Dear Member,

We are pleased to inform you that Value Pick of March 2017 is released by our team today on 23rd April'17. Value Pick stock of the month is Balaji Amines Ltd **(BSE Code: 530999, NSE Code: BALAMINES)**. Balaji Amines has a market capital of Rs. 1259 crores and operates in chemical Industry.

## 1. Company Background:

Balaji Amines is a leading manufacturer of Aliphatic Amines. It specialized in manufacturing Methylamines, Ethylamines and derivatives of them. Balaji Amines commenced manufacture of Methyl Amines in the year 1989 and subsequently added facilities for manufacture of Ethyl Amines and other derivatives of Methyl Amines and Ethyl Amines to cater to the growing requirements of value based Specialty Chemicals.

The majority of chemicals manufactured by the company are specialty and fine chemicals. Amines are derivatives catering primary to Indian pharmaceuticals, Agro chemicals, Textiles, Refineries, Paints Dyes and Water treatment chemicals among several other industries.

The company enjoys leadership position in many of its products like Monomethylamine (MMA), Dimethyl amine (DMA), Trimethylamine (TMA), Dimethyl Amino Ethanol (DMAE), Mono Methyl Amino Ethanol etc.

The company's three manufacturing facilities are located at Solapur and Osmanbad in Maharashtra and Hyderabad in Telangana. Balaji commissioned its expanded Methylamines plant at MIDC, Chincholi, Solapur with a capacity of 30,000 MT per annum in March 2012. The second plant for manufacture of Di Methyl Formamide (DMF) with an installed capacity of 30,000 MT a year at MIDC Chincholi, Solapur was commissioned in March, 2013.

About 75% of the company's revenue come from the pharma and pesticide sectors while the rest is split amongst a number of other end users like oil refineries, water chemicals, rubber chemicals etc.

Although the company has a strong presence in the domestic market, majority of its products are also being exported to major customers worldwide and company has become one of the leaders in Specialty Chemicals among the International Specialty Chemical players.

Apart from chemical business, Balaji Amines also started a 5 star hotel in Solapur in Oct'13 with an investment of Rs 110 cr. It is a 129 room facility. The company has tied

up with Sarovar group for the management of the Hotel on management fee plus nominal revenue sharing basis.

## 2. Recent Development

### i) Robust Growth Outlook of Specialty Chemical Industry in India

The chemical industry has seen an increasing shift towards the Asian countries. The chemical industry in India accounts for ~2.1% of the GDP, making it a key constituent of the Indian economy. However, despite its large size and significant GDP contribution, the industry accounted for ~3.4% of the global chemicals industry (~USD 4 Trillion). In terms of volume of production, Indian chemical industry is the third largest producer in Asia and sixth largest in the world. Indian chemical industry is expected to grow at 14% CAGR, reaching US$ 235 bn by 2021.

Bulk chemicals account for ~40% of the Indian chemical industry, followed by agrochemicals and specialty chemicals which account for ~19-20% each. Pharmaceuticals and biotechnology, accounted for ~17% and ~4%, respectively.

Specialty chemicals are relatively high valued; their demand is rapidly growing, catering to a diverse end-product market. The Indian specialty chemicals market is estimated to reach US$ 60-65 billion by 2020. Global amines market is expected to reach ~US$ 14 billion by 2020 growing at a CAGR of 3.3% from 2014 to 2020. Asia Pacific is expected to witness the fastest growth, at a CAGR of 4.0% from 2014 to 2020.

It's important to note that globally demand of specialty chemicals is shifting to India from China. This is mainly on account of stringent effluent norms and increasing wage costs in China.Specialty chemical companies will prosper in India because of its chemistry, R&D skillset and economies of scales achieved by the country. This is supported by a paradigm shift in Chinese markets towards urgency of reducing pollution and investing in labour cost across industries. Specialty chemical companies are under pressure in China mainly on account of compliance, cost, and capacity issues. Hence, global chemical innovators are looking to outsource their manufacturing processes to India. This creates an opportunity for Indian firms over the next 5-10 years.

India is only one-tenth, the size of the Chinese specialty chemicals market, which throws up a huge opportunity for Indian companies with the potential to scale up and grow on a sustained basis.

