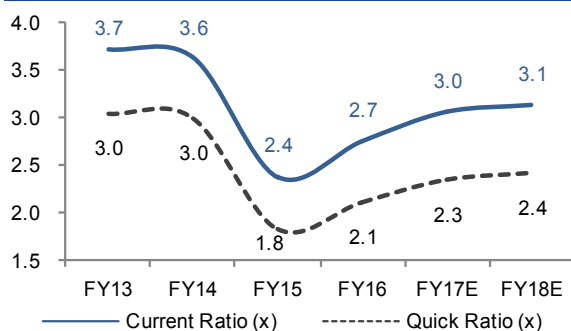


Source: Company, Karvy Research

FCL has recorded PAT growth of 29.8% CAGR during FY12-16. The momentum is likely to continue on the back of focus on higher margin and higher value product mix, register a growth momentum CAGR of 8.4% during FY16-FY18E.

Current Ratio

Exhibit 14:

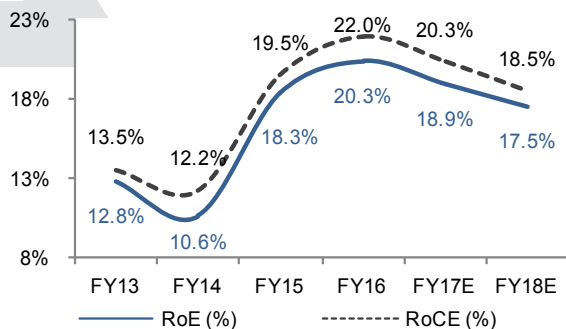


Source: Company, Karvy Research

FCL has average current ratio and quick ratio at 3.1x and 2.5x during FY13-FY16, respectively. During next couple of years, we are expecting average current ratio and quick ratio at 3.1x & 2.4x which show an overall good working capital management for the company.

RoE & RoCE to remain moderate growth during FY16-18E

Exhibit 15:

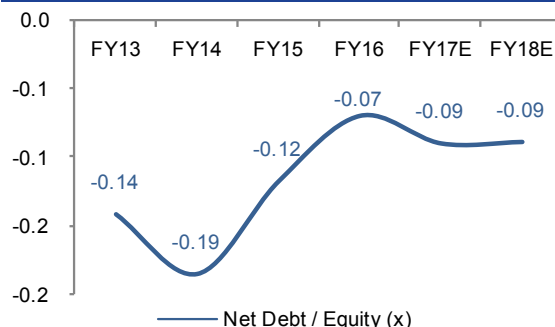


Source: Company, Karvy Research

FCL's RoE & RoCE stand at 20.3% and 22.0% respectively during FY16, which have grown up from 18.3% & 19.5% in FY15 due to strong growth in bottom line and operating margins. We believe that growth momentum likely to be continued for RoE and RoCE in next couple of financial years and register at 17.5%-18.9% and 18.5%-20.3%, respectively.

Net Debt / Equity Ratio

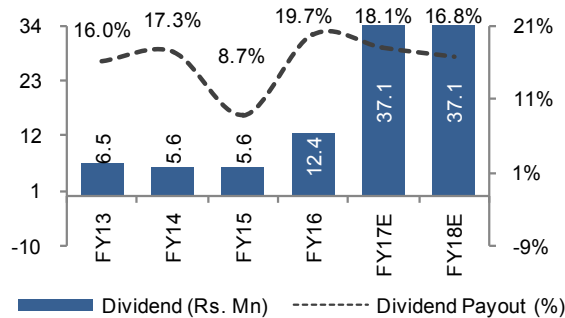
Exhibit 16:



Source: Company, Karvy Research

The company is debt free company having net debt to equity ratio of (0.07x) during FY16. We expect that the ratio will be at (0.09x) in next couple of financial years on the back of improving operating cash flows and repayment of debt through its internal accrual.

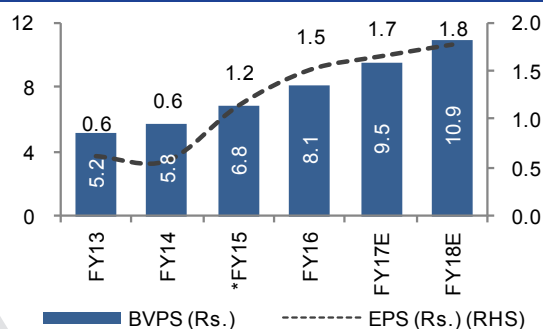
Dividend and Dividend Payout

Exhibit 17:


Source: Company, Karvy Research

Over the years, FCL has consistently distributed stable dividends with healthy payout ratios. We believe that the company is likely to continue its high dividend payout policy. The company also invested left over money in quoted and unquoted equity instruments and majority part of the amount in mutual funds.