### ii) Expansion of Morpholine & Acetonitrile Capacities

On the expansion front, the company has planned capex worth Rs ~30 crore through internal accruals to set up a Morpholine unit with an installed capacity of 7000 MTPA, which would give further strength to the company. According to the management, Morpholine capacity expansion is expected to come into the stream by end of quarter i.e. by the month of June 2017. Management expects 70% utilization level which will add 70 to 75 crores in the top line.

Moreover, Acetonitrile expansion is also in the pipeline and will come in stream by end of this year. Currently, environmental clearance is pending with the government of India. The company expects to get these approval soon to initiate further developments. Acetonitrile capacity will be about 18,000 MT per annum. However, management has planned 8000 to 9000 MT for the first year of operations.

### iii) Amalgamation of Balaji Greentech Products and Bhagyanagar Chemicals Ltd.

Management of the company approved in principle of Amalgamation of its subsidiaries, Balaji Greentech Products Ltd and Bhagyanagar Chemicals Ltd with Balaji Amines Ltd.

Bhagyanagar Chemicals Limited is limited to only a long term lease to its 100% holding company Balaji Amines Limited who is carrying out manufacturing activity. Balaji Greentech Products Limited is into manufacturing of energy efficient lamps and components. The company manufactures, supplies a comprehensive range of Compact Fluorescent Lamps (CFL).

## 3. Financial Performance

### Balaji Amines standalone net profit rises 47.48% in the Dec 2016 quarter

Net profit of Balaji Amines rose 47.48% to Rs 19.63 crore in the quarter ended December 2016 as against Rs 13.31 crore during the previous quarter ended December 2015. Sales rose 11.04% to Rs 180.22 crore in the quarter ended December 2016 as against Rs 162.30 crore during the previous quarter ended December 2015.

### Balaji Amines standalone net profit rises 84% in the September 2016 quarter

Net profit of Balaji Amines rose 84.00% to Rs 21.73 crore in the quarter ended September 2016 as against Rs 11.81 crore during the previous quarter ended September 2015. Sales declined 0.59% to Rs 172.15 crore in the quarter ended September 2016 as against Rs 173.18 crore during the previous quarter ended September 2015.

## 4. Investment Rationale

i) Amines technology is a closely guarded process with very few companies having access to such technology globally. Balaji Amines started developing these products for the first time in India and become a leading player in the segment commanding healthy market share of ~70% in domestic region for various products. Being it a complex process, we believe it will act as a major entry barrier for other domestic players, hence provide higher revenue and earning visibility to the company.

ii) Balaji Amines is the largest manufacturer of the widest range of aliphatic amines in India, which it manufactures largely for the pharmaceutical industry. Almost 50% of the Company's revenue comes from its pharmaceutical end users. Aliphatic amines are largely used by the pharma companies for creating antibacterial, anaesthetic, antibiotics, cardiac drugs, antidiabetics, and many more.

iii) Apart from the pharmaceutical industry, aliphatic amines are used by the agrochemical companies for creation of insecticides, pesticides, herbicides, insect repellent, animal feed, etc. India is an important player in the global agrochemicals industry, being fourth largest manufacturer of agrochemicals in the world and one of the largest exporters of agrochemicals globally.

iv) Balaji Amines has a large and reputed client base from pharmaceutical and Agro-chemicals Industry. Pharmaceutical contributes ~50% and Agrochemical contributes ~25% of company's total revenue. Some of the top customers of the company from Pharmaceutical segment include names like Aurobindo, Aventis, Cipla, Dr. Reddy's, Glaxo, Merck, Ranbaxy, Sun Pharma, Wyeth, Wockhardt etc. In Agrochemical segment, Balaji Amines client lists includes pesticide companies like Rallis, Meghmani, Gherdia Chemicals etc. Clients from other sectors include rubber chemical companies, refineries and water treatment companies. Well diversified clients from various sectors mitigates the risk of fall in demand of the company's product from a particular client or Industry.

v) The Indian pharmaceuticals market is the third largest in terms of volume and thirteen largest in terms of value. It accounts for ~2.4% of the global pharmaceutical industry in value terms and ~10% in volume terms and is expected to expand at a CAGR of ~16% to ~US$ 55 billion by 2020. Moreover, Indian agrochemical industry is expected to expand at 12-13% CAGR to reach ~US$ 7.5 billion by FY18-19. Industries like Pharmaceutical and Agrochemicals, among others, are growing at a good pace and thus, will result in the growth of Balaji Amines.

vi) Balaji Amines continue to focus on its core strength with emphasis on R&D, diversifying into new products with high growth potential, with particular emphasis on overseas market. This strategy will offset possible external turbulences like downturn in

market demand, escalation in raw material prices and change in regulatory frameworks for the company.

vii) The company is expanding its Morpholine capacity from 3,000 MT to 10,000 MT by end of Jun'17 with capex of ~30 crores, which is funded by internal accruals. Morphaline is mainly used in water and rubber treatment plants and is having robust demand in domestic market. With limited no. of players manufacturing Morpholine worldwide and increasing demand, Balaji Amines will be able to increase its market share. The company has also planned Acetonitrile expansion which is expected to come in stream by end of this year.

viii) Currently, utilization level of Dimethyl formamide plant (setup in 2013 with capacity of 30,000 MT) is ~20%. Utilization level is low mainly on account of excess supply at lower prices from China. However, management is confident of anti-dumping getting imposed on Dimethyl formamide (DMF). Any such development will boost the company's volumes and margins going forward.

ix) With the setup of first 5 Star hotel in the city, Solapur has started to be actively considered as a venue for large national conferences of Doctors as well as other professionals which works well in their budget. Management is optimistic to derive better operating margins from the hotel with increase in occupancy and better utilization levels of hotel's conference facility.

x) The company has stopped all the manufacturing activities at its loss making subsidiary – Balaji Greentech Products and has decided to merge it with itself. This would help the parent company in claiming the tax benefits on accumulated losses of its subsidiary. Balaji Greentech Products is into manufacturing and supplying of energy efficient lamps and components.

xi) Balaji Amines has a strong financial track record with ambitious growth plans. The company has registered sales CAGR of 12.9% and profit CAGR of 18.2% with ROE of 20.5% over last 5 years, its debt to equity ratio is 0.55 with high ROE and ROCE. The company's management has rewarded shareholders by paying regular dividend since FY2000, dividend yield at current price is 0.51%.

xii) As of Mar'17, promoter's shareholding in the company is 54.46% out of which 1.93% is pledged. With higher operating margins, company has reduced its debt significantly and also reduced pledged stake from 30.8% in Mar'15 to 1.9% in Mar'17. Moreover, promoters increased their shareholding marginally by 0.04% doing open market purchase during Dec'16 quarter.

## 5. Key Concerns & Risks

i) Balaji Amines faces stiff competition on few products from China mainly due to large scale production of Chemicals in China and incentives provided by its government. Any further competition from China for its other products can impact the growth forecasts of the company.

ii) Balaji Amines derives ~25% of its revenue from exports, hence any adverse currency movement could impacts its sales and profitability.

## 6. Saral Gyan Recommendation

As per our estimates, Balaji Amines is expected to deliver PAT of Rs. 119.3 crores in FY17-18 and Rs. 155.1 crores in FY18-19 with annualized EPS of Rs. 36.83 and Rs. 47.88 respectively. At current price of 388.70, stock is available at forward P/E multiple of 8.1X based on FY18-19 earnings which makes it attractively valued compared to other specialty chemical companies.

Considering robust growth in the high value, low volume specialty chemical segment with growing demand from pharmaceuticals, agrochemicals and other industries, expected increase in utilization level of company's Dimethyl formamide (DMF) plant going forward, planned expansion of Morpholine & Acetonitrile capacities during FY17-18, merging of loss making subsidiary Balaji Greentech Products to claim tax benefits on accumulated losses and company's attractive valuations with strong fundamentals, Saral Gyan team recommends **"Buy"** on **Balaji Amines Ltd** at current market price of Rs. 388.70 for target of 590 over a period of 12 to 24 months.

**Buying Strategy:**

- 70% at current market price of 388.70
- 30% at price range of 310-330 (in case of correction in stock price in near term)

**Portfolio Allocation: 3% of your equity portfolio.**

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a. Buy recommendation: This means that the investor could consider buying the concerned stock at current market price keeping in mind the tenure and objective of the recommendation service.
b. Hold recommendation: This means that the investor could consider holding on to the shares of the company until further update and not buy more of the stock at current market price.
c. Buy at lower price: This means that the investor should wait