EPS Vs Book value

Exhibit 18:


Source: Company, Karvy Research

*Bonus shares issued in proportion of 1:1 on face value of Rs. 10 in FY15.

On the back of value added services and product innovation would drive bottom line, the company's adjusted EPS (adjusted sub-division of one equity share having face value of Rs. 10 into five equity shares of face value Rs. 2 from FY13-16 and bonus shares issued in the proportion of 1:1 from FY12-14) has increased from Rs. 0.5 in FY12 to Rs. 1.5 in FY16 and is further expected to increase to Rs. 1.7 in FY17E and Rs. 1.8 in FY18E. On the back of strong performance and healthy balance sheet, the company's book value (adjusted equity share from FV Rs. 10 to FV Rs. 2) has increased from Rs. 6.8 in FY15 to Rs. 8.1 in FY16 which is further expected to increase to Rs. 9.5 in FY17E and Rs. 10.9 in FY18E.

Exhibit 19: Company Snapshot (Ratings)

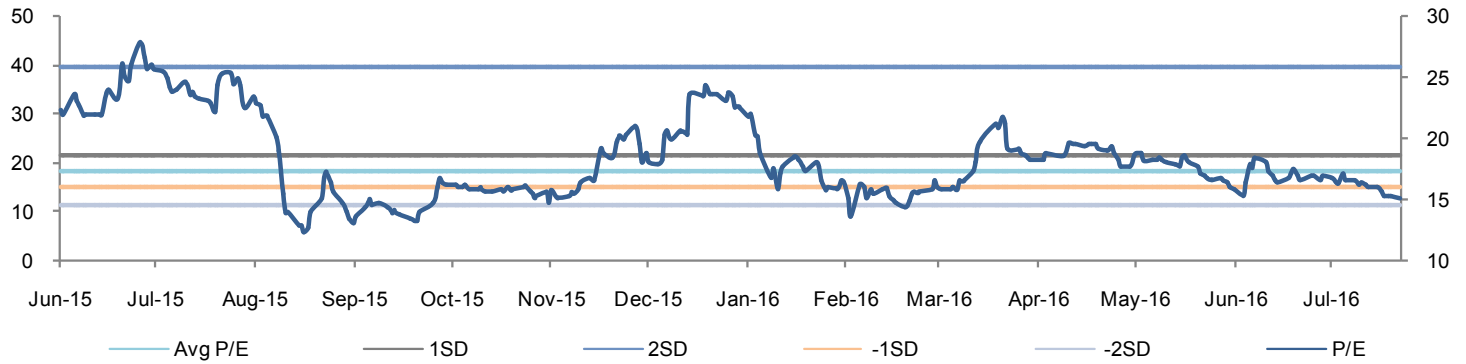
	Low					High
	1	2	3	4	5	
Quality of Earnings				✓		
Domestic Sales				✓		
Exports			✓			
Net Debt/Equity				✓		
Working Capital Requirement			✓			
Quality of Management			✓			
Depth of Management			✓			
Promoter			✓			
Corporate Governance			✓			

Source: Company, Karvy Research

Valuation & Outlook

FCL majorly focuses on high margin specialty chemical business and capacity expansion plan with healthy financials coupled with zero debt and is currently trading at CMP of Rs.26.9, representing PE 15.1x FY18E EPS. We value the company at average P/E of 18.2x FY18E EPS. We initiate the coverage of the company with “**BUY**” recommendation on the stock with the target price of Rs. 33.0, representing an upside potential of 22.7%, for a time frame of 9-12 months.

Exhibit 20: PE Band



Source: BSE, Karvy Research

Key Risks

- Intense competition.
- Foreign exchange risk.
- Switching sticky customers.

Financials

Exhibit 21: Income Statement

YE Mar (Rs. Mn)	FY14	FY15	FY16	FY17E	FY18E
Revenues	867	1020	1087	1175	1236
Growth (%)	(9.6)	17.7	6.6	8.0	5.2
Operating Expenses	774	855	822	886	929
EBITDA	92	165	265	289	307
Growth (%)	10.7	16.2	24.4	24.6	24.8
Depreciation & Amortization	3	5	6	8	11
Other Income	28	45	33	36	38
EBIT	118	205	292	317	333
Interest Expenses	4	3	4	6	0
PBT	112	202	289	311	333
Tax	33	56	91	98	106
Adjusted PAT	65	129	170	187	200
Growth (%)	(7.6)	98.7	31.9	9.5	7.3

Source: Company, Karvy Research

Exhibit 22: Balance Sheet

YE Mar (Rs. Mn)	FY14	FY15	FY16	FY17E	FY18E
Cash & Cash Equivalents	127	100	95	96	109
Trade Receivables	219	217	254	257	271
Inventories	114	104	115	117	122
Loans & Advances & Others	184	177	158	161	164
Investments	158	293	390	468	561
Net Block	76	117	131	203	271
Total Assets	879	1008	1142	1302	1499
Current Liabilities & Provisions	147	166	145	160	166
Debt	7	10	30	0	0
Other Liabilities	77	69	53	79	107
Total Liabilities	231	244	229	239	273
Shareholders Equity	112	225	225	225	225
Reserves & Surplus	535	539	688	838	1001
Total Networth	648	763	913	1062	1225
Total Networth & Liabilities	879	1008	1142	1302	1499

Source: Company, Karvy Research

Exhibit 23: Cash Flow Statement

YE Mar (Rs. Mn)	FY14	FY15	FY16	FY17E	FY18E
PBT	112	202	289	311	333
Depreciation	3	5	6	8	11
Finance Costs	4	3	4	6	0
Tax Paid	(26)	(43)	(91)	(98)	(106)
Inc/dec in Net WC	(59)	4	(58)	6	(15)
Other Income	(25)	(43)	(33)	(36)	(38)
Other non cash items*	1	(9)	(26)	0	0
Cash flow from operating activities*	9	120	89	197	186
Inc/dec in capital expenditure	(7)	(52)	(20)	(80)	(80)
Inc/dec in investments	142	(97)	(97)	(78)	(94)
Others	(16)	25	33	36	38
Cash flow from investing activities	119	(124)	(84)	(122)	(136)
Changes in Debt	(28)	(19)	20	(30)	0
Dividend paid [#]	(6)	(6)	(12)	(37)	(37)
Interest paid	(4)	(3)	(4)	(6)	0
Cash flow from financing activities	(38)	(28)	4	(73)	(37)
Net change in cash	90	(32)	9	1	13

Source: Company, Karvy Research, *Includes Foreign Exchange translation effect, # Includes dividend distribution tax

Exhibit 24: Key Ratios

YE Mar	FY14	FY15	FY16	FY17E	FY18E
EBITDA Margin (%)	10.7	16.2	24.4	24.6	24.8
EBIT Margin (%)	13.6	20.1	26.9	26.9	27.0
Net Profit Margin (%)	7.5	12.7	15.7	15.9	16.2
Dividend Payout Ratio (%)	17.3	8.7	19.7	18.1	16.8
Net Debt/Equity (x)	(0.2)	(0.1)	(0.1)	(0.1)	(0.1)
RoE (%)	10.6	18.3	20.3	18.9	17.5
RoCE (%)	12.2	19.5	22.0	20.3	18.5

Source: Company, Karvy Research

Exhibit 25: Valuation Parameters

YE Mar	FY14	FY15	FY16	FY17E	FY18E
EPS (Rs.)*	0.6	1.2	1.5	1.7	1.8
DPS (Rs.)*	0.1	0.1	0.3	0.3	0.3
BVPS (Rs.)*	5.8	**6.8	8.1	9.5	10.9
PE (x) [#]	10.2	19.4	21.3	16.2	15.1
P/BV (x) [#]	1.0	3.3	4.0	2.8	2.5
EV/EBITDA (x) [#]	6.4	15.0	13.7	10.4	9.8
EV/Sales (x) [#]	0.7	2.4	3.3	2.6	2.4

Source: Company, Karvy Research, *Adjusted for stock split of 1:5, ** Bonus shares issued in proportion of 1:1 on face value of Rs. 10 in FY15., # Represents multiples for FY14, FY15 & FY16 are based on historic market price

Stock Ratings	Absolute Returns
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